



February 13, 2012

VIA ELECTRONIC SUBMISSION

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

Re: Comments on Interpretation Regarding Retail Commodity Transactions Under Commodity Exchange Act (RIN 3038-AD64)

Dear Mr. Stawick:

Constellation NewEnergy, Inc., Green Mountain Energy Company, Direct Energy Services, LLC, Exelon Energy Company, Reliant Energy Retail Holdings, LLC, Liberty Power Corporation, and Champion Energy Services, LLC (directly or through one or more affiliates, the “**Retail Suppliers**”) respectfully submit these comments in response to the Commodity Futures Trading Commission’s (the “**Commission**”) request for comment in connection with its proposed interpretation regarding Retail Commodity Transactions Under Commodity Exchange Act¹ (the “**Retail Commodity Transaction Interpretation**”), issued on December 14, 2011 pursuant to Section 742(a) of Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “**Dodd-Frank Act**”).²

Section 742(a) of the Dodd-Frank Act expands the Commission’s jurisdiction to include “retail commodity transactions” that are “entered into, or offered (even if not entered into), on a leveraged or margined basis, or financed by the offeror” with a person who is not an eligible contract participant or an eligible commercial entity.³ The statute also provides certain exemptions from the Commission’s expanded jurisdiction, including exempting transactions that “result[] in actual delivery within 28 days or such other longer period as the Commission may

¹ *Retail Commodity Transactions Under Commodity Exchange Act*, 76 Fed. Reg. 77670 (Dec. 14, 2011).

² Pub. L. No. 111-203 (2010).

³ CEA § 2c(2)(D).

determine.”⁴ Using a functional approach, the Commission issued the proposed interpretation to provide guidance as to how the Commission will assess whether any given transaction results in “actual delivery” within the meaning of the statute and to receive comment on whether its interpretation accurately construes the statutory language.⁵

The Retail Suppliers believe that the Commission should adopt a similar functional approach in its interpretation of the Commission’s expanded authority under Section 742(a) more generally. Specifically, we request that the Commission clarify that “retail commodity transactions” entered into on a “leveraged or margined basis, or financed by the offeror” (“**leverage contracts**”) do not include residential supply agreements for electricity or natural gas where the customer receives delivery of, and consumes, the commodity, but is billed 30 to 60 days later per the standard industry billing cycle (“**residential supply contracts**”).⁶

The Retail Suppliers, along with many other retail electric and gas suppliers, regularly enter into residential supply contracts under which we provide residential customers with either, or both, electricity or natural gas service. The mere fact that customers pay for the commodity *after* they have accepted delivery of and used the commodity should not transform these basic supply agreements into leverage contracts. As discussed in further detail below, these residential supply contracts are not the type of contracts Congress intended to authorize the Commission to regulate under Section 742(a). Residential supply contracts are not fraudulent “rolling spot contracts” seeking to evade the Commission’s jurisdiction over futures contracts, but rather are legitimate, industry-standard commodity supply agreements with residential customers.

I. Description of the Retail Suppliers’ Interest in the Interpretation.

The Retail Suppliers are leading providers of electricity or natural gas services to retail electric or natural gas customers in competitive markets. Our standard retail customer supply transactions supply full energy and capacity requirements to commercial, industrial, governmental, and residential customers.

While our residential supply agreements differ based upon the type of commodity we are providing, either electricity or natural gas, the basic form and function of the transactions are substantially the same. Typically, the residential customer would sign an electric or natural gas supply agreement under which the retail supplier agrees to sell, and the customer agrees to buy, the customer’s full requirements for residential power or natural gas service at the price and on

⁴ CEA § 2c(2)(D)(ii)(III)(aa).

⁵ 76 Fed. Reg. at 77671.

⁶ In the same regard, the Commission recently observed that consumer contracts “involving periodic or future purchases of consumer products and services, such as agreements to purchase energy commodities to heat or cool consumers’ homes” should not be regulated as swaps because they are “more akin to forward purchase agreements.” See Further Definition of “Swap,” “Security-Based Swap,” and “Security-Based Swap Agreement;” Mixed Swaps; Security-Based Swap Agreement Recordkeeping, 76 Fed. Reg. 29818, 29832 (May 23, 2011).

the terms and conditions specified in the contract for an initial term of 24 months. In addition to the price for power and energy service, the customer is also typically responsible for applicable taxes and certain fees (*e.g.*, tariffs) charged by the local utility.

