

The Dodd-Frank Act: Why Utilities Need to Understand the CFTC

By Patricia Dondanville and Melody R. Barron

The dust has settled from the battles on Capitol Hill over financial reform. After President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”) in July, the handshakes were exchanged and the Oval Office pictures were snapped. The ink is now dry on an historic piece of legislation. But the work to make financial reform a reality is far from complete. The Dodd-Frank Act has now been handed off to the “would-be regulators” and the “to-be-regulated” for translation into practical, clear, workable rules.

The initial reactions from American business leaders to the Dodd-Frank Act ranged across the spectrum. Some companies assumed it would not affect them, and so cheered its Wall Street reform headlines without analyzing the text. From the perspective of many of those who have delved into its provisions, a common reaction seems to be that the Dodd-Frank Act is scary. And it is. It probably scares the people the law was intended to scare, like speculators who make their money gambling recklessly in swaps markets and may be manipulating the markets or taking large risks that could threaten the financial system. But it also scares the companies, including energy companies, whose businesses depend on physical commodity transactions and related over-the-counter derivatives to manage the commercial risks of their day-to-day activities.

The over-the-counter or “OTC” (bilateral contract) markets for energy and energy-related commodities and derivatives have been developing rapidly over the past 20 years. These markets have become an essential risk management tool for an industry that the American public relies on year-round and around-the-clock for lights, heat, and computers in industrial plants, commercial businesses, and residences. In the wake of the 2008-2009 financial market meltdown, the federal government’s



Patricia Dondanville



Melody R. Barron

Patricia Dondanville is a partner and Melody R. Barron is an associate at Schiff Hardin LLP. This article represents the views of the authors, and does not necessarily reflect the views of Schiff Hardin LLP or any of its clients.

reaction was to immediately and comprehensively regulate the “unregulated,” “dark” derivatives markets. But in doing so, little distinction was made in the legislation between the financier on Wall Street and the electric company down the street. The sweeping nature of the Dodd-Frank Act will impose many new burdens on industries that were already comprehensively regulated and did nothing to cause the financial market meltdown. The discussion of the legislation’s unintended consequences has reached a fevered pitch on blogs and editorial pages.¹

Title VII of the Dodd-Frank Act is the section that deals with the OTC derivatives markets. Since the passage of the Commodity Futures Modernization Act of 2000, OTC derivatives based on energy and energy-related commodity transactions have been explicitly exempt from the Commodity Exchange Act (CEA). Energy commodities were “exempt” commodities, and swap agreements were exempt as well.² Title VII of the Dodd-Frank Act summarily eliminates the current exclusions and exemptions from the Commodity Exchange Act on which energy companies have relied for a decade to transact in the OTC derivatives markets. The Dodd-Frank Act instead brings all “swaps” under the jurisdiction of the Commodity Futures Trading Commission (CFTC) and all “securities-based swaps” under the jurisdiction of the Securities Exchange Commission. The law will require anyone considered a “swap dealer” or “major swap participant” to register and follow strict requirements for recordkeeping, reporting, business practices, capital, margin, and position limits. And the law requires any person or entity that enters into a “swap,” to either clear that swap and transact on a CFTC-regulated exchange or other regulated entity, or to find an exception from the clearing and/or exchange-trading requirements.

The Dodd-Frank Act fundamentally altered the rules, the playing field, and the referees for transacting in energy and energy-related commodities and derivatives. Utilities will be affected and the cost of energy to the consumer will increase. The only question that remains is by how much. And the answer to that question will become clear over the next five months as the regulators convert hundreds of pages of law into dozens and dozens of rules that may or may not allow utilities to continue cost-effective hedging of the commercial risks inherent in their businesses.

Background: How Do Utilities Use “Swaps” Today?

