DUKE ENERGY®

February 10, 2014

Ms. Melissa Jurgens, Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581
Telefacsimile: (202) 418-5521 and
Email to secretary@cftc.gov and electronically to http://comments.cftc.gov

Re: Joint Comments of the Duke Energy Utilities to the Commodity Futures Trading Commission's ("CFTC" or "Commission") Notice of Proposed Rulemaking ("NOPR") Regarding Position Limits for Derivatives, RIN 3038-AD99 pursuant to Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("DFA")

Dear Ms. Jurgens:

The Duke Energy Utilities respectfully submit the following comments in response to the Commission's request for public comment concerning the above-referenced NOPR.

I. Introduction.

The "Duke Energy Utilities" are the following six load serving electric utilities that provide electric service to millions of residential, commercial, and industrial customers in the Northeastern, Midwestern, and Southeastern United States: Duke Energy Carolinas, LLC, Duke Energy Progress, Inc., Duke Energy Florida, Inc., Duke Energy Indiana, Inc., Duke Energy Ohio, Inc., and Duke Energy Kentucky, Inc. The Duke Energy Utilities are hereby submitting these comments jointly.

As background, the Duke Energy Utilities are regulated electric service providers, each regulated by the public utility regulatory or public service commission ("PUCs") in its respective state(s) of operations, as well as the Federal Energy Regulatory Commission ("FERC") for wholesale electricity sales. The Duke Energy Utilities provide firm native load electric service, consisting of delivery and generation service, as applicable, to their retail electric customers at cost-based rates regulated by their respective PUCs. The PUCs determine the prudency of each respective utility's activities pursuant to applicable state laws and regulations. Additionally, the Duke Energy Utilities provide FERC-jurisdictional wholesale service at just and reasonable prices to other load serving entities, such as municipally owned and cooperatively owned electric utilities, which in turn provide retail service to their customers.

The Duke Energy Utilities reliably provide essential electric services to their customers, and own and operate distribution and transmission electric facilities and energy generating power plants, as applicable. Duke Energy Carolinas, LLC, Duke Energy Progress, Inc., and Duke Energy Florida, Inc. are balancing area authority operators in their service territories. Duke Energy Indiana, Inc., Duke Energy Kentucky, Inc., and Duke Energy Ohio, Inc. are members of regional transmission organizations that coordinate the movement of electricity through their service territories, as well as the Midwest and Northeast. The Duke Energy Utilities are not traders or speculators in the swaps marketplace. Duke Energy Utilities need stable and reliable access to the swaps markets to manage the commercial risk associated with their public utility functions and to provide least cost service to their customers.

The following comments discuss how some of the proposals in the NOPR have the effect of creating significant uncertainty as to the rules of the swaps marketplace, thereby reducing access to those markets for commercial end-users such as the Duke Energy Utilities, and in turn increasing the risks and costs of providing electric service. In submitting these comments, the Duke Energy Utilities respectfully request the Commission issue and implement rules that are consistent, straightforward to apply, and regulate market participants based upon the participant's purpose for participating in the marketplace (e.g., to hedge or speculate/make markets), proportionate to the level of risk that the participants may create or incur (e.g., systemic risk that the Commission should manage or mere transactional risk associated with commercial activity), and considering the costs and burdens of compliance.

Correspondence with respect to these comments should be directed to the following:

Bobby Singh
Associate General Counsel
Duke Energy Corporation
410 S. Wilmington Street, NCRH 20
Raleigh, North Carolina 27601
Email: bobby.singh@duke-energy.com
Phone: 919.546.6826
Fax: 919.546.2920

Teresa Reed
Senior Compliance Analyst
Duke Energy Corporation
Email: teresa.reed@duke-energy.com
Phone: 919.546.7859
Fax: 919.546.2169

II. <u>Comments on the Proposed Rule</u>.

1. <u>The Commission Should Implement a Consistent and Reasonable Definition of What Constitutes "Bona Fide Hedging"</u>.

In its NOPR, the CFTC provides the fifth - and the narrowest - definition of "hedging" in its DFA rulemakings. The Duke Energy Utilities have set forth the five definitions of "hedging" consisting of Proposed Rule 150.1; Rule 1.3(z); Rule 1.3(ggg)(6)(iii); Rule 1.3(kkk); and Rule 50.50, from the most narrow to the least narrow, from left to right, in the attached chart.

The Duke Energy Utilities are commercial end users. They access the swaps markets to hedge their commercial risks to prudently manage the costs of producing and delivering electricity to customers. *As commercial end users, the Duke Energy Utilities want to be able to hedge with reasonable certainty that they are not running afoul of position limits and the other DFA rules and regulations*. The Duke Energy Utilities do not want to become swaps dealers or be otherwise classified as swap market participants that are in the business of providing swaps, making markets as a commercial enterprise, or speculating. To do so, the Duke Energy Utilities need to be able to rely on clear and consistent rules and regulations. It seems to the Duke Energy Utilities that the purpose of position limits is, or should be, to control speculative activity, not to burden or complicate the markets for commercial end users.

