



December 2, 2014

Via Electronic Submission

Chris Kirkpatrick, Secretary
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants (RIN Number 3038-AC97)

Dear Mr. Kirkpatrick:

The American Gas Association (“AGA”), the American Public Power Association (“APPA”), the Edison Electric Institute (“EEI”), the Electric Power Supply Association (“EPSA”), the Large Public Power Council (“LPPC”), and the National Rural Electric Cooperative Association (“NRECA”) (hereafter “Joint Associations”), respectfully submit these comments in response to the proposed rules on Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants (“Proposed Margin Rule”)¹ of the Commodity Futures Trading Commission (“CFTC” or “Commission”). The Joint Associations have been active participants in many aspects of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”) implementation process and welcome the opportunity to continue to discuss commercial end user-related issues with the Commission and staff.

I. Description of Joint Associations and Their Interest in the Proposed Rule

¹ Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 79 Fed. Reg. 59898 (October 3, 2014)(“Proposed Rule”).

AGA is the national trade association representing U.S. shareholder-owned natural gas distribution companies. There are more than 71 million residential, commercial and industrial natural gas customers in the U.S., of which 94 percent — over 68 million customers — receive their gas from AGA members. AGA is an advocate for natural gas utility companies and their customers and provides a broad range of programs and services for member natural gas pipelines, marketers, gatherers, international natural gas companies and industry associates. Today, natural gas meets more than one-fourth of the United States' energy needs. AGA's members engage in financial risk management transactions with counterparties that may be considered swap dealers or major swap participants that are regulated by the CFTC. As such, AGA's members will be directly affected by regulations promulgated under the Dodd- Frank Act.

APPA is the national service organization representing the interests of publicly-owned electric utilities in the United States. More than two thousand public power systems provide over fifteen percent of all kilowatt-hour sales to ultimate customers. APPA's member utilities are not-for-profit utility systems that were created by state or local governments to serve the public interest. Some publicly-owned electric utilities generate, transmit, and sell power at wholesale and retail, while others purchase power and distribute it to retail customers, and still others perform all or a combination of these functions. Public power utilities are accountable to elected and/or appointed officials and, ultimately, the American public. The focus of a public power utility is to provide reliable and safe electricity service, keeping costs low and predictable for its customers, while practicing good environmental stewardship.

EEl is the association of U.S. shareholder-owned electric companies. EEl's members serve 99 percent of the ultimate consumers in the shareholder-owned segment of the U.S. electricity industry, and represent approximately 70 percent of the U.S. electric power industry. EEl also has more than 65 international electric companies as Affiliate members, and more than 170 industry suppliers and related organizations as Associate members.

EPSA is the national trade association representing leading competitive power suppliers, including generators and marketers. These suppliers, who account for nearly 40 percent of the installed generating capacity in the United States, provide reliable and competitively priced electricity from environmentally responsible facilities. EPSA seeks to bring the benefits of competition to all power customers.

The Large Public Power Council is an organization representing twenty-six of the largest locally owned and operated public power systems in the nation. LPPC members own and operate over 75,000 megawatts of generation capacity and nearly 34,000 circuit miles of high voltage transmission lines. Collectively, LPPC members own nearly ninety percent of the transmission investment owned by non-federal public power entities in the U.S. LPPC member utilities supply power to some of the fastest growing urban and rural residential markets in the country. Members are located in eleven states and Puerto Rico and provide power to some of the

largest cities in the country, including Los Angeles, Seattle, Omaha, Phoenix, Sacramento, Jacksonville, San Antonio, Orlando, and Austin.

Formed in 1942, NRECA is the national service organization for more than nine hundred not-for-profit rural electric utilities and public power districts that provide electric energy to approximately forty-two million consumers in forty-seven states or twelve percent of the nation's population. Kilowatt-hour sales by rural electric cooperatives account for approximately eleven percent of all electric energy sold in the United States. Because its members are customers of the cooperative, all the costs of the cooperative are directly borne by its consumer-members.²

The Joint Associations' members are physical commodity market participants that rely on commodity derivative contracts primarily to hedge and mitigate their commercial risk. Regulations that make effective risk management options more expensive for commercial end users of swaps will likely lead to higher energy prices if the costs associated with new regulations are passed through to retail energy consumers and commercial and industrial electric consumers, or will result in more volatile prices if commercial end users decide to hedge a smaller portion of their commercial risk. Accordingly, as end users of commodity swaps to hedge commercial risk, the Joint Associations' members have a direct and significant interest in margin rules that may adversely affect the end user margin requirements.