Utilities use swaps to manage the commercial risks inherent in their public service business, risks like commodity

price and availability risk for the commodities they deliver to the consumers in their service territories. Those who pay attention to their monthly electric bill can understand the volatility of the price of power and gas. Price volatility in a commodity market derives principally from changes in market fundamentals—supply and demand in economic terms. In the energy industry, electric generation, natural gas production, and transmission or transportation events are economic supply issues. “Load” or “demand” for energy are utility terms for economic demand. As usual in the energy business, weather is the wild card (as is the inability to store power in commercial quantities). When a heat wave hits the entire Midwest in mid-July, the demand for electricity skyrockets. If the heat wave hits at the same time as a generation outage in Michigan or Illinois, Midwest utilities have a problem. The same holds true for an unexpected and extended ice storm or blizzard during the long, cold Midwest winter.

To plan for both expected and unexpected, but always unpredictable, swings in supply and demand, utilities turn to the energy and energy-related commodities and derivatives markets. There, the companies are able to buy and sell natural gas, electric power or capacity, fuel for generation, or other energy-related products. The companies can also hedge commercial risks using financially-settled transactions. Utilities contract with each other or with other types of market participants, such as financial entities (banks, bank affiliates, or hedge funds), merchant generators, and natural gas producers, to obtain certainty and reduce the volatility of the prices they will pay and receive for energy. The utilities can then pass the hedging benefits on to the ultimate consumers of energy—American businesses and households.

Today, most energy hedging transactions are bilateral commercial contracts between “counterparties.” Typically in each of these contract relationships, the legal and administrative terms are initially documented on a standard master or “umbrella” agreement form developed by an industry group (such as the ISDA Master Agreement or the EEI Master Agreement). The form documents are negotiated by attaching schedules and annexes to the form master agreement, and each such set of documents is tailored to meet the requirements and needs of each pair of counterparties. Credit support/credit risk management terms for the trading relationship are carefully negotiated under an annex to the master agreement. In assessing relative credit risk, each party assesses the financial and operating strength of its potential counterparty and determines what sort of credit support, if any, would be required to transact once or many times with that counterparty. The counterparties may then decide to transact without credit support, collateral, or “margin,” or they may then set up a protocol for measuring net (unsecured) credit exposure, and posting and exchanging credit support or collateral based on several factors, including the type of transactions that are contemplated

between the parties.

Once a master agreement is in place, the two counterparties are then able to agree quickly and efficiently on individual transactions, without having to spend time and resources renegotiating the broader contractual and credit risk framework. Utilities seeking to hedge and mitigate their commercial risk typically have a number of these master agreement relationships in place so that they have many counterparty options for each hedge—taking into account the proposed size, duration, pricing, and other transaction-specific terms of the potential hedge and weighing that against the net credit risk exposure to and from the counterparty.

The Regulators

(And How the Dodd-Frank Act Changes the Landscape)

Natural gas and electric utilities are subject to comprehensive regulation on the federal, state, and, sometimes, on the local level. Moreover, the “markets” for natural gas and electricity transactions are also heavily regulated. The Federal Energy Regulatory Commission (FERC) is tasked with regulating the transportation and sale of electricity and natural gas in interstate commerce under the Federal Power Act (16 USC 791 *et seq.*) and the Natural Gas Act (15 USC 717 *et seq.*). FERC’s mission is to ensure that utilities provide reliable natural gas and electricity to American consumers and businesses, and to ensure that rates, terms, and conditions for such natural gas and electricity are “just and reasonable.” Any rule that FERC promulgates, and any action FERC takes, is guided by that underlying mission.

In contrast, the mission of the CFTC under the CEA is to regulate commodity and derivatives trading markets. The CFTC’s purpose is to promote price discovery and price transparency, so that commodity futures transactions can be conducted on liquid, fair, and financially-secure trading facilities. The public interest that drives the CFTC is to keep commodity trading markets transparent, liquid, and efficient. The CFTC has no statutory mandate to ensure the reliable, affordable delivery of energy.

The Dodd-Frank Act authorizes the CFTC to establish and define a new market structure for energy and energy-related commodity and derivatives transactions, and all other forms of OTC derivatives transactions. It empowers the CFTC to establish this new structure, and to exercise jurisdiction over all OTC derivatives, by regulating the derivatives transactions and by regulating the persons and entities that engage in such transactions.

