



September 28, 2017

2017 Project KISS (Miscellaneous)

Via Electronic Submission

Michael Gill, Regulatory Reform Officer
c/o Christopher Kirkpatrick, Secretary
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street, N.W.
Washington, D.C. 20581

RE: Request for Public Input on Simplifying the Application of Rules, Regulations and Practices (“Project KISS,” RIN 3038-AE55) - Miscellaneous

Dear Mr. Gill:

The National Rural Electric Cooperative Association (“NRECA”) and the American Public Power Association (“APPA”) (collectively referred to as the not-for-profit or “NFP Electric Associations,” whose members are customer-owned electric utilities),¹ welcome the Commodity Futures Trading Commission (“CFTC” or “Commission”) “Project KISS” review of its rules, regulations, and practices to identify areas where the CFTC’s requirements can be applied in a simpler, less burdensome and less costly manner. The NFP Electric Associations respectfully submit these comments and recommendations on the Project KISS topic of “Miscellaneous.”²

¹ See Attachment A for a description of the members of each of the NFP Electric Associations. The comments contained in this filing represent the comments and recommendations of the NFP Electric Associations, but not necessarily the views of any particular member of any NFP Electric Association. The NFP Electric Associations are authorized to note to the Commission the involvement of ACES in preparing these comments, and to indicate its full support of these comments and recommendations. ACES provides commercial risk management and energy advisory and operations services for electric cooperatives and government-owned electric utilities in various RTO/ISO regions.

² The NFP Electric Associations have also filed comments on the Project KISS topic “Reporting.” The NFP Electric Associations do not have recommendations on the other Project KISS topics. The members of the NFP Electric Associations are not registered with the Commission (no recommendations on the “Registration” topic). The NFP Electric Association’s members are commercial end-users and enter into swaps solely to hedge or mitigate commercial risks of electric operations, not to trade, deal or speculate in cleared financial instruments (no recommendations on the “Clearing” topic). The NFP Electric Association’s members typically “execute” or enter into a limited number of financial commodity swaps (interest rate and, in a few cases, currency swaps). The members typically enter into nonfinancial commodity swaps (derived on electricity, natural gas and other utility

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The NFP Electric Associations have been active participants in rulemakings implementing the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”),³ which expanded the Commission’s jurisdiction to include regulation of “swaps,” both as traded or “executed” on registered trading facilities and as entered into “over-the-counter,” as bilateral commercial contracts between two counterparties. Beginning in September 2010, the NFP Electric Association and other energy industry trade associations⁴ asked the Commission to clearly define in its rules which nonfinancial energy commodity transactions, entered into as bilateral contracts (off-facility, uncleared), should be considered “swaps” for purposes of the Commission’s rules.⁵ In July of 2011, the NFP Electric Associations proposed language for consideration by the Commission, to more clearly define in the Commission’s rules what is and is not a “swap” for nonfinancial energy commodity transactions.⁶

Throughout the Commission’s Dodd-Frank Act rulemakings, the NFP Electric Associations comments have been narrowly focused on issues important to energy industry “commercial end-users”⁷. We have asked the Commission to use one defined term to describe that important type of entity.⁸ Our members are not financial entities, and their core business is not participation in financial market transactions. The NFP Electric Association members are

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operations-related commodities) as part of the normal course of their electric operation – not on a regulated trading facility, but as bilateral contracts under the Uniform Commercial Code and basic contract law principles (no recommendations on the “Execution” topic, where the topics at issue are almost exclusively related to financial commodity swaps executed on a regulated designated contract market (“DCM”) or a swap execution facility (“SEF”).

³ Pub.L. No.111-203 (2010)

⁴ The NFP Electric Associations have often filed comments with the Large Public Power Council (“LPPC”). Just as APPA’s members are not-for-profit government-owned electric utilities, LPPC’s members are 26 of the largest not-for-profit government-owned electric utilities in the United States. See <http://www.lppc.org/who-we-are/our-members>. In other Dodd-Frank Act rulemaking dockets, the NFP Electric Associations joined the Edison Electric Institute (“EEI”), the Electric Power Supply Association, the American Gas Association, or the Natural Gas Supply Association (in various combinations referred to as the “Joint Electric Associations” or the “Joint Associations”).

⁵ See the NFP Electric Associations initial comment letter in the Dodd-Frank Act rulemakings in response to the Definitions ANOPR: “swap,” “swap dealer,” “major swap participant,” and “eligible contract participant,” 75 Fed. Reg. 51,429 (August 20, 2010), available on the Commission’s website at <http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=26217&SearchText>, as well as EEI’s comment letter in the same docket, available on the Commission’s website at <http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=26193&SearchText>.

⁶ For the NFP Electric Association’s request and proposed rule language, see the comment letter filed July 22, 2011, which is available on the Commission’s website at: <https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=47934&SearchText=>

⁷ The term “commercial end-user” is used herein to mean the category of entities that Congress identified as being “not responsible for the global financial markets crisis of 2008-2009.” See the Lincoln-Dodd letter, dated June 30, 2010, available at <http://online.wsj.com/article/SB10001424127887324059704578473310943230002.html>.

