March 28, 2011

VIA ELECTRONIC SUBMISSION

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

Re: Comments on Proposed Rule Regarding Position Limits for Derivatives (RIN 3038–AD15 and 3038-AD16)

Dear Mr. Stawick:

The Edison Electric Institute ("EEI") and Electric Power Supply Association ("EPSA") (hereafter "Joint Associations") respectfully submit these comments in response to the notice of proposed rulemaking ("Proposed Rule") issued by the Commodity Futures Trading Commission ("CFTC" or "Commission") regarding position limits for certain physical commodity derivatives pursuant to Section 737 of Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act").[1] The Joint Associations have been active participants in the Commission's Dodd-Frank Act rulemaking process and welcome the opportunity to continue to discuss issues of interest to their members with the Commission and its staff.

The Dodd-Frank Act and the Commission's implementing regulations will profoundly change the way in which end-users and other market participants use swaps and other commodity derivatives to manage their commercial risk. Accordingly, the Joint Associations appreciate the Commission's willingness to consult with, and to solicit thoughtful comments from, market participants who will be affected by the regulations it issues as part of implementing the provisions of the Dodd-Frank Act. In particular, the Joint Associations support the Commission's decision not to include in the Proposed Rule a provision that crowds

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[1] Position Limits for Derivatives, 76 Fed. Reg. 4,752, RIN 3038-AD15 and 3038-AD16 (Jan. 26, 2011); Pub. L. No. 111-203 (2010).

out the ability of a hedger to take speculative positions once it relies on a hedge exemption,[2] and to include an exemption from the aggregation requirement for owned non-financial entities.[3]

The Joint Associations respectfully submit that the Commission does not yet have sufficient information to make the finding required by Commodity Exchange Act ("CEA") Section 4a(a)(1) that position limits are "necessary to diminish, eliminate, or prevent" excessive speculation in any commodity. As a result, the Commission should withdraw the Proposed Rule until it has adequate data to justify the need for new position limit regulations. Instead of reasoned analysis based on objective facts, the Proposed Rule assumes that excessive speculation exists (or could exist) and then establishes a pervasive and burdensome regulatory regime to remedy this assumed problem. Such an approach likely will make the U.S. derivatives markets less efficient and more expensive for commercial entities seeking to manage the risks they incur in their businesses. The Joint Associations urge the Commission to reconsider the Proposed Rule and to adopt new position limits only after it has the information it needs to determine that such limits are, in fact, necessary.[4]

If the Commission decides to adopt a position limits rule notwithstanding the lack of market data, the Joint Associations encourage the Commission to reconsider the Proposed Rule to minimize the potential burdens it will impose upon market participants. Merely creating the systems needed to comply, in real-time, with the Proposed Rule will place a significant administrative and financial burden on market participants with little discernable benefit, particularly in light of the fact that the Commission has not articulated why the Proposed Rule is necessary. In addition, the Joint Associations remain concerned that other aspects of the Proposed Rule are unnecessary, and would be detrimental to, the efficiency and competitiveness of the U.S. derivatives markets. Accordingly, the Joint Associations submit these comments to identify potential unintended consequences of the Proposed Rule and to propose several commercially practicable solutions.

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[2] On January 26, 2010, prior to the enactment of the Dodd-Frank Act, the Commission proposed a position limits rule that would have prohibited any person operating under a *bona fide* hedge exemption from also holding a speculative position (of any size) in the same contract. The Joint Associations commented that such a prohibition would create significant operational problems because it is often difficult to definitively categorize a single position as purely hedging or speculative, and such a prohibition was contrary to the plain language of the Commodity Exchange Act, which expressly permits speculation below any limits set by the Commission.

[3] The January 26, 2010 proposed position limits rule would have imposed a rigid 10% ownership test for aggregation of accounts within a single corporate group regardless of actual control. The Joint Associations commented that, to the extent such accounts were independently managed and controlled, the proposed aggregation requirement would have no effect on "excessive speculation."

[4] CEA § 4a(a)(1).

The Joint Associations recommend that the Commission modify the Proposed Rule by:

- Updating the definition of "deliverable supply" used to calculate spot-month position limits to reflect new settlement options for physically-settled commodity transactions;
- Eliminating (or providing more flexible) position limits for cash-settled contracts to reflect the fact that the markets for such contracts are inherently less susceptible to price disruptions and manipulation;
- Adopting federal single month and all-months combined accountability levels rather than position limits or position visibility levels, and only adjusting such thresholds when necessary;
- Allowing market participants to define what constitutes an "economically equivalent" contract based on current commercial practices rather than a mere physical connection or sporadic economic correlation;
- Providing a commercially practicable hedge exemption process that: (1) accommodates common categories of risk management transactions; (2) provides an exemption process for non-enumerated hedging transactions; (3) allows end-users relying on a *bona fide* hedge exemption to provide monthly, rather than daily, reports; (4) includes a simple, one-time representation process rather than a complex and time-consuming verification procedure; and (5) expressly permits anticipatory hedges for non-agricultural commodities of longer than one year; and
- Simplifying the aggregation requirement by making exemptions to the aggregation requirement effective when filed and permitting market participants to manage risk on an enterprise basis across affiliates.

I. Description of the Joint Associations and their Interest in the Proposed 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.

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 not financial entities. Rather, they are physical commodity market participants that rely on swaps primarily to hedge and mitigate their commercial risk. 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 retail, commercial, and industrial customers. As end-users of commodity swaps to hedge commercial risk, the Joint Associations' members have a direct and significant interest in when and to what extent the Commission exercises its authority to establish speculative position limits.

II. The Commission Should Withdraw the Proposed Rule Until it is Able to Determine Whether Position Limits for the Referenced Contracts are "Necessary."