The Dodd-Frank Act Authorizes the CFTC to Regulate Transactions and Persons

The CFTC’s general directive from Congress under the Dodd-Frank Act is to have as many “swaps” as possible cleared by central clearing entities in order to reduce “systemic risk” to the financial markets, and to have as

many “swaps” as possible traded on CFTC-regulated exchanges, or on or through other CFTC-regulated entities, in order to increase transparency in the markets. The CFTC has taken this directive to heart. As CFTC Chairman Gary Gensler noted in a speech: “We intend to comply fully with the statute’s provisions and the Congressional intent to lower risk and bring transparency to the markets.”³ Commissioner Jill E. Sommers stated that “[g]enerally the headline is that swaps will now be subject to stringent regulatory oversight.”⁴ And, as Commissioner Bart Chilton commented:

This new regulation is a game changer. Sometimes, as a regulator, I’ve felt they gave me a striped shirt and a whistle but not enough authority to really enforce the rules. Now the rulebook has been expanded. There will be more referees. The game will be a safer and sounder one.⁵

What seems to have been lost in the fervor of regulatory reform is that the CFTC, along with its sister regulators, is walking into a world of existing commercial transactions and relationships. The Dodd-Frank Act has painted all “swaps” with a single brush—“requires regulation”—and handed everything over to the regulatory agencies to sort out. Congress has given expansive new authority to the CFTC, a financial markets regulator whose mission is focused on commodity transaction price transparency and that has historically not been involved in regulating the commodities and derivatives markets between commercial businesses. The CFTC must now regulate scores of commercial transactions between and among nonfinancial entities that utilize derivatives for myriad different reasons—some for commercial risk management reasons, some for speculative purposes, and everything in between.

Regulating Transactions: What Is a “Swap”?

The Dodd-Frank Act makes it unlawful for a person to enter into a “swap” without complying with the CEA and the related rules to be published by the CFTC. If a company uses “swaps” in any part of its business, then the CEA will regulate those transactions beginning in July 2011.⁶ The amended CEA contains a lengthy definition of the term “swap” that seems to encompass any transaction that transfers any financial risk from one contract party to the other contract party. The expansive nature of this definition is no accident.

The definition of a “swap” casts as wide a net as possible, rather than defining a closed universe list of transaction types. It then lists limited exclusions for transactions that Congress determined did not require new regulations, such as futures or options that are already traded on a CFTC-regulated exchange. For utilities, a key exclusion from the definition of “swap” is the exclusion for the sale of “a nonfinancial commodity . . . for deferred

shipment or delivery . . . so long as the transaction is intended to be physically settled.”⁷ However, none of these underlined words is defined in or correlates directly to the wording in or interpretations under the pre-Dodd-Frank Act CEA, leaving little guidance for the future.

The imprecise wording of this and other provisions in the Dodd-Frank Act leaves much to the discretion of CFTC rulemaking in terms of how intrusive the new regulatory scheme will be for utilities. In the coming months, the CFTC must clarify what will and what will not be considered a “swap,” as well as clarify the exclusions and a host of related definitions. Hopefully, by doing so, the CFTC will give market participants certainty as to what transactions it intends to regulate. The CFTC has also been asked to clarify whether certain existing regulatory exemptions, e.g., for commercial commodity options, are still applicable. In addition, the Dodd-Frank Act permits the CFTC to exempt certain energy industry specific transactions (tariffed transactions) from this new regulatory regime. But it will be up to the utility industry (along with other interested parties and, perhaps, FERC or the RTOs) to request, and explain to the CFTC the need for, such broad conceptual exemptions.

Regulating Persons: Who Is Regulated?

