



Via <https://comments.cftc.gov>

May 9, 2016

Christopher Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

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

Dear Mr. Kirkpatrick:

The Electric Power Supply Association (“EPSA”) respectfully submits these comments on the Commodity Futures Trading Commission (“CFTC” or “Commission”) guidance proposed in response to commenters’ requests regarding certain natural gas and electric power contracts.¹ EPSA appreciates the CFTC’s efforts to add more clarity to the current interpretations excluding certain energy delivery contracts from the definition of a “swap”² in conjunction with the statutory definition of “swap” under the Commodity Exchange Act (“CEA”).³

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. EPSA members utilize a broad variety of commercial tools to ensure the reliable delivery of natural gas, oil, power, and other nonfinancial commodities to their facilities and plant assets located throughout the United States. The proposed guidance will impact how EPSA’s members and other end-users may rely on relief the CFTC has already issued to ensure that their commercial business operations are not unduly encumbered by Dodd-Frank regulations. As such, EPSA has a significant interest in this proceeding. EPSA is very appreciative of the opportunity to comment in this proceeding, as a public comment period can help ensure that the final guidance affirms and does not detract from necessary regulatory relief for commercial end-users. EPSA reiterates that these regulations were not designed to burden nonfinancial entities in the business of delivering affordable and reliable energy to U.S. commercial, industrial, and residential consumers.

¹ Proposed Guidance, Certain Natural Gas and Electric Power Contracts, RIN 3235-AL93, 81 Fed. Reg. 20583 (April 8, 2016) (citing Letter from Cogen Technologies Linden Venture, L.P. (“Linden”) (June 22, 2015); Letter from the International Energy Credit Association (June 22, 2015)). [“Proposed Guidance”].

² Final Rule, Further Definition of “Swap,” Security-Based Swap,” and “Security-Based Swap Agreement”; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, Fed. Reg. 48207 (August 13, 2012). [“Products Release”].

³ Commodity Exchange Act, Definition of “Swap”, 7 U.S.C. Section 1a(47). [“CEA”].

I. Comment Summary

EPSA supports the CFTC's proposal to exclude certain natural gas and power agreements under Section II.B.3 of the Products Release. However, the CFTC should state in its final guidance that these clarifications should only be read in conjunction with, and not to modify, how market participants may apply other interpretations in the Products Release, at Section II.B.2, and/or the more recently finalized EVO Interpretation,⁴ to substantially similar contracts for the purchase and sale of a nonfinancial energy commodity.

The CFTC's proposal discusses excluding from "swaps" certain "capacity" agreements which serve resource adequacy needs. EPSA agrees that these products qualify as "customary commercial arrangements" per the CFTC's proposed guidance and prior interpretations. However, EPSA requests that the CFTC ensure that this guidance will be read consistently with prior Commission and/or staff issuances under which capacity products fall outside the scope of a CFTC-regulated "swap."

The CFTC's proposal would also exclude from "swaps" a fairly unique natural gas commodity/transportation agreement used by Cogen Technologies Linden Venture, L.P. ("Linden").⁵ EPSA supports Linden's request. Further, EPSA strongly urges the CFTC to broaden this clarification to have wider applicability to more commonplace, customary commercial arrangements which include nominal/zero-delivery terms to provide flexibility to end-users, including electric utilities (IOUs), gas utilities (LDCs), and generators:⁶ these entities enter into "peaking" and other customary commercial arrangements that provide for a contractual right but not the obligation to take physical delivery of the nonfinancial commodity to serve load obligations⁷ and/or directly supply end-use residential, commercial, and/or industrial customers.

⁴ Final Interpretation, Forward Contracts with Embedded Volumetric Optionality, 80 Fed. Reg. 28239 (May 18, 2015). ("EVO Interpretation").

⁵ Proposed Guidance (Citing Letter from Cogen Technologies Linden Venture, L.P. ("Linden") (June 22, 2015)).

⁶ See, e.g., Energy Information Administration Glossary, Defined Term: Exempt Wholesale Generator ("Wholesale generators created under the 1992 Energy Policy Act that are exempt from certain financial and legal restrictions stipulated in the Public Utilities Holding Company Act of 1935") at https://www.eia.gov/tools/glossary/index.cfm?id=E#exempt_wg (accessed May 4, 2016). ("EWG").