The electricity or natural gas supply agreement specifies the date on which delivery will begin, which is dependent on when the local utility can process the customer's enrollment. The residential retail contract informs the customer that switching to one of the Retail Suppliers may take up to two billing cycles while the utility processes the customer's enrollment. Consequently, under residential supply agreements, there is frequently at least a 30 to 60 day delay between when the residential customer signs the supply agreement and when the commodity is first delivered to the customer. After the initiation of service, the Retail Suppliers continue to supply the residential customer throughout the term of the contract, billing the customer on either a 30 or 60 day billing cycle for the customer's prior month(s) electricity or natural gas usage.⁷

II. Congress Enacted Section 742(a) to Regulate Fraudulent “Rolling Spot Contracts” in Commodities with Retail Customers, Not to Regulate Legitimate Residential Supply Contracts.

As the Commission notes in its Retail Commodity Transaction Interpretation, Congress enacted Section 742(a) to extend the so-called “*Zelener* fraud fix” to retail commodity transactions.⁸ In *CFTC v. Zelener*, the Court held that certain speculative foreign currency transactions were “rolling spot contracts” outside of the Commission's jurisdiction despite the fact that the contracts functioned for all practical purposes like futures contracts.⁹ In so holding, the Court looked to the language of the contract itself, rather than the intent of the parties, to determine that the contracts at issue were spot contracts. In response to the *Zelener* case, Congress granted the Commission additional authority over certain retail foreign currency transactions in the CFTC Reauthorization Act of 2008.¹⁰ Subsequently, during its consideration of the Dodd-Frank Act, Congress enacted Section 742(a) to extend the Commission's jurisdiction over similar non-foreign currency retail commodity transactions. Senator Blanche Lincoln (D-AK) explained that Section 742(a) was enacted to extend the “*Zelener* fraud fix” to

⁷ Frequently the local utility will provide consolidated billing where the customer receives one monthly billing statement including both the utility's delivery charges and the Retail Suppliers' supply charges. The local utility then forwards the applicable payments to the Retail Supplier.

⁸ 76 Fed. Reg. at 77671.

⁹ *CFTC v. Zelener*, 373 F.3d 861 (7th Cir. 2004). In drawing the parallel to futures contracts, the Court noted that the defendants' customers never requested delivery of the currency and that offsetting transactions were always entered into.

¹⁰ Food, Conservation, and Energy Act of 2008, Pub. L No. 110-246 (2008).

other *Zelener*-type contracts in other commodities, such as energy and metals, to ensure that “rolling spot contracts” with retail customers could not evade the Commission’s jurisdiction.¹¹

Section 742(a) generally provides the Commission with jurisdiction over leverage contracts in any commodity entered into with retail customers. However, Section 742(a) excludes certain types of retail commodity transactions from the Commission’s new jurisdiction, including contracts that (1) result in actual delivery of the commodity within 28 days, or (2) create an enforceable obligation to deliver between a seller and buyer that have the ability to deliver and accept delivery, respectively, in connection with the line of business of the seller and buyer.¹² In creating these two exemptions, Congress recognized that these types of contracts were legitimate business transactions that should continue to be outside of the Commission’s jurisdiction.¹³

Because of the nature of the residential electric and gas industry, it is unclear whether residential supply contracts fall within the technical parameters of these narrow exceptions. As explained above, typically more than 28 days lapses between when the customer first enters into the residential supply contract and when delivery of the natural gas or electricity first begins.¹⁴ For residential customers, the delay is usually one to two months, but may be longer. For retail supply contracts with small commercial customers, the delay may be even longer.¹⁵ Indeed, retail supply contracts with small commercial customers are in most material respects the same as residential supply contracts. In both instances, the customer has the ability to accept delivery of the commodity, and there is actual delivery and consumption of the commodity. However, while the Retail Suppliers’ retail supply contracts with small commercial businesses, like our supply contracts with other commercial, industrial, and governmental entities, fall under the second exemption for transactions “in connection with the line of business of the seller and buyer” and consequently are not covered by the statute, there is less clarity for our residential retail contracts.

¹¹ 156 Cong. Rec. S5,924 (daily. ed. July 15, 2010).

¹² CEA § 2(c)(2)(D)(ii)(III)(aa)-(bb).