The CFTC has also been given the power to regulate participants in the markets for swaps. The CFTC will register and regulate existing and new market infrastructure entities like central clearing organizations and “designated contract markets” (i.e., CFTC-regulated exchanges), as well as new entities labeled “swap execution facilities” and “swap data repositories” under the Dodd-Frank Act market structure. In addition, the CFTC will continue to register and regulate “futures commission merchants,” “commodity trading advisors,” and “introducing brokers,” as it does now, even if those entities are engaged only in swaps, and not futures or exchange-traded options. Moreover, the CFTC will register and regulate two newly defined types of market participants—“swap dealers” and “major swap participants.” These new types of market professionals will have reporting and recordkeeping requirements, mandatory clearing and on-exchange trading, capital and margin, and other business conduct standards.

The Dodd-Frank Act provides an exception from clearing and exchange-trading requirements for “end users”—nonfinancial entities that use swaps to mitigate or hedge “commercial risk” so long as certain CFTC filings are made. However, the definition of “commercial risk,” along with the details about applicability of the end-user exception, is left to the CFTC rulemaking process. Until the CFTC rules are finalized, utilities cannot be sure that they will be able to use the end-user exception or, if so, which risks they can hedge using swaps. Moreover, regardless of whether an entity is excepted from clearing and exchange-trading requirements, all market participants

will still face new recordkeeping and reporting obligations under the Dodd-Frank Act.

The definitions of these new types of professional participants in the swap market—“swap dealers” and “major swap participants”—focus, among other criteria, on entities that make a market in swaps, have a substantial position in swaps, or whose positions create substantial swaps exposure for counterparties. It is unlikely that many natural gas or electric utilities will fall within either of these defined categories. But, once again, it bears noting that these terms are subject to CFTC rulemaking.

Important Questions for Which Utilities Need CFTC Answers

Once the definitions are clarified by the CFTC rulemakings, one of the two most important questions for utilities is whether they will be protected in their hedging activities by the “end user exception.” End users of swaps will be able to opt out of clearing and, in most cases, will be concurrently exempt from a requirement to transact on an exchange.⁸ In theory, the end-user exception *should* allow nonfinancial entities, such as utilities, which use swaps to hedge or mitigate “commercial risk,” to continue to hedge that risk as they have done historically in the OTC markets. However, end users are concerned that the exemption will be lost or made unusable during the CFTC rulemaking process—resulting in end users being inadvertently swept up in the Dodd-Frank Act regulations where Congress did not intend for them to be burdened.⁹ That congressional “intent” is most clearly laid out in a letter written by Senators Dodd and Lincoln, as chairs of the responsible Senate committees, to Representatives Frank and Peterson, as chairs of the correlated House committees in Congress (the “Dodd-Lincoln Letter”). The Dodd-Lincoln Letter is cited numerous times in the congressional colloquies prior to voting on the Dodd-Frank Act. However, as the chair of the CFTC, Gary Gensler, has pointed out, it is not the Dodd-Lincoln Letter that guides the CFTC rulemaking, it is the Dodd-Frank Act itself.¹⁰

Even if an entity utilizes the “end user exception” from clearing and exchange-trading, end users who engage in swaps will still have to comply with CFTC registration, recordkeeping, and reporting regulations. And such regulatory compliance may be burdensome and costly. This, too, will be determined during the CFTC rulemaking process. The Dodd-Frank Act requires reporting of non-cleared swaps to one of the new registered entities or to the CFTC, and a swap to which no swap dealer or major swap participant is a party must be reported by one of the two parties to the transaction. Moreover, broad, internal recordkeeping policies are applicable in order for an end user to be in a position to comply with the CFTC reporting requirements. Finally, if a utility presumes it will always be an end user and the nonreporting party, the end-user exception itself is predicated on

the requirement that the end user notify the CFTC “how it generally meets its financial obligations associated with entering into non-cleared swaps.”¹¹ The Dodd-Frank Act has authorized the CFTC to establish how detailed that notification needs to be (and how frequently it will need to be made.) These types of regulations will directly affect (increase) the costs borne by utilities to hedge their commercial risks using swaps.