⁸ See the NFP Electric Associations’ comment letter, dated February 22, 2011 on the proposed End-User Exception to Mandatory Clearing of Swaps, RIN 3038-AD-10, available at: <https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=27916&SearchText>.

electric utilities, and they enter into nonfinancial commodity swaps solely “to hedge or mitigate commercial risks”⁹ that arise from each member’s ongoing electric operations. Their nonfinancial commodity transactions, including swaps, are typically with other utilities or other commercial energy companies (not intermediated by banks or other financial market professionals), and are governed by state law, including the Uniform Commercial Code where it is applicable to the sale of goods. Our members’ electric operations are not-for-profit. NRECA’s member cooperatives are directly or indirectly owned by the consumers who receive electric service from the member’s electric operations. APPA’s members are not-for-profit government-owned electric utilities. Each dollar spent on compliance with financial markets rules and regulations is a dollar less that can be invested in infrastructure and electric operations to “keep the lights on” for Main Street businesses and consumers, and is likely to result in higher and more volatile costs for residential, commercial and industrial electricity customers.¹⁰

For commercial end-users like the NFP Electric Associations’ members, the challenge of understanding how to comply with the complex new CFTC rules, interpretations and other guidance applicable to “swap” transactions, begins with the lack of clear definitions for two important terms: “swap” and “commercial end-user.” The NFP Electric Associations respectfully submit the following recommendations to assist the Commission in simplifying the application of its rules, regulations and practices:¹¹

- We recommend the Commission adopt a rule, or one clear set of separately-published interpretations, that distinguishes a “swap” from a nonfinancial energy commodity transaction that is not a “swap,” particularly as the “swap”/not a “swap” line is drawn for off-facility, uncleared transactions entered into as bilateral contracts between commercial end-user counterparties. As part of this recommendation, we urge the Commission to confirm that nonfinancial commodity trade options, where the parties intend physical settlement, are not “swaps,” whether such options are embedded in other transactions, or stand-alone options.
- We recommend the Commission adopt a single definition of “commercial end-user,” and provide an interpretation or a cross-reference list on its

⁹ The quoted language is from subsection (A)(ii) of the Commodity Exchange Act Section 2(h)(7), and subsection (c) of CFTC rule 50.50 promulgated thereunder, which is commonly referred to as the “end-user exception” to clearing a swap subject to a CFTC clearing mandate. The end-user exception was a lynchpin provision of the financial reform legislation that became the Dodd-Frank Act, and a key indicator of Congress’ intention that end-users of “swaps”(entities that use such transactions to hedge or mitigate *commercial* risks), are to be encouraged to hedge or mitigate such commercial business risks, and should be excluded or exempted to the maximum extent possible from the new burdens and costs imposed on swap market participants by the Dodd-Frank Act regulations.

¹⁰ For a more expansive description of the diverse nature of NFP Electric Association members’ electric operations and the commercial risks that arise from such operations, see Attachment B.

¹¹ Each of these recommendations has been made, and explained in more detail, in the prior NFP Electric Association comment letters. For a complete list of the comment letters filed by the NFP Electric Associations in the Dodd-Frank Act rulemakings, please contact one of the signatories to this letter.

website of other entity descriptor terms used in its rules, interpretations and guidance that have the same meaning as, or encompass the term, “commercial end-user,” as well as terms in which the Commission does not intend to include “commercial end-users.”

- We recommend the Commission establish a staff Division or an Ombudsman Office for commercial end-users of nonfinancial commodity transactions: with a policy development function for the Commission’s rules, regulations and practices, as well as an educational portal for commercial end-users seeking to understand the Commission’s jurisdiction.¹²

I. BACKGROUND

The statutory definition of “swap” was enacted as section 721 of the Dodd-Frank Act (“DFA Section 721”), and became Section 1a(47) of the Commodity Exchange Act (the “CEA”) (“CEA 1a(47)”) – a cornerstone of the CFTC’s new and expanded regulatory authority over “swaps.” In the Dodd-Frank Act, Congress also directed the CFTC and the Securities and Exchange Commission (the “SEC”) to engage in a joint rulemaking, in consultation with the Federal Reserve Board, to further define the term “swap”¹³ -- due to the potential overlap in jurisdiction over certain financial commodity derivatives, which were to be regulated by the CFTC, and “security-based swaps,” which were to be regulated by the SEC.

In August 2012, several final rules applicable to insurance products were published jointly by the two Commissions under this authority. These final rules were discussed in Section II.B.1. of the “Joint Final Rule and Interpretations on Further Definition of “Swap,” “Security-Based Swap,” “Security-Based Swap Agreement”; Mixed Swaps; Security-Based Swap Agreement Recordkeeping (17 CFR Part 1) RIN No. 3038-AD46, 77 Fed. Reg. 48208 (the “Products Release”), and the resulting final CFTC rules are found in certain subsections of CFTC rule 1.3(xxx)(4).

Separately, in Sections II.B.2(a) and (b) of the Products Release, the CFTC acting on its own (without the SEC) published several interpretations with respect to nonfinancial commodity transactions that the Commission found to be “outside the scope of the definition of the term ‘swap.’”¹⁴ It is these CFTC interpretations in the Products Release, and not the final rules

¹² In addition to these broad Project KISS recommendations, the NFP Electric Associations are working with other electric trade associations to compile a list of commercial end-user requests for more detailed rule amendments, clarifications of certain inconsistencies in rules, regulations and/or interpretations, as well as requests for codification of interpretations, other guidance and no-action relief that have been submitted to the Commission or the staff over the past 7 years during its Dodd-Frank Act rulemakings. We look forward to working with the Commission and the staff to advance the Project KISS goals.

¹³ See section 712(d) of the Dodd-Frank Act.

¹⁴ See page 48,227 of the Products Release, and footnote 205 which notes that the interpretations in II.B.2(a) and (b) speak only to the definition of “swap” in the CEA, not to the parallel definition of “swap” in the securities laws. In addition to the joint rulemakings with the SEC further defining and interpreting DFA Section 721 and CEA 1a(47),

applicable to insurance products, that are the focus of the ongoing concerns of the NFP Electric Associations and other energy industry commenters.

