



Swap Definition

## What is a “Swap” from the CFTC’s Perspective

- The term ‘swap’ under the Dodd – Frank Act means any agreement, contract, or transaction that
  - is a put, call, cap, floor, collar, or similar option of any kind that
  - is for the purchase or sale, or based on the value, of one or more interest or other rates, currencies, commodities, securities, instruments of indebtedness, indices, quantitative measures, or other financial or economic interests or property of any kind.
- Under the Dodd – Frank Act there are **specific exclusions** relevant to the energy / commodity markets including:
  - “any contract of sale of a commodity for future delivery (or option on such a contract)..... or any sale of a nonfinancial commodity or security for deferred shipment or delivery, **so long as the transaction is *intended to be physically settled.***”
  - Under the CEA, the CFTC does **not** regulate forward contracts (see following page).

## CFTC Guidance Regarding Physical Transactions (May 2011)

- Through a recent elaboration on the definitions of swaps and security-based swaps, the CFTC has clarified the Forward Contract exclusion in what is captured under the definition of Swaps.
- Specifically the definition of a Swap would exclude any sale of a non-financial commodity for deferred shipment or delivery so long as the transaction is intended to be physically settled.
  - This is similar to prior distinctions made by the CFTC between forward contracts and futures contracts.
- From the CFTC's perspective, Forward Contracts are "commercial merchandising transactions" where the primary purpose or intent is to transfer ownership not price risk.
- In addition, the Commission has addressed transactions with embedded commodity options, which on a standalone basis (and as noted in the D-F definition), are included in the definition of Swaps.
- The CFTC has proposed to exclude embedded options within forward contracts if the option(s):
  - i. Adjust price but do not undermine the overall nature of the contract as a forward contract
  - ii. Do not alter the physical delivery term; and
  - iii. Cannot be severed and/or marketed separately
- As an example, if the option(s) renders delivery optional, then it is not a forward contract.

## Examples of “Swaps” Under Dodd-Frank (Sect 721)

- (I) an interest rate swap;
- (II) a rate floor;
- (III) a rate cap;
- (IV) a rate collar;
- (V) a cross-currency rate swap;
- (VI) a basis swap;**
- (VII) a currency swap;
- (VIII) a foreign exchange swap;
- (IX) a total return swap;
- (X) an equity index swap;
- (XI) an equity swap;
- (XII) a debt index swap;
- (XIII) a debt swap;
- (XIII) a debt swap;
- (XIV) a credit spread;
- (XV) a credit default swap;
- (XVI) a credit swap;
- (XVII) a weather swap;**
- (XVIII) an energy swap;**
- (XIX) a metal swap;**
- (XX) an agricultural swap;
- (XXI) an emissions swap; and
- (XXII) a commodity swap**

## Definition of a Swap from Dodd-Frank Act (Sect 721)

- (B) EXCLUSIONS —The term ‘swap’ does not include:
  - “(i) any contract of sale of a commodity for future delivery (or option on such a contract), leverage contract authorized under section 19, security futures product, or agreement, contract, or transaction described in section 2(c)(2)(C)(i) or section 2(c)(2)(D)(i);
  - “(ii) any sale of a nonfinancial commodity or security for deferred shipment or delivery, so long as the transaction is intended to be physically settled;

## Company Overview

Eco Risk Markets LLC is a private firm which specializes in helping companies manage commodity, interest rate, and foreign exchange risks.

Our team has worked with leading companies to establish a practical approach to managing these risks through the execution of consistent, efficient and well-communicated hedge programs and credit management processes.

In addition, we believe an integrated approach to managing overall commodity, FX and I-rate exposures is imperative, as new derivative legislation is enacted, and markets become increasingly complex from a compliance and execution perspective.

## Our Mission

Our mission is to help our clients manage market and credit risks in a manner consistent with shareholder expectations, sustainability initiatives, and transparency needs



## Company Overview

Eco Risk Markets has offices in Texas and Connecticut. Our primary office is in the Houston area:

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