In addition to these direct costs, the CFTC’s regulation of other market participants will likely cause end-user utilities to incur indirect burdens and costs. After the definition of swap and the end-user exception, the third most important question for utilities is whether and how new CFTC margin rules for swap dealers and major swap participants will affect a utility’s costs to engage in non-cleared swaps. The Dodd-Frank Act requires the CFTC to write margin rules that ensure the safety and soundness of swap dealers and major swap participants, and to avert systemic risk to the American financial system. However, if end users are (through broad or ambiguous rules) required to post margin for non-cleared hedging transactions, the economic benefit of the end-user clearing exception may be negated. The Dodd-Lincoln Letter made it clear this was not Congress’s intent.

The other, more subtle problem related to margin rules, is that if the end user’s counterparty is required to maintain a certain amount of regulatory capital against an end user’s transactions, it will pass those costs on to the end user. And, if the swap dealer is required for some reason to *post* margin to the end user, then the end user has to hold and administer that margin. In a bilateral, non-cleared world there is no central clearinghouse or exchange clearing member to hold and administer margin. There is only the other contract counterparty. And most utilities do not have sufficient back office staff to perform the necessary daily mark-to-market valuations on all outstanding transactions and hold, post, and exchange daily margin.

The whole concept of “marginizing” presumes a financial-intermediated world like the system that currently exists in the CFTC-regulated markets. And the costs of such financial-intermediation are one of the primary reasons why utilities today manage their commercial risks in the OTC markets.

The reforms Congress enacted under the Dodd-Frank Act were intended to bring “transactions and counterparties into a robust, conservative and transparent risk management framework.” However Congress has acknowledged that not every transaction and counterparty needs to be regulated in this way.¹² Unfortunately, the text of the Dodd-Frank Act is broad and ambiguous, with additional confusion caused by missing cross-references and undefined or inconsistently referenced terms. The CFTC has been given the momentous task of creating regulatory order out of a sometimes chaotic and always complex tome of legislation. Although the CFTC has the ambition to bring order out of the chaos, the sweeping scope of change and the fragility of the various financial markets

may require more time and study in order to impose such order without unintended and harmful consequences.

The Rulemaking Marathon (the CFTC Task Forces)

The CFTC rulemaking process began in September 2010, and the CFTC has, as of January 25th, published two final rules, 33 proposed rules, and four of Advanced Notices of Proposed Rule-making for public comment.¹³ As time marches forward, the overwhelming scope of this regulatory task is becoming clearer. The CFTC must promulgate and finalize rules under the Dodd-Frank Act that are effective to regulate a wide variety of markets, often in an environment of existing, specialized, and unique commodities and derivatives market structures.

The CFTC has established 30 “task forces,” each comprised of CFTC staff members, and each focused on a specific topic under the Dodd-Frank Act. No one task force is dealing with all energy and energy-related (utility) issues. Some of the more important task forces for utilities include: “Capital & Margin for Non-Banks” and “End User Exception.” Each task force will recommend rules to the CFTC on its designated topics, and the public is invited to submit comments on those rules. Each task force has its own page on the CFTC website and its own e-mail address through which interested parties can submit comments. Utilities and utility trade associations are planning comments on 12 to 20 task force topics.

Although the CFTC has attempted to make the task forces an efficient division of labor, given the press of statutory deadlines, some in the industry have expressed concern that the task forces have evolved into separate “silos” of rulemaking—a structure that frequently requires commenters to repeat concepts and explanations to ensure that each individual task force is educated on the breadth of issues implicated by each discrete area of rulemaking. If each task force completes its marathon, and yet commercial business concepts and issues fall between the silos, the new Dodd-Frank Act market structure may yet prove unworkable.