For the reasons set forth in these comments, the Duke Energy Utilities respectfully encourage the Commission to:

(a) Provide and apply a single definition of hedging in Proposed Rule 150.1 that is the same as the definition in Rule 1.3(ggg)(6)(iii); and

(b) Entirely exempt from the position limits rules load serving entities, such as the Duke Energy Utilities, that are commercial end users.

Currently, the Duke Energy Utilities rely on Rule 1.3(ggg)(6)(iii) to enter into swap transactions exclusively for the purpose of hedging (and avoid being classified as a swap dealer). By proposing a new, and narrower, definition of hedging, the Commission has for all intents and purposes significantly narrowed what can be classified as a hedge. Inasmuch as the need for five different definitions of hedging is unclear, compliance-focused commercial end users, such as the Duke Energy Utilities, and their counsel and auditors, will seek to determine whether or not a transaction is a hedge based on the narrowest definition. Counsel who now rely upon their reading of the definition of hedging or mitigating commercial risk in Rule 1.3(ggg)(6)(iii) to determine that their clients are not swap dealers will have to identify whether or not a transaction is a hedge based on the overly narrow definition of hedging proposed with the position limits rules. The effect of this change will be to reduce hedging activity to avoid the consequence of being defined as a swap dealer and to avoid being required to meet the compliance burden and expense that goes with being a swap dealer.

The Duke Energy Utilities respectfully request the Commission to differentiate between market makers (speculators) and end users that are transacting for the sole purpose of mitigating risk. The market needs both market makers and hedging end users; but each has different incentives and purposes to participate in the swaps market. End users are using the market to reduce risk, while market makers are using the market to initiate a position that contains risk and uncertainty for the purpose of making a profit. Therefore, the rules of engagement with the market for a speculator should be different than for a hedger, who executes a transaction to "lay off" risk and to leave the rest to the market maker.

Utilities, such as the Duke Energy Utilities, are regulated by state and federal utility commissions, and have conducted their activities without disrupting markets for generations. Electric utilities have regulated rates of return and have no incentive to speculate, because the costs of imprudent speculative ventures are ultimately borne by shareholders. The positions the Duke Energy Utilities take in commodity and swap markets are for the benefit of their ratepayers, so that they may provide ratepayers with reliable and least cost electric service. For example, in North Carolina and South Carolina alone, Duke Energy Carolinas, LLC and Duke Energy Progress, Inc. can currently burn in excess of one billion cubic feet of natural gas a day to generate electricity. Duke Energy Carolinas, LLC and Duke Energy Progress, Inc. rely on financial hedging to manage price risk associated with this very volatile commodity. The Commission's rules should not limit the Duke Energy Utilities access to the financial hedging markets. Relying on fixed price contracts reduces procurement efficiencies while increasing commodity costs, credit risks and expenses, and counterparty risk.

Therefore, as noted above, the Duke Energy Utilities need access to *the financial hedging markets under clear and transparent rules, without the risk of unintentionally running afoul of regulations* designed to target and limit speculative behaviors. Hence, the Duke Energy Utilities respectfully encourage the Commission to: (a) provide and apply a single definition of hedging in Proposed Rule 150.1 that is the same as the definition in Rule 1.3(ggg)(6)(iii); and (b) entirely exempt from the position limits rules load serving entities, such as the Duke Energy Utilities, that are commercial end users.

2. The Commission's New "Duty of Care" for "Orderly Trading" Exposes Commercial End Users, such as the Duke Energy Utilities, to Transactional Uncertainty and Increased Litigation.

The Commission proposes that a "*position must be established and liquidated in an orderly manner* in accordance with sound commercial practices";[1] and that the "orderly trading requirement is intended to impose on bona fide hedgers *a duty of ordinary care when entering, maintaining and exiting the market* in the ordinary course of business and in order to avoid as practicable the potential for significant market impact in establishing, maintaining or liquidating *a position in excess of position limitations*."[2]

The Commission further states that it "believes that *negligent* trading, practices, or conduct should be a sufficient basis for the Commission *to disallow a bona fide hedge exemption*."[3]

The Commission goes on to say that "in fulfilling their *duty of ordinary care* when entering, maintaining and exiting a position, market participants should *assess market conditions and consider how* their trading practices and conduct affect the orderly execution of transactions when establishing, maintaining or liquidating a position in excess of a speculative limit."[4]

By this proposal the Commission has introduced "negligence" as the standard for compliance with the Commission's regulations based upon applying a "duty of ordinary care," which is an element of the tort of negligence determined based on an after-the-fact review of activities based upon a "knew or should have known standard".[5] In the view of the Duke Energy Utilities, regulations applicable to commercial end users should provide transparent standards to achieve compliance. Regulations should not be based on nebulous tort standards with a retroactive judgment of what "should have been known" about a complex and vast marketplace, particularly by commercial end users that are not in the business of swap markets. Further, for the Commission to discuss "negligent trading practices" in its rules and imply a "duty of ordinary care" owed, apparently to third parties in the marketplace, with respect to the "execution of transactions," seems to create a new private tort right of action that could be brought against a bona fide hedger by market participants or shareholder derivative litigants that pursue deep pockets. The Commission, not market participants, should oversee and regulate the

---

[1] 78 F.R. 75707 col. 1 (emphasis added).