First and of most concern, the Products Release contains the CFTC's determination, articulated as an interpretation of DFA Section 721 and CEA 1a(47), that all commodity options are "swaps," including nonfinancial commodity trade options (the "All Options are 'Swaps' Interpretation").¹⁵ The Products Release also contains several other interpretations with which the energy industry has struggled for more than five years: an interpretation on "forward contracts with embedded volumetric optionality (the "EVO Interpretation"),¹⁶ an interpretation that certain options with non-nominal put/call volumes might be "swaps" (the "Zero Volume Option Interpretation"),¹⁷ an interpretation on "certain physical commercial agreements, contracts or transactions for the supply and consumption of energy" (the "Physical Energy Transactions Interpretation"),¹⁸ and the Commission's withdrawal of its 1993 "Energy Exemption."¹⁹

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the Commission also unilaterally undertook a separate rulemaking, in a parallel docket, to propose an exemption from its "swap" rules for nonfinancial commodity trade options. The NFP Electric Associations and other energy industry groups have filed comments in both dockets, due to the fundamental importance of distinguishing "swaps" from bilateral energy transactions that are not "swaps," in the context of the CFTC's new regulatory regime. In recent comments on proposed amendments to the commodity trade option exemption, the NFP Electric Associations, LPPC, EEI and EPSA (the "Joint Electric Trade Associations"), discussed the likely reason for the Commission's two-track rulemaking proposals on this topic, and the resulting regulatory complexity, ambiguities and confusion that have resulted. See the Joint Electric Trade Association comment letter on the nonfinancial commodity trade option rules, which can be found on the Commission's website at: <http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=60437&SearchText=wasson> (the "2015 CTO Comment Letter").

¹⁵ This fundamental misinterpretation of the DFA Section 721 and CEA 1a(47) appears at pages 48236-48237 of the Products Release, and is based on two CFTC assumptions, rather than on the words of the statute. In the Products Release, the Commission mistakenly refers to CEA 1a(47)(B)(ii) as the "forward contract exclusion." In subsequent rulemakings, this labeling continues, but without an examination of the words of the statute. Instead, the Commission misinterprets the new statutory exclusion from "swap" narrowly to apply only to forward contracts because of a Commission assumption that the words appear to be *similar* to the pre-Dodd-Frank Act exclusion of nonfinancial commodity forward contracts from the Commission's jurisdiction over futures contracts. In addition, the Commission makes a second assumption: that Congress intended the Dodd-Frank Act to require a significant change to existing law, precedent, economics and commercial business practice and intended the Commission to regulate nonfinancial commodity trade options (physically-settled transactions, previously exempt from financial markets regulation), as if they were financially-settled transactions, i.e., as if physically-settled options were "swaps."

¹⁶ See Products Release at page 48,237.

¹⁷ See Products Release at page 48,239, footnote 343.

¹⁸ See Products Release at page 48,242. This section of the Products Release also contained the Commission's determination not to publish a rule or rules with respect to nonfinancial commodity transactions, as requested by commenters seeking regulatory certainty. See the Products Release at page 48,241. Instead, the Commission explained its history of "facts and circumstances" analysis in distinguishing forward contracts from futures contracts, noting that futures market participants are familiar with that approach, as well as its concern about providing "a roadmap to evasion" (footnote 370). Many commercial end-users of bilateral nonfinancial energy commodity transactions and swaps have remarked that commercial end-users are respectfully seeking a roadmap to regulatory compliance in their bilateral commercial transactions. This section of the Products Release also

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Concurrently with publishing the Products Release, the Commission invited post-publication public comments on these interpretations relative to nonfinancial commodity transactions. In response, the NFP Electric Associations requested reconsideration of the Commission's All Options are 'Swaps' Interpretation, focusing on the fact that nonfinancial commodity trade options are intended to physically-settle.²⁰ The NFP Electric Associations and other energy industry trade associations and commenters also requested withdrawal or clarification of each of the other interpretations applicable to nonfinancial energy commodity transactions.²¹

In December of 2014, the Joint Electric Associations²² reiterated the request for reconsideration of the All Options are 'Swaps' Interpretation, in comments submitted on the proposed revisions to the Commission's EVO Interpretation.²³ Again in June of 2015, the Joint Electric Associations made the same request in comments submitted on the proposed amendment to the Commission's trade option exemption rule.²⁴

The CFTC's determinations and interpretations in the Products Release have been the subject of several subsequent rulemaking proposals, clarifications and other published commentary by the Commission. Various energy industry groups have had discussions with staff. The Office of the General Counsel posted guidance on Physical Energy Transactions Interpretation that has not been codified, and much discussion about the Products Release interpretations has taken place at several Public Roundtables and meetings of the Commission's Energy and Environmental Markets Committee. This evolutionary regulatory process makes it more and more difficult commercial end-users to answer yes or no to a simple question: "is the transaction I am about to enter into a 'swap'?"

As this regulatory evolution has been taking place, the Commission has at the same time been proposing, developing and finalizing many other rules, interpretations and guidance to

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contained other provisions of ongoing concern to the energy industry, including an interpretation requiring "confirmation" of certain "book-out" transactions that are customary commercial arrangements in the energy industry (the "Book-Out Interpretation"). See Products Release at page 48,230.

¹⁹ Exemption for Certain Contracts Involving Energy Products, 58 Fed. Reg. 21,286-02 (April 20, 1993)(the "1993 Energy Exemption Order").

²⁰ See Section X of the October 12, 2012 comment letter, available at: <http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=59235&SearchText> (the "NFP Electrics Products Release Comments").

²¹ See the NFP Electrics Products Release Comments, and many other energy industry comments in that docket.

