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July 22, 2011

Via Online Submission and Email

Mr. David A. Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581
File No. S7-16-11

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F St., NE
Washington, D.C. 20549
rule-comments@sec.gov
File No. S7-16-11

Re: **COMMENTS OF COALITION OF PHYSICAL ENERGY COMPANIES**
Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, RIN 3038-AD46 (CFTC), RIN 3235-AL14 (SEC)

Dear Mr. Stawick and Ms. Murphy:

By publication in the Federal Register on May 23, 2011, the Commodity Futures Trading Commission ("CFTC") and the Securities and Exchange Commission ("SEC") (collectively the "Commissions") issued joint proposed rules and proposed interpretations titled "Further Definition of 'Swap,' 'Security-Based Swap,' and 'Security-Based Swap Agreement'; Mixed Swaps; Security-Based Swap Agreement Recordkeeping" (the "Product Definition NOPR").[1] The Product Definition NOPR was issued by the Commissions pursuant to Section 712(d)(1) of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd Frank"),[2] which provides that the Commissions shall further define various terms for purposes of Dodd-Frank beyond the definitions provided in the statute, including the term "swap." By this letter, the

[1] 76 Fed. Reg. 29818 (May 23, 2011).

[2] Public Law No. 111-203, 124 Stat. 1376 (2010).

Coalition of Physical Energy Company ("COPE")[3] provides comments on the Product Definition NOPR.

The members of COPE are physical energy companies in the business of producing, processing, and merchandising energy commodities at retail and wholesale. COPE members utilize swaps to hedge the commercial risk of their physical businesses. COPE members have diverse business models and legal entity structures, but all share the fundamental need to understand what products and transactions will be considered "swaps" under the Commissions' regulatory framework implementing Dodd-Frank.

COPE believes that the Commissions must make clear in any final rules based upon the Product Definition NOPR that a "swap" is a financially settling agreement that derives its value from the change in price of an underlying commodity or security. Conversely, the Commissions must also make clear that any contract, agreement or transaction for the sale of any physical commodity, environmental attribute, emissions credit or other similar products is not a swap.[4] In addition, a physical transaction that is ultimately settled financially is not a swap. Swaps must be clearly defined as derivatives.

While the Commissions' commentary in the Product Definition NOPR gives market participants some comfort toward the conclusion that a swap is a financially settling agreement, there is still ambiguity on this score both in the preamble and the proposed regulatory text. The Product Definition NOPR consists of seventy pages of preamble (out of a total of eighty-three pages of the NOPR) leading to the following fundamental proposed regulatory text for the definition of "swap": "The term *swap* has the meaning set forth in section 1a(47) of the Commodity Exchange Act."[5] The definition of "swap" from revised Section 1a(47) of the Commodity Exchange Act ("CEA")[6] is far from clear and requires attention from the Commissions in the regulations. COPE believes that the Commissions should act on their authority and draft regulations which will bring greater clarity and specificity to the definition.[7] To that end, the Commission has devoted the eighty-three pages of the Product Definition NOPR in an attempt to clarify the statutory definition of a "swap." Unfortunately, as a general matter, while the Commissions' preamble attempts to bring clarity to the definition, that clarity has not made its way into the proposed regulatory text.

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[3] The members of COPE are: Apache Corporation; El Paso Corporation; Enterprise Products Partners L.P; Iberdrola Renewables, Inc.; Kinder Morgan; MarkWest Energy Partners, L.P.; Noble Energy, Inc.; NRG Energy, Inc.; Shell Energy North America (US), L.P.; SouthStar Energy Services LLC; and Targa Resources Partners LP.

[4] The same result must be made clear by the Commissions with respect to options on such products which, if exercised, require physical delivery.

[5] Product Definition NOPR at 29888 (proposed § 1.3(xxx)(1)) (emphasis in original).

[6] Dodd Frank § 721(a)(21).

[7] *See id.* at § 712(d)(1).