II. Summary of Joint Associations' Comments

The Joint Associations' support the Commission's proposal allowing covered swap entities ("CSE") that transact with non-financial end users to continue to negotiate the terms of their swaps free from any mandatory minimum margin rules and instead to allow bilaterally negotiated credit support arrangements. This is consistent with Congress' intent, as reflected in the Dodd-Frank Act, to provide commercial end users with broad exemptions from the new registration and clearing requirements of the Commodity Exchange Act, as amended ("CEA")

² 13 C.F.R. §121.201, n.1. The vast majority of NRECA's members meet the definition of "small entities" under the Small Business Regulatory Enforcement Fairness Act ("SBREFA"). Only four distribution cooperatives and approximately twenty-eight G&Ts do not meet the definition. The RFA incorporates by reference the definition of "small entity" adopted by the Small Business Administration (the "SBA"). The SBA's small business size regulations state that entities which provide electric services are "small entities" if their total electric output for the preceding fiscal year did not exceed four million megawatt hours.

applicable to swaps and certain participants in the swap markets. However, there are aspects of the Proposed Rule that may cause additional uncertainty, which the Joint Associations respectfully request that the Commission revise in the Proposed Rule:

- Delete the proposal to require certain non-financial end users to be considered financial end-users for margin purposes;
- Delete the proposal to require documentation of transactions with non-financial entities under proposed section 23.158;
- Delete the proposal to require covered counterparties to calculate initial and variation margin on a mark-to-market basis for non-financial entities that hold material swaps exposure;
- Amend the Definition of “Eligible Master Netting Agreement” to recognize the ISDA Master Agreement; and
- Amend the proposed timing requirement for posting margin since non-financial entities may not be able to meet the T + 1 business process for posting margin.

III. Comments

The Joint Associations generally support the revisions in the Proposed Margin Rule and applaud the Commission’s efforts to revise the Proposed Margin Rule consistent with past comments. Section 4s(e)(3)(A) of the Commodity Exchange Act (“CEA”) states that to offset the risk to the financial system from the use of uncleared swaps, the Commission shall adopt rules for Swap Dealers (“SDs”) and Major Swap Participants (“MSPs”) imposing capital requirements and both initial and variation margin requirements on all such uncleared swaps.³ Such requirements will help ensure the safety and soundness of the SD or MSP and be appropriate for the risk associated with uncleared swaps.⁴

As the Joint Associations have previously indicated, the risk associated with any particular uncleared swap varies depending upon the individual characteristics of the transaction and the counterparty. The commodity swaps entered into by commercial end users for the purpose of hedging or mitigating commercial risk pose little risk to their counterparties or to the market as a whole. Since commercial end users rely on swaps to reduce their commercial risk,

³ 7 U.S.C. § 6s(e)(2)(B).

⁴ 7 U.S.C. §4s(e)(3)(A).

their hedging transactions increase the stability of the swaps market, and the broader financial system as a whole. As such, Joint Associations appreciate the Commission's recognition in the Proposed Rule of the reduced risk posed by non-financial end users to CSEs as well as the changes the Commission made from its 2011 Proposed Rule⁵ to limit the requirement that market participants post margin to those market participants that are considered CSEs⁶ or financial end users. Excluding non-financial end users, including the Joint Associations' members, is consistent with Congress' intent in enacting the statute and, as explained above, would not serve to strengthen the stability of the swaps market or the financial system as a whole. In order to ensure the highest level of protection to the swaps and financial markets from uncleared swaps transactions and provide the greatest clarity to market participants, and non-financial end users in particular, we propose the following changes and clarification to the Proposed Margin Rule.

A. The Commission Should Delete the Proposal Allowing the Commission to Require SDs/MSPs to Treat Certain Non-Financial End Users as Financial End Users for Margin Purposes

In the Proposed Margin Rule, the Commission sets forth a definition for the term "Financial End Users" that are not considered SDs or MSPs but whose business is financial in nature and, as such, whose "activities and risk profile would warrant inclusion" in the market participants required to comply with the Proposed Rule. The Commission states that "the proposal would not require CSEs to exchange margin with non-financial end users."⁷ The Commission explains that the proposed definition of "Financial End Users" "is an attempt to strike a balance between the need to capture all financial counterparties that pose significant risk to the financial system and the danger of being overly inclusive."⁸ The Proposed Rule sets forth an additional two-prong test for inclusion under the requirements of the Proposed Rule. The first prong would include any entity that "is, or holds itself out as being, an entity or arrangement that raises money from investors primarily for the purpose of investing in loans, securities, swaps, funds, or other assets for resale or other disposition or otherwise trading in loans, securities, swaps, funds or other assets."⁹

⁵ Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 76 Fed. Reg. 23,732 (April 28, 2011).