[2] 78 F.R. 75707 col. 1-2 (emphasis added).

[3] 78 F.R. 75707 col. 2 (emphasis added).

[4] 78 F.R. 75707 col. 3 (emphasis added).

[5] *Palsgraf v. Long Island RR. Co,* 248 N.Y. 339, 162 N.E. 99 (N.Y. 1928).

market. The Duke Energy Utilities respectfully take the view that there appears to be no intent on the part of Congress to create private attorney general enforcement of any part of DFA. And, indeed, the Commission itself has pointed out that Congress gave it "exclusive" enforcement authority in these markets.[6]

This proposal imposes an unreasonable and unjust standard for commercial end users, such as the Duke Energy Utilities, to achieve. The proposal creates a requirement for market participants to measure the "significant market impact" of their activities in establishing, maintaining or liquidating positions. The Duke Energy Utilities are limited participants in the swaps market and do not monitor the market as speculators or to engage in arbitrage. Therefore, it is unreasonable to impose a standard that requires monitoring of the markets and retroactively measures the impact of establishing, maintaining or liquidating a position in the swaps marketplace. The proposed rule does not clearly define what is a "significant market impact" that must be avoided and thereby creates regulatory uncertainty. This is a standard that should be directed to swaps dealers and major swaps participants, not commercial end users.

The proposed rule further states that "the Commission believes that negligent trading, practices, or conduct should be a sufficient basis for the Commission to *disallow* a bona fide hedging exemption."[7] This proposal allows the Commission (and apparently a market participant through litigation) to impose or effectuate a retroactive disallowance for transactions that would otherwise meet the definition of a bona fide hedge, based on the hindsight application of an ordinary negligence standard and determination of what a commercial end user "should have known" about the impact of its activity on the swaps marketplace. Taking this further, a commercial end user, such as the Duke Energy Utilities, with large hedge positions because of the size of their operations and exposure to commodity markets, could retroactively trigger swap dealer status based on events that occurred after the positions were established. With respect to the Duke Energy Utilities, the current system of the market and accountability to shareholders and regulators already provides sufficient basis and incentive to act prudently, including when to enter into or exit swaps. Regulated utilities are disciplined by their own PUCs to act prudently, and such regulators would not allow recovery of losses from trading practices that the PUCs deemed imprudent. Retroactive disallowances of bona fide hedging protections impose unreasonable regulatory uncertainty; particularly for regulated utilities that are entering into swap positions for the benefit of ratepayers and to otherwise manage commercial risk associated with a commodities-intensive enterprise.

This proposed rule creates an unreasonable and unjust standard for commercial end users, such as the Duke Energy Utilities, to achieve. Accordingly, the Duke Energy Utilities

[6] 77 F.R. 52139.

[7] 78 F.R. 75707 col. 2.

respectfully encourage the Commission to exempt commercial end users, such as the Duke Energy Utilities, from the proposed "Duty of Care" and "Orderly Trading" requirements.

3. Trade Options Entered Into by Commercial End Users Should Be Exempt From the Position Limits Rules.

Trade options are primarily a mechanism to transfer ownership of physical commodities, rather than price risk. The Commission has itself noted that many trade options are hedges, and therefore, would not be counted towards the position limits.[8] The Commission also indicates in the NOPR[9] that physical forwards with embedded volumetric options, which operate solely to transfer the ownership of a physical commodity, are not the same as swaps.

As commercial end users, the Duke Energy Utilities use, and need to use, trade options to hedge risk associated with buying or selling physical commodities. As operators of physical assets, such as electric generating facilities, the Duke Energy Utilities need to able to manage the risks and the costs associated with volumetric fluctuations to serve load and to otherwise operate large commercial enterprises. End users engaging in transactions, and counsel advising them, need transparent rules to achieve compliance. It is impractical from a compliance view to use the various tests in the bona fide hedging definition to determine whether predominantly physically delivered transactions meet those tests. The proposed rule creates hindrances to the use of trade options necessary to manage risk, and therefore, should be exempted from position limits. The Duke Energy Utilities respectfully request the Commission to issue and implement rules that are straightforward to apply. Accordingly, the Duke Energy Utilities submit to the Commission that it should exempt trade options from position limits when one party to the trade option is a commercial end user, rather than requiring commercial end users to again demonstrate that the transaction is a bona fide hedge within the position limits requirements.

4. The Commission's Proposed Utility Hedging Exemption Should Be Broader to Comport With State Utility Regulation.

The Commission's "proposed new exemption would recognize a bona fide hedge position where a utility is *required or encouraged* to hedge by its public utility commission."[10]

---

[8] CFTC Trade Option FAQ fn. 29.

[9] 78 F.R. 75758 fn. 699 ("Derivative contracts – i.e., futures, options and swaps – may not transfer any ownership interest in the underlying commodity, but their prices are substantially derived from the value of the underlying commodity.").

