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Emissions groups join fight against proposal for mandatory OTC clearing

Unhappy with market oversight language in a House energy and climate change bill approved late last week, carbon market participants are joining opponents of additional regulation of energy commodities in objecting to mandatory clearing of trades.

Passed by a 219-212 vote, H.R. 2454 would require that over-the-counter carbon derivative deals clear through an exchange and would have the Commodity Futures Trading Commission oversee allowance derivatives tied to a national cap-and-trade scheme set to open in 2012 *(GD 6/29).*

Proponents of mandatory clearing say it is a way to reduce the risk from trading based on unsecured credit and to provide greater price transparency. In offering the derivatives language in May, Representative Bart Stupak, Democrat-Michigan, said it would protect consumers from speculation and spiking allowance prices.

“Gas prices, home heating oil, natural gas and now carbon derivative prices should be based on supply and demand, not whimsical speculation by price manipulators,” Stupak said.

Emissions Marketing Association representative Jeremy Weinstein, in a recent memo to EMA members, noted that requiring OTC derivatives be cleared through a central counterparty could “substantially increase collateral requirements on market participants, which are now generally transacted with substantial unsecured credit. The need for collateral will affect funding liquidity for market participants, and thus reduce market liquidity.”

Weinstein said Monday that the cost of that collateral would flow down to customers such as utility ratepayers. Ultimately, Weinstein said the House bill’s language presumes the US carbon market will be rife with the gaming seen in other commodity markets. “They’re criminalizing conduct before a market begins,” he said.

International Emissions Trading Association President Henry Derwent said the bill “appropriately calls for regulatory oversight of the carbon market, but its provisions do not take into account market requirements and will therefore increase costs unnecessarily.”

“In particular, forcing all OTC trades to settle and clear on exchanges will impair the ability of the market to deliver the risk-management tools that reduce costs for companies and consumers,” Derwent said. “Industry needs the full range of these tools to finance a new, clean-energy infrastructure cost-effectively.”

In a June 25 letter to House leaders, the International Swaps and Derivatives Association, the Futures Industry Association, the Securities Industry and Financial Markets Association and the Business Roundtable said the House oversight language “would disrupt the risk management capabilities of businesses and strip liquidity from important price discovery markets.”

The trade groups requested that the provisions be removed from the bill. “Comprehensive derivatives reform legislation should be considered on its merits and subject to the full range of input from the appropriate committees of jurisdiction,” they said. — *Christine Cordner*