⁶ The Commission defines CSEs as "SDs and MSPs for which there is no Prudential Regulator" in the Proposed Margin Rule. See 79 Fed. Reg. 59902. Therefore, for purposes of the Joint Associations' comments on this Proposed Margin Rule, the term "CSEs" also includes SDs and MSPs.

⁷ Proposed Rule at 59906.

⁸ *Id.*, at 59902.

⁹ *Id.* at 59903.

The second prong of the proposal would permit the Commission to require that a SD or MSP “treat an entity as a financial end user for margin purposes, even if the person is not specifically listed within the definition of “financial end user” or if the entity is excluded from the definition of “financial end user”” as described in the Proposed Margin Rule.¹⁰ The Commission explains that such proposal “was included out of an abundance of caution to act as a safety mechanism in the event that an entity didn’t fall squarely within one of the listed categories but was effectively acting as a financial end user.”¹¹ It appears that the Commission included this provision due to concerns “that one or more types of financial entities might escape classification under the specific Federal or State regulatory regimes included in the proposed definition of a financial end user and whether it adequately maintains a distinction between financial end users and commercial end users.” The Joint Associations believe that this provision is vague and potentially allows for arbitrary categorization of non-financial commercial end users as financial end users, bringing unnecessary uncertainty to non-financial/commercial end users accessing the swaps markets to hedge.

The Joint Associations request that the Commission delete this provision from the Proposed Margin Rule or, in the alternative, clarify that non-financial/commercial end users are exempt from this provision. Implementing such a vague requirement would not serve the intended purpose of providing greater safety to the market. The proposal only adds another layer of uncertainty to the rules as exercise of the provision would have a material economic impact on the commercial end user affected. The Commission provides no parameters, objective standards, or procedural protections for how such a decision to treat non-financial end users as financial end users for margin purposes would be made. The Commission proposed no specific metrics, either on a quantitative or qualitative basis, outlining how it would make such a determination and the proposal lacks a method for sufficient notice and comment to be made to the affected non-financial end user. The Commission fails to describe how requiring such treatment of non-financial end users under such vague circumstances would enhance the safety of the marketplace or otherwise further the stated goals of the statute to increase the stability of the swaps market or the broader financial system.

The Joint Associations argue that the other elements of the existing proposal contain sufficient rules and safeguards that avoid the need for any perceived “safety” that such a vague provision as that proposed herein would achieve. As such, the Joint Associations request that the Commission delete this provision from the regulations.

¹⁰ *Id* at 59903.

¹¹ *Id* at 59903.

B. The Commission Should Delete the Documentation Requirement For Non-Financial Entities Under Proposed Section 23.158

In the Proposed Margin Rule, the Commission proposes to require that covered entities enter into certain documentation with all counterparties – including non-financial end users – to provide clarity about the counterparties’ rights and obligations.¹² For uncleared swaps with non-financial end-users, the proposed documentation would specify whether initial and/or variation margin will be exchanged, and if so, include information about the methodology and data sources used to value positions, calculate initial margin and variation margin, dispute resolution procedures, and any margin thresholds employed.¹³ The Commission explained that while the 2013 international framework does not include a specific requirement for documentation, the Commission’s proposed documentation for swaps with non-financial end users is consistent with preexisting CFTC swap trading documentation rules.¹⁴ While the Prudential Regulators’ proposal generally requires the same documentation for covered entities’ uncleared swaps, they do not extend this requirement to their swaps with “other counterparties.”¹⁵

The Joint Associations request that the Commission delete the proposed provision requiring documentation for uncleared swaps between a CSE and a non-financial entity. Such a requirement is inconsistent with the overall purpose of the rule in that there is no requirement that a non-financial entity post margin, so imposing a requirement that a CSE and a non-financial entity that decide not to post margin to document such decision is unduly burdensome and increases the regulatory burden upon the non-financial entities.