[10] 78 F.R. 75713 col. 3 (emphasis added).

The Duke Energy Utilities appreciate and agree with the intent behind this proposal, and respectfully request that this exemption should be broadened to be consistent with how utilities are regulated by their state PUCs. Generally, PUCs do not "require or encourage" particular or specific commercial activity, rather they leave it to the utility to operate its business in a prudent manner and then disallow cost recovery for imprudent activity. Stated differently, PUCs may not "require" hedging, but rather regulate it after the fact as part of a general prudency and least cost review. For example, PUCs may (i) disallow recovery after the fact if a hedge is not deemed prudent; or (ii) disallow recovery after the fact because of a failure to hedge when a hedge might have been prudent. Adding to the complexity of abiding by the requirements of multiple regulators, PUCs may approve general risk management guidelines or may approve proscriptive risk management protocols, which "encourage" entities they regulate to be prudent, but generally don't engage in before-the-fact approval of transactions or other commercial activity in the marketplace. The burden of proof to show the CFTC that a PUC "required" or "encouraged" hedging may not be achievable under current PUC regulatory models. These models of PUC regulation are unlikely to be changed at the behest of Commission rules, and would still vary across different jurisdictions.

The Duke Energy Utilities do not speculate and do not have an incentive to speculate. The Duke Energy Utilities do not profit from the results of hedging activity, such as that associated with managing fuel costs (natural gas, oil, coal, and nuclear fuel), because the cost savings derived from hedging are passed on to customers in the form of lower rates. Therefore, a bona fide hedge should not be limited to those "where a utility is *required or encouraged* to hedge by its public utility commission."[11] Instead, the Duke Energy Utilities respectfully encourage the Commission to *expand this rule to exempt from the position limits requirements all of the hedging activities of load serving entities regulated by PUCs*, and to provide a single and reasonable definition of what activity constitutes hedging.

5. <u>The Proposed "Economically Appropriate" Rules Are Impracticable</u>.

While it is reasonable for the Commission to expect that bona fide hedge positions be "economically appropriate for the reduction of risk in the conduct of a commercial enterprise," the Commission is proposing the unworkable interpretation that "[i]n order for a position to be economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise, the enterprise generally should take into account all inventory or products that the enterprise owns or controls, or has contracted for purchase or sale at a fixed price."[12] This requires market participants to hedge risks on an aggregate, enterprise-wide basis, which would mean the hedges of specific risks in isolation of the whole enterprise would not generally

[11] 78 F.R. 75713 col. 3 (emphasis added).

[12] 78 F.R. 75709 col. 3.

be considered "economically appropriate" under the NOPR. This approach is not practical and, if implemented, would impede risk mitigation activities.

Requiring an entity to hedge on an aggregate, enterprise-wide basis does not account for other regulatory requirements imposed by states and the operational complexities of the utility industry. The Duke Energy Utilities are regulated by separate and independent PUCs depending upon the state or states in which the utility operates. Duke Energy Progress, Inc. and Duke Energy Carolinas, LLC, are, for example, regulated by the North Carolina Utilities Commission and by the Public Service Commission of South Carolina, and each separate regulatory commission has its own rules and regulations applicable to its respective jurisdiction. Each of these operating utilities has separate tariffs and operating requirements. Further, each utility has separately owned assets and generating facilities located across a state and in different states that cannot, and should not, be aggregated on an enterprise-wide basis.

For example, each generating facility operated by a utility is different and has a different operating environment and dispatch characteristics, even among facilities that are gas-fired or coal-fired. Each natural gas generating facility is being dispatched differently and has different transmission and fuel-availability challenges. An electric utility should be able to hedge fuel supply in a manner that reflects the physical characteristics of its generating fleet and the regulatory environment in which it operates. It should be able to hedge its fuel supply to support its generation needs, and should not be required to take into account fuel purchases and consumption by plant. Applying the proposed enterprise-wide rule will require an electric utility to move a new "long" gas position that develops at a generator with a forced outage to another operating gas generator before it could hedge the operating unit's new "short" gas position. There could be pipeline and other transmission constraints between the plants, and such an exercise would impact operational efficiency and reliability, in order to enable hedging. Having to take such actions as a prerequisite to hedging would create risks and increase costs.

As a general principle, being required to hedge across plants in a fleet that may include a commodities-intensive portfolio of natural gas, coal, oil, nuclear fuels, and/or reach across different regulatory jurisdictions could be so fundamentally complicated and unworkable as to require utilities to eschew hedging altogether, or to otherwise reduce hedging and forego risk mitigation, or to hedge through other inefficient practices, all to the detriment of ratepayers. This is particularly important for utilities regulated by PUC-specific and FERC-specific standards of conduct, codes of conduct, and affiliate restrictions,[13] which require, for example, the independent functioning of regulated businesses, and prevent the sharing of certain types of information between a utility's operating functions and businesses. With such limitations on information sharing, it is unclear how a regulated entity could properly verify whether a hedge or offsetting position is present in another business unit or function. A total enterprise-wide

[13] See, e.g., 73 FR 63829, October 27, 2008.

hedging requirement could effectively precondition and, therefore, effectively prohibit, bona fide hedging dependent on certain types of impermissible information sharing.

