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June 22, 2015

Christopher Kirkpatrick, Secretary  
Commodity Futures Trading Commission  
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**Re: Comments of the International Energy Credit Association with respect to the CFTC's Notice of proposed rulemaking entitled "Trade Options," 80 Fed.Reg. 26200 (May 7, 2015), RIN 3038-AE26**

Dear Mr. Kirkpatrick:

The International Energy Credit Association ("IECA") is pleased to submit the comments set forth herein ("TO Comments") to the Commodity Futures Trading Commission ("Commission" or "CFTC") with respect to the CFTC's proposed rule on Trade Options, published on May 7, 2015, RIN 3038-AE26 ("Trade Options Proposal").

Following the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("DFA") and its amendments of the Commodity Exchange Act ("CEA"), the IECA has filed numerous comments with the Commission seeking to protect the rights and advance the interests of the commercial end-user community that makes up the majority of its membership. Most of the IECA's members are representatives of commercial end-users that rely on swaps to help them mitigate and manage (i.e., hedge) the risks of energy commodity price volatility to their physical energy businesses.

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

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**I. IECA Supports and Commends the Commission for Proposing Various Changes (Eliminating Form TO, Deleting the Reference to Part 151, and Reducing the Recordkeeping Requirement) set forth in its Trade Options Proposal**

The IECA commends the CFTC for its proposal to amend the trade option exemption. The continued evaluation of the trade option exemption highlights the laborious yet important balance between the needs of market participants and the need for regulatory oversight. We commend the Commission’s endeavor for seeking this balance through the proposed specific elimination of Part 45 reporting and Form TO, and the proposed deletion of the reference to Part 151. Eliminating these items will further the ability of commercial end-users to engage in healthy economic transactions, benefiting our entire economic system.

**II. Concerns with Recordkeeping Requirements**

***A. Recordkeeping Requirement.***

In order to qualify for the relief provided under the Trade Options Proposal, §32.3(b)(1) of the Trade Options Proposal requires each non-SD/MSP counterparty to “[c]omply with the swap data recordkeeping requirements of §45.2 of this chapter, as otherwise applicable to any swap transaction”. Pursuant to §45.2, non-SD/MSP counterparties subject to the jurisdiction of the CFTC are required to:

- (i) keep full, complete, and systematic records, together with all pertinent data and memoranda, with respect to each swap in which they are a counterparty, including, without limitation, all records demonstrating that they are entitled, with respect to any swap, to elect the clearing requirement exception in CEA section 2(h)(7);
- (ii) retain all records required to be kept pursuant to this section with respect to each swap throughout the life of the swap and for a period of at least five years following the final termination of the swap;

- (iii) retain the records required to be kept pursuant to this section in either electronic or paper form, so long as they are retrievable, and information in them is reportable, as required by this section;
- (iv) keep such records required by this section so they are retrievable by within five business days throughout the period during which it is required to be kept; and
- (v) allow inspection of such records upon request by any representative of the Commission, the United States Department of Justice, or the Securities and Exchange Commission, or by any representative of a prudential regulator as authorized by the Commission. Copies of all such records shall be provided, at the expense of the entity or person required to keep the record, to any representative of the Commission upon request. Copies of records required to be kept by any registrant shall be provided either by electronic means, in hard copy, or both, as requested by the Commission, with the sole exception that copies of records originally created and exclusively maintained in paper form may be provided in hard copy only. Copies of records required to be kept by any non-SD/MSP counterparty subject to the jurisdiction of the Commission that is not a Commission registrant shall be provided in the form, whether electronic or paper, in which the records are kept.

In addition to the recordkeeping requirements set forth in §45.2, §1.31 sets forth recordkeeping requirements that purport to apply to “all books and records required to be kept by the Act or by these regulations...”<sup>1</sup> Some of the requirements in §1.31 appear to impose different, more stringent, requirements than those imposed in §45.2 with respect to non-SD/MSP counterparties. For instance:

- (1) under §45.2, a non-SD/MSP is permitted to retain the required records “in either electronic or paper form, so long as they are retrievable, and information in them is reportable.”<sup>2</sup> Whereas, §1.31 requires the records to be “kept in their original form (for paper records) or native file format (for electronic records)” for the required period<sup>3</sup>.
- (2) §45.2 provides that a non-SD/MSP may provide records requested by the Commission in the form “whether electronic or paper, in which the records are kept,”<sup>4</sup> whereas §1.31(a)(2) requires each person required to keep records to “produce such records in a form specified by a representative of the Commission.”