In these comments, COPE requests that the Commissions bring needed clarity to the regulatory text in any final rules based upon the Product Definition NOPR. The term "swap" is the bedrock element of Title VII of Dodd-Frank. Since virtually all other Dodd-Frank regulation under Title VII flows from a given transaction's characterization as a swap, there should be absolute clarity as to what is a swap. COPE sees no reason why such clarity cannot be included in the regulations defining the term. In fact, the regulations should be as crystal clear as possible. As COPE has pointed out with respect to the Commissions' notice of proposed rulemaking regarding entity definitions under Dodd-Frank,[8] a regulatory preamble is to a regulation as legislative history is to a statute.[9] The preamble is not controlling and is only relevant to the degree that the regulator finds the regulation to be ambiguous.[10]

In the Product Definition NOPR, rather than presenting a proposed rule and the basis therefore, the Commissions have taken the approach of reacting to comments filed to their Advanced Notice of Proposed Rulemaking ("ANOPR").[11] Thus, the Product Definition NOPR consists of discussion of issues raised by ANOPR commentors. As the ANOPR did not include a "strawman" proposed rule, the Product Definition NOPR is fragmented and reactive rather than making clear exactly what the Commissions are proposing. This indirect approach is a further reason why specificity and clarity in the regulatory text is critical to the definition of the term "swap."

In the Product Definition NOPR, the Commissions address a myriad of agreements and conclude that they are not swaps. These include insurance contracts, consumer agreements, and commercial agreements which would not be considered swaps under the Commissions' proposed interpretive guidance.[12] The NOPR states:

> In determining whether similar types of agreements, contracts, and transactions entered into by consumers or commercial entities are swaps or security-based swaps, the Commissions intend to consider the characteristics and factors that are common to the consumer and commercial transactions listed above:

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[8] Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant" and "Eligible Contract Participant," 75 Fed. Reg. 80174 (Dec. 21, 2010) (the "Entity Definitions NOPR").

[9] COPE Comments to Entity Definitions NOPR at 2-3 (February 22, 2011) (citing *Nat'l Wildlife Fed'n v. E.P.A.*, 286 F.3d 554, 569-70 (D.C. Cir. 2002), *supplemented sub nom. In re Kagan*, 351 F.3d 1157 (D.C. Cir. 2003) (noting that the preamble of an agency's rule is akin to the preamble or legislative history of a statute, and the regulatory text is controlling).

[10] *Id.*

[11] Definitions Contained in Title VII of Dodd-Frank Wall Street Reform and Consumer Protection Act, 75 FR 51429 (Aug. 20, 2010).

[12] Product Definition NOPR at 29822.

- They do not contain payment obligations, whether or not contingent, that are severable from the agreement, contract, or transaction;

- They are not traded on an organized market or over-the-counter; and

- In the case of consumer arrangements, they:

  - Involve an asset of which the consumer is the owner or beneficiary, or that the consumer is purchasing, or they involve a service provided, or to be provided, by or to the consumer, or

- In the case of commercial arrangements, they are entered into:

  - By commercial or non-profit entities as principals (or by their agents) to serve an independent commercial, business, or non-profit purpose, and

  - Other than for speculative, hedging, or investment purposes.[13]

While COPE agrees with the Commissions that it is helpful to provide clarification as to what types of agreements are not swaps, COPE strongly believes it is critical for the Commissions to provide the essential elements of what types of agreements are swaps under Dodd-Frank, beyond the general definition provided in the statute. COPE recommends that the Commissions include the following overarching definition of the term "swap" in their regulations:

> **A "swap" means "a derivative agreement, contract or transaction intended to settle financially, the value of which is based upon the change in value of an underlying commodity."**

A definition such as that set forth above would provide much greater clarity than merely referring to the statute and providing a list of agreements which include the term "swap" (e.g. "cross-currency swap") as the proposed regulation currently does.[14] COPE believes that the Commissions should use their Congressional mandate to provide a clear regulatory

[13] *Id.* at 29833.

[14] *Id.* at 29888 (proposed § 1.3(xxx)).

definition;[15] referring to CEA Section 1a(47) as revised by Dodd-Frank in the absence of clarifying regulatory text is not a helpful approach.