Therefore, the Duke Energy Utilities respectfully submit that the proposed "Economically Appropriate" rules are impracticable with respect to the hedging and risk mitigation needs of load serving commercial end users, such as the Duke Energy Utilities, and should not apply to load serving commercial end users, such as the Duke Energy Utilities.

III. <u>Conclusion.</u>

The Duke Energy Utilities respectfully appreciate the opportunity to provide the foregoing comments and information to the Commission. Please contact us as indicated above if you would like to discuss any of the above comments.

Yours truly,

On Behalf of:
Duke Energy Carolinas, LLC
Duke Energy Progress, Inc.
Duke Energy Florida, Inc.
Duke Energy Indiana, Inc.
Duke Energy Ohio, Inc.
Duke Energy Kentucky, Inc.

By: *<u>/s/ Bobby Singh</u>*
Associate General Counsel
Duke Energy Corporation

DUKE ENERGY UTILITIES

"HEDGING" DEFINITIONS IN COMMODITY FUTURES TRADING COMMISSION (CFTC) REGULATIONS

MOST NARROW **LEAST NARROW**

<u>Proposed</u> Rule 150.1	**Rule 1.3(z)**	**Rule 1.3(ggg)(6)(iii)**	**Rule 1.3(kkk)**	**Rule 50.50**
Defines "bona fide hedging" transactions that are exempt from position limits for Referenced Contracts.	Defines "hedging" transactions for position limits on excluded commodity transactions.	Excluding swaps, entered into for hedging physical positions, from "swap dealer" determinations.	Defines "hedging or mitigating commercial risk" for "major swap participant" regulation.	"Hedging or mitigating commercial risk" for the end-user exception from mandatory clearing regulation.
any position whose purpose is to offset price risks incidental to commercial cash, spot, or forward operations, and such position is established and liquidated in an orderly manner in accordance with sound commercial practices, *provided that:* (1) … For a position in commodity derivative contracts in an excluded commodity …: (i) Such position is economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise; **<u>and</u>** (ii)(A) Is enumerated in paragraph (3), (4) or (5) of this definition; or (B) Such position is recognized as a bona fide hedging position by the designated contract market or swap execution facility that is a trading facility, pursuant to such market's rules submitted to the Commission, which rules may include risk management exemptions consistent with Appendix A of this part; and	any agreement, contract or transaction in an excluded commodity on a designated contract market or swap execution facility that is a trading facility, where such transactions or positions normally represent a substitute for transactions to be made or positions to be taken at a later time in a physical marketing channel, and where they are economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise, and where they arise from: (i) The potential change in the value of assets which a person owns, produces, manufactures, processes, or merchandises or anticipates owning, producing, manufacturing, processing, or merchandising, (ii) The potential change in the value of liabilities which a person owns or anticipates incurring, **<u>or</u>** (iii) The potential change in the value of services which a person provides, purchases, or anticipates providing or purchasing.	In determining whether a person is a swap dealer, a swap that the person enters into shall not be considered, if: (A) 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— (*1*) Assets that the person owns, produces, manufactures, processes, or merchandises or anticipates owning, producing, manufacturing, processing, or merchandising; (*2*) Liabilities that the person owns or anticipates incurring; **<u>or</u>** (*3*) Services that the person provides, purchases, or anticipates providing or purchasing; (B) 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; (C) The swap is economically	a swap position is held for the purpose of hedging or mitigating commercial risk when: (1) Such position: (i) Is economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise (or of a majority-owned affiliate of the enterprise), where the risks arise from: (A) The potential change in the value of assets that a person owns, produces, manufactures, processes, or merchandises or reasonably anticipates owning, producing, manufacturing, processing, or merchandising in the ordinary course of business of the enterprise; (B) The potential change in the value of liabilities that a person has incurred or reasonably anticipates incurring in the ordinary course of business of the enterprise; or (C) The potential change in the value of services that a person provides,	a swap is used to hedge or mitigate commercial risk if: (1) Such swap: (i) Is economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise, where the risks arise from: (A) The potential change in the value of assets that a person owns, produces, manufactures, processes, or merchandises or reasonably anticipates owning, producing, manufacturing, processing, or merchandising in the ordinary course of business of the enterprise; (B) The potential change in the value of liabilities that a person has incurred or reasonably anticipates incurring in the ordinary course of business of the enterprise; (C) The potential change in the value of services that a person provides, purchases, or reasonably anticipates providing or purchasing in the ordinary course of business of the