¹³ Senator Lincoln explained that these transactions were purposefully excluded from the Commission’s expanded jurisdiction, noting that “[C]ash or spot contracts, forward contracts, securities, and certain banking products are excluded from this provision in Section 742, just as they were excluded in the Farm Bill.” 156 Cong. Rec. S5,924 (daily. ed. July 15, 2010).

¹⁴ Although not the focus of these comments, the Retail Suppliers believe that the appropriate test for determining “actual delivery” is when physical delivery *commences* under a contract, not when delivery is *completed*. The examples used in the proposed Commission interpretation all involve completion of delivery within 28 days, which is not workable for many standard physical energy transactions. A standard retail commodity contract may require the supply of a commodity over a period of one to 10 years.

¹⁵ Small commercial businesses occasionally enter into retail supply contracts up to one-to-two years in advance of when they anticipate the need for delivery of the desired commodity. The Retail Suppliers recognize that the Commission has the discretion under the statute to establish a longer delivery period than 28 days for retail supply agreements. However, given the nature of the industry and the needs of small retail commercial customers, it may be impracticable to identify a delivery period that covers all legitimate retail customer supply transactions.

III. Residential Supply Agreements Are Not Leverage Contracts As Defined Under CEA Section 19 and Part 31 of the Commission's Regulations.

Since Congress first granted the Commission authority over certain leveraged retail foreign currency transactions in the CFTC Reauthorization Act of 2008, the Commission has not provided further guidance as to what constitutes a leveraged transaction.¹⁶ Accordingly, the Retail Suppliers look to the Commission's treatment of certain leverage transactions in precious metals under CEA Section 19 and the regulations thereunder for guidance. Similar to the fraudulent "rolling spot contracts" that Congress sought to regulate under Section 742(a), Congress subjected retail transactions in precious metals covered by Section 19 to heightened regulation due to their volatility and high degree of risk.¹⁷ Thus, the Commission's further definition of "leverage contract" under Commission Rule 31.4 provides some guidance as to how the Commission should interpret leverage contracts under its new authority over retail commodity transactions.

A. Residential Supply Agreements Are Substantially Different from Leverage Contracts Under CEA Section 19 and Part 31 of the Commission's Regulations.

Commission Rule 31.4(w) defines a "leverage contract" as "a contract, standardized as to terms and conditions, for the long-term (ten years or longer) purchase ("long leverage contract") or sale ("short leverage contract") by a leverage customer of a leverage commodity" which also provides for, among other things:

- Initial and maintenance margin payments by the leverage customer;
- Periodic payment by the leverage customer or accrual by the leverage transaction merchant of a variable carrying charge or fee on the unpaid balance of a long leverage contract, and periodic payment or crediting by the leverage transaction merchant to the leverage customer of a variable carrying charge or fee on the initial value of the contract plus any margin deposits made by the leverage customer in connection with a short leverage contract; and
- Delivery of the leverage commodity after satisfaction of the balance due on the contract.¹⁸

¹⁶ The Commission did not address its interpretation of what constitutes a leverage transaction in its regulations implementing its additional authority over retail foreign exchange transactions granted by the CFTC Reauthorization Act of 2008 and the Dodd-Frank Act. *See* Regulation of Off-Exchange Retail Foreign Exchange Transactions and Intermediaries, 75 Fed. Reg. 55410 (Sep. 10, 2010).

¹⁷ Commission Rule 31.11 (requiring disclosure to customers of the risks of leverage transactions).

¹⁸ Commission Rule 31.4(w).

Residential supply agreements do not satisfy the foregoing criteria identified by the Commission as necessary elements of a leverage contract under CEA Section 19. As a result, they should not be considered leverage contracts for purposes of Section 742(a).

1. Initial and Maintenance Margin Payments by the Leverage Customer.

Residential customers do not pay initial or maintenance margin on their customer accounts.¹⁹ In fact, the concept of margin is inapplicable to residential supply agreements. As described above, residential customers are not generally required to make any payment until the first invoice *following* their first one to two months of usage.

2. Periodic Payment by the Leverage Customer of a Variable Carrying Charge or Fee on the Unpaid Balance.

The pricing and payment provisions of a residential supply contract do not provide for the payment of “variable carrying charges” by the residential customer. “Variable carrying charges” are the “service and interest charges” that accumulate while a leverage contract remains open.²⁰ Residential customer accounts do not operate on margin. Consequently, residential customers do not owe “service and interest” charges on their accounts unless they fail to make full payment on their bill. Instead, the residential supply agreements provide that customers are responsible for paying the price of the commodity as established by the agreement and any additional fees and taxes, including any charges imposed by the local utility.

