

May 9, 2016

Christopher Kirkpatrick
Secretary
U.S. Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: Certain Natural Gas and Electric Power Contracts, RIN 3235-AL93

Dear Secretary Kirkpatrick:

By notice issued April 8, 2016, the Commodity Futures Trading Commission (“CFTC”) and the Securities and Exchange Commission (“SEC”) (collectively “the Commissions”) issued proposed guidance (“Proposal”)¹ concerning “certain contracts that provide for rights and obligations with respect to electric power and natural gas.”² Substantively, the Proposal would remove what the Commissions have characterized as electricity capacity contracts and natural gas peaking supply contracts from the definition of “swap” under the Commodity Exchange Act (“CEA”). The Coalition of Physical Energy Companies (“COPE”) submits this letter in support of the proposal.

The members of COPE are physical energy companies in the business of producing, processing, and merchandizing energy commodities at retail and wholesale.³ COPE members utilize futures and swaps, mainly in order to hedge the risks arising due to commodity price fluctuations and other potential changes affecting their physical businesses. COPE members regularly enter into physical commodity contracts of the types considered in the Proposal and addressed herein. COPE appreciates the Commissions’ efforts to re-examine regulations and requirements implementing the Dodd-Frank Act in order to properly balance the statutory requirements with the need to avoid

¹ *Certain Natural Gas and Electric Power Contracts*, 81 Fed. Reg. 20583 (April 8, 2016).

² *Id.* at 20583.

³ The members are: Apache Corporation; EP Energy LLC; Iberdrola Renewables, LLC; Kinder Morgan, Inc.; MarkWest Energy Partners, L.P.; Shell Energy North America (US), L.P.; SouthStar Energy Services LLC; and Targa Resources.

undue burdens on commercial energy companies who use swaps primarily for hedging purposes, and trade options for supply or marketing purposes in the ordinary course of business.

COPE understands the Proposal to be in addition to, and not in replacement of, any of the Commissions' or CFTC's guidance with respect to the definition of the term "swap" and the transactions to be included thereunder. In other words, the forward/swap distinction articulated in the original "swap" definition release,⁴ the seven-part test for forwards with embedded volumetric optionality,⁵ the CFTC General Counsel Facility Usage Agreement Guidance,⁶ and the CFTC's regulations defining a "trade option"⁷ will continue to apply in full force. The Proposal represents further and independent guidance exempting the specified transactions from definition of "swap." It is based upon this understanding that COPE provides these comments.

COPE has been an active participant in the rulemaking process following the enactment of the Dodd-Frank Act.⁸ COPE has consistently advocated that physically settling transactions be excluded from the definition of swap under the CEA.⁹ The Proposal and the CFTC's recent actions concerning trade options¹⁰ are welcome steps in the right direction. COPE believes that the Commissions efforts to further clarify and refine its regulations are of real value in reducing the ambiguity that commercial energy companies face in their compliance efforts.¹¹ As set forth in this

⁴ Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping (Final Rule), 77 Fed. Reg. 48208, 48227 (Aug. 13, 2012).

⁵ Forward Contracts with Embedded Volumetric Optionality, 80 Fed. Reg. 28239 (May 18, 2015).

⁶ CFTC Office of General Counsel Response to Frequently Asked Questions Regarding Certain Physical Commercial Agreements for the Supply and Consumption of Energy, issued on November 14, 2012.

⁷ 17 C.F.R. § 32.3 (2015).

⁸ See, e.g., COPE Comments to Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping; Final Rule, RIN No. 3038-AD46, filed October 12, 2012; COPE Comments to Interim Final Rule – Commodity Options, RIN No. 3038-AD62, filed June 26, 2012; COPE Comments to Position Limits for Derivatives, RIN Nos. 3038-AD15, 3038-AD16 (filed March 28, 2011); COPE Comments to Interim Final Rule - CFTC Regulation 17 C.F.R. § 1.3(ggg)(iii) (Entity Definitions), RIN No. 3235-AK65, (filed July 23, 2012).