²² The NFP Electric Associations, EEI and EPSA.

²³ See <http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=60087&SearchText>, Section IV.

²⁴ See the 2015 CTO Letter (noted in footnote 13 above) at <http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=60437&SearchText=wasson>.

implement its new regulatory regime for “swaps.” Such rules include swap recordkeeping and reporting rules, registration requirements and business conduct and documentation rules for new entities like swap dealers, clearing mandates for swaps (and the end-user exception to clearing such swaps), margin rules for uncleared swaps, as well as exemption orders and no-action guidance. In these various dockets and publications, the CFTC often chooses different entity descriptors to identify the types of entities that must comply, or the entities that are exempt from compliance or that benefit from no-action relief and the conditions for such relief.

In order for a NFP Electric Association member to determine (before it enters into a nonfinancial commodity transaction) what its obligations are if the transaction is a “swap” and subject to the CFTC’s regulatory regime, here are just a few of the defined terms it needs to understand: eligible contract participant, swap dealer (“SD”), major swap participant (“MSP”) and non-SD/MSP, commercial market participant, commercial entity, financial entity, special entity, utility special entity, US person, affiliate (in several contexts, with different definitions), records entity, member, participant, unregistered member, reporting party or counterparty, non-reporting party or counterparty, reporting trader (with a reportable position), financial end-user, and “exempt entity” under one or more different definitions in one or more applicable exemption orders. There is no centralized place where the NFP Electric Association member can search for the term “electric utility” or “commercial end-user,” and no one Division or office at the CFTC from which the NFP Electric Association member can seek guidance.²⁵

II. RECOMMENDATIONS

For more than 30 years, energy companies, utilities and other commercial enterprises relied on the Commission’s pre-Dodd-Frank Act “forward contract exclusion,” the nonfinancial commodity “trade option exemption,” and the “swaps exemption” as the basis upon which to enter into commercial contracts and transactions involving nonfinancial commodities without considering the Commission’s regulatory jurisdiction over futures contracts and the futures markets.²⁶ The bilateral swaps markets developed separate and apart from the regulated futures

²⁵ An airline company, farmer, global oil company, cereal manufacturer, chemical company, natural gas local distribution company or any other commercial enterprise, large or small, that enters into nonfinancial commodity transactions as part of its business to produce, manufacture, process or merchandise goods faces the same complex challenge. See former Commissioner Scott O’Malia’s May 11, 2011 speech “Not All End-Users are Created Equal” on the CFTC website at: <http://www.cftc.gov/PressRoom/SpeechesTestimony/opaomalialia-6>.

²⁶ Bilateral commodity trade options and forward contracts are considered “physical” or “cash market” contracts -- transactions for which the parties anticipate or intend actual delivery of the “physical” commodity or the “cash commodity.” It is physical delivery/receipt of the nonfinancial commodity, also referred to as “physical settlement,” that distinguishes forward contracts and commodity trade options from financially-settled derivatives contracts, including futures contracts (“contracts of sale for future delivery of a commodity”), financially-settled options, and swaps. In addition, the energy industry relied on the 1993 Energy Exemption Order. Commercial energy companies enter into such nonfinancial energy commodity transactions in the ordinary course of their business with commercial contract counterparties (often with assets or operations in the same region) with whom they have done business for decades, on handshakes, on master contracts and periodic purchase orders, or on 100+ page, multiple commodity, multiple delivery point commercial contracts lasting decades or longer. Over-the-counter nonfinancial commodity swap documentation follows the same pattern. Such transactions are relationship based, and there may or may not be credit support posted by either side. Cash margin is seldom posted or exchanged daily on a trade-by-trade basis, as is the case in financial markets where anonymous dealers, buyers and sellers trade financial instruments or products.

contract trading markets, under commercial contracting laws, principles and practices customary in particular industries that required the underlying commodity, and mirrored the industry's need to hedge commercial risks associated with ongoing business operations.

During the last 7 years, the Commission's rules, regulations and practices implementing its new Dodd-Frank Act authority over "swaps" have become more and more complex and inaccessible for commercial end-users like the NFP Electric Associations' members, due in no small part to a lack of clarity as to what is and is not a "swap," which counterparties are and are not considered "commercial end-users" (either as an entity test for "commercial end-user only" entities or, if tested on a transaction-by-transaction basis, for commercial entities that enter into swaps to "hedge or mitigate commercial risks" rather than for speculating, trading or dealing), and what a commercial end-user's obligations are once it enters into a "swap" in order to comply with the CFTC's rules, regulations and practices.

- A. We recommend the Commission adopt a rule, or one clear set of separately-published interpretations, that distinguishes a "swap" from a nonfinancial energy commodity transaction that is not a "swap," particularly as the "swap"/not a "swap" line is drawn for off-facility, uncleared transactions entered into as bilateral contracts between commercial end-user counterparties. As part of this recommendation, we urge the Commission to confirm that nonfinancial commodity trade options, where the parties intend physical settlement, are not "swaps," whether such options are embedded in other transactions, or stand-alone options.**

When an NFP Electric Association member makes a long-term commitment that involves a nonfinancial commodity like electricity, generation capacity, natural gas, coal or another fuel for generation,²⁷ electric operations managers use business judgment to decide: (a) whether the electric company will "hedge or mitigate" anticipated commercial risks by (i) entering into a forward contract or a commercial (risk-reducing) contract or arrangement customary in its industry - the electric utility industry, or (ii) buying a futures contract, or (iii) entering into a "swap" or a commodity trade option, or (b) alternatively, whether the cost of hedging that commercial risk, including the regulatory uncertainty of whether a particular transaction is (or may be) a "swap," is simply too high.²⁸ Over the past 7 years, many commercial end-users have reduced their commercial risk hedging activities due to the regulatory uncertainty of potentially entering into a "swap," and the potential ongoing CFTC compliance burdens and costs if the particular transaction is determined to be a "swap."