Forward / Nonfinancial Commodity Contracts

Dodd-Frank provides that a "sale of a nonfinancial commodity . . . for deferred shipment or delivery . . . [that] is intended to be physically settled" is not a swap.[16] COPE believes the Commission has properly found that such nonfinancial commodity contracts should be viewed as forward contracts not to be included in the definition of "swap" in Dodd-Frank. As stated by the Commission "the definition[] of the term[ ] 'swap' . . . do[es] not include forward contracts."[17] The Product Definition NOPR further finds that "[t]he CFTC believes that the forward contract exclusion in the Dodd-Frank Act with respect to nonfinancial commodities should be read consistently with . . . [the] historical understanding that a forward contract is a commercial merchandising transaction."[18] The Commission summarized its findings with respect to forward contracts as follows:

> [T]he CFTC believes that: (i) The forward contract exclusion from the swap definition with respect to nonfinancial commodities should be interpreted in a manner that is consistent with the CFTC's historical interpretation of the forward contract exclusion from the definition of the term 'future delivery'; (ii) intent to deliver is an essential element of a forward contract excluded from both the swap and future delivery definitions, and such intent in both instances should be evaluated based on the CFTC's established multi-factor approach; and (iii) book-out transactions in nonfinancial commodities that meet the requirements specified in the Brent Interpretation, and that are effectuated through a subsequent, separately negotiated agreement, should qualify for the forward exclusion from the swap definition.[19]

As noted above, COPE agrees with the Commission that nonfinancial commodity forward contracts are not swaps under Dodd-Frank. As such, COPE believes the Commissions' regulations should include an unambiguous provision which so states.[20] However, COPE

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[15] Dodd-Frank § 712(d)(1) ("[T]he Commodity Futures Trading Commission and the Securities and Exchange Commission . . . shall further define the term[ ] 'swap' . . . .").

[16] *Id.* at § 721(a)(21) (adding new CEA § 1a(47)(B)(ii)).

[17] Product Definition NOPR at 29827.

[18] *Id.* at 29828.

[19] *Id.* at 29829.

[20] Any final rules should make clear that although an instrument that qualifies as a forward contract is not a "swap" for these regulatory purposes, that would not preclude a "swap" from being characterized as a forward for other purposes, including under the Bankruptcy Code.

believes the Commissions should go further and make clear that all contracts for the sale of a non-financial commodity that require physical delivery should be clearly recognized by the Commissions as forward contracts.[21] As opposed to the application of a multi-part test, the nature of a contract should be determined by its terms. It must be clear that if a contract, judged within its four corners, is for the sale and delivery of a non-financial commodity, including all energy commodities, environmental attributes, emissions credits and other similar products or an option thereon which requires delivery, it is not a swap. Under the contracts used in the physical commodity world, a party can unilaterally determine to fail to deliver and choose to settle financially. There must not be any ambiguity on such a fundamental point. Of course, as recognized by the Commissions, transactions under such agreements can be booked-out at a later date if both parties agree and not render the contract a "swap."[22]

COPE believes that the CFTC's determination that the term "swap" does not include nonfinancial commodity forward contracts and that book-outs qualify for the forward contract exclusion are such material aspects of the regulatory determination of what is a "swap" under Dodd-Frank that these findings should be included in the regulatory text defining that term.[23]

Physical Options Are Forward Contracts

As COPE explained in comments filed in response to the CFTC's proposed rules regarding Commodity Options and Agricultural Swaps,[24] physically settling options should not be regulated as swaps.[25] The only difference between a physically settling option and a pure nonfinancial commodity forward contract is that with the former, the seller is not required to deliver the product unless the buyer exercises its option.[26] In effect, a physically settling

[21] These contracts include the EEI Master Power Purchase & Sale Agreement, NAESB Base Contract for Sale and Purchase of Natural Gas, Master Coal Purchase and Sale Agreement, and the ISDA Master Agreement with annexes, schedules, etc.

[22] *See* Product Definition NOPR at 29829.

[23] COPE understands that the Commissions' treatment of book-outs will not necessarily require a written agreement, consistent with industry practice.

[24] Commodity Options and Agricultural Swaps, 76 Fed. Reg. 6095 (Feb. 3, 2011) (the "Options NOPR").

[25] COPE Comments to Options NOPR at 3 (April 4, 2011).

[26] *See* Edison Electric Institute, *Master Power Purchase and Sales Agreement* (Apr. 25, 2000) at 9, in which "Option" is defined as "the right but not the obligation to purchase or sell a Product as specified in a Transaction" and "Product" is defined as "electric capacity, energy or other product(s) related thereto as specified in a Transaction by reference to a Product listed in Schedule P hereto or as otherwise specified by the Parties in the Transaction." Further, the agreement contemplates that all transaction are made pursuant to a FERC-jurisdictional tariff. *See Master Power Purchase and Sales Agreement* at Cover Sheet.

option is an option on a nonfinancial commodity forward contract. If exercised, physical delivery is required. Like a nonfinancial commodity forward contract, there is no ability for a party to unilaterally require a financial settlement.