⁹ See, e.g., COPE Comments to CFTC Request for Comment Regarding "Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping; Final Rule, RIN No. 3038-AD46, filed October 12, 2012 ("COPE believes and has advocated that any contract, agreement, or transaction that, by its terms, can only be settled with physical delivery should not be included within the definition of a Swap"); accord Comments of the Coalition of Physical Energy Companies re: Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping (Notice of Proposed Rulemaking)", filed July 22, 2011.

¹⁰ Trade Options (final rule), 81 Fed. Reg. 14966 (March 21, 2016).

¹¹ For example, COPE members have relied on the CFTC's "Office of General Counsel Response to Frequently Asked Questions Regarding Certain Physical Commercial Agreements for the Supply and

letter, COPE believes there is a wide scope of physically-settling transactions that, similar to electricity capacity contracts and natural gas peaking supply contracts, should be excluded from the definition of “swap”.

In the Proposal, the Commissions noted that certain contracts by commercial entities would not be considered swaps. It noted certain characteristics that such contracts shared, which would be as follows (the “Commercial Contract Analytical Framework”):

- They do not contain payment obligations, whether or not contingent, that are severable from the agreement, contract, or transaction;
- They are not traded on an organized market or over-the-counter; and . . .
- In the case of commercial arrangements, they are entered into:
 - By commercial or non-profit entities as principals (or by their agents) to serve an independent commercial, business, or non-profit purpose, and
 - Other than for speculative, hedging, or investment purposes.¹²

The Commissions further noted that the Commercial Contract Analytical Framework set forth above is “not intended to be a bright-line test for determining whether a particular . . . commercial arrangement is a swap.”¹³ COPE agrees with the Commissions that the electricity capacity contracts and natural gas peaking supply contracts meet the Commercial Contract Analytical Framework and should not be considered swaps. Further, COPE can attest that in its experience, virtually every contract that qualifies as a “trade option” under the Commission’s regulations will also meet the Commercial Contract Analytical Framework. As a result, the Commissions should exclude trade options entered into in the normal course of business by commercial firms from the definition of swap.

The fact that the identified contracts include those certain electricity or natural gas contracts should not preclude other energy commodity contracts from receiving similar treatment if they exhibit similar characteristics. For example contracts for serving variable commercial needs of customers for crude oil, propane, jet fuel, and gasoline should be included.

The Commissions’ approach be would more efficient and would remove significant burdens on commercial energy companies if, rather than acting on specific contract types in actions like the Proposal, the Commissions recognized that trade options that are entered into by commercial firms generally meet the standards supporting exclusion under the Proposal and revised the swap definition to only include financially oriented and/or speculative transactions. Since the transactions that would be considered swaps under that standard would only occur in relatively

Consumption of Energy”, issued on November 14, 2012, concerning the interpretation of the “swap” definition with respect to certain physical agreements for facility usage (“OGC Facility Usage Agreement Guidance”). COPE believes that the Commission could proceed to codify the interpretation set forth in the OGC Facility Usage Agreement Guidance in its regulations, as in COPE’s experience the guidance has been relied on by most market participants since its issuance.

¹² Proposal at 20585 (internal citation omitted).

¹³ *Id.* at 20585 (internal citation omitted).

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rare instances, if at all, commercial physical energy companies would be exposed to a significantly lower burden and the Commissions would only be concerned with transactions that are properly considered swaps.

Respectfully Submitted,

/s/ David M. Perlman

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CC: COPE Members

Request for Comment

Request for Comment #1

Request: Are there natural gas and electric power contracts that would not qualify as trade options within the scope of CFTC regulation 32.3 but which would be covered by the proposed guidance? If so, should the proposed guidance be limited so that it encompasses only contracts that do qualify as trade options? Why or why not?

Response: Assuming the proposed guidance is limited to electricity capacity contracts and natural gas peaking supply contracts, then there do not appear to be contracts that would not qualify as trade options. The proposed guidance should be broadened to encompass all trade options – not just electricity capacity contracts and natural gas peaking supply contracts.