Under CEA Section 4a(a)(2), as amended by the Dodd-Frank Act, the Commission has the authority to establish, "as appropriate," limits on speculative positions in derivatives contracts that are "necessary to diminish, eliminate or prevent" the burden on interstate commerce caused by excessive speculation (*i.e.*, by commodity price fluctuations that are sudden, unreasonable, or unwarranted).[5] The Commission has interpreted CEA Section 4a(a)(2) in a manner that does not require it to make a finding that excessive speculation exists or is likely to occur, or to find that position limits are necessary to prevent sudden or unreasonable fluctuations or unwarranted changes in prices. Rather, the Commission has stated that CEA Section 4a(a)(2) allows it to "impose position limits prophylactically, based on its reasonable judgment that such limits are necessary . . . ."[6]

The Joint Associations are concerned by the Commission's position that it does not need to make a finding explaining why the proposed position limits are "necessary." We do not believe that the Commission's statements regarding its authority to impose position limits are supported by the language of CEA Section 4a(a)(1), which expressly defines the Commission's responsibility with respect to position limits:

> [T]he Commission shall . . . fix such limits . . . *as the Commission finds are necessary* to diminish, eliminate, or prevent such burden."[7]

CEA Section 4a(a)(1) does not authorize the Commission to fix position limits "prophylactically, based on its reasonable judgment that such limits are necessary."[8] On the contrary, CEA Section 4a(a)(1) manifestly *requires* the Commission to make a finding that the proposed position limits are "necessary."

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5 CEA § 4a(a)(2).

6 76 Fed. Reg. at 4,754.

7 CEA § 4a(a)(1) (emphasis added).

8 *Compare* 76 Fed. Reg. at 4,754 *with* CEA § 4a(a)(1).

Absent a finding that explains why particular position limits are "necessary" to diminish, eliminate, or prevent excessive speculation, the Joint Associations believe that the Commission lacks the statutory authority to set, and therefore should not set, position limits. Moreover, the Commission does not articulate in the Proposed Rule any factual basis or substantive analysis to support its "reasonable judgment" that the proposed position limits are "necessary to diminish, eliminate or prevent" excessive speculation or otherwise "appropriate."[9] Indeed, until the CFTC collects and analyzes position data for the markets it seeks to regulate, which the Commission itself notes cannot even begin until the third quarter of 2011, it would be difficult, if not impossible, for the CFTC to have the information it needs to make such a determination. It is difficult to understand how the Proposed Rule can reasonably be designed to prevent excessive speculation in markets that, at present, are of unknown size and used by unknown entities in ways not known to the Commission. Furthermore, without a reasoned explanation as to why the Commission has chosen to establish position limits for the 28 specific core referenced futures contracts ("Referenced Contracts"), market participants cannot provide informed and meaningful comments on the Proposed Rule.

Accordingly, the Joint Associations request that the Commission explain why position limits are necessary and appropriate in the form proposed or withdraw the Proposed Rule until after it is able to determine whether position limits are, in fact, necessary for each of the Referenced Contracts and their economic equivalents. Moreover, without making the required finding, the Commission has no objectively reviewable basis for concluding that the proposed position limits are necessary to prevent market manipulation, ensure sufficient market liquidity, and ensure that price discovery is not disrupted, particularly for commercially important contracts like the NYMEX Henry Hub Natural Gas contract.[10]

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[9] *See*, *e.g.*, Opening Statement of Commissioner Michael Dunn at CFTC Public Meeting on Proposed Rules Under Dodd-Frank Act, January 13, 2011 ("To date, CFTC staff has been unable to find any reliable economic analysis to support either the contention that excessive speculation is affecting the markets . . . or that position limits will prevent excessive speculation. The task then is for the CFTC staff to determine whether position limits are appropriate. With such a lack of concrete economic evidence, my fear is that, at best, position limits are a cure for a disease that does not exist or at worst, a placebo for one that does."); Interim Report on Crude Oil, Interagency Task Force on Commodity Markets, at p. 5 (Jul. 2008) ("[speculators have] not resulted in systematic changes in price" . . . [on the contrary, there is evidence] suggesting instead that their positions might have provided a buffer against volatility-inducing shocks."); Staff Report on Cotton Futures and Options Market Activity During the Week of March 3, 2008 (Jan. 4, 2010); the Report on Large Short Trader Activity in the Silver Futures Market (May 2008).

[10] *See* CEA §§ 4a(a)(2)(C) and 4a(a)(3)). The Joint Associations also note that, as proposed, the Commission's position limit rule appears to be designed to prevent *concentration* in the derivatives markets rather than excessive speculation. Concentration and excessive speculation are unrelated concepts. However, the Proposed Rule uses concentration as an imperfect and inappropriate proxy for excessive speculation. This approach, which is not contemplated under the Dodd-Frank Act, will make it more difficult for commercial entities to manage the risk associated with their businesses effectively and will not, as CEA Section 4a(a) requires, "diminish, eliminate or prevent" excessive speculation. 76 Fed. Reg. at 4,771 (proposed Rule 151.5(a)(iv)(B)); CEA § 4a(a).

III. The Proposed Rule Will Impose Substantial Technological and Operational Burdens on all Market Participants.

The Proposed Rule would impose substantial burdens on market participants in terms of time, money, and other resources. Due to the potentially significant costs and uncertain benefits, the Joint Associations urge the Commission to reconsider the Proposed Rule and its approach to the following issues:

- Information Technology. The Proposed Rule would require all commonly controlled entities to aggregate and monitor positions in futures and economically equivalent swaps on a continuous, real-time basis. Many of the Joint Associations' members do not have systems in place that enable them to reconcile and aggregate trading positions across affiliates instantly. An aggregation provision that demands a constant, consolidated portfolio will require, at great expense, the development of new, or the expansion of existing, company-wide monitoring systems.

- Reporting. The Proposed Rule would require all entities holding positions in excess of the applicable speculative limit to submit detailed daily reports by 9:00 a.m. the following business day substantiating the basis for the entity's bona fide hedging exemption. The proposed Position Visibility regulations would impose an additional reporting requirement on certain market participants, including large end-users that are merely hedging their own commercial risk. Preparing (and reviewing) these reports will create substantial technological and operational difficulties for market participants (and the Commission).

- Operational Complexity. The Proposed Rule is significantly (and unnecessarily) more complex than the current position limits system. Currently, traders track discrete positions held on individual exchanges. The main focus of these limits is typically only a few days surrounding expiration of the contract. In contrast, the Proposed Rule would require traders to determine which swaps are subject to position limits, convert them to futures equivalents, aggregate swaps and futures positions, and then monitor these positions continuously and in real-time for the spot month, each individual month, and for all-months-combined. The combined effect of the Proposed Rule is a highly complex and operationally burdensome system that is not tailored to preventing excessive speculation or market manipulation.

The Joint Associations believe that developing the systems needed to comply with the Proposed Rule will impose significant administrative and financial burdens on many market participants with little discernable benefit for the CFTC's goal of reducing excessive speculation.[11]

If, despite the questionable legal basis for its proposed position limits and the potentially substantial burdens that they may impose upon market participants, the Commission elects to issue a final position limit regulation, the Joint Associations request that the Commission make substantial modifications to the Proposed Rule.