As both are intended to settle by physical delivery, a physical option and a nonfinancial commodity forward contract should have the same regulatory treatment. That is, neither of them is a swap.

Contracts for the Sale of RECs and Emission Credits Are Nonfinancial Commodity Forward Contracts

The Commissions should affirmatively find that renewable energy credits ("RECs") are not swaps and are further exempt from regulation as swaps by the nonfinancial commodity forward contract exemption. RECs are products that account for the environmental benefits of certain types of electricity generation.[27] They are the product of the physical generation of electricity and are typically used by retail providers of electricity to meet state-mandated "portfolio standards" associated with the procurement of supply from environmentally preferred generation sources.[28]

Unlike swaps, RECs do not derive value from an underlying cash market. They are not derivatives but are instead cash market products. REC contracts are not satisfied with a cash payment; the REC itself must be delivered to the buyer. RECs are recorded, monitored and accounted for by entities that are recognized by the relevant regulatory authorities.[29] In these features, they are similar to the emissions allowances created by the Clean Air Act amendments, which are delivered to buyers who must hold sufficient allowances to meet their regulatory requirements, and which are recorded, monitored and accounted for on the Environmental Protection Agency registry.

Accordingly, contracts for the sale of RECs and emissions credits are non-financial commodity sales for immediate or deferred delivery which are intended to be physically settled. RECs and emissions credits are not swaps.

RTO/ISO Products Should Be Affirmatively Found Not To Be Swaps

The Commissions have proposed to avoid addressing the question of whether certain transactions in Regional Transmission Organizations ("RTO") and Independent System Operators ("ISO") are swaps.[30] Instead, the Product Definition NOPR indicates that "persons

[27] Jeremy D. Weinstein, *The ABA/EMA/ACORE Master Renewable Energy Certificate Trading Agreement*, (August 28, 2009).

[28] *Id.*

[29] NORTH AMERICAN RENEWABLES REGISTRY, http://narecs.com/index.htm (lasted visited Jul. 15, 2011).

[30] Product Definition NOPR at 29839.

with concerns about whether FERC-regulated products may be considered swaps (or futures) should request an exemption pursuant to section 722 of the Dodd-Frank Act."[31]

COPE respectfully submits that this approach will leave significant regulatory ambiguity for market participants. The Federal Energy Regulatory Commission ("FERC") already has complete authority over RTO/ISO markets. Section 722 of Dodd-Frank confirms that Dodd-Frank does not disturb that authority.[32] FERC is both the architect and front line regulator of these institutions and markets since, unlike CFTC-regulated exchanges, RTOs and ISOs do not have self-regulatory authority. Simply put, FERC created RTO/ISOs, intimately understands them and their products, and regulates them to ensure their rates and practices are just, reasonable and not unduly discriminatory. In addressing the jurisdictional issues between the CFTC and FERC, Congress clearly intended for the agencies to avoid duplicative and potentially conflicting regulation.[33] As FERC is the unitary regulator of RTO/ISO products, any additional regulation would be violative of this Congressional intent. As such, Congress expected the CFTC and FERC to provide for such an outcome in a Memorandum of Understanding ("MOU"), directing the agencies to work together to resolve "conflicts concerning overlapping jurisdiction" and avoid "conflicting or duplicative regulation."[34] The reasonable expectation of the content of such an MOU would be that RTO/ISO products would not be swaps.

The Commissions should therefore state affirmatively that RTO/ISO products are not swaps. Instead, they are integral elements of the wholesale physical electricity market regulated by FERC and cannot be divorced from FERC regulation of such markets. In fact, if the Commissions claimed jurisdiction over RTO/ISO products, it may be preferable for market participants if FERC were to find their inclusion in its jurisdictional markets to no longer be just and reasonable under the Federal Power Act. It is clear that these integrated electricity markets can only have one regulator and that regulator must be FERC.

There is no reason that the Commissions cannot find that, similar to the insurance contracts, consumer agreements, and commercial agreements it has addressed in the Product Definition NOPR, that RTO/ISO products are not swaps. Alternatively, the CFTC could enter into an MOU with FERC delineating jurisdiction to address the issue.

By proposing an exemptive process in the Product Definition NOPR, the Commissions will be scrutinizing FERC's regulation to determine if it is adequate for the CFTC to find that the

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[31] *Id.*

[32] Dodd-Frank § 722(e) (adding new § 2(a)(1)(I)(i) to the CEA).