MOST NARROW **LEAST NARROW**

<u>Proposed</u> Rule 150.1	Rule 1.3(z)	Rule 1.3(ggg)(6)(iii)	Rule 1.3(kkk)	Rule 50.50
Defines "bona fide hedging" transactions that are exempt from position limits for Referenced Contracts.	Defines "hedging" transactions for position limits on excluded commodity transactions.	Excluding swaps, entered into for hedging physical positions, from "swap dealer" determinations.	Defines "hedging or mitigating commercial risk" for "major swap participant" regulation.	"Hedging or mitigating commercial risk" for the end-user exception from mandatory clearing regulation.
(2) … For a position in commodity derivative contracts in a physical commodity: (i) Such position: (A) Represents a substitute for transactions made or to be made, or positions taken or to be taken, at a later time in a physical marketing channel; (B) Is economically appropriate to the reduction of risks in the conduct and management of a commercial enterprise; (C) Arises from the potential change in the value of— (*1*) Assets which a person owns, produces, manufactures, processes, or merchandises or anticipates owning, producing, manufacturing, processing, or merchandising; (*2*) Liabilities which a person owes or anticipates incurring; **<u>or</u>** (3) Services that a person provides, purchases, or anticipates providing or purchasing; **<u>and</u>**	(iv) Notwithstanding the foregoing, no transactions or positions shall be classified as bona fide hedging unless their purpose is to offset price risks incidental to commercial cash or spot operations and such positions are established and liquidated in an orderly manner in accordance with sound commercial practices and, for transactions or positions on contract markets subject to trading and position limits in effect pursuant to section 4a of the Act, unless the provisions of paragraphs (z)(2) and (3) of this section have been satisfied. The definitions… includes, but is not limited to, the following specific transactions and positions: (i) Sales of any agreement, contract, or transaction in an excluded commodity on a designated contract market or swap execution facility that is a trading facility which do not exceed in quantity: (A) Ownership or fixed-price purchase of the same cash commodity by the same person;	appropriate to the reduction of the person's risks in the conduct and management of a commercial enterprise; (D) The swap is entered into in accordance with sound commercial practices; **<u>and</u>** (E) The person does not enter into the swap in connection with activity structured to evade designation as a swap dealer.	purchases, or reasonably anticipates providing or purchasing in the ordinary course of business of the enterprise; (D) The potential change in the value of assets, services, inputs, products, or commodities that a person owns, produces, manufactures, processes, merchandises, leases, or sells, or reasonably anticipates owning, producing, manufacturing, processing, merchandising, leasing, or selling in the ordinary course of business of the enterprise; (E) Any potential change in value related to any of the foregoing arising from interest, currency, or foreign exchange rate movements associated with such assets, liabilities, services, inputs, products, or commodities; <u>or</u> (F) Any fluctuation in interest, currency, or foreign exchange rate exposures arising from a person's current or anticipated assets or liabilities; **<u>or</u>** (ii) Qualifies as bona fide hedging for purposes of an exemption from position limits under the Act; **<u>or</u>**	enterprise; (D) The potential change in the value of assets, services, inputs, products, or commodities that a person owns, produces, manufactures, processes, merchandises, leases, or sells, or reasonably anticipates owning, producing, manufacturing, processing, merchandising, leasing, or selling in the ordinary course of business of the enterprise; (E) Any potential change in value related to any of the foregoing arising from interest, currency, or foreign exchange rate movements associated with such assets, liabilities, services, inputs, products, or commodities; **<u>or</u>** (F) Any fluctuation in interest, currency, or foreign exchange rate exposures arising from a person's current or anticipated assets or liabilities; **<u>or</u>** (ii) Qualifies as bona fide hedging for purposes of an exemption from position limits under the Act; **<u>or</u>** (iii) Qualifies for hedging treatment under:

MOST NARROW **LEAST NARROW**

<u>Proposed</u> Rule 150.1	Rule 1.3(z)	Rule 1.3(ggg)(6)(iii)	Rule 1.3(kkk)	Rule 50.50
Defines “bona fide hedging” transactions that are exempt from position limits for Referenced Contracts.	Defines “hedging” transactions for position limits on excluded commodity transactions.	Excluding swaps, entered into for hedging physical positions, from “swap dealer” determinations.	Defines “hedging or mitigating commercial risk” for “major swap participant” regulation.	“Hedging or mitigating commercial risk” for the end-user exception from mandatory clearing regulation.
(D) Is enumerated in paragraph (3), (4) or (5) of this definition; or (ii)(A) ...Such position reduces risks attendant to a position resulting from a swap in the same physical commodity that was executed opposite a counterparty for which the position at the time of the transaction would qualify as a bona fide hedging position pursuant to paragraph (2)(i) of this definition (a pass-through swap counterparty), *provided that* no such risk-reducing position is maintained in any physical-delivery commodity derivative contract during the lesser of the last five days of trading or the time period for the spot month in such physical-delivery commodity derivative contract; **<u>and</u>** (B) … Such swap position was executed opposite a passthrough swap counterparty and to the extent such swap position has been offset pursuant to paragraph (2)(ii)(A) of this definition. (3) … A bona fide hedging position includes any of the following specific positions:	and (B) Twelve months’ unsold anticipated production of the same commodity by the same person provided that no such position is maintained in any agreement, contract or transaction during the five last trading days. (ii) Purchases of any agreement, contract or transaction in an excluded commodity on a designated contract market or swap execution facility that is a trading facility which do not exceed in quantity: (A) The fixed-price sale of the same cash commodity by the same person; (B) The quantity equivalent of fixedprice sales of the cash products and byproducts of such commodity by the same person; and (C) Twelve months’ unfilled anticipated requirements of the same cash commodity for processing, manufacturing, or		(iii) Qualifies for hedging treatment under: (A) Financial Accounting Standards Board Accounting Standards Codification Topic 815, Derivatives and Hedging (formerly known as Statement No. 133); **<u>or</u>** (B) Governmental Accounting Standards Board Statement 53, Accounting and Financial Reporting for Derivative Instruments; **<u>and</u>** (2) Such position is: (i) Not held for a purpose that is in the nature of speculation, investing or trading; **<u>and</u>** (ii) Not held to hedge or mitigate the risk of another swap or security-based swap position, unless that other position itself is held for the purpose of hedging or mitigating commercial risk as defined by this rule or § 240.3a67–4 of this title..	(A) Financial Accounting Standards Board Accounting Standards Codification Topic 815, Derivatives and Hedging (formerly known as Statement No. 133); **<u>or</u>** (B) Governmental Accounting Standards Board Statement 53, Accounting and Financial Reporting for Derivative Instruments; **<u>and</u>** (2) Such swap is: (i) Not used for a purpose that is in the nature of speculation, investing, or trading; and (ii) Not used to hedge or mitigate the risk of another swap or security-based swap position, unless that other position itself is used to hedge or mitigate commercial risk as defined by this rule or § 240.3a67–4 of this title.

MOST NARROW **LEAST NARROW**

<u>Proposed</u> Rule 150.1	Rule 1.3(z)	Rule 1.3(ggg)(6)(iii)	Rule 1.3(kkk)	Rule 50.50
Defines “bona fide hedging” transactions that are exempt from position limits for Referenced Contracts.	Defines “hedging” transactions for position limits on excluded commodity transactions.	Excluding swaps, entered into for hedging physical positions, from “swap dealer” determinations.	Defines “hedging or mitigating commercial risk” for “major swap participant” regulation.	“Hedging or mitigating commercial risk” for the end-user exception from mandatory clearing regulation.
(i) *Hedges of inventory and cash commodity purchase contracts.* Short positions in commodity derivative contracts that do not exceed in quantity ownership or fixed-price purchase contracts in the contract’s underlying cash commodity by the same person. (ii) *Hedges of cash commodity sales contracts.* Long positions in commodity derivative contracts that do not exceed in quantity the fixed-price sales contracts in the contract’s underlying cash commodity by the same person and the quantity equivalent of fixed-price sales contracts of the cash products and by-products of such commodity by the same person. (iii) *Hedges of unfilled anticipated requirements. Provided that* such positions in a physical-delivery commodity derivative contract, during the lesser of the last five days of trading or the time period for the spot month in such physical-delivery contract, do not exceed the person’s unfilled anticipated requirements of the same cash commodity for that month and for the next succeeding month:	feeding by the same person, provided that such transactions and positions in the five last trading days of any agreement, contract or transaction do not exceed the person’s unfilled anticipated requirements of the same cash commodity for that month and for the next succeeding month. (iii) Offsetting sales and purchases in any agreement, contract or transaction in an excluded commodity on a designated contract market or swap execution facility that is a trading facility which do not exceed in quantity that amount of the same cash commodity which has been bought and sold by the same person at unfixed prices basis different delivery months of the contract market, provided that no such position is maintained in any agreement, contract or transaction during the five last trading days. (iv) Purchases or sales by an agent who does not own or has not contracted to sell or purchase the offsetting cash commodity at a fixed			

MOST NARROW **LEAST NARROW**

Proposed Rule 150.1	Rule 1.3(z)	Rule 1.3(ggg)(6)(iii)	Rule 1.3(kkk)	Rule 50.50
Defines “bona fide hedging” transactions that are exempt from position limits for Referenced Contracts.	Defines “hedging” transactions for position limits on excluded commodity transactions.	Excluding swaps, entered into for hedging physical positions, from “swap dealer” determinations.	Defines “hedging or mitigating commercial risk” for “major swap participant” regulation.	“Hedging or mitigating commercial risk” for the end-user exception from mandatory clearing regulation.
(A) Long positions in commodity derivative contracts that do not exceed in quantity unfilled anticipated requirements of the same cash commodity, and that do not exceed twelve months for an agricultural commodity, for processing, manufacturing, or use by the same person; and (B) Long positions in commodity derivative contracts that do not exceed in quantity unfilled anticipated requirements of the same cash commodity for resale by a utility that is required or encouraged to hedge by its public utility commission on behalf of its customers’ anticipated use. (iv) *Hedges by agents.* Long or short positions in commodity derivative contracts by an agent who does not own or has not contracted to sell or purchase the offsetting cash commodity at a fixed price, *provided that* the agent is responsible for merchandising the cash positions that are being offset in commodity derivative contracts and the agent has a contractual arrangement with the	price, provided that the agent is responsible for the merchandising of the cash position that is being offset, and the agent has a contractual arrangement with the person who owns the commodity or has the cash market commitment being offset. (v) Sales and purchases described in [(i) through (iv) above] may also be offset other than by the same quantity of the same cash commodity, provided that the fluctuations in value of the position for in any agreement, contract or transaction are substantially related to the fluctuations in value of the actual or anticipated cash position, and provided that the positions in any agreement, contract or transaction shall not be maintained during the five last trading days. (3) *Non-Enumerated cases.* A designated contract market or swap execution facility that is a trading facility may recognize, consistent with the purposes of this section, transactions and positions other than those enumerated in paragraph (2) of this section as bona fide hedging. Prior			