There is no need for the Commission to impose prescriptive documentation requirements for swaps that are entered into by commercial end users. The terms of a bilaterally negotiated, uncleared swap are mutually agreed upon by the parties and, as such, legally enforceable. The Joint Associations see no compelling public policy reason to impose additional burdens through increased documentation requirements as those proposed in this provision. The requested changes would also make the Commission’s proposal consistent with that of the Prudential Regulators, ensuring a level playing field for non-financial entities and the CSEs they may rely on that are subject to either the Prudential Regulators’ or the Commission’s rules. For these

¹² Proposed Rule at 59906.

¹³ *Id.* at 59915.

¹⁴ *Id.* at 59915 (citing CFTC Rule §23.504, Swap Trading Relationship Documentation).

¹⁵ Margin and Capital Requirements for Covered Swap Entities, 79 Fed. Reg. 57,348 (September 24, 2014) (“Prudential Regulators Proposal”)

reasons, the Joint Associations request that the Commission delete the documentation requirement for swaps with non-financial end users from section 23.158 in the Proposed Margin Rule.

C. The Commission Should Delete the Proposal to Require that Covered Swap Entities Calculate Initial and Variation Margin on a Marked to Market Basis for Positions Held by Non-Financial End User Counterparties.

In the Proposed Margin Rule, the Commission proposes to address the statutory mandate to enact rules to help ensure the safety and soundness of SDs and MSPs by requiring CSEs to enter into certain documentation with all counterparties, including non-financial end users, to provide clarity regarding the counterparties' respective rights and obligations.¹⁶ This would permit the SDs and MSPs to establish margin requirements of their own determination based upon the representations made by the counterparties. Additionally, the Proposed Margin Rule would require each CSE to "calculate hypothetical initial and variation margin amounts each day for positions held by non-financial entities that have material swaps exposure to the covered counterparty."¹⁷

The Joint Associations request that the Commission delete the second requirement that CSEs calculate hypothetical valuation amounts for initial and variation margin for positions held by non-financial end user counterparties. Such a requirement is overly burdensome and unnecessary to ensuring that the Proposed Rule satisfies the statutory mandate to ensure the safety and soundness of the swaps markets. As the Joint Associations stated in our previous comments, there is no need to for the Commission to impose prescriptive documentation, collateral valuation, or exposure calculations on swaps that are entered into by non-financial end users.¹⁸ The terms of a bilaterally negotiated, uncleared swap are mutually agreed upon by the parties and, as such, legally enforceable. The Joint Associations see no compelling public policy reason to impose additional burdens through increased valuation calculations as those proposed in this provision.

¹⁶ *Id.* at 59906.

¹⁷ *Id.* at 59907.

¹⁸ The Edison Electric Institute, the Electric Power Supply Association, the National Rural Electric Cooperative Association, the American Public Power Association, the Large Public Power Council, and the American Gas Association Comments on the Proposed Rules on Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants (RIN 3038-AC97) and Capital Requirements for Swap Dealers and Major Swap Participants (RIN 3038-AD54) at 8-9 (July 11, 2011).

Additionally, the proposed provision states that such a requirement would apply to positions held by non-financial end users that “have material swaps exposure” to the CSE. The Proposed Margin Rule defines “material swaps exposure” as swap positions with a gross notional amount of \$3 Billion or more. The proposal is unclear how or when, if at all, such non-financial end-users that are counterparties to CSEs would be notified that a counterparty has reached that threshold. Such a requirement would demand that the CSE and the end user counterparty have much greater knowledge of all positions held, which would be unduly burdensome and unnecessary, particularly given the nature of such non-financial end user counterparties. As such, the Joint Association’s reiterate their request that the Commission exclude transactions with non-financial end users from this requirement in the Proposed Rule.

D. The Commission Should Recognize the ISDA Master Agreement as an “Eligible Master Netting Agreement”

In the Proposed Rule, the Commission proposes a definition of the “Eligible Master Netting Agreement (“EMNA”).”¹⁹ Such an agreement would create a single legal obligation for all transactions covered by that agreement. The proposed definition includes a requirement ensuring that such an agreement would be found “to be legal, valid, binding, and enforceable under the law of the relevant jurisdictions” And that such an agreement would be required to establish and maintain “written procedures to monitor possible changes in relevant law and to ensure that the agreement continues to satisfy the requirements of this definition.”²⁰

The Joint Associations understand that the EMNA does not apply to non-financial end users²¹ but are concerned that the precedent established in the proposed rule could be applied to them at a future time. A failure to find that the ISDA documentation meets EMNA requirements could have a broader application than the Proposed Rule. The Joint Associations request that the Commission amend the proposed definition of EMNA to include and recognize the ISDA Master Agreement. Since many Joint Associations members rely on the ISDA Master Agreement for netting swap transactions, including the ISDA Master Agreement within the definition of, or at the very least, recognizing the ISDA Master Agreement as an appropriate netting agreement, would provide certainty to many market participants that rely upon the ISDA Master Agreement, including Joint Associations’ members. Without such recognition and clarification, there is the potential that countless transactions would be required to be re-negotiated and re-executed in order to ensure compliance with the proposed definition of EMNA. This would be extremely

¹⁹ *Id.* at 59926.