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<sup>1</sup> See §1.31(a)(1).

<sup>2</sup> See §45.2(d)(2).

<sup>3</sup> See §1.31(a)(1).

<sup>4</sup> See §45.2(h).

- (3) §45.2 does not identify any specific requirements for records that are stored electronically, other than they must be retrievable within 5 business days. Under §1.31(b), however, there are extensive and onerous requirements that apply to records stored as reproductions offline in an electronic medium, which require immediate accessibility, certain minimum indexing and duplicate storage and indices at separate locations.<sup>5</sup>

We seek clarification that only the recordkeeping requirements in §45.2 apply to non-SD/MSP counterparties and that any inconsistencies, or additional requirements set forth in §1.31 do not apply to non-SD/MSP counterparties with respect to Trade Option transactions. We urge the Commission to take a holistic review of the interaction between its various recordkeeping requirements and ensure that they work together in a rational matter and do not impose unnecessary or inconsistent requirements on commercial end-users.<sup>6</sup>

### ***B. Record Retention Period for Trade Options with Multiple Constituent Parts.***

As stated in Sub-Part II.A.(ii) above in these TO Comments, an entity that is required to maintain records relating to transactions in commodity trade options, is generally required to maintain such records through the term of the transaction and for a period of five years thereafter.<sup>7</sup> However, it is unclear due to ambiguity in the language

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<sup>5</sup> The *Recordkeeping 1.31 Final Rule*, 64 Fed.Reg. 28735, 28736 (May 27, 1999) specifically discusses the Commission's understanding that it needs to reevaluate §1.31 periodically as technology changes. ("The Commission recognizes the important role improved technology can play in the continued development of the futures industry. Minimizing unnecessary regulatory obstacles to the adoption of improved technology is a goal of industry members, customers, and the Commission. Indeed, the pace of technological changes will require the Commission continually to review the standards articulated in this rule to ensure that the recordkeeping requirements reflect to the extent possible the reality of established technological innovation. The Commission therefore welcomes consultation with industry participants and specific proposals regarding how the regulations might be amended in the future to permit the futures industry to use available technology and to respond to the Commission's legitimate need to have access to complete and accurate records when necessary.") Commissioner Giancarlo acknowledged this need with the fourth question in his Dissenting Statement to the *Notice of Proposed Rulemaking on Records of Commodity Interest and Related Cash or Forward Transactions*, 79 Fed.Reg. 68140, 68147 (November 14, 2014) ("4. Is there a need to revise Rule 1.31 given advancements in technology and current business practices?").

<sup>6</sup> For a more thorough discussion see January 13, 2015 Comments of International Energy Credit Association to the CFTC's proposed "Records of Commodity Interest and Related Cash or Forward Transactions," RIN 3038—AE23, published in 79 Fed.Reg. 68140 on November 14, 2014 (the "Proposal").

<sup>7</sup> This standard does not, however, apply to a person subject to recordkeeping obligations with respect to certain nonfinancial commodity swaps or swaptions under CFTC Regulation 20.6(c). Instead, it is permitted to keep the records in accordance with its recordkeeping schedule and in its normal record retention format, in lieu of following the requirements of Regulation 1.31. Such a person, though, would also likely be subject to recordkeeping obligations relating to its nonfinancial commodity swaps and swaptions under Regulation 45.2, which in contrast imposes the "term plus five years" record retention period for data and memoranda pertinent to a swap transaction. This is an example of the potentially overlapping or inconsistent requirements that commercial end-users face under the Recordkeeping Rules.

of Regulation 45.2(c) how the record retention period applies to records relating to a trade option that is comprised of multiple underlying trade options that are exercised daily or on another periodic and frequent interval.