IV. The Commission Should Only Impose Position Limits Based on Adequate Market Information and in Response to a Demonstrated Market Need.

A. Spot-Month Position Limits Should be Based on an Appropriate Measure of Deliverable Supply.

The Proposed Rule would establish spot-month position limits for the Referenced Contracts and physical commodity swaps that are economically equivalent to the Referenced Contracts based on the estimated deliverable supply for each contract.[12] As in the past, the definition of "deliverable supply" in the Proposed Rule would include the quantity of the commodity meeting a contract's delivery specifications that a market participant could, with "prudent planning," procure during the relevant time period from available local supply, deliverable non-local supply, and comparable supply (based on factors such as product and location).[13] The Joint Associations believe that the Commission should update its definition of "deliverable supply" to reflect the complexities and commercial realities of the current commodity markets.

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[11] The Commission acknowledges that "the compliance cost associated with all of [the filings required under the Proposed Rule, plus start-up costs] will be substantial, particularly in the case of the 404S filings [for swaps], which may require the collection and storage of information on counterparties that firms have hitherto not conducted." 76 Fed. Reg. at 4,766. More specifically, the Proposed Rule states that the visibility level-related reporting regulations would result in $2.4 million in annual labor costs (30,400 annual hours) and $27.3 million in annualized capital and start-up costs. *Id.* More striking, the requirements for the aggregation of trader accounts would result in 300,000 annual labor hours (no cost estimate provided) and $9.9 million in annualized capital and start-up costs, plus operating and maintenance costs. *Id.* at 4,766-67. The Joint Associations respectfully submit that such estimates, which may substantially underestimate the time and expense required to implement the technology upgrades required by the Proposed Rule, should give the Commission pause, particularly where there is no evidence that such costs are necessary.

[12] The Proposed Rule would define "deliverable supply" as: "the quantity of the commodity meeting a derivative contract's delivery specifications that can reasonably be expected to be readily available to short traders and saleable by long traders at its market value in normal cash marketing channels at the derivative contract's delivery points during the specified delivery period, barring abnormal movement in interstate commerce." 76 Fed. Reg. at 4,757.

[13] In re Cox, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,786, at 34,062-65 (CFTC Jul. 15, 1987).

The markets for futures, swaps, and other derivatives products have fundamentally changed since the Commission last considered making significant modifications to the rules governing position limits in 1987.[14] Many of the market-related changes have practical implications for the Commission's traditional definition of "deliverable supply." For example, in response to demand from market participants for more flexible settlement options for physically-settled commodity transactions, futures exchanges developed a new category of transactions collectively known as "exchanges for related positions" ("EFRPs"). EFRPs include:

- Exchange for physical transactions. A privately negotiated and simultaneous exchange of a futures position for a corresponding position in the underlying physical commodity.

- Exchange for risk transactions. A privately negotiated and simultaneous exchange of a futures position for a corresponding over-the-counter ("OTC") swap or other OTC derivative in the same or a related instrument.

- Exchange of options for options transactions. A privately negotiated and simultaneous exchange of an exchange-traded option position for a corresponding OTC option position or other OTC contract with similar characteristics in the same or a related instrument.

These new transactions, particularly exchange for physical transactions ("EFP"), make physical settlement of exchange-traded commodity futures and option contracts unnecessary in many circumstances, and therefore, increasingly less common. For example, the parties to an EFP could agree to exchange a position in the NYMEX Henry Hub Natural Gas contract for a related natural gas position at a delivery point other than Henry Hub. This transaction permits the buyer and seller of natural gas to negotiate a physical transaction that more precisely accommodates each party's commercial and economic needs. At the same time, the EFP makes the NYMEX Henry Hub Natural Gas futures contract substantially less vulnerable to a corner or squeeze because, in effect, the EFP has introduced meaningful flexibility to an otherwise limited physical settlement process.

The Joint Associations encourage the Commission to update the proposed definition of "deliverable supply" to account for settlement options and other new market mechanisms that provide flexibility to users of physical commodity futures, swaps, and other derivatives products. These market changes enable the Commission to expand the definition of "deliverable supply" (and increase the applicable spot-month position limits) without making the markets' physical commodity products more susceptible to price disruptions or manipulation. A well-tailored definition of deliverable supply that includes new but widely accepted alternative settlement

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[14] *See* Revision of Federal Speculative Position Limits, 52 Fed. Reg. 38,914 (Oct. 20, 1987).

methods will promote liquidity, encourage effective risk management, and ultimately reduce the threat of price volatility and manipulation.

B. The Commission Should Adopt More Flexible Position Limits for Cash-Settled Referenced Contracts.

The Proposed Rule would set separate spot-month position limits for contracts that settle by physical delivery and contracts that settle financially. In addition, the Proposed Rule provides for a conditional-spot-month position limit equal to five times the standard spot-month position limit for cash-settled contracts, provided that an entity relying on the conditional limits: (1) does not hold or control positions in a physically-settled Referenced Contract for the same commodity; (2) does not hold or control cash or forward positions in a Referenced Contract's spot-month in an amount greater than 25% of deliverable supply for the same commodity and the same delivery points as the Referenced Contract; and (3) would remain in compliance with any otherwise applicable single month position limits.[15]

To the extent that position limits on cash-settled Referenced Contracts are necessary at all, we agree that they should be subject to different, more flexible position limits than contracts that settle by physical delivery because they are inherently less susceptible to price disruptions and manipulation. However, the Commission's proposed restrictions on holding concurrent positions in related physically-settled Referenced Contracts are unnecessary and will be burdensome for market participants. Contrary to the Commission's current proposal, it previously has advised market participants and designated contract markets that "[in] general, position limits are not necessary for markets where the threat of excessive speculation or manipulation is nonexistent or very low."[16] It also has explained that *no* position limits are necessary for "contracts specifying cash settlement where the potential for distortion of such price is negligible."[17] The Joint Associations request that the Commission either continue to apply its existing policy and eliminate the limiting conditions imposed on spot-month position limits for cash-settled contracts, or explain why its prior policy is no longer valid.[18]

C. Single Month and All-Months-Combined Position Limits Should be Based on Adequate Information on the Relevant Markets and Adjusted Only When Necessary.

The Proposed Rule also would impose new limits on single month and all-months-combined positions based on a specific percentage of open interest for each Referenced Contract,

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[15] 76 Fed. Reg. at 4,770.