3. Delivery of the Leverage Commodity After Satisfaction of the Balance Due on the Contract.

Under residential supply agreements, the amount owed under the agreement is not due until *after* the customer has received delivery of, and used, the commodity. Consequently, residential supply agreements do not satisfy this third criteria of being a leverage contract. For this reason alone, residential supply contracts should not be treated as leverage contracts for purposes of Section 742(a).

¹⁹ Commission Rule 31.4(q) defines “initial leverage margin” as the “the amount of funds, excluding initial charges, which a leverage customer is required to deposit with a leverage transaction merchant when entering into a leverage contract.” Commission Rule 31.4(r) defines “maintenance leverage margin” as the “level to which the funds in a leverage customer's account must be restored after a margin call to the leverage customer has been effected by the leverage transaction merchant.”

²⁰ Commission Rule 31.4(l) defines “carrying charges for a leverage contract” to mean “all service and interest cha[r]ges paid periodically by a leverage customer to a leverage transaction merchant, or accrued by a leverage transaction merchant, while a long leverage contract remains open, or all service and interest charges paid periodically by a leverage transaction merchant to a leverage customer, or accrued by a leverage customer, while a short leverage contract remains open.”

IV. Conclusion.

The Retail Suppliers appreciate the opportunity to comment on the proposed Retail Commodity Transaction Interpretation. For all of the reasons discussed above, we request that the Commission interpret a “transaction entered into, or offered (even if not entered into), on a leveraged or margined basis, or financed by the offeror” to exclude the types of residential supply agreements that the Retail Suppliers, and other commercial energy companies, regularly execute. When Congress expanded the Commission’s authority over leveraged retail commodity transactions under Section 742(a), it did not intend to encompass the types of legitimate, residential supply agreements described above, where each party has the ability either to make or take delivery and the commodity is actually consumed prior to billing. Accordingly, the Retail Suppliers respectfully ask the Commission to clarify that such residential supply agreements are not leverage contracts within the meaning of the statute.

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

Respectfully submitted,



David O. Dardis
Chief Regulatory Counsel
Constellation Energy Group, Inc.
100 Constellation Way, Suite 1200C
Baltimore, MD 21202
Phone: (410) 470-3417
David.Dardis@constellation.com

/s/

Bridgett Neely
Sr. Advisor, Regulatory Affairs
Green Mountain Energy Company
300 West 6th Street
Austin, TX 78701
Phone: (917) 533-2250
bridgett.neely@greenmountain.com

/s/

Christopher C. O'Hara
NRG Energy, Inc.
General Counsel, Gulf Coast Region
General Counsel, Reliant
1201 Fannin Street, The Pavilions
Houston, Texas 77002
Phone: (713) 537-2245
chris.ohara@nrgenergy.com

/s/

Brenda Crockett
Vice President, Regulatory Affairs
Champion Energy Services, LLC
13831 NW Freeway, Ste. 250,
Houston, TX 77040
Phone: (281) 653-5071
bcrockett@championenergyservices.com

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/s/

Ronald M. Cerniglia
Director – National Advocacy
Governmental & Regulatory Affairs
Direct Energy Services, LLC
7240 Ryehill Drive
Cary, NC 27519
Phone: (919) 267-5503
Ron.Cerniglia@DirectEnergy.com

/s/

Harris M. Rosen, Esq.
Vice President and General Counsel
Liberty Power
1901 West Cypress Creek Road, Suite 600
Fort Lauderdale, FL 33309
Phone: (954) 598-7061
hrosen@libertypowercorp.com

/s/

Kathleen L. Barron
Vice President, Federal Regulatory Affairs
and Policy
Exelon Corporation
101 Constitution Avenue, N.W.
Suite 400 East
Washington DC 20001
Phone: (202) 637-0357
Kathleen.Barron@exeloncorp.com

cc: Honorable Gary Gensler, Chairman
Honorable Jill E. Sommers, Commissioner
Honorable Bart Chilton, Commissioner
Honorable Scott D. O'Malia, Commissioner
Honorable Mark P. Wetjen, Commissioner
Rosemary Hollinger, Regional Counsel, Division of Enforcement
Martin B. White, Assistant General Counsel, Office of the General Counsel