In the energy sector, it is common for a commercial end-user to enter into long-term physically-settled trade options, frequently with overall transaction durations of up to 20 years, or even longer. If a 20 year Serial Trade Option were treated as one ongoing transaction, the recordkeeping requirement would mandate keeping all accreting transaction records for up to 25 years after the individual trade option component was exercised or allowed to expire and, therefore, if viewed as a distinct option, terminated. Therefore, we respectfully request clarification that, for recordkeeping purposes only, a person may treat each constituent trade option in a trade option as a separate transaction, with the consequence that the records pertaining to that constituent transaction must be kept for five years following the termination of the constituent option, whether through exercise, expiration or otherwise. We believe that approach strikes an appropriate balance in preserving records that may be useful for market surveillance without imposing unnecessary and costly recordkeeping burdens on commercial end-users.

### *C. Voluntary Recordings of Oral Conversations.*

A commercial end-user may be subject to recordkeeping obligations under multiple CFTC rules, including Regulations 1.35(a) (if a member of a DCM or SEF), 18.05 (if a large futures trader or a futures or swaps volume threshold account holder or controller), 20.6(c) (if a large trader for certain commodity swaps), 32.3(b) (if it enters into a commodity trade option) and 45.2(b) (if it enters into a swap), with the overlay of Regulation 1.31 records format, retention and inspection requirements in certain cases (the “Recordkeeping Rules”). Various Recordkeeping Rules identify the types of records that a person subject to the rules is required to maintain, including the information or content to be covered.

None of the Recordkeeping Rules imposes an explicit obligation on a commercial end-user that is not registered with the Commission (that is, an Unregistered Member) to make recordings of oral conversations, nor do we read the Recordkeeping Rules to explicitly require such an entity to retain recordings if it voluntarily makes them.

Some commercial end-users find it a convenient or prudent business practice to record telephone conversations with brokers or with bilateral swap counterparties for use in the unanticipated event of a dispute with the broker or counterparty over a term of an oral transaction or instruction, even though Unregistered Members are clearly excluded from the requirement to record oral communications under Regulation 1.35(a)(1)(vii). If a commercial end-user elects voluntarily to record a telephone conversation, it is our understanding that those recordings do not become records that such person must then retain under Regulation 45.2(c) or the other Recordkeeping Rules, and we believe that is how the rules are widely interpreted by commercial end-users.

Some commercial end-users are concerned that voluntary telephone recordings may be subject to the Recordkeeping Rules, including the applicable record retention period requirements. We believe such an interpretation is contrary to the Commission's deliberate decision in its December 2012 Adaptation Rulemaking amendments to Regulation 1.35(a) to exclude Unregistered Members from the obligation to record conversations, which was first imposed on various Commission registrants in that rulemaking. Moreover, such an interpretation would lead to the illogical result that commercial end-users must retain recordings of conversations for five years, or longer for swap transactions including commodity trade options, or related cash or forward transactions, whereas CFTC registrants are required to maintain certain recordings they prepare as required by Regulation 1.35(a) for only one year as provided in Regulation 1.31(a).<sup>8</sup>

Faced with such a costly recordkeeping burden, a commercial end-user may have to forgo what it views as an otherwise sound business practice (recording conversations as a source of evidence to resolve a dispute with its broker or counterparty). That outcome, too, would be illogical, as the Commission's rules would be interpreted to actively discourage a commercial end-user from potentially protecting its own interests vis-a-vis a broker, dealer or other registered market intermediary, contrary to the Commission's policy goal of customer protection.

Such an interpretation is also, in our view, contrary to the Commission's 1996 *Gilbert v. Lind-Waldock & Co.*<sup>9</sup> decision in which the Commission determined that a person is not required under Regulation 1.35(a) to keep tape recordings it prepares when such records are not records it is required to prepare. Finally, nothing in the adopting releases for the Recordkeeping Rules suggests the Commission intended to require a person to retain recordings of oral conversations that the person voluntarily prepares.