Request for Comment #2

Request: Does the proposed guidance provide sufficient clarity on whether the specific types of natural gas and electric power contracts in question should or should not be considered to be swaps? If not, how should the guidance be revised to provide more clarity?

Response: Assuming the proposed guidance is limited to electricity capacity contracts and natural gas peaking supply contracts, then it appears to provide sufficient clarity to determine which contracts are covered. In the event the Commissions determine they would like to clarify the Proposal, COPE believes it is imperative that any clarification be made subject to comment. There are technical components and industry conventions relating to such contracts that could be inadvertently impacted by the Commissions' clarification, rendering qualifying contracts to be excluded.

Request for Comment #3

Request: Are there other facts and circumstances that the CFTC should consider in determining whether the contracts described in Part II.A. are swaps? If so, what are these factors and how should they be considered?

Response: As set forth above, in COPE's experience virtually all trade options meet the types of standards that electricity capacity contracts and natural gas peaking supply contracts meet, causing them to qualify for non-swap treatment. For example, any contract that permits the buyer of an energy commodity to call upon needed supply to satisfy its physical commercial business needs should not be viewed as a swap. That should include crude oil, propane, jet fuel, gasoline, and other such commodities.

Request for Comment #4

Request: Are there contracts (other than those described in Part II.A.) that are entered into by participants in the electric power and natural gas markets and necessitated by, or closely tied to, compliance with regulatory obligations or frameworks that are similar to those described in Part II.A.?

Response: Yes. COPE notes that the Commissions stated that the common characteristics of the specified contracts are that “the particular commodities covered by the contract are needed by at least one of the parties for the normal operation of its business, and the specific identity of the counterparty is an important consideration because of, for example, concerns about reliability or the practicability of supply.”¹⁴

Many trade options used by commercial energy companies meet the listed characteristics and the commercial contract requirements. For example, retail energy marketers providing electricity or natural gas to retail customers must make provision to supply the entire full requirements usage of those customers on a real-time basis. While these are not regulated utility contracts, they share the common need to supply the commodity to end-use retail customers’ demand.

Request for Comment #5

Request: Are there other types of commodity contracts, outside of the electric power and natural gas markets, which are necessitated by, or closely tied to, compliance with regulatory obligations or frameworks that should be considered under the interpretation in the Products Release? If so, please describe these contracts and the regulatory obligations and frameworks to which they are closely tied.

Response: Yes. See response to Request for Comments #4. There are other commodity contracts that “are needed by at least one of the parties for the normal operation of its business, and the specific identity of the counterparty is an important consideration because of, for example, concerns about reliability or the practicability of supply[,]” or otherwise meet the Commercial Contract Analytical Framework. Such contracts would be used to meet immediate commercial needs for commodity supplies to meet the needs of the normal operation of a business. They could include supply of crude oil to a refinery or jet fuel to an airline.

Request for Comment #6

Request: Are there public interest considerations regarding the natural gas and electric power contracts in question that should be reflected in the proposed guidance? If so, why and how?

Response: No.

Request for Comment #7

Request: Does the proposed guidance provide sufficient clarity that it does not supersede or modify the CFTC OGC FAQ referenced in footnote 34? Is there any potential overlap between the proposed guidance and the CFTC OGC FAQ that should be further clarified? If so, what elements of the proposed guidance should be clarified to indicate that the proposed guidance does not supersede or modify the CFTC OGC FAQ?

Response: Yes, sufficient clarity is provided.

¹⁴ Proposal at 20585.

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Request for Comment #8

Request: With respect to natural gas peaking contracts, are there natural gas providers other than LDCs, such as Intrastate and Interstate Natural Gas Pipelines (as those terms are defined by the Energy Information Administration), which are subject to regulatory obligations to prioritize and serve residential demand for natural gas, such that the providers are obligated to curtail service to electric utilities under certain circumstances? If so, please explain.

Response: Not that COPE is aware of.