Interim Deadlines

While all this rulemaking is proceeding, the CFTC has several interim statutory deadlines with which to contend. For example, in October the CFTC issued an “interim final rule” on swap reporting and record-keeping for non-cleared “swaps.” The interim final rule was supposed to tell entities transacting in non-cleared swaps what CFTC reports they would need to file and, consequently, what records they should retain in order to be in a position to comply with CFTC reporting rules for “swaps” entered into prior to the enactment date of the Dodd-Frank Act. Unfortunately, the interim final rule was less than clear, partly because the definition of “swap” has yet to be finalized. Actual reporting has been deferred until new market infrastructure entities called “swap data repositories” are established (again through CFTC rulemaking). Most

market participants are being advised that they should hold *all* information *related* to non-cleared swaps entered into prior to the enactment date of the Dodd-Frank Act, freezing those records for and construing the term “swap” broadly until the CFTC gives further guidance. Some market participants have also asked the CFTC to implement a “safe harbor,” so when the CFTC does begin requesting records, companies who have made a good-faith attempt to comply with the interim final rule will not be subject to penalties for inadvertently discarding information.

In late December, the CFTC issued a second “interim final rule” that purported to impose, without notice, record-keeping obligations in respect of “transaction swaps”—those transactions entered into post-enactment date, but prior to the effective date of final recordkeeping and reporting rules (which have not yet been proposed). The lack of notice, the accretive nature of the ongoing recordkeeping requirements, and the continuing ambiguities of undefined terms in the second interim final rule are troublesome.

The reporting requirements present an entire host of problems for energy utilities. Ultimately, the CFTC will have to identify precisely what will have to be reported, by whom, how it must be reported, to whom, in what format, and within what time periods. The Dodd-Frank Act calls for “real-time reporting.” But, in the utility industry, the primary business focus is to deliver power and gas year-round and around-the-clock to Main Street. Utilities are concerned that complying with such financial markets reporting rules will divert significant resources from utility operations while doing little to reduce systemic risk or bring “transparency” to the global financial markets.¹⁴

Another interim statutory deadline was for the CFTC to establish new regulatory position limits for futures, exchange-traded options, and “swaps” where the underlying asset is an “exempt commodity,” which includes energy commodities. The position limits to be established are to be as appropriate to limit excessive speculation. According to the Dodd-Frank Act, the CFTC was to establish such position limits by January 17, 2011. But the CFTC has acknowledged that it does not have enough information about swaps markets (or the markets for individual underlying exempt commodities) to appropriately establish such limits.¹⁵ Moreover the definitions and other rules that make up the foundation of the new market structure (including the definition of a “swap”) were not finalized by the position limits deadline. Instead, on January 26, 2011, the CFTC issued for comment a proposed rule setting forth position limits for certain types of positions on certain exempt commodities.¹⁶ Some CFTC commissioners have questioned whether position limits in energy swaps and commodities are appropriate at all, a matter that was debated by the CFTC even prior to the enactment of the Dodd-Frank Act.¹⁷

An additional statutory deadline of note was for a memorandum of understanding (MOU) establishing new jurisdictional lines between FERC and the CFTC, to be filed with relevant

congressional committees by January 17, 2011.¹⁸ The jurisdictional MOU was intended by Congress to encourage the agencies to work together to reduce overlapping and duplicative regulation of the energy markets, where in the past jurisdictional conflicts have been rife. The agencies were “to establish procedures to avoid any conflicting or overlapping regulation” so that the two agencies apply their respective authorities to ensure that the regulations created under the Dodd-Frank Act are effective and efficient. The utility industry was hopeful that the MOU would reflect agreement as to which regulator has primary (or secondary) jurisdiction over identified types of energy and energy-related physical or financial transactions, rather than continue the reciprocal “we have exclusive jurisdiction” standoff that has plagued the industry with unnecessary costs and compliance complexity. However, the statutory deadline passed, and as of February 1, 2011, it seems no MOU has yet been agreed upon between the CFTC and FERC.

New “Cops” on the Energy Markets Beat

The Dodd-Frank Act gave the CFTC substantial new enforcement powers in the “swaps” markets—without guidance as to how the existing enforcement regimes in some markets should be coordinated. These new CFTC powers will likely result in more CFTC-FERC duplicative requirements and requests, and more compliance and enforcement complexity for utilities and other energy companies.