In light of the forgoing, we respectfully request the Commission to confirm our understanding that a commercial end-user that is an Unregistered Member may voluntarily record oral conversations relating to its commodity trade option transactions without creating an obligation to retain such records in accordance under Regulations 45.2(c) or other Recordkeeping Rules.<sup>10</sup>

### **III. IECA Supports Commissioner Giancarlo's Statement that Trade Options Should Be Excluded From Position Limits in the Final Trade Options Rule**

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<sup>8</sup> The one-year record retention period also applies to recordings made by swap dealers in accordance with Regulation 23.202.

<sup>9</sup> [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,720 (June 17, 1996). The Commission rejected a Judgment Officer's determination that Lind-Waldock, a registered futures commission merchant, violated Regulation 1.35(a) by not retaining tape recordings it prepared of conversations with a futures customer. See footnote 23 of the decision.

<sup>10</sup> Likewise, other persons, including CFTC registrants, that are not otherwise required to record conversations under CFTC Regulation 1.35(a) should be permitted to voluntarily record their conversations without an obligation to retain such records under any of the Recordkeeping Rules.

The IECA agrees with Commissioner Giancarlo's support of the CFTC's proposed removal of the reference to part 151 (position limits) in § 32.3(c)(2). In addition, the IECA joins Commissioner Giancarlo in his concern that the simple removal of the reference to part 151 does not go far enough. As noted by Commissioner Giancarlo, "position limits for trade options are not 'necessary to diminish, eliminate, or prevent' excessive speculation. The final trade options rule should make clear that trade options are exempt from position limits."<sup>11</sup> The IECA concurs with the reasoning in Commissioner Giancarlo's statement and with his conclusion that the Commission has the authority to exempt trade options from position limits under § 4a(a)(7) of the CEA.<sup>12</sup>

In addition to the reasons included in Commissioner Giancarlo's statement, the IECA believes that the exclusion of trade options from position limits should be covered in the trade options final rule because it will make the industry's feedback in the position limits rulemaking more targeted and meaningful. For example, the industry is currently proposing certain changes to the proposed position limits rule that might not be necessary if the proposed position limits rule excludes trade options. However, if the Commission elects not to clarify the application of position limits to trade options until the position limits final rule, then all the opportunities for feedback (and the dialogue between the CFTC and the industry) during the position limits rulemaking will not have the benefit of this clarification. Moreover, the industry's ability to adequately provide feedback to the Commission on the applicable burdens and costs of implementing position limits will be significantly impacted, which will serve as an impediment to the Commission's and United States Office of Management and Budget's ("OMB") ability to conduct the required cost-benefit analysis and compliance with the Paperwork Reduction Act.

As was the case for the CFTC's swap definition rulemaking, many of the key Dodd-Frank rules were issued prior to defining the term swap.<sup>13</sup> In this regard, it was difficult for impacted parties to provide meaningful comments to the Commission in these rulemakings prior to the Commission providing the swap definition because it was unclear what issues needed to be addressed.<sup>14</sup> This same timing issue is reoccurring between the proposed position limits rule and the trade options rule. Accordingly, as noted by Commissioner Giancarlo, the Commission should clarify the applicability of position limits in the trade options final rule so that the position limits rulemaking can occur in a more targeted and meaningful manner.

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<sup>11</sup> *Notice of Proposed Rulemaking*, 80 Fed. Reg. 26200, 26210 (May 7, 2015)(citations excluded).

<sup>12</sup> *Id.*

<sup>13</sup> For example, the final rules relating to the End-User Exception, Swap Dealer definition, swap recordkeeping and swap reporting were issued before the CFTC issued the swap definition.

<sup>14</sup> [A subsequent comment period was needed after the CFTC issued its swap definition (cite).]

**IV. IECA Is Encouraged by Commissioner Bowen’s Concurring Statement and Urges the Commission to Consider Contracts for the Purchase and Sale of the Capacity to Produce, Generate or Transmit a Nonfinancial Commodity as Itself the Sale of a Nonfinancial Commodity, Which is Coupled with the Sale of a Second Volumetrically Variable Nonfinancial Commodity. Taken Together Such Physical Supply Contracts Satisfy a Specified Portion of an Entity’s Physical Need for Two Nonfinancial Commodities (Including, But Not Limited to Peaking Supply Contracts) and, Therefore, are Not Commodity Options and Should be Excluded from the Definition of Swap**