The NFP Electric Associations recommend that the Commission simplify its rules, regulations and practices by clearly defining what is and is not a nonfinancial commodity

²⁷ For example, how to hedge the risk (weather) that necessary natural gas fuel supply will be interrupted next winter, whether to sign a 20-year tolling agreement for a coal plant, whether to buy a storage facility for fuel for generation or a battery storage unit for electricity, whether to build generation or buy electric commodities to reliably serve its utility customers in the future.

²⁸ See comments made at the Commission's Public Roundtable on April 3, 2014, where participants noted that even the larger, more sophisticated energy companies have dramatically reduced their use of nonfinancial energy commodity swaps to hedge or mitigate commercial risks of ongoing business operations.

“swap,” in a rule or in a separately-published set of interpretations focused on the plain language of the CEA 1a(47)(A) and (B)(ii).²⁹

Section 1a (47) provides in relevant part that:

“1a (47) SWAP—

(A) IN GENERAL— Except as provided in subparagraph (B), the term “swap” means any agreement, contract, or transaction—

(i) that is a put, call, cap, floor, collar, or similar option of any kind that is for the purchase or sale, or based on the value, of 1 or more interest or other rates, currencies, commodities, securities, instruments of indebtedness, indices, quantitative measures, or other financial or economic interests or property of any kind;

(B) EXCLUSIONS.—The term “swap” does not include—...

(ii) any sale of a nonfinancial commodity or security for deferred shipment or delivery, so long as the transaction is intended to be physically settled;”(emphasis added)

CEA 1a(47) provides that a commodity option is a “swap,” *except* (as noted in the lead in to CEA 1a(47)(A)) if the nonfinancial commodity transaction for deferred shipment or delivery is intended to be physically settled. Whether the transaction at issue is a nonfinancial commodity forward contract without or with “embedded optionality,” or a “standalone” commodity trade option, if the transaction is intended at inception to be physically settled(if indeed by its terms the transaction can *only* be physically settled and not financially settled), the transaction is simply not a “swap.” The transaction is excluded from the term “swap” by CEA 1a(47)(B)(ii).

The NFP Electric Associations respectfully reiterate earlier requests that the Commission withdraw or reconsider the All Options are ‘Swaps’ Interpretation. In addition, the NFP Electric Associations respectfully reiterate earlier requests that the Commission confirm that nonfinancial commodity trade options, whether such options are embedded in forward contracts or stand-alone, are excluded from the definition of “swap” by CEA 1a(47)(B)(ii).³⁰

²⁹ As noted, the NFP Electric Associations have commented on this topic since September 2010, and proposed language for Commission rules in July of 2011 (see the comment letter links at footnotes 5 and 6 above. In the 2015 CTO Comment Letter, the Joint Electric Trade Associations explain in detail how the Commission’s publication of the Products Release interpretations and the CFTC Rule 32.3 in 2012 initially created the confusion, and also how the evolution of those two rulemaking dockets since 2012 bridges some, but not all, of the regulatory uncertainty in evaluating nonfinancial energy commodity transactions. The 2015 CTO Comment Letter nonetheless reiterates the 2012 request that the Commission withdraw or reconsider the Products Release interpretations. See section VI of the 2015 Comment Letter.

³⁰ This will simplify the Commission’s rulemaking going forward, as it will no longer be necessary to confirm in future rulemakings, such as the speculative position limits rules or swap recordkeeping or reporting rules, that commodity trade options (which will no longer be interpreted to be “swaps”) are not included. It will also simplify rulemaking by other regulatory agencies that incorporate by reference the Commission’s defined term “swap.” The appropriate answer in each case will be built into the defined term: regulations that cover “swaps” do not and should not cover a commodity trade option, because a commodity trade option is not a “swap.”

The NFP Electric Associations also respectfully recommend that the Commission simplify compliance by withdrawing the Zero Volume Option Interpretation and the EVO Interpretation. These two interpretations essentially become unnecessary once the All Options are ‘Swaps’ Interpretation is withdrawn, i.e., once stand-alone or embedded options or “optionality” are not viewed as potential indications that the transaction may be a “swap.” The NFP Electric Associations also respectfully recommend that the Commission simplify compliance by withdrawing the Physical Energy Contracts Interpretation, which similarly raises confusion about certain “option-like” characteristics in nonfinancial energy commodity transactions. Such commercial energy transactions (including tolling agreements, and natural gas transportation and storage contracts) are customary commercial arrangements in the energy industry. Absent atypical facts and circumstances, such arrangements are, and should be, excluded from the definition of “swap” under the separate “Customary Commercial Arrangements” interpretation, adopted jointly by the CFTC and the SEC in section II.B.3. of the Products Release.³¹

At Public Roundtables and EEMAC Meetings subsequent to the Products Release, each of these interpretations has been raised as a potential misunderstanding by the Commission or staff of the way in which certain energy commodity markets work, and/or a potential misunderstanding about the various ways in which different types of commercial energy companies transact to hedge or mitigate commercial risks arising from ongoing business operations.³²

³¹ See Products Release at page 48,246 et seq. In response to questions about how the Physical Energy Contracts Interpretation should be applied, first the Office of General Counsel issued guidance (that has not been codified or even included in a Commission interpretation) about one paragraph, commonly referred to as the “however” provision, in the Products Release. More recently, the Commission published additional proposed guidance where it validated the use of the “Customary Commercial Arrangement” interpretation exclusion from the definition of “swap” for certain nonfinancial energy commodity transactions. See Proposed Guidance on Certain Natural Gas and Electric Power Contracts (RIN 3235-AL93), 81 Fed. Reg. 20,583 April 8, 2016 (the “2016 Proposed Guidance”). See also the NFP Electric Associations’ comments, filed in conjunction with EEI, in that docket, available at <http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=60795&SearchText=>. All of the physical energy contracts listed as potentially of concern in the Physical Energy Contracts Interpretation are Customary Commercial Arrangements in the energy industry, and meet the criteria to benefit from the Customary Commercial Arrangements interpretation. There is no reason to leave in place the Physical Energy Contracts Interpretation that has created confusion since 2012.

