

ISDA
International Swaps and
Derivatives Association, Inc.
One New Change
London, EC4M 9QQ
Tel: 44 (0) 20 7330 3550
Fax: 44 (0) 20 7330 3555
Email: isdaeurope@isda.org
Website: www.isda.org

FOA
Futures and Options Association
2nd Floor
36-38 Botolph Lane
London, EC3R 8DE
Tel: 44 (0) 20 7929 0081
Fax: 44 (0) 20 7621 0223
Email: info@foa.co.uk
Website: www.foa.co.uk

EFET
European Federation of Energy Traders
Amstelveenseweg 998
1081 JS Amsterdam
Tel: 31 (0)20 5207970

Email: secretariat@efet.org
Website: www.efet.org

M E M O R A N D U M

TO: CFRC Working Group
FROM: Emmanuelle Sebton
DATE: 4 November 2005
RE: Notes of meeting of 19 October 2005

The CFRC Working Group met for the second time on 19 October 2005. The agenda for the meeting is attached, together with a list of participants.

1- Discussion of postponement of MiFID implementation and new article 45d of the CRD

The Working Group considered the implications, for its own work schedule, of the postponement of MiFID implementation and of the adoption of the CRD, particularly CAD article 45d instituting a prudential carve-out for commodity firms.

The Group felt that the delay in MiFID implementation would entail a similar six months' delay to the date by which the review of Article 2.1 exemptions by the Commission has to be completed. The exemptions might therefore not be removed or amended, if at all, before March/April 2008. The Treasury confirmed this interpretation at a meeting of the FSA Commodities Standing Group held on 25 October.

CAD Article 45d exempts commodity firms from the CRD requirements until the earlier of either December 2010 or the time by which the Commission has completed its review and an appropriate capital regime is in place for these firms.

The Commission is aiming to conduct both this capital review and the MiFID exemptions review concurrently, and should accordingly propose a new capital regime for commodity firms by early 2008. The Commission is expected to establish two working groups to conduct the reviews, in Q1 or Q2 of 2006.

The CFRC Working Group confirmed its original target of the summer of 2006 to have a full capital proposal ready for the Commission.

It was noted that the Commission had invited a presentation by firms when their capital working group gathers for the first time next year. It was proposed to attempt to converge this event with the conference being envisaged by RWE next year, as a follow-up to the workshop held in Dusseldorf on 2 December.

Participants also discussed the legal format of the commodity firms' capital proposal. It was agreed that form was secondary to substance. The Working Group was willing to support the preparation of a new directive if the substance of the regime rendered it necessary and that it would be preferable timewise if the new regime could be brought into force by making use of the CRD comitology provisions.

2- US regulatory treatment of specialist commodity dealers (presentation by Hunton Williams)

Jonathan Marsh, of law firm Hunton Williams, gave a presentation on the regulation of specialist commodity dealers in the US.

A key conclusion was that OTC commodity derivatives business is not, in general, regulated for conduct of business purposes in the US, with the exception of agricultural commodity underlyings; and, as a result, entities which are otherwise classified in the EU as "specialist commodity dealers" would not be subject to capital requirements by the CFTC.

3- Discussion of the scope of the capital treatment (Chris Bates, Clifford Chance)

Chris Bates summarized his memorandum circulated to the Working Group ahead of the meeting.

The memo, which provided an update on the perimeter of activities/ instruments covered by MiFID, including a review of the exemptions, was meant as an introduction to the WG's debate on the desired scope of the capital regime. Participants noted that a number of key questions needed addressing, including the following :

- 1) Should the proposed capital regime apply to the whole consolidated balance sheet of firms ? Or just to its trading activities ?
- 2) Do participants believe that the scope of the proposed capital framework should be the same as that of MiFID ? In particular, would it make sense to also include SPOT commodity positions in the calculation of market risk capital ? Further, for credit risk purposes, is it reasonable to focus purely on derivatives entered into for non commercial purposes, where netting sets might also include commercial transactions ?
- 3) If a firm has trading outlets in several EU countries, should it be supervised at a consolidated level ? On what basis should the consolidating supervisor be determined ?

4- Update on FOA-KPMG questionnaire

Anthony Belchambers outlined the timetable for the completion of the KPMG questionnaire and the enlargement of the team for taking forward the work. He confirmed that the FOA had arranged for a meeting of the data providers on 27 October, where KPMG will go through the contents of the questionnaire and answer participants' queries. ISDA will also present on its counterparty credit risk supplement to the KPMG questionnaire at the meeting.

5- Update on hypothetical portfolio testing by RWE-EON

Hung Boc (RWE) and Bernd Kaelber (EON) gave a brief presentation of the portfolio testing exercise that they have launched jointly with Vattenfall. The content of the test portfolios (power, oil, gas and coal) was detailed, as well as the assumptions under which capital needs were assessed (type of market and credit risk methodology employed). Preliminary capital results were displayed for the power portfolio.

6- Next meeting- key issues for discussion

A more complete presentation of the hypothetical portfolio study will be given to the working group at the next meeting. It was agreed that the discussion of market risk, originally tabled for November, would be pushed back to the December session of the Working Group. The November meeting will focus on high level issues or questions raised by the hypothetical testing exercise, as well as the draft of section III of the Working Group's paper already circulated for review by ISDA.

Three questions are of particular relevance:

- 1) What commodity business should be regulated under MiFID?
- 2) Should commodity firms be regulated at all for capital purposes?
- 3) If a form of light touch prudential regulation applies, how should it differ from the CRD?

CFRC Working Group

Second meeting – 19 October 2005

Agenda:

- 1- Assessment of impact of CRD article 45d on the CFRC WG's and the Commission's work plan US regulatory treatment of specialist commodity dealers (presentation by Jonathan Marsh, Hunton Williams)
- 2- CFRC WG's recommendation to the Commission : discussion on the scope of the proposed treatment, led by Chris Bates (Clifford Chance).
- 3- Brief update on co-operation with KPMG
- 4- Hypothetical portfolio testing

CFRC – LIST OF ATTENDEES
ISDA, One New Change
Weds 19 Oct 2005, 2.00-5.00pm

Name	Company	Attend (A=Attend, C=Call-in)
Alistair Rapley	Amalgamated Metal Trading	A
Thomas Fuhr	Becker Büttner Held	A
Hamilton Hinds	BP	A
Karla Barton	BP	C
Chris Bates	Clifford Chance	C
Nelida Lifac	ConocoPhillips	A
Bernd Kälber	E.ON Sales & Trading	A
Dirk Eichholz	E.ON Sales & Trading	A
Vincent Mohy	Electrabel	A
Cristina Fernandez-Ludena	Endesa	C
Anthony Belchambers	FOA	A
Arnaud Cruiziat	Gaselys	A (til 3pm)
Jonathan Marsh	Hunton & Williams	A (Speaker)
Emmanuelle Sebtou	ISDA	A
Gideon Hollis	Koch Metals	C
Liam McCarthy	Koch Metals	A
Katherine Seal	LIBA	C
Karl-Peter Horstmann	RWE Trading	A
Nhu Hung Boc	RWE Trading	A
Claude Casset	Totsa	A