[16] 17 C.F.R. § 38, Appendix B.

[17] *Id*.

[18] *See*, *e.g.*, *Motor Vehicle Mfrs. Ass'n v. State Farm Mut. Auto Ins. Co.*, 463 U.S. 29, 34 (1983) (holding that an agency must provide an adequate basis and explanation before rescinding a prior regulation).

either in the aggregate or on a per class basis.[19] Because the Commission does not currently have adequate market data for the Referenced Contracts, the Proposed Rule provides a formula that would be used to calculate specific position limits when open interest data for each contract is available. The single month and all-months-combined position limits would then be recalculated on an annual basis to reflect changes in the market size of each of the Referenced Contracts. In addition, the Proposed Rule would establish a separate reporting requirement that would be triggered any time an entity controls a net position (including both hedges and speculative trades) in one or more of nine enumerated futures contracts, including four energy products.

1. *The Commission Could Adopt Federal Accountability Levels Rather than Position Limits.*

In the alternative, keeping in mind the financial, technological, and operational concerns expressed herein, the Commission's existing system of requiring exchanges to set accountability levels for referenced energy contracts appears to have worked well for many years. It may be possible to establish federal accountability levels outside the spot month without imposing undue burdens on market participants. Federal accountability levels would provide market participants with greater flexibility than position limits and, at the same time, would enable the Commission to request information about positions in and underlying Referenced Contracts once a market participant exceeds the applicable level. Accountability levels also would eliminate the need for the Commission's proposed position visibility level regime by providing the Commission with comparable access to information about large positions and traders through a familiar and well-understood regulatory regime.

If the Commission nevertheless decides to adopt the proposed visibility levels, the Joint Associations believe that the proposed threshold for the NYMEX Henry Hub Natural Gas futures contract is too low and will capture far more than the "30 unique owners" per year estimated by the Commission. This is particularly true if the CFTC adopts a definition of "economically equivalent" that includes basis swaps and contracts that settle on prices at locations other than those in the Referenced Contracts.[20] Any visibility level should be set no lower than 5% of open interest for the Referenced Contract, or approximately 50,000 contracts for the NYMEX Henry Hub Natural Gas contract.[21]

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[19] 76 Fed. Reg. at 4,758.

[20] *Id*. at 4,761.

[21] The Joint Associations note that the proposed position visibility regulations would impose an additional reporting burden on certain market participants with little corresponding benefit, particularly if the CFTC does not have the resources to compile and review the reported data.

In addition, if the Commission declines to adopt accountability levels and proceeds with the Proposed Rule in its current form, the formula for calculating the single month and all-months-combined position limits should be based on ten percent of the first 25,000 contracts of open interest plus five percent of the remaining open interest contracts. However, the Joint Associations request that the Commission clarify that it will not apply single month limits to deferred months when open interest is below 5,000 contracts.[22] Without this limitation, it may be impossible for market participants to execute the first trade in a given month without violating a position limit.

2. *The Commission Should Not Adjust Position Limits Annually.*

The Commission should revise the Proposed Rule to provide market participants with greater certainty regarding any changes that might be made to the position limits in the future. The Commission's current proposal to recalculate position limits annually based on changes in open interest likely will introduce significant uncertainty into the derivatives markets, particularly for long-term contracts that include positions in relatively illiquid deferred months. For example, a speculator may be wary of entering into a long-term transaction if the position limit that makes the trade permissible at one point in time may be reduced in the future. In order to secure financing for many energy projects, including transmission lines and new solar, wind and other renewable power generation, the Joint Associations' members must be able to hedge price risk many years into the future. The uncertainty associated with potentially adjustable position limits may inadvertently discourage speculators from assuming the risks necessary to provide the Joint Associations' members with the ability to execute long-term hedges which, in turn, would make it difficult for them to finance crucial infrastructure projects.

The Joint Associations recommend that the Commission only adjust position limits when necessary, rather than on an automatic, annual basis. Alternatively, the Joint Associations request that the Commission clarify that the exemption in proposed Rule 151.9(a) allowing position limits to be "exceeded to the extent that such positions remain open and were entered into in good faith prior to the effective date of any rule, regulation, or order that specifies a position limit," also applies to existing positions affected by an adjustment based on changes in open interest.[23]

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[22] For example, the Commission states that accountability levels may be appropriate in lieu of position limits for contracts in excluded commodities with open interest below 5,000 contracts. 76 Fed. Reg. at 4,763.

[23] 76 Fed. Reg. at 4,775.

D. The Commission Should Allow Market Participants to Define what Constitutes an "Economically Equivalent" Contract Consistently with Commercial Practices.

CEA Section 4a(a)(5) requires the Commission to "establish limits on the amount of positions . . . that may be held by any person with respect to swaps that are economically equivalent" to each Referenced Contract. However, the Proposed Rule does not define with sufficient specificity what constitutes an economically equivalent contract. Rather, the proposed regulatory text defines a Referenced Contract simply as:

> on a futures equivalent basis with respect to a particular core referenced futures contract, a futures listed in § 151.2, or a referenced paired futures contract, option contract, swap or swaption, other than a basis contract or contract on a commodity index.[24]

In contrast, in the preamble to the Proposed Rule, the Commission suggested that Referenced Contracts also include derivatives that are "based on the price of the same commodity for delivery at the same location(s) as that of a . . . listed contract, or *another* delivery location with substantially the same supply and demand fundamentals as the delivery location of a . . . listed contract."[25] According to the Proposed Rule, the Commission could treat contracts settled to prices that are merely correlated as "economically equivalent."[26]

Contracts based on the same underlying commodity, but priced at different delivery locations, are not economically equivalent, even though they may at times demonstrate some degree of price correlation. Treating economically distinct contracts as equivalent will unnecessarily complicate the way in which many important commodity markets operate. For example, the NYMEX Henry Hub Natural Gas contract is one of the futures contracts listed in the Proposed Rule and settles based on the price of natural gas delivered to the Henry Hub in Louisiana. In contrast, the ICE Transco Z6 (NY) Financial Index Swap contract settles based on the price of natural gas delivered on the Transcontinental Pipeline near New York City, New York. Even though natural gas underlies both contracts, they are not "economically equivalent" because they are based on the price of delivery to two geographically and commercially distinct locations.[27] The Commission suggested in a separate rulemaking that the spot-markets for natural gas at Transco Z6 and Henry Hub were "physically linked" by the Transcontinental Pipeline; however, the Joint Associations respectfully suggest that a physical connection cannot

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[24] *Id*. at 4,768.

