

Resolution on Financial Reform Legislation Affecting Over-the-Counter Risk Management Products and Its Impacts on Consumers

WHEREAS, There is a diverse group of end-users, consisting of electric and natural gas utilities, suppliers, customers, and other commercial entities who rely on over-the-counter (“OTC”) derivative products and markets to manage electricity and natural gas price risks for legitimate business purposes, thereby helping to keep rates stable and affordable for retail consumers; *and*

WHEREAS, The United States Congress is considering financial reform legislation with the goal of ensuring that gaps in regulation, oversight of markets and systemic risk do not lead to economic instability; *and*

WHEREAS, Previous NARUC resolutions support federal legislative and regulatory actions that fully accommodate legitimate hedging activities by electric and natural gas utilities; *and*

WHEREAS, The proposed legislation would, among other things, provide the Commodity Futures Trading Commission (CFTC) with oversight of OTC risk management products, including mandatory centralized clearing and exchange trading of all OTC products; *and*

WHEREAS, Mandatory centralized clearing of all OTC contracts will increase expenses associated with hedging activity, and ultimately end-user prices, due to increased margin requirements; *and*

WHEREAS, A report by the Joint Association of Energy End-Users stated that the effect of margin requirements resulting from mandatory clearing for electric utilities would have the unintended effect of reducing or eliminating legitimate hedging practices and could jeopardize or reduce investments in Smart Grid technology; and for natural gas utilities and production companies could reduce capital devoted to infrastructure and natural gas exploration; *and*

WHEREAS, The laudable goals of reform that ensure market transparency and adequate regulatory oversight can be accomplished by means other than mandatory clearing of OTC risk management contracts and the anticipated extra expense. For example, a requirement that natural gas and electric market participants engaging in legitimate hedging report all OTC derivative transactions to a centralized data repository, like the CFTC, provides sufficient market transparency without the costs associated with mandatory clearing; *and*

WHEREAS, Proposed reforms would cause regulatory uncertainty with regard to the oversight of Regional Transmission Organizations (RTOs) and Independent System Operators (ISOs), where such uncertainty and/or overlapping jurisdiction can lead to negative impacts on liquidity, market confidence and reliability; *and*

WHEREAS, The Federal Energy Regulatory Commission (FERC), and the Public Utility Commission of Texas (PUCT) for Texas/ERCOT, as the regulators with the necessary expertise and statutory mandates to oversee electricity and natural gas markets to protect the public interest and consumers, should not be preempted by the financial reform legislation from being able to

continue exercising their authority to ensure reliable, just and reasonable service and protect consumers; *and*

WHEREAS, Energy markets currently regulated by FERC or the PUCT (for Texas/ERCOT) under accepted tariffs or rate schedules should continue to be subject to FERC's and the PUCT's (for Texas/ERCOT) exclusive Federal jurisdiction, including jurisdiction over physical and financial transmission rights, and market oversight; and should themselves not be subject to CFTC jurisdiction as a clearinghouse due to the financial and other settlement services they provide those transacting in regional electricity markets; *now, therefore be it*

RESOLVED, That the Board of Directors of the National Association of Regulatory Utility Commissioners, convened at its 2010 Winter Committee Meetings in Washington, D.C., supports passage of financial reform legislation ensuring that electric and natural gas market participants continue to have access to OTC risk management products as tools in their legitimate hedging practices to provide more predictable and less volatile energy costs to consumers; *and be it further*

RESOLVED, That new financial legislation being considered by Congress should weigh the costs of potential end-user utility rate increases versus the benefits of new standards for the clearing of OTC risk management contracts used by natural gas and electric utilities for legitimate hedging purposes; *and be it further*

RESOLVED, That any federal legislation addressing OTC risk management products should provide for an exemption from mandatory clearing requirements for legitimate hedging activity in natural gas and electricity markets; *and be it further*

RESOLVED, That any exemption to the mandatory clearing requirement for OTC derivatives be narrowly tailored as to not allow excessive speculation in natural gas and electricity markets; *and be it further*

RESOLVED, That the FERC, and the PUCT for Texas/ERCOT, charged with the statutory obligation to protect the public interest and consumers, should continue to be the exclusive Federal regulators with authority to oversee any agreement, contract, transaction, product, market mechanism or service offered or provided pursuant to a tariff or rate schedule filed and accepted by the FERC, or the PUCT for Texas/ERCOT; *and be it further*

RESOLVED, That NARUC authorizes and directs the staff and General Counsel to promote with the Congress, the Commodity Futures Trading Commission and other policymakers at the federal level, policies consistent with this statement.

*Sponsored by the Committee on Gas, Consumer Affairs, and Electricity
Adopted by the NARUC Board of Directors February 17, 2010*