***A. Physical Supply Contracts that Contain Some Elements of the CFTC’s Traditional Definition of “Commodity Options” Should Not Be Relegated to Swap Status Without Considering How Such Contracts Are Used and the Intent of the Parties to Such Contracts.***

Commissioner Bowen’s Concurring Statement contains the following statements about which we wish to comment:

“Today, we are approving a proposed rule that would implement changes to the Commission’s Trade Option exemption to reduce the burden on commercial entities seeking to hedge risks associated with their physical businesses. ... Further, these physical contracts are often handled and accounted for separately from other derivatives, such as futures contracts or cash-settled swaps, according to market participants. Treating some portion of these physical contracts as swaps simply because they may contain some characteristics of commodity options can lead to significant costs and difficulties. For instance, companies may have to reconfigure their business systems to parse transactions where there was, before Dodd Frank, no need to undertake such a reconfiguration. ... Market participants have also expressed concerns about the appropriate treatment of “peaking supply contracts” which are often used by companies to manage the risks attendant to their need for physical commodities that may be used to generate electricity, run an operating plant, or manufacture or supply other goods and services.”

The IECA thanks Commissioner Bowen for recognizing these bona fide concerns and giving commercial participants an opportunity to respond to her request for comments.

Commissioner Bowen’s Concurring Statement also contains the following statement:

“Market participants have raised concerns about whether or not these contracts could be considered commodity options. In instances where these contracts represent a reservation of a portion of [a] supplier’s capacity to provide a particular commodity and not a transaction for the commodity itself, it seems possible these contracts may not be commodity options.” (Emphasis added.)



The IECA agrees with Commissioner Bowen's statement and urges the Commission to conclude that contracts in which a buyer reserves (i.e., purchases) "a portion of a supplier's capacity to provide a particular commodity" is not a commodity option, but is a forward contract in which the seller sells, and the buyer purchases, a portion of the seller's capacity to provide a particular nonfinancial commodity.

The IECA is attempting to clarify in these TO Comments that the actual purchase of a portion of a supplier's capacity to provide a nonfinancial commodity should, itself, be seen as the purchase and delivery of a nonfinancial commodity.

In many instances, regulatory requirements from a State public utility commission ("PUC") obligate natural gas and electric utilities in that State to purchase "capacity" (sometimes referred to as "resource adequacy") from suppliers and transporters of electricity and natural gas to ensure that the utility can call on that capacity to ensure delivery of the electricity and natural gas required by the utility's customers on one or more days during a month.

In fact, if the utility purchaser does not call on the supplier to deliver the underlying natural gas or electricity, the utility purchaser is recognized by State PUCs and the Federal Energy Regulatory Commission ("FERC") as having purchased control of that capacity and, therefore, having satisfied that portion of its obligation to purchase the ability to supply the underlying natural gas or electricity when and as needed by the utility's customers.

Similarly, when the owner of an electricity generating facility purchases the capacity of a natural gas supplier to provide or transport natural gas to that generator, that purchaser has purchased the ability to procure the fuel required to operate its power plant when and as needed.

In each of these instances, regardless of whether the natural gas or electricity underlying that capacity is called upon and delivered, the purchaser has purchased the supplier's capacity to generate, produce and deliver a nonfinancial commodity and that purchase of capacity itself should be viewed as the purchase of a nonfinancial commodity, rather than the purchase of a commodity option.

The IECA also wishes to make clear that in each of the above instances the buyer is not "hedging" its physical needs for a nonfinancial commodity, at least not "hedging" in the sense of how a commodity option is normally used by a commercial end-user as a financial hedge.

Thus, for example, the buyer is not procuring the right to profit from a change in the value of the underlying commodity, which the buyer will then financially settle and use the financial proceeds to offset the price volatility risk of some underlying physical transaction in the cash market. Rather the buyer is purchasing a supplier's capacity to produce, generate, and deliver the underlying natural gas or electricity thereby ensuring that the purchaser will be able to obtain physical delivery in the moment that natural gas

or electric energy is required by the purchaser to meet the needs of its commercial business.