[33] *Id.* ("Nothing in this Act shall limit or affect any statutory authority of [FERC] . . . with respect to an agreement, contract or transaction that is entered into pursuant to a tariff or rate schedule approved by [FERC] . . . and is . . . executed, traded or cleared on a registered entity or trading facility owner or operated by [an RTO/ISO].").

[34] *Id.* at § 720(a)(1).

public interest can be served if the CFTC exempts RTO/ISO products from Dodd-Frank. Implicit in this approach is the finding that certain RTO/ISO products are swaps. This implication amply demonstrates the importance of simply finding that RTO/ISO products are not swaps. If such a finding is not stated clearly in any final rule, market participants will be left with potentially debilitating uncertainty as to whether the CFTC will: (1) not grant an exemption for a given RTO/ISO transaction; (2) later revoke an existing exemption; (3) grant a partial or conditional exemption; or (4) limit an exemption to an existing product, requiring further future Commission action before a FERC-approved product can be found to meet a 'public interest' test.

Therefore, COPE requests that the Commissions definitively find that FERC-jurisdictional RTO/ISO products are not swaps. If the CFTC believes that there is ambiguity in Dodd-Frank on this point, it should enter into a MOU with FERC to bring the clarity to the market that the statute fails to bring.

The Anti-Evasion Provision Should Be Clarified

COPE understands that the Commissions have been charged with ensuring that market participants do not evade the requirements of Dodd-Frank without a legitimate business purpose or through fraud, deceit or unlawful activity.[35] COPE does not oppose the Commissions taking action to address such circumstances.

However, COPE believes that swaps markets under Dodd-Frank regulations will be more complex, burdensome and expensive than today's market. As a result, physical energy companies may migrate transactions now conducted in derivatives markets to physical markets. COPE requests that the CFTC make that clear movement away from swaps towards physical trades will not be considered evasion under the final rule. As such transactions would take the form of legitimate nonfinancial commodity forward contracts, no evasion of swap regulation would or could occur.

Conclusion

COPE respectfully requests that the Commissions clarify the Product Definition NOPR to include in the final regulations a clear definition of the term "swap," as well as provide in such regulations that nonfinancial forward contracts, physical commodity options, RECs and emissions credits are not swaps. The Commissions should also address RTO/ISO products and make clear that they are not swaps.

It is critical that the Commissions provide the requested clarity in the final regulations. The term "swap" should not be ambiguous under Dodd-Frank. The final regulations should make clear that the physical commodity products including options entered into by COPE members are not swaps. RTO/ISOs should not be subject to direct or indirect overlapping regulation.

[35] *See id.* at § 721(c) (directing the CFTC to further define terms including "swap" to "include transactions . . . that have been structured to evade" regulation under the statute).

The Commissions should take this opportunity to make the definition of "swap," this key element of the implementation of Dodd-Frank, as clear as possible.

Respectfully submitted,

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cc: COPE Members

APPENDIX – COPE RESPONSES TO SELECT QUESTIONS POSED IN PRODUCT DEFINITION NOPR

22. The Commissions request comment on all aspects of the proposed interpretive guidance set forth in this section regarding the forward contract exclusion from the swap and security based swap definitions with respect to nonfinancial commodities and securities.

As stated in COPE's comments, the Commissions should provide as much meaningful clarity as possible in the regulatory text and rely less upon interpretive guidance. For example, if the Commissions would affirmatively define a "Swap" as "a derivative agreement, contract or transaction intended to settle financially based upon the change in value of an underlying commodity," much less interpretive guidance would be required.

23. Is the proposed interpretive guidance set forth in this section sufficient with respect to the application of the forward contract exclusion from the swap definition with respect to nonfinancial commodities? If not, what changes should be made? Commenters also are invited to comment on whether the application of the Brent Interpretation generally, and its conclusions regarding book-outs in particular, is appropriate to the forward exclusion from the swap definition with respect to nonfinancial commodities. Would it permit transactions that should be subject to the swap regulatory regime to fall outside of the Dodd-Frank Act?

As a general matter the use of the existing forward contract exemption is very useful in defining the scope of the term "Swap." However, like the need for an affirmative definition of the term "Swap" in regulations, the regulations should provide that "an agreement, contract, or transaction for the sale of a nonfinancial commodity that is intended to be physically settled shall not be considered a swap."

