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July 23, 2012

Mr. David A. Stawick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st St NW
Washington, DC 20581

***RE: Interim Final Rule Excluding Swaps Entered Into For Hedging Physical Positions,* 17 CFT Part 1, RIN 3038-AD06, "Further Definition of 'Swap Dealer,' 'Security Based Swap Dealer,' 'Major Swap Participant,' Major Security-Based Swap Participant' and 'Eligible Contract Participant'" and 17 CFR 1.3 (ggg)(6)(iii)**

Dear Secretary Stawick:

In response to the request for comments in connection with the Interim Final Rule,[1] Energy Services Providers, Inc. ("ESPI") and U.S. Gas & Electric, Inc. ("USG&E", with ESPI, the "USG&E Companies") offer the following comments in support of the Interim Final Rule.

USG&E and ESPI are each retail energy marketers authorized in various state jurisdictions to provide electric energy and/or natural gas to commercial and residential end users (*i.e.,* customers), at either fixed or variable rates. Neither of the USG&E Companies is a financial entity whose primary business is dealing in swaps.

Swaps that are entered into for hedging physical positions or mitigating risks should not be considered in determining whether a person (*i.e,* company or other entity) is a Swap Dealer. Consistent with this approach, and *bona fide* hedging principles, the CFTC has adopted as an Interim Final Rule CFTC Regulation § 1.3(ggg)(6)(iii), which provides that a person will not be subject to the Swap Dealer analysis if all of the following five (5) conditions are met:

> (i) the person enters into the swap for the purpose of offsetting or mitigating the person's price risks that arise from the potential change in the value of one or several (a) assets that the person owns, produces, manufactures, processes, or merchandises or anticipates owning, producing, manufacturing, processing, or merchandising; (b) liabilities that the person owns or anticipates incurring; or (c)

[1] Further Definition of 'Swap Dealer,' 'Security Based Swap Dealer,' 'Major Swap Participant,' Major Security-Based Swap Participant' and 'Eligible Contract Participant,' 77 Fed. Reg. 30,596 (May 23, 2012).

services that the person provides, purchases, or anticipates providing or purchasing;
(ii) the swap represents a substitute for transactions made or to be made or positions taken or to be taken by the person at a later time in a physical marketing channel;
(iii) the swap is economically appropriate to the reduction of the person's risks in the conduct and management of a commercial enterprise;
(iv) the swap is entered into in accordance with sound commercial practices; and
(v) the person does not enter into the swap in connection with activity structured to evade designation as a swap dealer.[2]

USG&E Companies Seek Confirmation that Hedging Activities Typically Undertaken by Retail Energy Marketers to Hedge Commercial Risk Will Be Exempt from the Swap Dealer Definition Analysis

The Interim Final Rule generally provides an exclusion in the form of a safe harbor for swaps entered into for hedging physical positions ("Hedge Exclusion"). In the Interim Final Rule, the CFTC specifically distinguished "[e]ntering into swaps for the purpose of hedging one's own risks" against swap dealing as a "regular business".[3] Further, the Commission specifically stated, "entering into a swap for the purpose of hedging is inconsistent with swap dealing."[4] Consistent with the safe harbor contemplated by the Commission in the Interim Final Rule, the USG&E Companies use swaps to hedge the commercial risks associated with the physical delivery of natural gas or electricity to their retail residential and commercial customers.

Generally, retail energy marketers purchase electricity and/or natural gas several months in advance, based on anticipated customer demand. As with most retail energy marketers, the USG&E Companies use an electric or natural gas swap to hedge against the price risk associated with the underlying physical energy product. The USG&E Companies note that some retail energy marketers use a combination of both physical and financial products to manage price risk. In the interest of providing further guidance to the energy industry, the USG&E Companies request that the Commission confirm that the use of a combination of both physical and financial products would not increase an entity's likelihood of being classified as a Swap Dealer. As discussed in further detail below, retail energy marketers are not financial entities and are not dealers as contemplated in the legislative history of the Dodd-Frank legislation.