³² The NFP Electric Associations recommend that the Commission also consider whether it should reinstate the Energy Exemption (as an exemption from the definition of “swap”) until such time as its rules, interpretations and guidance are revised. As an ancillary matter, we also recommend the CFTC withdraw the Documentation of Bookouts Interpretation in the Products Release, which requires written confirmation of an oral “book-out” of a nonfinancial commodity forward transaction to assure that such transaction will not be considered a “swap.” As described in numerous post-publication comments on the Products Release, and in energy industry meetings with the Commission and staff, this is an unnecessary documentation requirement for a transaction otherwise outside the Commission’s regulatory jurisdiction and for a customary commercial arrangement in the energy industry. The interpretation seems retroactively to call into question whether a nonfinancial commodity forward contract was or was not, or is or is not, a “swap.” Finally, we recommend that the CFTC withdraw another confusing (and incomplete) interpretation found in the Products Release, that a guarantee of a swap is considered part of, or may be itself, a “swap.” See the Products Release at 48,226. In that interpretation, the Commission again speaks only for itself, and not for the SEC, and promises to address the practical implications of this interpretation in a separate release, which the CFTC has never published. Parent guarantees are a customary form of counterparty credit

- B. We recommend the Commission adopt a single definition of “commercial end-user,” and provide an interpretation or a cross-reference list on its website of other entity descriptor terms used in its rules, interpretations and guidance that have the same meaning as, or encompass the term, “commercial end-user,” or terms in which the Commission does not intend to include “commercial end-users.”³³**

The CFTC could fundamentally simplify its rules, regulations and practices by clearly defining the term “commercial end-user,” and providing an interpretation or guidance document on the CFTC website identifying all the entity descriptor terms used by the Commission and the staff in various rules, interpretations and guidance that mean or, in effect include, “commercial end-users.”

The NFP Electric Associations’ members are commercial businesses (the term includes not-for-profit businesses)³⁴, as distinguished from financial entities, institutions or dealing or trading operations. Commercial end-users own physical assets, manufacture or distribute goods, buy and sell commercial goods or provide commercial services. They are Main Street businesses whose primary business is not investing in, trading or dealing in financial assets or financial instruments. Commercial end-users are not registered as financial market professionals with the CFTC, the SEC, or comparable global financial market regulators; nor are such commercial end-users “prudentially regulated” by banking, or “safety and soundness,” regulators. Nonetheless each commercial business involves managing, mitigating, hedging or accepting the specific commercial risks that arise in its nonfinancial industry. For the NFP Electric Associations’ members, our industry is the electric utility industry.

If a member of the NFP Electric Association (or another commercial end-user) wants to understand the CFTC’s rules govern its nonfinancial energy commodity transactions, there is no way to search seven years (and counting) of CFTC rules, interpretations and guidance in the Federal Register and/or on the CFTC’s website for the term “commercial end-user” used within a certain proximity to the word “swap.” In the CFTC’s pre-Dodd-Frank Act rules and regulations, these entities were commonly referred to as “customers.” In the various Dodd-Frank Act rulemakings, and in current CFTC rules, interpretations and guidance, there are many different entity descriptors. For example, the Products Release uses futures industry terms such as “commercial market participant”³⁵ and “commercial entity,” but not “commercial end-user.” In

Continued from previous page

support in the commercial energy industry, and this dangling five year old interpretation causes unnecessary regulatory uncertainty and costs.

³³ Concurrently, we recommend excluding or exempting “commercial end-users,” or swaps to which two commercial end-users are contractual counterparties, from complex and burdensome financial market Reporting obligations in the Project KISS Reporting docket.

³⁴ See the adopting release for the End-User Exception to the Clearing Requirement for Swaps, 77 Fed. Reg. 42,560 (July 19, 2012) at 42,572, text at footnote 56.

³⁵ From the Brent Interpretation with respect to nonfinancial commodity transactions in the global oil markets, and distinguishing forward contracts in such markets from futures contracts. See the Products Release discussion of the Brent Interpretation at 77 Fed. Reg. 48,228 et seq.

some Dodd-Frank Act swap reporting rules, these entities are called “non-SD/MSPs” or “non-SD/MSP counterparties,” to distinguish them from registered swap dealers (“SDs”), major swap participants (“MSPs”). For purposes of understanding other Dodd-Frank Act swap rules and no-action relief, a commercial end-user must also determine that it is not a “financial entity” (a term used in the end-user exception to clearing), and not a “financial end-user” (a term used in the margin rules for uncleared swaps). In the 2014 Commission staff request for comments on its Review of Swap Data Recordkeeping and Reporting Requirements (79 Fed. Reg. 16689, RIN 3038-AE12) (the “2014 Staff Review,” see Section II below), the term used was “non-registrant,” meaning that commercial end-users are not registered with or regulated as entities by the Commission. In the Commission staff’s request for comments on draft technical specifications for certain swap data elements, issued December 22, 2015 (the “2015 Tech Spec Request”), commercial end-users were designated “unregistered swap counterparties” to distinguish them from the swap data reporting parties otherwise registered under the CFTC rules, including SDs, MSPs, DCMs, SEFs, and derivatives clearing organizations (“DCOs”). See the 2015 Tech Spec Request, in footnote 5, at page 4. In the recent amendments to the Commission’s general recordkeeping rules, a new term “records entity” is defined and assigned regulatory obligations. See 82 Fed. Reg. 24,479 (May 30, 2017). Only by identifying where a commercial end-user’s regulatory obligations might be more narrowly “specified elsewhere in the [Commodity Exchange] Act or Commission regulations in this chapter,” and presumably in other Commission interpretations and guidance, can a commercial end-user understand its recordkeeping obligations as a “records entity.”