⁷ FERC Energy Primer: A Handbook of Energy Market Basics, "Supplying Load" (November 2015), at 57-58 ("Suppliers serve customer load through a combination of self-supply, bilateral market purchases and spot purchases. In addition to serving load themselves, load-serving entities (LSEs) can contract with others to do so. The choices are: - Self-supply means that the supplying company generates power from plants it owns to meet demand. - Supply from bilateral purchases means that the load-serving entity buys power from a supplier. - Supply from spot RTO market purchases means the supplying company purchases power from the RTO. LSEs' sources of energy vary considerably. In ISO-NE, NYISO and CAISO, the load-serving entities divested much or all of their generation. In these circumstances, LSEs supply their customers' requirements through bilateral and RTO market purchases. In PJM, MISO and SPP, load-serving entities may own significant amounts of generation either directly or through affiliates and therefore use self-supply as well as bilateral and RTO market purchases."). See also Energy Information Administration Glossary, Defined Term: Load-serving entity (electric) ("Secures energy and transmission service (and related Interconnect Operations Services) to serve the electrical demand and energy requirements of its end-use customers"). ("LSEs").

EPSA also requests that the Commission formally adopt the CFTC staff document – the OGC FAQ Responses⁸ – to provide greater regulatory certainty on the question of which commercial lease-like agreements may be excluded from “swaps.” As the CFTC has inquired how the proposed guidance should interact with the OGC FAQ Responses,⁹ EPSA recommends that the guidance on both counts be formalized together as binding Commission policy. In the event the Commission does not consider formalizing this policy, EPSA requests that the Commission at minimum confirm in its final guidance that it is intended to supplement and complement prior-issued guidance, including the OGC FAQ Responses.

II. Comments

While it is much appreciated that the Commission proposes further clarity, EPSA believes the clarification is too narrowly-construed as proposed. Per the comments below, EPSA respectfully contends that it is more efficient and valuable – for market participants and for the regulator – to issue comprehensive guidance. In general, the proposed guidance can be clearer on the point that both the original Products Release Section II.B.2, and the guidance offered herein under Section II.B.3, provide alternative pathways for similarly situated physical commercial agreements to be excluded from the definition of “swap.”

Additionally, EPSA is concerned that the guidance may have the effect of adding confusion as to the clarity already provided by the CFTC, unless it is expanded to cover commonplace and widely used capacity and natural gas (and other commodity/fuel) arrangements that provide a right but not an obligation to take a minimum delivery to facilitate routine commercial operations without unnecessary disruptions. Finally, EPSA requests that the OGC FAQ Responses be incorporated as formal Commission policy so that all relevant guidance on excluded forward contracts carries the same regulatory weight and can be widely relied on by commercial end-users.

A. The Commission Should Finalize the Proposed Guidance to be Consistent with the Scope of the Products Release Final Rule regarding Excluded Forward Contracts.

1. Capacity Contracts

In its proposal, the Commission states its view that the power “capacity” contracts discussed by certain commenters should be excluded from the “swap” definition under the “customary commercial arrangements” analysis offered in Section II.B.3 of the Products Release.¹⁰ As noted in the proposal, capacity is the ability to generate, *i.e.* to produce some quantity of electric energy in a defined period of

⁸ CFTC’s Office of General Counsel—“Response to Frequently Asked Questions Regarding Certain Physical Commercial Agreements for the Supply and Consumption of Energy,” at http://www.cftc.gov/idc/groups/public/@newsroom/documents/file/leaselike_faq.pdf. (“OGC FAQ Responses”).

⁹ Proposed Guidance, Question 7 (“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?”).

¹⁰ Products Release, 77 Fed. Reg. at 48247.

time, and generally reflects costs associated with operating and maintaining the physical facility so that it can produce the physical commodity when dispatched to serve demand.¹¹ “Capacity” is a separate and distinguishable commodity from “energy,” as “energy” refers to actual generation and reflects more short-term fundamentals such as weather, demand, fuel costs and transmission constraints.

EPSA agrees with the Commission’s analysis that the capacity products discussed in the proposal may be analyzed as customary commercial arrangements excluded from the “swap” definition.¹² However, EPSA requests that the Commission ensure this guidance is provided to supplement, and not to modify in any respect, the prior-issued Products Release and guidance¹³ under which even where certain capacity products do not qualify as customary commercial arrangements, they would still be considered outside the category of “swaps.”

EPSA requests that the CFTC clearly state in its finalized guidance that its interpretation of capacity as a “customary commercial arrangement” is not intended to modify the application of the Products Release and interpretations therein, the ISO/RTO Exemption Order, or the OGC FAQ Responses, to exclude physical commodities such as capacity from the definition of “swap.”¹⁴ This clarification is important to avoid disrupting settled expectations, as the industry has relied on the Products Release final rule and other guidance to exclude physical market capacity products from regulation as “swaps.” EPSA also believes this clarification furthers the Commission’s work to implement the FERC-CFTC Memorandum of Understanding on Jurisdiction. The industry at large will benefit from as much clarity as the Commission can provide in the area of potentially conflicting or overlapping jurisdiction as between state regulators and the CFTC, and between the CFTC and the FERC.