[25] *Id*. at 4,753 (emphasis added).

[26] *Id*.

[27] For example, although Henry Hub and Transco Z6 are physically connected, the pipeline can become capacity constrained or may experience an outage that results in dramatically different markets for natural gas in Louisiana and New York.

be used as a proxy for economic equivalence.[28] There are ample data showing that, although the prices at Transco Z6 and Henry Hub may be highly correlated during certain periods (*e.g.*, low-demand, summer months), prices diverge substantially during other extended periods (*e.g.*, high-demand, winter months) and also tend to change gradually over time.[29] Regardless of any physical connection or occasional correlation, the two markets are independent and distinct from one another.

Similarly, a Referenced Contract and a basis swap that is, in part, linked to the price of that Reference Contract are not economically equivalent.[30] Even though the prices of two such contracts are to a degree correlated, the basis swap is specifically designed to reflect supply and demand fundamentals at *two* distinct delivery locations. In other words, the value of a basis swap is driven by the transportation dynamics *between* two delivery points, not the commodity price at any single location. Indeed, if the two legs of a basis swap were, in fact, economically equivalent, the swap would serve no purpose because each party to the transaction would assume essentially the same risk that it was giving up. Instead, commercial parties use basis swaps precisely to manage the economic differences between two locations.[31] In practice, certain basis swaps may be flat for a long period of time, however, this does not mean that the transaction itself is economically equivalent to any Referenced Contract.[32] On the contrary, commercial entities enter into such transactions as a hedge against unexpected circumstances that could magnify the differences between two delivery locations that, under ordinary conditions, exhibit similar economic characteristics. For example, a commercial consumer of natural gas may enter

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[28] *See* Position Reports for Physical Commodity Swaps, 75 Fed. Reg. 67,258, 67,261 (Nov. 2, 2010).

[29] For example, the correlation between cash market prices at the Henry Hub and Transco Z6 New York has fallen from 0.88 in the 12 months ending March 21, 2010 to 0.34 in the 12 months ending March 21, 2011.

[30] Although the definition of "referenced contract" in the Proposed Rule excludes basis contracts and contracts on commodity indices, the Commission has indicated in other proposed rules that such categories of contracts may be economically equivalent to core referenced futures contracts and, therefore, "paired" for position limits purposes. *See*, *e.g.*, 75 Fed. Reg. at 67,260 (describing the Argus Sour Crude Index as "a paired swap" with respect to the NYMEX WTI futures contract because the index partially settles based on the price of a listed contract). The Joint Associations request that the Commission determine that basis swaps, contracts based on the settlement price of a commodity index, and other contracts with different supply and demand fundamentals are not economically equivalent to the core referenced futures contracts.

[31] The Joint Associations' members often purchase or sell financial commodity contracts at locations other than major pricing hubs, like the Henry Hub, precisely because the linkages between prices at those hubs and other locations can be difficult to predict. Entering into financial commodity contracts referencing more local, but less liquid delivery points provides a more effective hedge.

[32] In fact, the price volatility of a basis swap is commonly much lower than the price volatility of either underlying reference price. Accordingly, a basis swap can only be "economically equivalent" to a Referenced Contract if the notional quantity of the basis swap is increased substantially and adjusted constantly, but this defeats the purpose that the basis swap is meant to serve, and therefore, is not a common commercial practice.

into a basis swap linked to the NYMEX Henry Hub Natural Gas contract and the price of natural gas delivered at TETCO M-1 30 in order to hedge the risk of transporting gas from Henry Hub in Louisiana to Market Zone 1 of the Texas Eastern Transmission company's pipeline in Mississippi. This basis swap is economically *linked* to the price of the NYMEX Henry Hub Natural Gas contract, but the two contracts are not economically *equivalent*.

The Commission should not adopt a final rule that blurs commercial reality and requires an economically irrational result. Recognizing the nearly infinite complexity of the commodity and derivatives markets, the Joint Associations urge the Commission to allow market participants to determine, based on their own commercial observations and experience, which contracts should be treated as economic equivalent. Any good faith determination that two contracts are or are not economically equivalent should be sufficient to protect a market participant from penalties or other liability. If the Commission does not provide sufficient certainty with regards to which contracts must be treated as equivalent, market participants will be unable to carry out their compliance obligations accurately or efficiently.

V. The Commission Should Adopt a Commercially Practicable Hedge Exemption Process.

A. The Commission Should not Limit the Scope of the *Bona Fide* Hedge Exemption to the Enumerated Hedging Transactions in the Proposed Rule.

CEA Section 4a(c)(2), as amended by Section 737 of 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 CFTC's regulations.[33] 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 five categories of enumerated hedging transactions.[34] In particular, the Proposed Rule excludes several common categories of risk management transactions from the definition of *bona fide* hedging, including:

- Hedges of inventory or other assets that a hedger anticipates owning;
- Hedges of liabilities or services that a hedger anticipates incurring, providing or purchasing;

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[33] The definition of *bona fide* hedging in Part 1.3(z) of the CFTC'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. According to the Commission, the definition in Section 737 defines *bona fide* hedging for derivatives that are subject to the Proposed Rule "only if such transactions or positions represent cash market transactions and offset cash market risks, as opposed to the acceptance of *bona fide* hedging transactions and positions as activity that normally, but not necessarily, represents a substitute for cash market transactions or positions." 76 Fed. Reg. at 4,761.

[34] *Id*. at 4,771.

- Hedges of assets that a person merchandises or anticipates merchandizing;
- Swaps used to hedge "[s]ales of any underlying commodity;"[35] and
- Hedges of certain swaps that qualify for the end-user clearing exception.[36]

Most important, unlike the current definition in Part 1.3(z), the Proposed Rule provides no mechanism through which market participants may request an exemption for non-enumerated hedging transactions even though Section 737 of the Dodd-Frank Act provides the Commission with broad authority to grant exemptive relief.[37]

The Joint Associations believe that the proposed definition of *bona fide* hedging transactions or positions is unnecessarily narrow and, if adopted, may discourage or drive to foreign markets a significant volume of important and beneficial risk management activity. This will 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. The Joint Associations recommend that the Commission retain a procedure for exempting non-enumerated hedging transactions from position limits. Such a provision is expressly authorized under CEA Section 4a(a)(7) and would provide essential flexibility for market participants that engage in legitimate risk management activity that does not fall within one of the categories of enumerated hedging transactions.[38]

B. The Commission Should Allow End-Users Relying on a *Bona Fide* Hedge Exemption to Provide Monthly Reports.

Under the Proposed Rule, a person intending to rely upon the *bona fide* hedge exemption would be required to notify the Commission that it has exceeded a position limit in reliance on the *bona fide* hedge exemption by submitting a detailed report to the CFTC by 9:00 a.m. on the

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35 *Id.*

36 In its December 21, 2010 proposed rule further defining the terms "swap dealer" and "major swap participant", the Commission defines "hedging or mitigating commercial risk" to include any swap that:

- qualifies as a bona fide hedging transaction;
- qualifies for hedging treatment under FASB Accounting Standards Codification Topic 815; or
- is economically appropriate to the reduction of risks in the management of a commercial enterprise (*e.g.*, the swap hedges potential changes in the value of assets or liabilities).

Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant," and "Eligible Contract Participant," 75 Fed. Reg. 80,174, 80,214-15, RIN 3038-AD06 (Dec. 21, 2010). Swaps that fall only under the second and third prongs of the definition of commercial risk do not appear to be included in the definition of *bona fide* hedging transactions or positions.

37 Dodd-Frank Act § 737(a)(4) (codified as CEA § 4a(a)(7)).

38 CEA § 4a(a)(7).

business day following *each day* that the trader exceeds a position limit.[39] The Joint Associations support the Commission's efforts to ensure that the *bona fide* hedge exemption is not abused. However, the Joint Associations believe that the proposed process for reporting and verifying *bona fide* hedging transactions can be made more efficient and commercially practicable without limiting the Commission's ability to prevent abuse. Requiring market participants to track, aggregate, and analyze their entire portfolio of spot, single month, and all-months-combined positions in all Referenced Contracts in order to prepare and submit the *daily* reports required under the Proposed Rule will be costly and difficult to implement and to consistently manage.[40]

We recommend that the Commission revise the proposed reporting requirements to provide that a trader must file reports only when its position first exceeds a position limit. This initial notice, which could be supplemented by monthly reports when the trader's position remains in excess of the limit, would provide the Commission with the information it needs to monitor traders' use of the *bona fide* hedge exemption without subjecting market participants and the Commission to potentially unmanageable filing requirements.

C. The Commission Should Adopt a Verification Process Based on a Simple, One-Time Representation.

Like the proposed reporting requirements, the verification requirements in the Proposed Rule also may create significant operational and commercial difficulties for market participants. For example, proposed Rule 151.5(g) would require any entity relying on a *bona fide* hedge exemption to provide a written representation to its swap counterparty verifying that the swap qualifies as a *bona fide* hedging transaction. Upon receipt of the hedger's written representation, the other party to the swap then would be required to confirm receipt (also in writing) of the hedger's representation. The Proposed Rule would require this verification procedure to be completed for *every* swap that relies on a *bona fide* hedge exemption. In addition, the parties to such a transaction would be required to retain the hedger's representation and the counterparty's confirmation so that it may be provided to the Commission upon request.

The Joint Associations respectfully submit that the proposed verification process is too time-consuming and cumbersome to be workable in many common commercial contexts, particularly where hedgers must respond to rapidly changing markets and risks. For example, hedgers concerned that a transaction may not qualify for a *bona fide* hedge exemption until the

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[39] Because the specific questions contained in any form associated with a new or revised mandatory reporting requirement can have a material impact on market participants subject to regulation, the Joint Associations request that the Commission publish for public comment the various forms described in the Proposed Rule.

[40] In addition, the Joint Associations note that the proposed reporting requirement also would impose a correspondingly substantial burden on the CFTC to process, review, and analyze the reports submitted under proposed Rule 151.5(b). It is likely that the CFTC will find it difficult to process, review, and analyze this volume of information to a meaningful degree on a daily basis.

required verifications and confirmations have been exchanged may delay executing a swap by hours, if not days. While the transaction is pending, the hedger's counterparty would implicitly assume the risk that the market might move before the trade is finalized. In some cases this would result in the counterparty internalizing this risk in the commercial terms of the transaction, effectively increasing the hedger's costs. In other cases, particularly where the market for the underlying commodity becomes volatile, the hedger's counterparty could decide to abandon the transaction altogether. Both outcomes make the hedge exemption process less effective for commercial entities that rely on derivatives to manage their business risks, and are contrary to Congress's goal of ensuring sufficient market liquidity for *bona fide* hedgers.

As a result, the Joint Associations recommend that the Commission replace proposed Rule 151.5(g) with a simpler, yet equally effective, verification process. Specifically, the Commission should allow the parties to rely upon a one-time representation that each swap that it enters into with a *bona fide* hedger qualifies as a *bona fide* hedging transaction. Such a verification process would be a commercially reasonable means of ensuring the integrity of the *bona fide* hedge exemption process, and would be consistent with comments that the Commission has received from market participants concerning the proposed regulations implementing the end-user clearing exception and other provisions of the Dodd-Frank Act.

The Joint Associations further request that the Commission clarify Rule 151.5(g) to provide that all swaps entered into opposite a counterparty for which the swap qualifies as a *bona fide* hedging transaction will, similarly, qualify as a *bona fide* hedging transaction for the other party to the transaction. As currently drafted, Rule 151.5(g) appears to limit the ability of one swap counterparty to "pass-through" a hedge to another counterparty to those cases where one of the parties to the transaction "is relying on a *bona fide* hedge exemption to *exceed* the position limits . . . ."[41] If read literally, the Proposed Rule would significantly limit the ability of hedgers to use swaps to mitigate their risk because, as a practical matter, their counterparties would be unable to offset the risk associated with the underlying transaction in many cases. This is inconsistent with sound risk management practices and contrary to the plain language in CEA Section 4a(c)(1) which prohibits the Commission from placing any limits on *bona fide* hedging transactions, regardless of whether a party's total positions are above or below the applicable speculative position limit.[42] The Joint Associations' members rely on speculators to assume the risks that they and other commercial entities seek to hedge. Whether through futures or swaps, speculation that enables hedging is not "excessive," but rather an integral part of a well-functioning market.[43]

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[41] 76 Fed. Reg. 4,773 (emphasis added).

[42] CEA § 4a(c)(1).

[43] *See* CEA § 3(a)("The transactions subject to this Act are . . . affected with a national public interest by providing a means for managing and assuming price risks. . . .")

