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March 30, 2015

Via Electronic Submission

Mr. Christopher J. Kirkpatrick
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581

Re: Position Limits for Derivatives, RIN 3038-AD99
Aggregation of Positions, RIN 3038-AD82

Dear Mr. Kirkpatrick:

By notices dated February 25, 2015 and March 25, 2015,[1] the Commodity Futures Trading Commission ("CFTC" or "Commission") re-opened the comment period to address certain issues with respect to the Commission's proposed position limits and aggregation rules,[2] which also were addressed at a meeting of the Commission's Energy and Environmental Markets Advisory Committee ("EEMAC") on February 26, 2015.

As set forth in the February 25, 2015 Notice (at 10024):

> To provide interested persons with a sufficient period of time to respond to questions raised and points made at the Energy and Environmental Markets Advisory Committee meeting, the Commission is reopening both the Position Limit Proposal and the Aggregation Proposal for an additional 30-day comment period. The Commission is providing notice that, in addition to commenting on the agenda issues, comments may be made on the issues addressed at the meeting or in associated materials posted to the Commission's Web site, as they pertain to energy commodities, including hedges of a physical commodity by a commercial enterprise, as pertains to energy commodities.

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1 *See* 80 Fed. Reg. 10022 (February 25, 2015) and 80 Fed. Reg. 15699 (March 25, 2015).

2 *See* Position Limits for Derivatives, 78 Fed. Reg. 75680 (Dec. 12, 2013) and Aggregation of Positions, 78 Fed. Reg. 68946 (Nov. 15, 2013).

Sempra Energy ("Sempra Energy" or "Sempra") appreciates the opportunity to submit comments in response to the Notice and to supplement the comments Sempra Energy previously submitted on July 25, 2014. In these comments, Sempra Energy urges the Commission to:

- Set initial spot-month limits based on updated estimates of deliverable supply to more accurately reflect current market conditions;
- Reinstate unfilled storage capacity as an enumerated bona fide hedge and delegate to the exchanges the authority to grant exemptions for non-enumerated hedges, thereby leveraging the exchanges' expertise and resources; and
- Be cognizant of the operational and feasibility difficulties companies with multiple subsidiaries will face in implementing the rules if changes are not made to the proposed rules.

I. DESCRIPTION OF SEMPRA ENERGY AND ITS SUBSIDIARIES

A. Sempra Energy

Sempra is a Fortune 500 energy-services holding company whose operating units develop energy infrastructure, operate utilities, and provide related services to their customers. Sempra's operations are divided principally between (a) its two wholly-owned California utilities, Southern California Gas Company ("SoCalGas") and San Diego Gas & Electric Company ("SDG&E") (collectively, "California Utilities") and (b) Sempra U.S. Gas & Power and Sempra International.

B. California Utilities

SoCalGas is regulated by the California Public Utilities Commission ("CPUC") as a public utility, as defined by California law. SoCalGas is the nation's largest natural gas distribution utility. It owns and operates a natural gas distribution, transmission and storage system that supplies natural gas throughout its service territory, which consists of approximately 20,000 square miles. SoCalGas' service territory extends from San Luis Obispo, California in the north to the Mexican border in the south, excluding San Diego County, the city of Long Beach and the desert area of San Bernardino County. SoCalGas also provides natural gas service to residential, commercial, industrial, utility electric generation and wholesale customers through 5.9 million meters, covering a population of 21.4 million.

SDG&E also is a CPUC-regulated public utility, as defined by California law. SDG&E has a franchised service territory that provides electric and natural gas service in San Diego County and southern Orange County, California. SDG&E owns electric transmission facilities in the market operated by the California Independent System Operator Corporation and has an open access transmission tariff on file with the Federal Energy Regulatory Commission. SDG&E provides electricity to approximately 3.5 million consumers and natural gas to approximately 3.2

million consumers. SDG&E delivers electricity through approximately 1.4 million meters in San Diego County and an adjacent portion of southern Orange County, California. The electricity that SDG&E provides to its customers is either purchased from third parties or generated from SDG&E's electric generation facilities. SDG&E also delivers natural gas through 0.9 million meters in San Diego County and transports electricity and natural gas for others. SDG&E's service territory encompasses 4,100 square miles.

C. Sempra U.S. Gas & Power and Sempra International

Sempra U.S. Gas & Power develops, owns and operates renewable energy generation projects in several states, a natural gas-fired electric generation facility in Arizona, natural gas pipelines and storage facilities in Louisiana, Mississippi and Alabama, natural gas distribution utilities in Mississippi and Alabama, and a terminal in Louisiana for the import and export of liquefied natural gas ("LNG"). Sempra International includes for financial reporting purposes a Sempra Mexico segment and a Sempra South American Utilities segment.[3]

Sempra Energy's California Utilities – SoCalGas and SDG&E – and Sempra U.S. Gas & Power all engage in the purchase and/or sale of Henry Hub natural gas futures contracts and swaps that would be subject to the Commission's proposed position limits and aggregation rules.