2. Natural Gas “Peaking” Supply Contracts

Although the CFTC’s proposal only addresses Linden’s specific natural gas replacement supply/transportation contract, it is helpful for the CFTC to demonstrate that the Linden contract may be classified as “a contract that would be considered not to be a swap because it is a customary commercial

¹¹ Proposed Guidance at 5-6. *See also* FERC Market Oversight Glossary, Defined Term: Capacity Markets (“A market for the trading of capacity credits (the ability to produce electricity in the market area during a defined period) usually between parties obligated to deliver electricity to customers and power plant owners.”).

¹² Proposed Guidance, at 12.

¹³ Final Interpretation, Forward Contracts with Embedded Volumetric Optionality, 80 Fed. Reg. 28239 (May 18, 2015). (“EVO Interpretation”).

¹⁴ *See, e.g.*, Products Release, Section II.B.2(a) – Interpretation, Nonfinancial Commodities; Final Interpretation, Forward Contracts with Embedded Volumetric Optionality, 80 Fed. Reg. 28239 (May 18, 2015)(“EVO Interpretation”); Final Order in Response to a Petition From Certain Independent System Operators and Regional Transmission Organizations To Exempt Specified Transactions Authorized by a Tariff or Protocol Approved by the Federal Energy Regulatory Commission or the Public Utility Commission of Texas From Certain Provisions of the Commodity Exchange Act Pursuant to the Authority Provided in the Act, 78 Fed. Reg. 19880 (April 2, 2013). (“2013 ISO/RTO Order”).

arrangement” under Products Release Section II.B.3.¹⁵ EPSA supports providing specific clarity to Linden in final guidance stating that such contracts – with or without a minimum delivery term – will not be considered swaps because they are customary commercial arrangements of the type described in the Products Release.¹⁶

However, EPSA does not agree with the CFTC’s preliminary view that the specific contract described in the Linden request is similar to the broad array of commonplace natural gas contracts used by LDCs, IOUs, and generators (with or without a minimum gas delivery requirement.) Linden explains that it sells electricity to a load-serving entity (Consolidated Edison) and also sells the co-generated steam to an end-use customer (Bayway Refinery). It requires replacement contracts to meet these delivery obligations given that it is located behind an LDC city-gate and the LDC has its own priority service obligations which may result in Linden being “bumped” pursuant to the terms of its service from the LDC. Therefore, Linden explains that it must stand ready with contingent supply/transportation contracts in place that can be used to procure fuel from an alternative transportation source. The contracts described by Linden are certainly physical arrangements that qualify for exclusion from the “swap” definition. However, they are dissimilar as compared to more commonplace natural gas and other fuel commodity supply contracts used by generators and utilities¹⁷ to satisfy their own load or directly serve end-use customers.¹⁸ Similar to Linden’s contracts, these physical arrangements also call for the right but not the obligation to take delivery of the commodity (not necessarily transportation).¹⁹

EPSA is very concerned that the current guidance cannot be read to apply to the above-described, broader group of “peaking” and other contingent supply agreements which are pervasive commercial procurement tools used throughout the wholesale and retail natural gas and power markets – especially so by generators, IOUs, and LDCs that have end-use customers and load obligations. Such agreements are substantially similar to Linden’s agreement in that they are being driven exclusively by a commercial purpose in the ordinary course of business. Therefore, the CFTC’s guidance regarding “customary commercial arrangements” should be clarified as having applicability more broadly to nonfinancial commodity supply contracts that are used to meet operational and reliability needs and

¹⁵ Proposed Guidance, at 12, n. 25 (citing the Products Release, 77 Fed. Reg. 48247 (the contracts “do not contain payment obligations, whether or not contingent, that are severable from the agreement, contract, or transaction; [and]...are not trader on an organizer market or over-the-counter.”)).

¹⁶ Proposed Guidance, at 13.

¹⁷ Proposed Guidance, at 6, n.14 (citing as support for “peaking supply contracts” which are “entering to by electric utilities” the letter from the American Gas Association, December 14, 2014, and, letter from the American Gas Association, June 22, 2015).

¹⁸ See, e.g. FERC Energy Primer: A Handbook of Energy Market Basics, “Local Distribution,” (Nov. 2015) at 27 (“Distribution lines typically take natural gas from the large interstate pipelines and deliver the gas to retail customers. While some large consumers – industrial and electric generators, for example – may take service directly off an interstate pipeline, most receive their natural gas through their LDC. LDCs typically purchase natural gas and ship it on behalf of their customers.”).

¹⁹ See, e.g., FERC Energy Primer, *supra*. n. 17, at 37 (“Utilities use algorithms for optimizing the commitment of their generating units, while day-ahead market software does this for suppliers bidding into regional transmission organization markets. In real time, demand is changing all the time. Without storage and responsive demand, the output of some generators must change to follow constantly changing demand.”).

which have variable quantity terms with no specific non-nominal delivery requirement. EPSA suggests that the CFTC state in its finalized guidance that commercial contracts permitting firm variable delivery of a nonfinancial commodity (with or without a minimum delivery obligation) may also be analyzed as a customary commercial agreements excluded from the definition of “swap,” or addressed through interpretations already issued by the Commission in the Products Release.