We wish to clarify that such a purchase of “capacity” is not a financial instrument, but is itself the purchase of a nonfinancial commodity that will enable the purchaser to ensure that the underlying natural gas or electricity (itself also a nonfinancial commodity) is delivered when needed by the purchaser’s commercial business.

As the State PUCs and the FERC recognize, purchasing “capacity” is much more than purchasing a financial instrument or an option, the buyer of capacity is purchasing the physical ability to ensure delivery of the underlying nonfinancial commodity.

***B. The Commission’s Historical Interpretation of Commodity Options, as set forth in the 1985 OGC Interpretation, In Re Wright, the Energy Exemption of 1993, and the Commission’s Recent Products Definition Final Rule Never Addressed the Factual Application of the Forward Contract versus Commodity Option Distinction to the Energy Commodity Transactions Used Today by the Natural Gas and Electric Industries.***

In each of these seminal decisions, the Commission was focused on one key factual question in addressing each of the contracts, namely whether those contracts “impose binding delivery obligations on the parties.”<sup>15</sup> And that became the bright-line test for whether a contract is an excluded forward contract or a regulated commodity option. As described above in Part IV.A of these TO Comments, however, a contract to purchase the “capacity” to produce, generate, supply, or transmit natural gas, electricity (or another nonfinancial commodity), may not impose a binding obligation on the parties to make and take delivery of a specific quantity of natural gas or electricity, but it does impose a binding obligation on the parties to make and take delivery of the capacity. The IECA believes this distinction justifies a conclusion that such capacity contracts are not commodity options, but are in fact excluded forward contracts.

On this basis, the IECA submits that how a contract is used and the intent of the commercial parties to such contract should be the determining factor in the Commission’s analysis of whether a transaction for the purchase of capacity is a commodity option or an excluded forward contract.

Simply saying that any transaction involving a nonfinancial commodity that has a zero or nominal delivery quantity cannot be a forward contract, must be a commodity option, and must, therefore, be a swap, without considering how that contract is used and the intent of the commercial parties to that contract does an injustice to the Commission’s historical analyses of forward contracts.

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<sup>15</sup> See Exemption for Certain Contracts Involving Energy Products, 58 Fed.Reg. 21286 at 21293, published on April 20, 1993 (“Energy Exemption of 1993”).

In many contracts entered into in the natural gas and electric industries, a buyer purchases the seller's capacity to generate or transmit electricity or the capacity to produce or transport natural gas, so that when the buyer's commercial business needs the physical quantities of electricity or natural gas capable of being sold and delivered from that capacity, it can call on that capacity and the nonfinancial commodity will be physically delivered to its commercial business.

Such a physical supply contract has everything in common with the use and objectives of a forward contract entered into by a commercial business and nothing in common with the use and objectives of a speculative commodity option transaction entered into by an investor. And yet, the Commission applies its bright-line test and says this physical supply contract and a speculative commodity option are identical!

Historically, with respect to physical supply contracts, which were given the name forward contracts, the Commission made an exception from its regulatory requirements. The Commission recognized that physical supply contracts, when used by commercial entities to meet their obligations to purchase or sell the physical quantities of a nonfinancial commodity they used in their commercial business, were distinctly different from the way investors used futures and options on futures solely to achieve speculative profits based on the potential change in price of that nonfinancial commodity.

These contracts to purchase the "capacity" do not involve payment of a nominal option premium, followed by payment of the full market price of the nonfinancial commodity if and when the "option" is exercised. Instead, the payment for the capacity quite often recovers for the seller of that commodity the entire fixed cost of producing, generating, supplying or transmitting that commodity. The price to be paid by the purchaser when the capacity is called upon is much less, sometimes only the variable cost incurred by the producer, generator, supplier or transmitter in delivering the nonfinancial commodity.

A commodity option, on the other hand, involves a payment of a somewhat nominal dollar amount as the option premium, followed by payment of the full fixed or floating price of the commodity if and when that option is exercised.

On this basis alone, equating a contract for capacity with a commodity option makes very little sense.

