

June 29, 2012

Via Electronic Filing

David Stawick  
Secretary  
Commodity Futures Trading Commission  
Three Lafayette Centre  
1155 21st Street, NW  
Washington, DC 20581

Re: Aggregation, Position Limits for Futures and Swaps, RIN No. 3038-AD82

Dear Mr. Stawick:

By Notice of Proposed Rulemaking, published May 30, 2012, the Commodity Futures Trading Commission (“CFTC” or “the Commission”) proposed to revise its final rule on Position Limits for Futures and Swaps<sup>1</sup> by creating a more expansive exemption to the requirement that persons with a certain amount of equity ownership in common aggregate their positions for the purpose of compliance with CFTC position limits (the “Aggregation NOPR”).<sup>2</sup>

By this letter, the Coalition of Physical Energy Companies (“COPE”)<sup>3</sup> provides comments on the Aggregation NOPR. COPE members are physical energy companies in the business of producing, processing, and merchandizing energy commodities at retail and wholesale.

***The Aggregation NOPR Is A Welcome Step Towards Improving The Position Limits Rule, But More Needs to Be Done***

In the Aggregation NOPR, the Commission proposes to expand a person’s eligibility to be exempt from the aggregation requirement beyond the exemptions included in the Position Limits Final Rule if: (1) the person (i) owns more than ten percent but not more than fifty percent of the equity of another person; (ii) meets specified criteria establishing the separation of trading activities; (iii) files a notice with the Commission describing how the criteria is met; and (iv) provides a certification from a senior officer attesting to the accuracy

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<sup>1</sup> See *Position Limits for Futures and Swaps*, 76 Fed. Reg. 71626 (Final Rules), (Nov. 18, 2011) (the “Position Limits Final Rule”); 17 C.F.R. Part 151 *et seq.* (2012).

<sup>2</sup> *Aggregation, Position Limits for Futures and Swaps*, 77 Fed. Reg. 31767 (May 30, 2012).

<sup>3</sup> The members of the Coalition of Physical Energy Companies are: Apache Corporation; EP Energy LLC; 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.

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of the information provided; or (2) there is a reasonable risk that the person would be in violation of state or international law or regulations if it were to share information needed to aggregate positions, and an opinion of counsel is provided to that effect.<sup>4</sup>

COPE appreciates the Commission's decision to issue the Aggregation NOPR. By doing so, the Commission has taken an important step to address a significant flaw in the Position Limits Final Rule. COPE urges the Commission to not cease its efforts to remedy flaws in the Position Limits Final Rule with the Aggregation NOPR, but to instead take steps to correct other identified concerns with the Position Limits Final Rule such as the problematic definition of "Spot Month" and the overly limited set of enumerated Bona Fide hedges which are subject to outstanding petition requests.<sup>5</sup> The Commission should also provide compliance guidance with regard to the meaning of the Position Limits Final Rule components and how market participants are expected to comply with them, including the various associated forms.

The Position Limits Final Rule applies to a very broad and diverse set of market participants, ranging from sophisticated dealers to physically-oriented commercial firms like the members of COPE. Those market participants have received no compliance guidance beyond what is included in the Position Limits Final Rule itself. In contrast, the Commission's final rules on Large Trader Reporting for Physical Commodity Swaps,<sup>6</sup> which is applicable only to a sophisticated set of market participants, is the subject of a 172-page guidance manual that is now in its second edition.<sup>7</sup> If the Commission expects meaningful compliance with the Position Limits Final Rule, it is incumbent upon it to provide guidance and correct obvious flaws. The Aggregation NOPR can only be a first step in this process.

***COPE Generally Believes That The Proposed Separation Criteria Is Appropriate***

COPE generally supports the separation criteria proposed by the Commission, which are as follows:<sup>8</sup>

- (1) Any person with a 10 percent or greater ownership or equity interest in an owned entity need not aggregate the accounts or positions of the owned entity

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<sup>4</sup> See Aggregation NOPR at 31782 (proposed revisions to § 151.7).

<sup>5</sup> See Petition for Exemptive Relief for Certain *Bona Fide* Hedging Transactions of the Working Group of Commercial Energy Firms, filed January 20, 2012; Letter of the Coalition of Physical Energy Companies in Support of Working Group Petition, filed February 27, 2012.

<sup>6</sup> 76 Fed. Reg. 43851 (Final rules), (July 22, 2011); 17 C.F.R. Part 20, *et seq.*

<sup>7</sup> *Large Trader Reporting for Physical Commodity Swaps: Division of Market Oversight Guidebook for Part 20 Reports*, (Nov. 17, 2011)

<sup>8</sup> See Aggregation NOPR at 31782 (proposed §§ 151.7(b)(1)(i)(A)-(E)).

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with any other accounts or positions such person is required to aggregate, provided that:

(i) Such person, including any entity that such person must aggregate, and the owned entity:

(A) Do not have knowledge of the trading decisions of the other;

(B) Trade pursuant to separately developed and independent trading systems;

(C) Have and enforce written procedures to preclude each from having knowledge of, gaining access to, or receiving data about, trades of the other. Such procedures must include document routing and other procedures or security arrangements, including separate physical locations, which would maintain the independence of their activities;

(D) Do not share employees that control the trading decisions of either; and

(E) Do not have risk management systems that permit the sharing of trades or trading strategy; [and]

(ii) Such person does not have greater than a 50 percent ownership or equity interest in the owned entity[.]