24. Is it appropriate, in light of the Dodd-Frank Act, for the CFTC to withdraw the Energy Exemption while concurrently retaining the Brent Interpretation, and extending it to the forward contract exclusion from the definition of ''future delivery'' and the swap definition, for book-out transactions in all nonfinancial commodities? Why or why not? Is the conclusion that the Dodd-Frank Act supersedes the Swap Policy Statement appropriate? Why or why not?

The CFTC should codify in regulations that nonfinancial forward contracts are not swaps. In addition, it is appropriate for the CFTC to look to its precedent in either the Brent Interpretation or the Energy Exemption to help interpret issues that come up under the regulations. As Dodd-Frank creates a significant new regulatory regime, the CFTC should enact regulations and policies in the context of that regime. There should be no question that nonfinancial forward contracts are not swaps under Dodd-Frank.

25. Are there any provisions of the Energy Exemption or Swap Policy Statement that the Commissions should consider incorporating into the definitions rulemakings (other than the request already submitted by some commenters in response to the proposed Entity Definitions that the ''line of business'' provision of the Swap Policy Statement be incorporated into the definition of the term ''eligible contract participant'' (''ECP''))? If so, please explain in detail how such provisions are consistent with the requirements of the Dodd-Frank Act and would not

permit transactions that should be subject to the swap regulatory regime to fall outside of the Dodd-Frank Act.

See Response to Item 24 above.

26. How frequently do book-out transactions of the type described in the Brent Interpretation occur with respect to nonfinancial commodities? Please provide descriptions of any such transactions, and data with respect to their frequency. Are there any nonfinancial commodities or transactions to which the Brent Interpretation should not apply, either with respect to the forward contract exclusion from the definition of ''future delivery'' or the forward contract exclusion from the swap definition, or both? Why or why not?

As scheduling processes for forward agreements often occur well after the agreements are executed, parties which would otherwise deliver or receive can learn at that time that it may be more economic to book-out.

27. Should a minimum contract size for a transaction in a nonfinancial commodity (*e.g.*, a tanker full of Brent oil) be required in order for the transaction to qualify as a forward contract under the Brent Interpretation with respect to the future delivery and swap definitions? Why or why not? If so, what standards should apply to determine such a minimum contract size? Should the Brent Interpretation for nonfinancial commodities with respect to the future delivery and swap definitions be limited to market participants that meet certain requirements? Why or why not? If so, does the ''eligible commercial entity'' definition in CEA section 1a(17) 98 provide an appropriate requirement? Why or why not? What other requirements, if any, should be imposed?

Nonfinancial agreements which are intended to settle physically are not swaps. Congress did not impose any other requirements. The CFTC should not and cannot do differently.

28. How often, and to what extent, do entities that do not regularly make or take delivery of the commodity in the ordinary course of their business engage in transactions that should qualify as forward contracts? Should such contracts qualify for the safe harbor provided by the Brent Interpretation? Why or why not? If so, how can it be demonstrated that the primary purpose of such transaction is to acquire or sell the physical commodity? Would including these transactions in the scope of the Brent Interpretation permit transactions that should be subject to the swap regulatory regime to fall outside of the Dodd-Frank Act? If so, could this concern be addressed by imposing conditions in order to qualify for the forward exclusion? What conditions, if any, would be appropriate?

The obligations of a party under an agreement with respect to delivery are objectively ascertainable and can be drawn from within its four corners. If such an agreement requires delivery of a commodity and neither party can unilaterally settle otherwise, the contract is intended to settle physically. If such a contract was construed by a court, no evidence of intent would be permitted if the contract was clear on its face. In this case, the CFTC is not crafting an exemption. It is implementing a statue which provides that nonfinancial agreements which are intended to settle physically are not swaps.

29. Are ‘‘ring’’ or ‘‘daisy chain’’ markets for forward contracts, such as the 15-day Brent market, primarily used for commercial merchandising, or do they serve other purposes such as price discovery or risk management? Please explain in detail.

As physical delivery is required under the relevant agreements, they are used for merchandising. However, wherever there is liquidity there is price discovery.