The NFP Electric Associations’ members are all commercial end-users (and fall within each of these other defined terms in the CFTC’s rules). However, the NFP Electric Associations respectfully reiterate prior requests for a single defined term for “commercial end-user,” and consistent use of such term, to simplify and harmonize the various Commission rules, interpretations and guidance applicable to swaps, swap counterparty entities and swap compliance obligations.

Until such time as the CFTC’s rules can be adapted to use a single defined term, it would simplify the CFTC’s rules, regulations and practices for commercial end-users if, on the CFTC’s website, there were a cross-referencing of other defined terms that either mean, or include within their scope, commercial end-users and, conversely, a list of terms that the Commission does not consider to include commercial end-users.

C. We recommend the Commission establish a Division or an Ombudsman Office for commercial end-users of nonfinancial commodity transactions and “swaps”: with a policy development function for the Commission’s rules, regulations, interpretations, guidance and practices, as well as an educational portal for commercial end-users seeking to understand the Commission’s jurisdiction

Attachment C depicts the different stages of market structure development, and differing degrees of globalization, for swap asset classes, and various categories and types of nonfinancial commodity swaps. In the outer concentric circles, the swaps are almost exclusively bilateral contracts.³⁶ Moreover, as one moves toward the outermost circles, there is increased

³⁶ At this time, there are virtually no nonfinancial commodity swaps executed on a DCM or a SEF.

customization and complexity of swap data elements. In the outer concentric circles, there is also an increasing number of commercial end-user-to-end-user swaps.

In these outer concentric circles, there are large and small commercial end-users from many different industries.³⁷ Some of these commercial end-users, including many of the 2500 NFP Electric Association members, are “small entities,” as such term is defined for purposes of the Regulatory Flexibility Act, as amended by the Small Business Regulatory Enforcement Fairness Act (collectively, “SBREFA”). SBREFA requires Federal agencies to take steps to collect input from small entities on regulations, and to determine whether a rule is expected to have a significant economic impact on a substantial number of small entities.³⁸ Moreover, Federal agencies are required to identify alternative regulatory approaches to reduce regulatory burdens on small businesses, small governmental jurisdictions and non-profit organizations.³⁹ Some of these commercial end-users enter into very few swaps per year, and only to hedge or mitigate commercial risks of ongoing operations. In the outermost concentric circle, there is also at least one other Federal regulator of the underlying nonfinancial commodity markets, the Federal Energy Regulatory Commission (“FERC”). In the Dodd-Frank Act, Congress acknowledged and confirmed FERC’s jurisdiction over the natural gas and electric industries,

³⁷ For example, not-for-profit entities like the NFP Electric Associations members and utilities with public service obligations under state utility law or other governance regimes like electric cooperatives and government-owned utilities.

³⁸ SBREFA incorporates by reference the definition of “small entity” adopted by the Small Business Administration (the “SBA”). Using the SBREFA criteria for small business size regulations, the vast majority of NRECA’s 900 members meet the definition of “small entity” (13 C.F.R. §121.201, as modified effective January 22, 2014. See 78 Fed. Reg. 77343 (December 23, 2013)). Only three generation and transmission cooperatives would be expected not to meet the definition. In addition, most of APPA’s more than 2,000 members also meet the definition of “small entity.”

³⁹ As part of the Commission’s overview of its post-Dodd-Frank Act rulemakings implementing its regulatory jurisdiction over nonfinancial commodity swaps, the NFP Electric Associations’ respectfully reiterate prior requests in the Dodd-Frank Act rulemakings that the Commission conduct the required SBREFA analysis for the benefit of “small entities,” including the NFP Electric Associations’ members. The Commission should conduct the analysis not just on a rule-by-rule basis, but should consider the overall effect of its regulation of nonfinancial energy commodity swaps. To date, the Commission has dismissed such NFP Electric Association requests, or discounted its responsibilities, by repeatedly citing its own outdated determination, in a context separate from and well before the Dodd-Frank Act jurisdiction over “swaps,” that “eligible contract participants” are not “small entities,” in *Opting Out of Segregation*, 66 Federal Register 20740 at 20743, April 25, 2001. In other Dodd-Frank Act rulemakings, the Commission states, without support, that individual rulemakings would not directly affect a substantial number of “small entities.” See, for example, the Commission’s *Position Limits for Derivatives* rulemaking, 78 Fed. Reg. 75784 footnote 847. The 2001 determination cited by the Commission itself, not the Small Business Administration, contains no analysis as to why the Commission makes its conclusory assertion, and provides no analysis applying the SBREFA criteria to various categories of “eligible contract participants” in the bilateral nonfinancial commodity swaps markets. In other rulemakings, the Commission acknowledges that some number of eligible contract participants that transact in energy swaps may be “small entities,” but dismisses the NFP Electric Associations’ request on behalf of the small entities they represent to conduct the required SBREFA analysis by saying there are only a few such “small entities.” See, for example, the *Trade Option IFR* at 77 Fed. Reg. 25320 and 25335-25336 (April 27, 2012). The NFP Electric Associations respectfully submit that “small entities” that enter into bilateral nonfinancial commodity swaps, including the more than 2500 NFP Electric Association member “small entities,” deserve the full regulatory review afforded them by SBREFA.