MOST NARROW **LEAST NARROW**

Proposed Rule 150.1	Rule 1.3(z)	Rule 1.3(ggg)(6)(iii)	Rule 1.3(kkk)	Rule 50.50
Defines "bona fide hedging" transactions that are exempt from position limits for Referenced Contracts.	Defines "hedging" transactions for position limits on excluded commodity transactions.	Excluding swaps, entered into for hedging physical positions, from "swap dealer" determinations.	Defines "hedging or mitigating commercial risk" for "major swap participant" regulation.	"Hedging or mitigating commercial risk" for the end-user exception from mandatory clearing regulation.
person who owns the commodity or holds the cash market commitment being offset. (4) … A bona fide hedging position also includes the following specific positions, *provided that* no such position is maintained in any physical delivery commodity derivative contract during the lesser of the last five days of trading or the time period for the spot month in such physical-delivery contract: (i) *Hedges of unsold anticipated production.* Short positions in commodity derivative contracts that do not exceed in quantity unsold anticipated production of the same commodity, and that do not exceed twelve months of production for an agricultural commodity, by the same person. (ii) *Hedges of offsetting unfixed-price cash commodity sales and purchases.* Short and long positions in commodity derivative contracts that do not exceed in quantity that amount of the same cash commodity that has been bought and sold by the same person at unfixed prices:	to recognizing such non-enumerated transactions and positions, the designated contract market or swap execution facility that is a trading facility shall submit such rules for Commission review under section 5c of the Act and part 40 of this chapter.			

MOST NARROW **LEAST NARROW**

<u>Proposed</u> Rule 150.1	**Rule 1.3(z)**	**Rule 1.3(ggg)(6)(iii)**	**Rule 1.3(kkk)**	**Rule 50.50**
Defines "bona fide hedging" transactions that are exempt from position limits for Referenced Contracts.	Defines "hedging" transactions for position limits on excluded commodity transactions.	Excluding swaps, entered into for hedging physical positions, from "swap dealer" determinations.	Defines "hedging or mitigating commercial risk" for "major swap participant" regulation.	"Hedging or mitigating commercial risk" for the end-user exception from mandatory clearing regulation.
(A) Basis different delivery months in the same commodity derivative contract; or (B) Basis different commodity derivative contracts in the same commodity, regardless of whether the commodity derivative contracts are in the same calendar month. (iii) *Hedges of anticipated royalties.* Short positions in commodity derivative contracts offset by the anticipated change in value of mineral royalty rights that are owned by the same person, *provided that* the royalty rights arise out of the production of the commodity underlying the commodity derivative contract. (iv) *Hedges of services.* Short or long positions in commodity derivative contracts offset by the anticipated change in value of receipts or payments due or expected to be due under an executed contract for services held by the same person, *provided that* the contract for services arises out of the production, manufacturing, processing, use, or transportation of the commodity underlying the commodity derivative contract, and which may not				

MOST NARROW **LEAST NARROW**

Proposed Rule 150.1	**Rule 1.3(z)**	**Rule 1.3(ggg)(6)(iii)**	**Rule 1.3(kkk)**	**Rule 50.50**
Defines "bona fide hedging" transactions that are exempt from position limits for Referenced Contracts.	Defines "hedging" transactions for position limits on excluded commodity transactions.	Excluding swaps, entered into for hedging physical positions, from "swap dealer" determinations.	Defines "hedging or mitigating commercial risk" for "major swap participant" regulation.	"Hedging or mitigating commercial risk" for the end-user exception from mandatory clearing regulation.
exceed one year for agricultural commodities. (5) *Cross-commodity hedges.* Positions in commodity derivative contracts described in paragraph (2)(ii), paragraphs (3)(i) through (iv) and paragraphs (4)(i) through (iv) of this definition may also be used to offset the risks arising from a commodity other than the same cash commodity underlying a commodity derivative contract, *provided that* the fluctuations in value of the position in the commodity derivative contract, or the commodity underlying the commodity derivative contract, are substantially related to the fluctuations in value of the actual or anticipated cash position or pass-through swap and no such position is maintained in any physical delivery commodity derivative contract during the lesser of the last five days of trading or the time period for the spot month in such physical-delivery contract.				