The price of energy typically and suddenly increases drastically if energy products (*e.g.,* oil, natural gas, etc.) are destroyed by a weather event or unavailable due to an international crisis. By utilizing financial and physical hedging products, each USG&E Company is able to provide energy and natural gas to its customers at consistently competitive prices. Hedging to manage price risk of energy products is a fundamental

[2] See 17 C.F.R. § 1.3(ggg)(6)(iii).
[3] 77 Fed. Reg. at 30,611, n.214.
[4] *Id.* at 30,611.

business practice for most retail energy marketers, such as ESPI and USG&E. In an effort to provide clarity to the energy industry, the USG&E Companies respectfully suggest that the Commission develop a list of examples of transactions that meet the Hedge Exclusion, and include as an example, typical hedging activity undertaken by retail energy marketers to protect themselves against price risk.[5]

Interim Final Rule is Consistent with Congressional Intent to Limit the Scope of the Swap Dealer Definition to Financial Entities that Engage in Swap Dealing in the Regular Course of Business

Members of Congress emphasized that it is important for the Commission to finalize the Swap Dealer definition in a manner that is not overly broad and that will not impose significant new regulations on entities Congress did not intend to be regulated as Swap Dealers. For example, in letter dated March 29, 2012 from Senators Stabenow and Lucas, state that "[w]e do remain concerned that the breadth of the proposed rule further defining "swap dealer" will result in the registration of many entities that Congress never intended to be regulated as dealers."[6] The Senators further explained "[i]t is important to note that the 'swap dealer' designation is not its singular means for overseeing entities in the Swap Market."[7] By providing a safe harbor for entities that engage in swaps to hedge physical positions, and otherwise mitigate commercial risk, the Interim Final Rule strikes the critical balance the Senators were referencing.

The Interim Final Rule provides that swap activity for hedging and mitigating commercial risks is not "swap dealing activity" that would bring an entity within the scope of the Swap Dealer definition. In fact, the Commission's discussion of the proposed definition distinguishes between "swap dealing activities" and "commercial activities". This approach is consistent with Congress' intended implementation of Dodd Frank.

Further, under the approach proposed, the Commission can focus on the market elements that pose the greatest amount of risk to the system – that is, financial entities that hedge as their regular course of business and not to mitigate commercial risks.

[5] Enumerated examples of hedge activity that meet the exclusion contemplated by the Interim Final Rule would provide desirable clarity to the energy industry. See, for example, the enumerated examples listed under 17 C.F.R. §151.5(a)(2) and Appendix B to Part 151 of the Commission's regulations. The USG&E Companies would be happy to assist the Commission in further drafting an example of typical hedging activity undertaken by retail energy marketers to protect themselves against price risk.

[6] Letter from Senator Debbie Stabenow, Chairwoman, Senate Committee on Agriculture, Nutrition and Forestry and Senator Frank D. Lucas, Chairman of the House Committee on Agriculture, to CFTC Chairman G. Gensler (March 29, 2012).

[7] *Id.*

Financial Risk Associated with the Energy Industry is Heavily Regulated by the Federal Energy Regulatory Commission & State Agencies

The activities of retail energy marketers are overseen and regulated by state public utility commissions, independent system operators/regional transmission organizations, ("ISO/RTOs") and/or the Federal Energy Regulatory Commission ("FERC"). As detailed in various comments submitted by FERC and the ISO/RTO, among other entities, there are a number of comprehensive credit and collateral requirements already in place that accomplish the objectives laid out in Dodd Frank. Requiring more would be duplicative, burdensome and extremely costly to entities in the energy sector, such as retail energy marketers.

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Please do not hesitate to contact me should you have any questions, or if you would like to further discuss the issues raised herein.

Very truly yours,

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CC: Hon. Gary Gensler, Chariman
Hon. Bart Chilton, Commissioner
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