D. The Commission Should Permit Anticipatory Hedges Longer than One Year.

The Proposed Rule permits market participants to request an anticipatory hedge exemption for "unsold anticipated commercial production or unfilled anticipated commercial requirements connected to a commodity underlying a referenced contract" by submitting certain information to the Commission no less than ten days prior to the date on which any applicable transactions or positions would be established.[44] Although the anticipatory hedge provision permits market participants to request a *bona fide* hedge exemption proactively, as written the Proposed Rule appears only to permit anticipatory hedges for a period of one year or less, regardless of the underlying commodity.[45]

The Joint Associations request that the Commission reconsider the proposed anticipatory hedge exemption procedure and permit *bona fide* hedgers to request exemptions from position limits for any period of time. Limiting the availability of an anticipatory hedge exemption to one year may make sense in certain markets. For example, the risks associated with most agricultural commodities are typically linked to an annual crop cycle. However, in many other circumstances, limiting the availability of an anticipatory hedge exemption to just one year may restrict the ability of commercial entities to effectively manage their commercial risk. In particular, electric generators, utilities, and other energy companies operate commercial businesses with time horizons substantially longer than one year. Electric generators, for example, periodically enter into long-term fuel supply agreements to ensure a reliable supply of fuel, and then use derivatives to hedge the price risk associated with these agreements. These fuel supply agreements, and the corresponding hedges, often span multiple years. Moreover, because electricity essentially cannot be stored and, therefore, must be generated on demand, all electricity hedges are, in a sense, "anticipatory." If the Commission limits the ability of market participants to obtain anticipatory hedges for commercial risk more than a year in the future or places impractical limitations on what constitutes "anticipated" supply and demand, it will make it difficult for many market participants, including the Joint Associations' members, to manage their long-term commercial risk completely.

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[44] 76 Fed. Reg. at 4,772.

[45] Rule 151.5(a)(2) lists the enumerated hedging transactions that qualify as *bona fide* hedging, which includes "[s]ales of any commodity underlying referenced contracts which do not exceed . . . unsold anticipated production . . . which may not exceed one year *for referenced agricultural contracts*" and "[p]urchases of referenced contracts which do not exceed in quantity . . . [u]nfilled anticipated requirements . . . which may not exceed one year for *referenced agricultural contracts* . . . ." 76 Fed. Reg. at 4,771 (emphasis added). Rule 151.5(a) does not impose a one year limitation on anticipatory hedges for non-agricultural contracts, however, the reporting requirement for anticipatory hedges in Rule 151.5(c) appears to limit *all* anticipatory hedge exemptions to transactions "which may not exceed one year." *Id*. at 4,772. The Joint Associations understand that, notwithstanding the language in the Proposed Rule, the Commission may have intended to permit non-agricultural hedgers to obtain anticipatory hedge exemptions more than one year in advance, provided that they renew their applications on an annual basis. The Joint Associations would support such a provision if it were proposed.

VI. The Commission Should Adopt a Commercially Practicable Aggregation Requirement.

To determine whether an entity is in compliance with its applicable position limits, the Proposed Rule would require it to aggregate the positions of each account where it "directly or indirectly holds positions or controls trading."[46] In addition, the Proposed Rule would require, regardless of actual control, an entity to aggregate positions and accounts anytime it "directly or indirectly has a 10 percent or greater ownership or equity interest" in another account or portfolio of positions.[47] However, the Proposed Rule provides a limited exemption from the aggregation requirement for the positions of an owned non-financial entity, provided that the parties can demonstrate to the Commission that the non-financial entity's trading "is independently controlled and managed."[48] The Proposed Rule notes that it will consider an entity's requiring separate employees and risk management systems to be two indicia of an owned non-financial entity's independence.[49]

Although the Joint Associations appreciate the Commission's decision to provide an exemption from the aggregation requirement for owned non-financial entities in the Proposed Rule, we respectfully submit that the aggregation requirement will only allow market participants to manage their commercial risk effectively if it is revised in two significant ways:

- Exemptions from the aggregation requirement should be effective when filed; and
- Entities should be permitted to manage risk on an enterprise basis.

Without these revisions, the Joint Associations believe that the aggregation provision could result in significant unintended consequences for many market participants.

A. The Commission Should Revise the Aggregation Provision to Provide that Exemption Requests are Effective When Filed.

The Joint Associations are concerned that making requests for exemptions from the aggregation requirement effective only after review and acceptance by the Commission may have a significant adverse effect on every market participant that operates as part of larger corporate entity. If the Proposed Rule is adopted in its current form, the Joint Associations expect that the Commission may receive hundreds of exemption requests. During the period of time when this initial backlog of applications is pending, market participants will be forced either to aggregate their positions, even among independently managed and controlled accounts, or to

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46 76 Fed. Reg. at 4,774.

47 *Id*.

48 *Id*.

49 *Id*. at 4,763.

artificially allocate each position limit among its affiliated entities to ensure that it is not exceeded by the organization as a whole. Mandatory aggregation could inadvertently cause serious regulatory and operational problems. For example, in the electric power industry, federal energy regulators often require that strict information barriers be put in place between regulated and unregulated affiliated utility trading operations to ensure that each is operated independently.[50] Aggregating position information among affiliates will violate these prohibitions. Similarly, allocating position limits among affiliates would cause operational problems by substantially reducing the ability of each entity to trade without potentially exceeding its threshold.

To mitigate these potential problems, the Joint Associations recommend that the Commission allow applications for an exemption from the aggregation requirement to be provisionally effective when filed. The potential for abuse of the exemption process would be minimal because CEA Section 9(a)(3) expressly prohibits knowingly misrepresenting or omitting material facts in any required application.[51] Moreover, for utilities and other entities that are already subject to prohibitions on sharing information between affiliates, requiring an additional "waiting period" while the CFTC reviews an exemption request would be particularly superficial because such an entity could provide legal authority to support its claim of independent management and control. In any case, if the Commission decides to decline an exemption request, it could require the entity to begin aggregating its positions immediately and, if necessary, unwinding positions in excess of the limit in an orderly manner over a reasonable period of time.