These criteria, applied in a reasonable fashion, appear to establish an adequate basis to permit an exemption to aggregation.

However, COPE believes that one element of the criteria should be clarified and another revised to ensure a reasonable application. As such, COPE requests that the Commission clarify that (1) "knowledge of the trading decisions of the other" does not include information that is obtained as a counterparty; and (2) the requirement that trading systems must be "separately developed"<sup>9</sup> be deleted.

It is not usual for affiliated entities to be trading counterparties. In such cases, the entities interact on an arm arms-length basis, make their own trading decisions, and meet the other criteria proposed by the Commission. However, due to counterparty status, one entity can obtain knowledge of the trading decisions of the other entity. COPE does not believe the Commission intended that trading information obtained through transactions between the two entities sharing upstream equity ownership would disqualify them from eligibility for an exemption from aggregation. COPE requests that the Commission confirm its understanding and make clear that "knowledge of the trading decisions of the other" does not include knowledge obtained by virtue of acting as a counterparty.

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<sup>9</sup> *Id.* at proposed § 151.7(b)(1)(i)(A)-(B).

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Further, in COPE's experience, system development does not provide a vehicle for inappropriate information sharing. It is the data that is input into the system that matters, not the development of the system. A requirement that trading systems must be "separately developed" would require increased costs and create redundancy for market participants without any discernible regulatory purpose. Accordingly, COPE requests the Commission remove the separate development requirement from any final rule based on the Aggregation NOPR.

***An Aggregation Exemption Should Exist At Any Ownership Level If The Separation Criteria Is Met***

While COPE generally supports the proposed separation criteria, it believes that the Commission's proposed fifty percent equity limit for the exemption from the aggregation requirement in proposed § 151.7(b) is arbitrary and will require aggregation in circumstances where requisite separation exists and no trading/information overlap, nor is any information sharing present. In such cases, the entities which currently operate as separate and unconsolidated actors will be forced to aggregate their positions, causing unnecessary burdens and potential negative business impacts without providing the regulatory benefit of preventing excessive speculation by firms that are acting in concert or have access to each other's trading data.

A clear example of a circumstance that would be inappropriately excluded from eligibility for an aggregation exemption under the Aggregation NOPR is that of a limited partnership. A limited partnership contains a general partner and one or more limited partner(s). All control of the operations of a limited partnership resides with the general partner.<sup>10</sup> Accordingly, in a limited partnership structure, the limited partner does not manage or control the operations of the firm. Typically, at most, the limited partner has veto rights over a specific set of major actions such as the a sale of the partnership, the partnership's engaging in significant borrowing, or the initiation of a significant new business. The general partner manages the partnership and makes all operational decisions such as those associated with trading. Very often, a limited partner may hold more than fifty percent of the equity in the partnership.

A limited partnership is not the only type of legal entity in which a holder of over fifty percent equity can lack control or information sharing status. A limited liability company or a corporation can be structured with a member or class of equity effectively holding rights

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<sup>10</sup> See, e.g., 16 N.Y. Jur. 2d Business Relationships § 1946 ("General partners are vested exclusively with the management of the property and business of a limited partnership, and a sole general partner in a limited partnership must run, contract for, and otherwise manage the firm, and in fact is the only one who can act in its behalf.").

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similar to those of a limited partner.<sup>11</sup> In such cases, that owner of the affected class of equity would have limited involvement in the management of the firm.

In addition to the legal structures described above, holding companies with wholly owned-subsubsidiary businesses are often operated as completely separate and distinct businesses which operate apart from one another with completely independent management and no knowledge of the other's business or positions. These companies could be forced to implement costly and inefficient information sharing where none exists today solely to comply with the position limits rules, even if the Aggregation NOPR is adopted, and even though they could otherwise meet the Commission's separation criteria.

In the energy industry there are firms that: (1) operate in separate and distinct geographic regions; (2) are in different lines of business (large scale wholesale versus regional retail marketing); or (3) are in strategic partnerships that operate outside of the corporate group, any of which cause entities that have a common parent to operate separately but that still could meet the Commission's proposed separation criteria. If the criteria can be met at fifty-one percent or one hundred percent equity, the Commission's goal is met.

Accordingly, any entities that can satisfy the separation criteria and provide the requisite certification should be able to take advantage of the exemption to the aggregation requirements for position limits purposes. In other words, if the substantive elements are satisfied, the equity level should not matter.

***The Commission's Inclusion of State and International Law in the Exemption Is Appropriate***

As noted above, the Commission has proposed that if a firm reasonably believes that would be in violation of state or international law (in addition to federal law) and furnishes an opinion of counsel to that effect, the firm will be exempt from position limits aggregation.<sup>12</sup>

COPE supports the proposed expansion of the exemption to pick up state and international laws in addition to federal law. The proposed structure will permit COPE members to comply with the Commission's regulations while also complying with other applicable laws. COPE expects this provision will apply, at a minimum, to local gas distribution companies that are regulated on the state level.

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<sup>11</sup> The Federal Energy Regulatory Commission ("FERC"), for example, has found that owners of categories of passive equity in any legal entity with rights akin to a limited partner would similarly not be considered as affiliates for regulatory purposes. *See AES Creative Resources, et al.*, 129 FERC ¶ 61,239 (2009).

<sup>12</sup> Aggregation NOPR at 31782 (proposed § 151.7(i)).

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Very truly yours,

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