30. Should contracts in nonfinancial commodities that may qualify as forward contracts be permitted to trade on registered trading platforms such as DCMs or swap execution facilities (‘‘SEFs’’)? If so, are additional guidance or rules necessary to determine whether contracts traded on such platforms are excluded from the CEA definition of ‘‘future delivery’’ and/or the swap definition? If so, please describe in detail such markets and explain what further guidance or rules would be appropriate? Should conditions be imposed with respect to the nature of the market participants or the percentage of transactions that must result in delivery over a specified measurement period, or both? If so, what conditions would be appropriate?

Physically delivered contracts may be traded on exchanges but not cleared. Such contracts are traded on the Intercontinental Exchange today. No regulatory action need be taken.

31. Should the Commissions provide guidance regarding the scope of the term ‘‘nonfinancial commodity’’ in the forward contract exclusion from the swap definition? If so, how and where should the Commissions draw the line between financial and nonfinancial commodities?

No. A nonfinancial commodity should be self-evidently a commodity that is itself not a financial product.

32. Should the forward contract exclusion from the swap definition apply to environmental commodities such as emissions allowances, carbon offsets/credits, or renewable energy certificates? If so, please describe these commodities, and explain how transactions can be physically settled where the commodity lacks a physical existence (or lacks a physical existence other than on paper)? Would application of the forward contract exclusion to such environmental commodities permit transactions that should be subject to the swap regulatory regime to fall outside the Dodd-Frank Act?

Yes. Such products are not financial in nature. They are either physical certificates or an account in a registry. Their value is in the environmental commodities themselves – not in a derivative cash market price. The certificates are either physically delivered or the seller instructs the registry to convey title to the buyer.

33. Are there other factors that should be considered in determining how to characterize forward contracts with embedded options with respect to nonfinancial commodities? If so, what factors should be considered? Do provisions in forward contracts with respect to nonfinancial commodities other than delivery and price contain embedded optionality? How do such provisions operate? Please provide a detailed analysis regarding how such provisions should be analyzed under the Dodd-Frank Act.

A nonfinancial forward commodity contract that, by its terms, is intended to settle physically should be permitted to contain optionality without being transformed into a swap unless such

optionality negates the physical settlement element of the contract. That is, if one party can exercise an option to settle the contract financially based upon the value change in an underlying cash market, then the physical settlement intention is not contained in the four corners of the contract. In such a case, the embedded option may render the contract a swap. Any other embedded option (for example, price, quantity, delivery point, delivery date, contract term) that does not permit a unilateral election of financial settlement based upon the value change in an underlying cash market should not affect the conclusion that the contract is not a swap.

34. Is the analysis of forward contracts with embedded options in the 1985 Interpretation and the CFTC's *Wright* decision appropriately applied to transactions entered into after the effective date of the Dodd-Frank Act? Why or why not? If not, how should the analysis be modified?

See response to Item 33 above.

35. How would the proposed interpretive guidance set forth in this section affect full requirements contracts, capacity contracts, reserve sharing agreements, tolling agreements, energy management agreements, and ancillary services? Do these agreements, contracts, or transactions have optionality as to delivery? If so, should they—or any other agreement, contract, or transaction in a nonfinancial commodity that has optionality as to delivery—be excluded from the swap definition? If so, please provide a detailed analysis of such agreements, contracts, or transactions and how they can be distinguished from options that are to be regulated as swaps pursuant to the Dodd-Frank Act. To what extent are any such agreements, contracts, or transactions in the electric industry regulated by the Federal Energy Regulatory Commission (''FERC''), State regulatory authorities, regional transmission organizations (''RTOs''), independent system operators (''ISOs'') or market monitoring units associated with RTOs or ISOs?

All nonfinancial options which, when exercised, results in physical settlement are not swaps. They are not derivative agreements, contracts or transactions intended to settle financially based upon the change in value of an underlying commodity, and if the regulations affirmatively state that these are not swaps, much less interpretive guidance would be required. For example, a tolling agreement is effectively a payment to the owner of a power plant to convert a customer's physical fuel into physical power. Such an agreement has no financial elements other than a fee for service. The same is true for other physical options – there is a fee for service or an option premium and exercise results in physical performance.

Many wholesale power and certain natural gas agreements with optionality are regulated by the FERC. RTO/ISOs are not regulatory bodies and do not regulate transactions. The same is true of market monitors.

36. Is there any issue with respect to the treatment of commodity options that the Commissions have not addressed and that should be addressed as a definitional matter in this rulemaking?

As noted above and in COPE's comments, the proposed regulations which address the definition of "Swap" must be revised to provide clarity not contained in the existing proposal.