March 1, 2012

Via Electronic Submission

David Stawick, Secretary
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Petition for Exemptive Relief for Certain *Bona Fide* Hedging Transactions Under Section 4a(a)(7) of the Commodity Exchange Act

Dear Mr. Stawick:

The Edison Electric Institute ("**EEI**"), American Gas Association ("**AGA**"), and the Electric Power Supply Association ("**EPSA**") (hereafter "**Joint Associations**") respectfully submit these comments in support of the Working Group of Commercial Energy Firms' ("**Working Group**") Petition to the Commodity Futures Trading Commission (the "**Commission**") requesting an order granting exemptive relief from the Commission's regulations establishing speculative position limits ("**Position Limits Rule**") for certain *bona fide* hedging transactions (the "**Petition**").[1] Section 4a(a)(7) of the Commodity Exchange Act ("**CEA**") provides the Commission with authority to "exempt, conditionally or unconditionally . . . any transaction or class of transactions from any requirement it may establish . . . with respect to position limits."[2] For the reasons discussed below, the Joint Associations request that the Commission grant the Working Group's Petition for exemptive relief for certain *bona fide* hedging transactions pursuant to Section 4a(a)(7).

I. Description of the Joint Associations' Interest in the Petition and the Position Limits Rule

EEI is the association of U.S. shareholder-owned electric companies. EEI's members serve 95 percent of the ultimate customers in the shareholder-owned segment of the U.S. electricity industry, and represent approximately 70 percent of the U.S. electric power industry. EEI also has more than 65 international electric companies as Affiliate members, and more than 170 industry suppliers and related organizations as Associate members.

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1 *Position Limits for Futures and Swaps*, 76 Fed. Reg. 71626 (Nov. 18, 2011) [hereinafter *Position Limits Rule*].

2 CEA Section 4a(a)(7).

The AGA, founded in 1918, represents more than 200 local energy companies committed to the safe delivery of clean natural gas to more than 65 million customers throughout the United States. AGA's members use a variety of financial tools, such as futures contracts traded on CFTC-regulated exchanges and over-the-counter energy derivatives, to hedge the commercial risks associated with providing natural gas service, particularly volatility in natural gas commodity costs. AGA is an advocate for local natural gas utility companies and provides a broad range of programs and services for member natural gas pipelines, marketers, gatherers, international gas companies and industry associates. Today, natural gas meets almost one-fourth of the United States' energy needs.

EPSA is the national trade association representing competitive power suppliers, including generators and marketers. These suppliers, who account for nearly 40 percent of the installed generating capacity in the United States, provide reliable and competitively priced electricity from environmentally responsible facilities. EPSA seeks to bring the benefits of competition to all power customers.

The Joint Associations' members are physical commodity market participants that rely on swaps and futures contracts primarily to hedge and mitigate their commercial risk. They are not financial entities. Regulations that make effective risk management options more costly for end-users of swaps will likely result in higher and more volatile energy prices for residential, commercial, and industrial customers. As users of commodity swaps and futures contracts to hedge commercial risk, the Joint Associations' members have a direct and significant interest in how the Commission defines *bona fide* hedge transactions under CEA section 4a(c)(2) and Rule 151.5(a)(2) and (a)(5). To the extent that common risk-reducing hedging practices are not specifically enumerated as *bona fide* hedges under the Position Limits Rule, hedging may become more expensive for the Joint Associations' members. Accordingly, we urge the Commission to grant the Working Group's Petition and confirm that certain types of ordinary risk-mitigating hedging transactions are exempt from position limits.

II. The Joint Associations Support the Working Group's Petition and Urge the Commission to Grant the Requested Relief as Expeditiously as Possible

Pursuant to its authority under Section 4a(a)(7) of the CEA and Rule 151.5(a)(5) of the Position Limits Rule, the Commission should grant an Order providing exemptive relief for the classes of risk-reducing transactions described in the Working Group's Petition to the extent that they do not now qualify as enumerated *bona fide* hedging transactions. In the alternative, the Joint Associations respectively request that the Commission issue interpretive guidance to clarify that such classes of transactions qualify as *bona fide* hedging transactions under the Position Limits Rule. In particular, the Joint Associations support providing exemptive relief for the following types of transactions:

- Binding, irrevocable bids or offers. *Referenced contracts used to hedge exposure to market price volatility associated with binding and irrevocable fixed-price bids or offers should be treated as* bona fide *hedging transactions or positions*;

- Timing of hedging physical transactions. *Referenced Contracts used to hedge a physical commodity transaction that is subject to ongoing, good faith negotiations, and that the hedging party reasonably expects to conclude, should be treated as* bona fide *hedging transactions or positions*;

- Local utility hedging for customer requirements. *Referenced Contracts purchased by, or on behalf of, a state-regulated public utility to hedge the anticipated requirements of its retail natural gas, electric and/or steam customers should be treated as* bona fide *hedging transactions or positions*;

- Holding a hedge using a physical delivery contract into the spot month; generally. *Firms that use physical-delivery Referenced Contracts (in commodities other than metals or agriculture) as* bona fide *hedging transactions or positions should be permitted to hold these hedges into the spot month*;

- Holding a cross-commodity hedge using a physical delivery contract into the spot month. *Firms that use physical-delivery Referenced Contracts as a cross-commodity hedge should be permitted to hold these hedges into the spot month*;

- Holding a cross-commodity hedge using a physical delivery contract to meet unfulfilled anticipated requirements. *The Commission should reinstate existing Commission Rule 1.3(z)(2)(ii)(C) to permit firms to hold cross-commodity hedges involving physical-delivery Referenced Contracts into the spot month in order to meet their unfilled anticipated requirements*.

The Commission should also grant the Working Group's Petition for exemptive relief regarding the definitions of (a) "spot month" as set forth in Rule 151.3(c) of the Position Limits Rule, and (b) "swaption" as set forth in Rule 151.1 of the Position Limits Rule. The Joint Associations also request that the Commission make clear that any relief granted is applicable to all market participants who satisfy the specified conditions of the relief.

III. The Commission Should Grant Relief that Exempts the Legitimate Hedging Activities Identified in the Working Group's Petition from Position Limits

A. The Definition of *Bona Fide* Hedging Transactions Under the Position Limits Rule is Unnecessarily Narrow and Restrictive

The Joint Associations believe that the definition of *bona fide* hedging transactions or positions is unnecessarily narrow and, as adopted, may discourage a significant amount of important and beneficial risk management activity.[3] CEA Section 4a(c)(2), as amended by

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[3] EEI has previously provided the Commission with comments regarding the definition of "*bona fide* hedging" under the Proposed Rule. *See* Comments on Proposed Rule Regarding Position Limits for Derivatives (RIN 3038-AD15 and 3038-AD16) at 7-9 (March 28, 2011).

Section 737 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "**Dodd-Frank Act**"), defines what constitutes a *bona fide* hedging transaction or position in terms that are similar, though not identical, to the current definition in Part 1.3(z) of the Commission's regulations.[4] Rule 151.5(a)(1) implements the statutory definition, then narrows it considerably by providing that a transaction or position that would otherwise qualify as a *bona fide* hedge also must fall within one of eight categories of enumerated hedging transactions.[5] The Joint Associations believe that this restrictive definition of *bona fide* hedging transactions is not authorized by CEA section 4a(c)(2) and could disrupt the commodity markets, make hedging more difficult and costly, and may increase systemic risk by encouraging end-users to leave a relatively large portion of their portfolios un-hedged.

This result, however, is avoidable because the Position Limits Rule specifically allows market participants to petition the Commission to amend the current list of enumerated hedges to include additional classes of transactions that meet the general requirements of a *bona fide* hedge under Rule 151.5(a)(1).[6] In order to provide our members with certainty regarding their hedging activity, the Joint Associations request that the Commission clarify that our members will remain able to engage in the types of ordinary hedging transactions included in the Working Group's Petition. In particular, the Joint Associations request that the Commission confirm that our members will "be able to do that which they've been able to do in the past and hedge in the futures and swaps markets" as *bona fide* hedgers exempt from position limits.[7] Accordingly, the Joint Associations request that the Commission use its authority under CEA Section 4a(a)(7) and Rule 151.5(a)(5) to clarify that the legitimate risk management activities included in the Working Group's Petition are exempt from position limits.