New Jurisdiction to Prohibit Market Manipulation and “Disruptive Trading Activity”

The CFTC is a financial market regulator focused on its mission to bring price transparency, liquidity and financial security to commodity and derivatives markets. The CFTC has a strong and effective enforcement staff to police the markets it regulates, and to punish violators of its market rules. The Dodd-Frank Act gave the CFTC new and expanded jurisdiction to prosecute “market manipulation” in the energy markets. The CFTC’s enforcement jurisdiction is now concurrent with, if not broader than, FERC’s jurisdiction and, in some cases, the jurisdiction of the antitrust regulators. But the CFTC is not governed by any of those regulators’ enforcement precedents or agency interpretations. Again, utilities need to remember that the CFTC is not an energy market regulator. The activities of utilities as load serving entities will be analyzed not with their public service mission in mind, but with the same skeptical enforcement eye that analyzes the behaviors of any other market participant.

Be Aware—the Whistleblower Is Out There

Some commentators have called the Dodd-Frank Act whistleblower provisions the most dangerous and potentially costly provisions for energy companies. If a whistleblower provides to the CFTC “original information” that

contributes to a CFTC enforcement action, and the CFTC “monetary sanctions” (including penalties, disgorgement, restitution, and interest to be paid) exceed \$1 million, new CEA § 23 *requires* payment to the whistleblower of a bounty between 10 percent and 30 percent of the amount of any such monetary sanctions.¹⁹ Note that the whistleblower must be first in the door at the CFTC to be eligible for the bounty. But, if he or she qualifies, then there is a minimum reward of \$100,000 and potentially much, much more.²⁰ The Dodd-Frank Act whistleblower provisions also provide job security for a whistleblower, with a private right of action to federal court for any claim that the company has retaliated against the whistleblower. This potential for both a bounty and job security might be especially attractive to a utility employee during a time period of regulatory uncertainty, employment insecurity, and economic hardship. In light of these new whistleblower provisions, utilities should review the effectiveness of their internal compliance programs.

Conclusion

The Dodd-Frank Act was enacted to increase transparency and stability in the financial markets. With such a broad and ambitious goal and with the political winds of change blowing in Washington, it may not be surprising that the law itself was written in sweeping and sometimes ambiguous language. The hope is that the CFTC, and other regulators, will clarify and synthesize the legislation into a workable regulatory framework, appropriately tailored for each different kind of transaction and each different market structure. A year may have seemed to Congress like plenty of time for the CFTC (and other regulators) to construct a safe and secure market structure for over-the-counter derivatives. But the Dodd-Frank Act does not just affect sophisticated financial market participants but also every day commercial businesses, and the myriad “markets” to be covered by such a new regulatory structure are dizzyingly complex.

Natural gas and electric utilities are a unique type of market participant—an end user with a commercial business to run *and* a public service responsibility to uphold. The energy swap transactions into which utilities enter are tailored to mitigate the unique commercial risks involved in generating, transmitting or transporting, and delivering natural gas and electricity to American consumers and businesses. No one on Wall Street has a similar public service responsibility. The reason utilities are challenged by the Dodd-Frank Act is the concern that their public service responsibility will get lost in the torrent of reform and the urge to meet unrealistic deadlines. And, if this concern is not addressed by careful, thoughtful, detailed rulemaking, the unintended adverse consequences for American energy consumers could be significant.

Be Aware. Utilities will be affected by this legislation

and the rules that are being drafted. While end users will be likely be exempt from clearing and exchange-trading their swaps, there is no basis for assuming this will be a complete exemption from CFTC jurisdiction.

Be Prepared. Even the smallest natural gas and electric utilities should be educated about the potential changes the Dodd-Frank Act will require to energy and energy-related contracts, recordkeeping, and reporting requirements. Companies should begin to evaluate their energy contracting practices and current internal procedures, processes, and hedging with a view to the possible ways that the CFTC regulations will affect their businesses.

Get Involved. The CFTC is a financial markets regulator with little specialized knowledge of the energy industry. It is critical that the utility industry explain to the CFTC how it is different from the financial entities the CFTC is used to regulating. Utilities should consider joining in the public comment process to educate the CFTC on why the utilities have always been, and will always be, unique participants in the energy markets.