²⁰ *Id.*

²¹ *Id.* at 5990.

costly and unduly burdensome on Joint Associations' members. Since the ISDA Master Agreement has been used for these transactions for countless transactions and has become the industry standard, the Commission can easily remedy this potential burden by clarifying that the ISDA Master Agreement meets the Commission's requirements and include the ISDA Master Agreement within the definition of EMNA.

E. The Commission Should Revise the Proposed Timing Requirement for Posting Margin

In the Proposed Margin Rule, the Commission proposes to require each CSE to collect initial margin for every swap with a covered counterparty on or before the business day after execution.²² While the Joint Associations appreciate that non-financial end users are not required to post margin under the Proposed Rule, we request clarification that this time period for posting margin is not required for non-financial end users and that it will not be applied to them at a future time would provide additional clarity. The Joint Associations request that the Commission amend this proposal to allow two business days before collection of margin is required rather than the one day as proposed in §23.152(a). Such a change would still ensure that any necessary margin is collected within a reasonable time period, but would allow other non-financial entities otherwise required to post margin, sufficient time to ensure that any necessary transfer of funds can be fully implemented.

Without amending this proposal to allow for an extra day to post margin, any non-financial entities would face extreme challenges to ensure that appropriate margin is posted in a timely manner to comply with the rule since any entity would need to calculate the appropriate margin after daily close and then request from their financial institution to transfer the appropriate funds. Commercial end users that are members of the Joint Associations may utilize, for example, letters of credit ("LOCs") to support their collateral posting requirements for hedging transactions. The LOCs are typically provided by financial institutions, the terms of which often require the commercial end user to notify the bank two days in advance in order to amend and re-negotiate the LOC to meet a collateral posting requirement. Further, a request to an entity's financial institution to draw upon funds from a line of credit facility must be made before a notification time (*i.e.*, 11:00 a.m. New York time) to ensure next day availability. If the request to draw appropriate funds is received after the financial institution's notification time, the funds will not be available for a margin payment until the second business day. Therefore, amending the regulations to allow for two business days to post margin would ensure that all

²² *Id.* at 59907.

entities, regardless of their status, would have sufficient time to meet the requirement while still ensuring there is not an unreasonable time lag between the close and the posting of margin.

The Joint Associations also suggest eliminating §23.152(b)(2), as the requirement to recast Initial margin each day while simultaneously calculating/exchanging the required variation margin daily appears to double margin changes in the market value of a swap. Under the proposed initial margin requirements, the exchange of initial margin is already two-way, modeled at a 99% Confidence Interval with a 10 day holding period. This is substantial initial margin support. Adding a daily recast obligation, with the variation margin requirement, seems overly burdensome and unnecessary. The proposed rule doubles existing initial margin standards, through the two-way nature of margin posting, and doubles the apparent variation margin by requiring both the calculation of initial and variation margin each day.

IV. Conclusion

The Joint Associations appreciate the opportunity to submit comments on the Proposed Rule and the Commission's proposal not to require non-financial end users to post margin. As indicated above, Joint Associations request that the Commission provide additional clarity and certainty by: (1) deleting the provision in the definition of financial end user that allows certain non-financial end users to be considered financial end users for margin purposes; (2) deleting the proposal to require documentation of transactions with non-financial entities under proposed section 23.158; (3) deleting the proposal to require counterparties to calculate initial and variation margin on a mark-to-market basis for non-financial entities that hold material swaps exposure; (4) amending the definition EMNA to recognize the ISDA Master Agreement; and (5) amending the proposed timing requirement for posting margin.

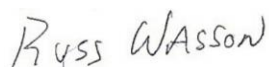
The Joint Associations appreciate the Commission's consideration of improvements to the Proposed Rule. Please feel free to contact us if you have questions or would like to discuss these comments in greater detail.

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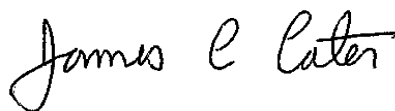
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