We submit that capacity contracts between commercial participants represent physical supply contracts that were entered into for an entirely different purpose than the purchase of a future or commodity option by a non-commercial participant simply as a speculative investment. The IECA believes this is the same rationale upon which the Commission historically excluded forward contracts necessary to an entity's commercial business as a "producer, processor, or commercial user of, or a merchant handling, a commodity or the products or by-products thereof," and that exception was limited to forward contracts entered into "solely for purposes related to its business as such."

What was important about those decisions, however, was NOT preserving the sanctity of the Commission's interpretive guidelines or a bright-line test. What was important was the Commission's recognition that forward contracts were used by commercial entities to meet the objective of purchasing or selling physical quantities of a nonfinancial commodity that was used in one or both of the counterparties' commercial businesses, while options on futures and commodity options were used by investors as an alternative means of speculating on the future changes in the price of that nonfinancial commodity.

***C. Recognizing the Purchase and Sale of Capacity as, Itself, a Forward Contract for the Sale of a Nonfinancial Commodity, the IECA Believes that Commissioner Bowen's Proposed New Section 32.3(f) can be a Useful Tool for the Commission to Ensure that the Features of a Commercial Participant's Purchasing Capacity to Require Delivery of a Nonfinancial Commodity Will Not be Used by Speculative Investors to Evade the Commission's Jurisdiction.***

Commissioner Bowen's Concurring Statement includes a proposed new Section 32.3(f) to be added to the Commission's regulations. Assuming that the Commission is in agreement with the IECA's clarification that contracts for the purchase of capacity by commercial participants are in fact forward contracts for a nonfinancial commodity (i.e., the capacity), as set forth in Parts IV.A and IV.B above, then the IECA believes that Commissioner Bowen's proposed new Section 32.3(f) is a potentially reasonable means of ensuring that the inclusion of contracts for the purchase and sale of capacity will not be used by speculative investors to evade or avoid the Commission's jurisdiction.

New Section 32.3(f), as proposed in Commissioner Bowen's Concurring Statement, reads as follows:

32.3(f) Instruments Containing a Forward Contract with Volumetric Variability. In the case of an instrument containing a forward contract with volumetric variability that meets the definition of a trade option (as defined by paragraph (a)), the component of such instrument that is a trade option shall be subject to only the requirements of paragraph (d) provided:

- (1) The volumetric variability is not severable nor separately marketable from the forward contract component;
- (2) The volumetric variability is related to and entered into concurrently with the forward contract component; and
- (3) The physical commodity underlying the volumetric variability is the same as that underlying the forward contract component."

So long as the Commission determines that contracts between commercial participants for the purchase and sale of capacity are, in fact, forward contracts, then the IECA suggests that the inclusion of new Section 32.3(f) may be a way forward that works for commercial end-users and achieves the Commission's regulatory goals.

Such a provision is consistent with the Commission’s historical analyses. For example, as the Commission recognized in issuing its Energy Exemption of 1993 (See 58 Fed.Reg. 21286 at 21293): “These Energy Contracts [referring to contracts for the purchase and sale of crude oil, condensate, natural gas, natural gas liquids, or their derivatives] do not provide either party with the unilateral right to offset the contract or discharge its obligations under the contract by a cash payment, except pursuant to a [bona fide termination right].”

The IECA submits that this new Section 32.3(f), coupled with a determination that a contract involving at least one commercial participant for the purchase and sale of the capacity to produce, generate, supply, or transmit a nonfinancial commodity is, in fact, an excluded forward contract, will continue to preserve the Commission’s long-standing recognition of distinguishing between (i) physical supply contracts used by commercial participants to physically settle their purchases and sales of nonfinancial commodities used in their commercial businesses, on the one hand, and (ii) commodity option transactions entered into by investors to speculate on the price movement of the underlying commodity on the other.

**Conclusion.**

The IECA appreciates the opportunity to provide the foregoing comments and information to the CFTC. This letter represents a submission of the IECA, and does not necessarily represent the opinion of any particular member. If you would like for us to expand our discussion of any of the above-listed discussion points, please let us know.

Yours truly,  
INTERNATIONAL ENERGY CREDIT ASSOCIATION

/s/ Phillip G. Lookadoo, Esq. Haynes and Boone, LLP	/s/ Jeremy D. Weinstein Law Offices of Jeremy D. Weinstein
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