B. The Commission Should Allow Entities to Manage Risk on an Enterprise Basis Across Affiliates.

The Proposed Rule suggests that independently managed and controlled entities would typically maintain separate risk management systems and related personnel.[52] The Joint Associations believe that such characteristics are inaccurate and inconsistent with the way in

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[50] The Federal Energy Regulatory Commission's ("FERC") rules require that a public utility with captive customers function independently of its market-regulated power sales affiliate and restrict the sharing of certain nonpublic information between them. *See* 18 C.F.R. 35.39. Those regulations currently are subject to a proposed rulemaking that likely will result in further clarification about the type of information that may not be shared. *See* FERC Order and Notice of Proposed Rulemaking dated April 15, 2010 (respectively the "April 15 FERC Order" and the "April 15 NOPR", and collectively the "April 15 FERC Announcements"). Paragraphs 41-43 of the April 15 FERC Order prohibit the sharing of information dealing with resource planning and fuel procurement between traditional regulated public utilities and market-regulated power sales affiliates. Depending on the outcome of the April 15 FERC Announcements, many of the Joint Associations' members may not be permitted to share the information necessary for them to coordinate their use of the commodities and derivatives markets to ensure that their positions (when aggregated) do not violate the speculative position limits.

[51] CEA § 9(a)(3).

[52] 76 Fed. Reg. at 4,763.

which many market participants currently operate. Many commercial entities consolidate their risk management operations in a single department or even a separate corporate entity. The individuals responsible for monitoring and managing a company's risk profile in such an organization do not control trading decisions and do not disseminate trading information among traders. On the contrary, their purpose is simply to serve as a single point from which the corporation as a whole can manage its risk in the most efficient and effective manner possible.

The Joint Associations generally support the indicia of independent management and control described in the Proposed Rule. However, the Joint Associations recommend that the Commission clarify that individual market participants have reasonable discretion in establishing the specific manner by which they may demonstrate independent management and control. In particular, the Joint Associations urge the Commission to acknowledge that affiliated entities may manage risk on an enterprise basis by using common personnel and compliance systems, provided that the risk management systems preserve the independent trading control and management of each affiliate. Requiring separate risk management systems and employees for each affiliated entity would be inefficient and unnecessarily burdensome for market participants. Moreover, by making it more difficult for entities to review and analyze the risk associated with their entire trading portfolio, such a provision could ultimately increase market risk.

VII. The Commission Should Provide an Adequate Transition Period that Allows All Market Participants to Come into Compliance in a Cost-Effective Manner.

All market participants, and in particular end-users, need a reasonable amount of time to comply with the new requirements imposed by the Dodd-Frank Act and the CFTC's implementing regulations. The Commission has previously recognized the potential need to provide market participants with more time to comply with the Dodd-Frank Act's new statutory and regulatory requirements. In its notice regarding Petitions Seeking Grandfather Relief for Trading Activity Done in Reliance Upon Section 2(h)(1)–(2) of the CEA, the Commission represented to the public that, while it was not granting such grandfather relief, it was "prepared to revisit its decision in the future should it be necessary in order to ensure a smooth transition to the new regulatory regime . . . ."[53] Furthermore, the Commission confirmed that it would "strive to ensure that current practices will not be unduly disrupted during the transition to the new regulatory regime" and would "use its available exemptive authorities to address" situations in which required regulations may pose "particular difficulties [for persons who rely on Section 2(h)] that cannot be addressed in final regulations . . . ."[54]

[53] Notice Regarding the Treatment of Petitions Seeking Grandfather Relief for Trading Activity Done in Reliance Upon Section 2(h)(1)-(2) of the Commodity Exchange Act, 75 Fed. Reg. 56,512, (Sept. 16, 2010).

[54] *Id*. at 56,513.

Although the Dodd-Frank Act provides that no final rule will become effective *less* than 60 days after its publication in the Federal Register, the Joint Associations' members and other similarly situated market participants need more time to come into compliance with the many new requirements in this and other proposed rules. Congress specifically included a grandfather clause authorizing the Commission to provide a reasonable compliance period, up to one year, for physical commodity market participants, because it recognized the potentially disruptive effect that the Dodd-Frank Act could have on them.[55] For example, some end-users have limited information technology capabilities and will need a reasonable period of time, after the issuance of final regulations, to update and modify their information technology systems to ensure compliance. Accordingly, the Joint Associations respectfully request that the Commission provide market participants with a transition period of at least one year from the date on which the final version of this rule is promulgated. Without such a reasonable transition period, many end-users and other similarly situated entities will have substantial difficulty complying in full with their new regulatory obligations.

VIII. Conclusion

The Joint Associations appreciate the Commission's willingness to consider and adopt many of the recommendations submitted by market participants earlier in the rulemaking process. As explained above, however, the Joint Associations encourage the Commission to withdraw the Proposed Rule until it has the market data it needs to determine whether position limits for the Referenced Contracts are "necessary."

The Joint Associations request that the Commission hold open and reopen the comment periods for all rules being promulgated under the Dodd-Frank Act for a reasonable period of time following the issuance of all rules to enable interested parties to consider and comment upon the regulations and the corresponding definitions as a whole. In addition, for purposes of these comments, the Joint Associations rely on the definition in Section 721(a) of the Dodd-Frank Act, which generally provides that "swap" means an agreement that, by its terms, settles financially and that, in most cases, involves an exchange of fixed-for-floating payments based upon the value of a notional quantity of a commodity.[56] To the extent the Commission further defines

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[55] *See* Section 723(c)(1) of the Dodd-Frank Act providing persons transacting in exempt commodities in reliance on Section 2(h) of the CEA the right to petition the Commission for grandfather relief.

[56] A fixed-for-floating swap falls within the definition of swap in Section 721(a), which provides that the term "swap" includes a contract "that provides on an executory basis for the exchange . . . of 1 or more payments based on the value . . . of 1 or more . . . commodities . . . and that transfers, as between the parties . . . the financial risk associated with a future change in any such value . . . without also conveying a current or future direct or indirect ownership in [the underlying commodity]." Dodd-Frank Act § 721(a) (to be codified as CEA § 1a(47)(A)(iii)).

"swap" in a manner that modifies materially the commonly understood meaning of this term, the Joint Associations respectfully reserve the right to amend and supplement these comments.[57]

Please contact us at the numbers listed below if you have any questions regarding these comments.

Respectfully submitted,

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Bruce Fekrat, Senior Special Counsel

[57] The Joint Associations refer the Commission to EEI's comments filed on September 20, 2010 in response to the Advance Notice of Proposed Rulemaking regarding key definitions in the Dodd-Frank Act. Definitions Contained in Title VII of Dodd-Frank Wall Street Reform and Consumer Protection Act, 75 Fed. Reg. 51,429 (Aug. 20, 2010).