II.
DISCUSSION

A. The Commission Should Set Initial Spot-Month Limits Based on Updated Estimates of Deliverable Supply to More Accurately Reflect Current Market Conditions

One of the questions raised for the EEMAC's consideration during Panel II of the February 26, 2015 meeting was whether "the Commission [should] consider updating estimates of deliverable supply to increase liquidity in the spot month."[4]

Sempra Energy and numerous other market participants previously have urged the Commission to update the estimates of deliverable supply, particularly in the context of the Henry Hub Natural Gas contract, to more accurately reflect current market conditions. The current proposed 1,000 spot-month limit for Henry Hub Natural Gas contracts is based on 1996

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[3] The Sempra Mexico segment involves the ownership and operation of natural gas transmission pipelines and propane and ethane systems, a natural gas distribution utility, electric generation facilities, including a wind-powered facility, a terminal for the import of LNG and marketing operations for the purchase of LNG and the purchase and sale of natural gas. The Sempra South American Utilities segment involves the operation of electric transmission and distribution utilities in Chile and Peru.

[4] Meeting Questions for EEMAC Consideration (February 26, 2015) at p. 2, Question 12. *See also* Question 13 of Panel II: "Is such an update more needed for some commodities than others? Is it relevant that an exchange would have the ability to set its spot month limits *lower* than 25% of updated deliverable supply, if the exchange believes doing so is appropriate." (emphasis original)

estimates of deliverable supply,[5] which clearly do not reflect the dramatic growth in the natural gas industry in the last twenty years. Using updated estimates of deliverable supply should prevent material reductions in liquidity by maintaining the number of counterparties with whom bona fide hedgers could contract.

Sempra Energy believes it is important for the Commission to set these limits right at the outset to avoid as much market disruption as possible. Updating the estimates of deliverable supply also would be consistent with one of the approaches already outlined in the proposed position limits rule.[6] Sempra Energy urges the Commission to move forward with this approach.

B. The Commission Should Reinstate Unfilled Storage Capacity as an Enumerated Bona Fide Hedge

During Panel III of the February 26, 2015 EEMAC meeting, there was a significant amount of discussion regarding the Commission's decision in the December 12, 2013 proposed position limits rule to withdraw the hedging exemption for unfilled storage capacity that had been part of the originally proposed rule (Section 151.5(a)(2)(v)).

In his presentation on behalf of the Commercial Energy Working Group, Mr. Oppenheimer made a compelling case for the Commission to reinstate unfilled storage capacity as an enumerated bona fide hedge, at a minimum in the context of the Henry Hub Natural Gas contract.[7] The American Gas Association's ("AGA") representative (Ms. Sharma Frank) reinforced this when she confirmed that the scenario the Commercial Energy Working Group depicted in its presentation represents a "bread and butter" transaction that AGA members "rely on to manage commercial risk."[8]

Sempra Energy set forth essentially the same scenario in its July 25, 2014 comments.[9] Slides 6 - 8 of Mr. Oppenheimer's EEMAC presentation describe a winter storage hedging strategy that natural gas suppliers and marketers commonly use to manage commercial risk. The sequence of events depicted in this example represents a hedging strategy used by many market participants to manage potentially wide fluctuations in prices and to lock in profits based on calendar spreads. The marketer or supplier first contracts for storage capacity, without which it

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[5] *See*, *e.g.*, the CME Group's February 10, 2014 comments on the proposed positions limit rule at pp. 3 and 20.

[6] In the proposed position limits rule (at p. 75727), the Commission explained that "[a]s an alternative to the initial spot month limits in proposed appendix D to part 150, the Commission is considering setting the initial spot month limits based on estimated deliverable supplies submitted by the CME Group in correspondence dated July 1, 2013." Under this alternative, the Commission "would use the exchange's estimated deliverable supplies and apply the 25 percent formula to set the level of the spot month limits in a final rule if the Commission verifies the exchange's estimated deliverable supplies are reasonable" (*Id.*) The Commission set forth the specific spot month limits that would result from application of the CME Group's updated estimated deliverable supplies in Table 9 of the proposed rule. (*Id.* at pp. 75727-28).

[7] *See* presentation titled "Illustrative Hedge Examples," at Slides 6, 7 and 8.

[8] Transcript ("Tr.") p. 176.

[9] *See* pp. 6-7.

could not realize the opportunity to profit from temporal differences in natural gas prices (i.e., the "calendar spread"). The marketer/supplier then buys a lower priced futures contract (October) and sells a higher priced contract (January) to lock in a profit based on the "spread" or difference between the two contracts. As the October futures contract nears expiration, the marketer/supplier will purchase physical gas to fill the storage capacity, and will subsequently withdraw the gas from storage and sell it as the January futures contract nears expiration. This transaction manages the risk associated with price fluctuations while the gas is in storage and locks in the profit of the marketer/supplier.