IV. The Commission Should Grant the Working Group's Petition for Exemptive Relief Clarifying the Definitions of "Spot Month" and "Swaption"

In addition to the exemptive relief regarding *bona fide* hedging transactions, the Joint Associations request that the Commission grant the Working Group's Petition for exemptive relief regarding the definitions of "spot month" and "swaption" under the Position Limits Rule.

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[4] Pub. L. No. 111-203 (2010). The definition of *bona fide* hedging in Part 1.3(z) of the Commission's regulations provides that a *bona fide* hedging transaction or position in a futures contract must "normally" represent a substitute for a physical market transaction. Section 737 of the Dodd-Frank Act omits the word "normally" from the definition. *Position Limits for Derivatives*, Proposed Rule, 76 Fed. Reg. 4752, 4761 (Jan. 26, 2011).

[5] *Position Limits Rule*, *supra* note 1, at 71689.

[6] *Position Limits Rule*, *supra* note 1, at 71649.

[7] Transcript from Commission Public Meeting on Final Rules Under the Dodd-Frank Act, at 143 (Oct. 18, 2011). Indeed, Chairman Gensler specifically invited market participants to seek interpretive guidance regarding their hedging activities: "If somebody thinks well, maybe we're not covered, they can come and knock on the door, and we can address that at staff level or Commission level." *Id.* at 145.

A. The Commission Should Clarify that, for Purposes of Referenced Contracts in "Energy Commodities" as Defined in Rule 151.3(c), the Term "Spot Month" Means Only "the Last Three Days of Trading of the Referenced Contract in Energy Commodities"

Rule 151.3(c) currently provides that the spot month for energy commodities commences at the close of business of the third business day prior to the last day of trading in the underlying Core Referenced Future Contract and terminates "at the end of the delivery period."[8] The Joint Associations agree with the Working Group's observation that the energy markets have traditionally viewed the "spot month" as only the last three days of trading. Accordingly, we join the Working Group in requesting that the Commission limit the spot month for energy contracts to the last three days of trading. By providing this relief, the Commission would ensure that the definition of "spot month" for energy contracts is aligned with current market practices. It also would avoid a result that is contrary to long-standing industry norms and that would create unnecessary confusion in the marketplace.

B. The Commission Should Issue an Exemptive Order Clarifying that the Definition of "Swaption" under Rule 151.1 Does Not Include a Physical Commodity Option

Rule 151.1 defines "swaption" as "an option to enter into a swap or a physical commodity option."[9] The Joint Associations believe that this definition is inappropriate because the Commission is still determining whether physical commodity options should fall within the definition of "swap" under its final "swap" product definition rule.[10] Accordingly, we request that the Commission grant an exemptive order pursuant to CEA Section 4a(a)(7) clarifying that physical commodity options are not swaptions for purposes of position limits.[11]

V. Conclusion

The Joint Associations appreciate the Commission's consideration of our comments in support of the Working Group's Petition. For the reasons stated herein, we respectfully request that the Commission grant the Working Group's Petition in full as expeditiously as possible to provide our members with certainty as they work to comply with the Position Limits Rule. By

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8 CFTC Rule 151.3(c).

9 CFTC Rule 151.1.

10 *See Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping*, Joint Proposed Rulemaking, 76 Fed. Reg. 29818 (May 23, 2011). EEI has previously provided the Commission with comments regarding the definition of "swap" under the Proposed Rule. *See* Comments on Joint Proposed Rules and Proposed Interpretations on Further Definition of "Swap," "Security-Based Swap," "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping (17 CFR Part 1)(RIN No. 3038-AD46), at 15-17 (July 22, 2011).

11 In the alternative, the Joint Associations request that the Commission clarify that physical commodity options are not swaptions or swaps in a future rulemaking.

clarifying that the common, risk-reducing transactions identified in the Petition are *bona fide* hedging transactions, aligning the definition of "spot month" for energy commodities with the traditional understanding of the energy markets, and excluding physical commodity options from the definition of "swaption," the Commission will ensure that commercial energy companies do not incur unnecessary costs as they implement the Position Limits Rule.

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Please contact us at the numbers listed below if you have any questions about our comments.

Respectfully submitted,

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