Endnotes

1. See *i.e. The Hangover, Part II*, WALL ST. J. (Nov. 29, 2010).
2. See CEA §§ 2(h)(1) and 2(g) (pre-amendment).
3. Speech before the Futures Industry Association's Futures and Options Expo (Nov. 3, 2010) at <http://www.cftc.gov/PressRoom/SpeechesTestimony/opagensler-57.html>.
4. Speech delivered at Georgetown University (Oct. 26, 2010) at <http://www.cftc.gov/PressRoom/SpeechesTestimony/opasommers-11.html>.
5. Speech delivered at the University of Notre Dame (Nov. 1, 2010) at <http://www.cftc.gov/PressRoom/SpeechesTestimony/opachilton-34.html>.
6. The Dodd-Frank Act was signed into law by President Obama on July 21, 2010 (the "Enactment Date"). It states that regulations "shall be issued in final form not later than 360 days after the date of enactment of [the Act]." The Dodd-Frank Act § 712(a)(3). The general effective date of Title VII, unless otherwise specified, is the later of 360 days after the Enactment Date or if a provision requires rulemaking, then 60 days after the rules are in final form. The CFTC shortens this definition to give its rulemakings focus, by identifying the generalized "Effective Date" as July 15, 2011. (See, *i.e.*, <http://www.cftc.gov/PressRoom/SpeechesTestimony/genslerstatement112310.html>).
7. CEA § 1a(47)(B) (as amended).
8. Commodity Exchange Act § 2(h)(7) and 2(h)(8) (as amended).
9. 156 Cong. Rec. H52248. Letter from the chairs of the U.S. Senate Committees on Financial Services and Agriculture (Sen. Christopher Dodd and Sen. Blanche Lincoln) to the chairs of the U.S. House Committees on Financial Services and Agriculture (Rep. Barney Frank and Rep. Colin Peterson) dated June 30, 2010.
10. MEGAWATT DAILY, Sept. 17, 2010, at 1.

11. Commodity Exchange Act § 2(h)(7) (as amended).

12. The Dodd-Lincoln Letter.

13. CFTC Commissioner Scott D. O'Malia, Keynote Address by Commissioner Scott D. O'Malia, Title VII of the Dodd-Frank Act: 732 Pages and Counting, January 25, 2011, *available at* <http://www.cftc.gov/PressRoom/SpeechesTestimony/opaomalia-3.html>. Many more proposed rules were issued for comment by the CFTC in December 2010 and January 2011. For a current list see <http://www.cftc.gov/LawRegulation/DoddFrankAct/Dodd-FrankProposedRules/index.htm>.

14. Commodity swaps overall (including energy, metals, agricultural, and other categories) represent less than one-half of 1% of the global OTC derivatives markets, *see* Table 19 of Bank for International Settlements semiannual OTC derivatives statistics at <http://www.bis.org/statistics/derstats.htm> (Dec. 31, 2009),

15. "In my view, no position limit is appropriate if it is imposed without the benefit of receiving and fully analyzing complete data concerning the open interest in each market." Concurring Statement Relating to the Commission's Proposal on Position Reports for Physical Commodity Swaps and Swaptions of Commissioner Jill Sommers dated October 19, 2010, at <http://www.cftc.gov/PressRoom/SpeechesTestimony/CommissionerJillESommers/sommersstatement101910.html>.

16. 76 Fed Reg. 4754 (Jan. 26, 2011)(Commissioner Bart Chilton concurring and Commissioner Jill Sommers dissenting).

17. "My grave concerns about moving forward with position limits have not been eased, and in fact, have only been heightened by certain provisions of Dodd-Frank. . . . I believe it is a mistake to interpret the arbitrary 180-day and 270-day deadlines as somehow trumping the requirement that the Commission make an appropriateness determination before imposing any position limits." Concurring Statement of Commissioner Jill Sommers., October 19, 2010.

18. The Dodd Frank Act § 720(b).

19. CEA § 23(b)(1) (as amended).

20. CEA § 23(c)(2)(C) (as amended).