Based on Sempra Energy's experience, this type of hedging strategy (in which the risk of price fluctuations associated with unfilled storage capacity is mitigated) is far more common in the wholesale natural gas industry than strategies based on hedging storage capacity that has already been filled. In most cases, it is not practical to contract for storage capacity, purchase the gas, and lock in the profit through a futures contract or swap all at the same time. Accordingly, the response of many market participants has been to acquire and hedge unfilled storage capacity. Yet, the currently proposed definition of a bona fide hedging position in omitting the enumerated hedge for unfilled storage capacity would unnecessarily constrain the use of this popular and common hedging strategy.

The Commission has now developed a robust record in support of reinstating Section 151.5(a)(2)(v) as an enumerated bona fide hedge and we urge the Commission to do so.

During the EEMAC meeting, there also was a significant amount of discussion regarding the need to create a workable process by which market participants can seek exemptions for non-enumerated hedges and to receive prompt responses to their requests for exemptions.[10] A number of market participants suggested that the Commission delegate this authority to the exchanges, thereby leveraging the exchanges' expertise and resources. Sempra Energy urges the Commission to adopt this recommendation.

C. The Commission Should be Cognizant of the Operational and Feasibility Difficulties Companies with Multiple Subsidiaries Will Face in Implementing the Rules if Changes are Not Made

During Panel III of the February 26, 2015 EEMAC meeting, the Southern Company's representative, Mr. Hughes, briefly described the difficulties from an "operational" and "feasibility" standpoint of having to manage hedging programs of diverse subsidiaries on an "enterprise-wide" basis.[11] Indeed, he indicated that having to do so would be "problematic at best."[12]

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[10] *See*, *e.g.*, Mr. Oppenheimer's remarks at Tr. p. 177: "There is no Rule 1.47 process in this proposal, so there is no ability to apply for a non-enumerated exemption that way. There is 4a(a)(7) which is a broad provision that allows the Commission to basically exempt anything from the position limit rule and one might have to go that way [but] [i]t's a fairly unsatisfying resolution . . ."

[11] Tr. pp. 216-217.

[12] *Id*. at p. 217.

Sempra Energy identified related concerns in its July 25, 2014 comments about the difficulties companies with multiple subsidiaries will face if the Commission does not revise certain aspects of the proposed position limits and aggregation rules. To be specific, heretofore, the exchanges have not required holding companies to aggregate the positions of its subsidiaries if they are separately and independently operated.[13]

Sempra Energy realizes that the proposed aggregation rule was not a focus of discussion at the February 26, 2015 EEMAC meeting, so it will not belabor the issue in these comments. But our hope is that the Commission is giving due consideration to the concerns Sempra Energy and numerous other parties with multiple subsidiaries raised in their prior comments about the proposed aggregation rule. In particular, Sempra Energy urges the Commission to:

- Modify its proposed conditional spot-month limit exemption to allow independently-operated subsidiaries within a corporate group that do not hold positions in physical-delivery contracts, where one independently-operated subsidiary in the group holds a physical delivery spot month contract, to qualify for the exemption under certain conditions (Section II.B at pp. 4-6 of Sempra Energy's July 25, 2014 comments); and

- Tailor the requirements for the aggregation exemption for majority owners to the purpose of the aggregation policy – "to prevent evasion of position limits through coordinated trading" – and revise the rule to permit notice filings for companies that have majority ownership in an owned entity, similar to the process for persons with an ownership or equity interest in an owned entity of 10 to 50 percent (Section II.D. at pp. 7-11 of Sempra Energy's July 25, 2014 comments).

III.
CONCLUSION

In conclusion, Sempra Energy respectfully urges the Commission to:

- Set initial spot-month limits based on updated estimates of deliverable supply to more accurately reflect current market conditions;

- Reinstate unfilled storage capacity as an enumerated bona fide hedge and delegate to the exchanges the authority to grant exemptions for non-enumerated hedges, thereby leveraging the exchanges' expertise and resources; and

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[13] *See*, *e.g.*, ICE Futures U.S. Inc.'s February 10, 2014 comments on the proposed aggregation rule at p. 2: "There are numerous instances in our markets where companies with 100% common ownership nonetheless operate in a manner where there is complete independence of decision-making and control of the trading decisions. The Exchange does not automatically aggregate such commonly owned entities, and based on the comment letters submitted in response to the original Part 151 amendments, it would seem that market participants across the broad variety of futures markets agree with this approach."

- Be cognizant of the operational and feasibility difficulties companies with multiple subsidiaries will face in implementing the rules if changes are not made to the proposed rules.

Sincerely,

/s/ *Steven C. Nelson*
Steven C. Nelson

cc: Honorable Timothy G. Massad, Chairman
Honorable Mark P. Wetjen, Commissioner
Honorable Sharon Y. Bowen, Commissioner
Honorable J. Christopher Giancarlo, Commissioner
Stephen Sherrod, Senior Economist
Riva Spear Adriance, Senior Special Counsel