Finally, the proposed guidance provides that it “would not preclude the CFTC from issuing further guidance considering other commodity contracts under the interpretation[s] in the Products Release.” EPSA respectfully requests that it will be more helpful for the guidance to also confirm that market participants may rely on the facts-and-circumstances approaches laid out in the Products Release, prior exemption orders, and interpretations, to exclude such contracts from “swaps” without having to seek contract-specific guidance. Importantly, neither the term “peaking” nor other such terms apply uniformly to describe a specific type of contract in the natural gas and power industries. Thus, Commission guidance referring only to certain “peaking” contracts would have the effect of providing vague and inconclusive guidance at best. To avoid inadvertent confusion about which entities and which contractual arrangements may rely on this clarification, EPSA urges the Commission to clearly state that beyond the contracts enumerated in its guidance, substantially similar contracts which satisfy the guidance may also be treated as “customary commercial arrangements” excluded from “swaps.”

B. The Commission Should Formalize OGC Guidance regarding Commercial Energy Supply Agreements to Provide Greater Regulatory Certainty to Commercial End-Users in the Natural Gas and Power Industries.

The OGC FAQ Responses document has been a critical piece of the regulatory analysis that end-users have applied to ensure that their ubiquitous, commonplace nonfinancial commodity transportation and storage agreements with pipelines transporting natural gas and/or their power plant tolling agreements, are not mistakenly regulated as “swaps.” Importantly, the same guidance has also been applied extensively to assure commercial, end-user market participants that typical energy commodity transport and storage contracts entered into between load-serving entities, generators, gas utilities, and their counterparty interstate pipelines, intrastate pipelines (under Natural Gas Policy Act Section 311 and intrastate authority), and Hinshaw pipelines (subject to Section 284.244 of FERC’s regulations) are excluded from the definition of a “swap.” This widespread relief has also been instrumental to preventing a serious jurisdictional conflict and overlap between the CFTC and the FERC, as well as between the CFTC and states. As such, the OGC FAQ Responses indicate meaningful progress in the Commission’s implementation of the FERC – CFTC MOU on Jurisdiction.

EPSA does not believe there are any grounds presented as to a question of conflict between the proposed guidance and the OGC FAQ Response.²⁰ Further, EPSA believes there is an opportunity for the Commission to provide heightened regulatory certainty regarding these critical commercial arrangements. EPSA requests that the Commission formally incorporate the OGC FAQ Response into its finalized Commission guidance. This step will creating a binding, reliable, and more resilient regulatory construct around the scope of the forward contract exclusion. Additionally, this request seeks

²⁰ Proposed Guidance, Request for Comment at 15, Q.7 (“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?”).

to formalize staff guidance that is analytically consistent with the Commission’s intended guidance. Both the proposal and the OGC FAQ Responses provide more clarity around the “facts-and-circumstances” approach to analyzing certain energy commodity contracts. And yet, the OGC FAQ Responses will remain a staff letter even though this guidance will be finalized as a Commission issuance. As both documents provide complementary guidance on the exempt status of certain energy contracts from the “swap” definition, the instant proceeding is an appropriate vehicle to jointly formalize both documents as Commission policy. In the event the Commission does not formalize the OGC document as its own guidance, EPSA requests that the Commission at minimum confirm that the guidance is intended to complement the OGC FAQ Responses.

III. Conclusion

EPSA thanks the Commission for the several iterations of interpretative relief that have been provided regarding the definition of “swap.” EPSA also appreciates that the Commission has taken significant action to revise the scope of CFTC Rule 32 so that end-users which do enter into commodity contracts with optionality have very limited recordkeeping requirements and no longer are required to track, quantify, and report their commodity trade options. EPSA also thanks the Commission for the opportunity to file comments in this proceeding. We respectfully request that the Commission revise the proposed guidance to address how it would apply the “customary commercial agreements” analysis to commonplace and widely used capacity and peaking supply contracts in the energy industry. We also request that the Commission incorporate the OGC FAQ Responses into its final guidance so that it bears the same regulatory weight as other interpretations and guidance on the definition of “swap.” Please contact the undersigned should the Commission require further information regarding these requests.

Respectfully Submitted,



Arushi Sharma Frank
Director of Regulatory Affairs and Counsel
Electric Power Supply Association
1401 New York Ave., NW | Suite 1230
Washington, DC 20005
202.349.0151 | asharmafrank@epsa.org

CC: Chairman Timothy Massad
Commissioner Sharon Bowen
Commissioner J. Christopher Giancarlo
CFTC Energy and Environmental Markets Advisory Committee C/O Ajay Sutaria