and instructed the Commission to work with FERC as the Commission implements its new regulatory authority for swaps, to avoid overlapping and duplicative regulation.⁴⁰

The Commission could simplify its rules, regulations and practices, and reduce regulatory costs and burdens for commercial end-users in many industries, by establishing a Division or Ombudsman office for commercial end-users of nonfinancial commodity swaps.⁴¹ In the post-Dodd-Frank Act world, there is no obvious entry point to the Commission for a commercial end-user that wants to understand the Commission's jurisdiction over its bilateral nonfinancial commodity swap transactions entered into to hedge or mitigate commercial risks. From an institutional perspective, there is also no centralized repository for staff expertise and ongoing interaction with commercial industry groups, such as the energy industry trade associations, and commercial end-users whose core business activities are in those industries. There is no particular CFTC Division responsible for understanding how different nonfinancial commodity markets function (which is differently than financial commodity markets), and the ways in which commercial end-users in different commercial industries hedge commercial risks that arise in their energy, agricultural and other "Other Commodity" businesses.⁴²

The NFP Electric Associations appreciate the opportunity to submit these comments on the Commission's Project KISS, and look forward to working with the Commission to simplify application of its swap rules.

[Signature page to follow]

⁴⁰ See Sections 720 and 722(e), (f) and (g) of the Dodd-Frank Act, as well as CEA Section 2(a)(1)(i) and 4(c)(6).

⁴¹ Before the Dodd-Frank Act, these commercial end-users (or "customers") were not directly regulated by the Commission as entities. Futures products were standardized and detailed product descriptions were submitted to the Commission by the exchanges. The Commission's divisional structure was divided appropriately to focus on registered futures market professionals and futures market utilities, including exchanges, clearinghouses, futures commission merchants, commodity trading advisors, etc.

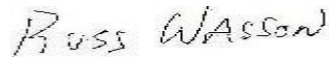
⁴² In 2014, then Commissioner Bart Chilton published an "End-User's Bill of Rights," which called for an "End-User Advisory Committee." <http://www.cftc.gov/PressRoom/SpeechesTestimony/chiltonstatement040313> See also the Commissioner Scott O'Malia's speech cited in footnote 23 above titled "'Not All End-Users are Created Equal.'" The NFP Electric Associations participate as advisory members on the EEMAC Advisory Committee, and appreciate that periodic opportunity to present views from the industries. However, we note that because the advisory committees focus on swaps *and futures* market issues, on-facility and off-facility transactions, and on issues facing market professionals and market utilities as well as commercial end-users, the advisory committees tend to focus on global, standardized, traded swaps that may be considered "lookalikes" to futures contracts, and not on off-facility, bilateral, customized swaps most used by commercial end-users to hedge commercial risks. We recommend a CFTC staff function to focus on the bilateral nonfinancial commodities markets by industry, in order to embed the commercial industry knowledge within the agency.

SIGNATURE PAGE

2017 PROJECT KISS (MISCELLANEOUS)

The NFP Electric Associations appreciate the opportunity to submit recommendations to be considered in connection with Project KISS (Miscellaneous).

Respectfully submitted,



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Honorable Rostin Behnam
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ATTACHMENT A

DESCRIPTION OF THE NFP ELECTRIC ASSOCIATIONS

The National Rural Electric Cooperative Association (NRECA) is the national service organization for America's electric cooperatives. The nation's member-owned, not-for-profit electric cooperatives constitute a unique sector of the electric utility industry – and face a unique set of challenges. NRECA represents the interests of the nation's more than 900 rural electric utilities responsible for keeping the lights on for more than 42 million people across 47 states. Electric cooperatives are driven by their public service purpose to power communities and empower their members to improve their quality of life. Affordable electricity is the lifeblood of the American economy, and for 75 years electric cooperatives have been proud to keep the lights on. Because of their critical role in providing affordable, reliable, and universally accessible electric service, electric cooperatives are vital to the economic health of the communities they serve.

America's electric cooperatives serve 56 percent of the nation, 88 percent of all counties, and 12 percent of the nation's electric customers, while accounting for approximately 11 percent of all electric energy sold in the United States. NRECA's member cooperatives include 63 generation and transmission (G&T) cooperatives and 834 distribution cooperatives. The G&Ts are owned by the distribution cooperatives they serve. The G&Ts generate and transmit power to nearly 80 percent of the distribution cooperatives, those cooperatives that provide power directly to the end-of-the-line consumer-owners. Remaining distribution cooperatives receive power directly from other generation sources within the electric utility sector. NRECA members account for about five percent of national generation and, on net, generate approximately 50 percent of the electric energy they sell and purchase the remaining 50 percent from non-NRECA members. Both distribution and G&T cooperatives share an obligation to serve their members by providing safe, reliable, and affordable electric service.

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

ATTACHMENT B

NFP ELECTRIC ASSOCIATIONS' MEMBERS COMMERCIAL RISK HEDGING

As discussed in Prior Comments, Utility Operations-Related Swaps are much more likely than financial commodity swaps to be customized, to be transacted or executed off-facility (via bilateral contracts), and to be uncleared. Each commodity type underlying a Utility Operations-Related Swap has its own unique quantification measures (MMBtus, MWs, decatherms, or other units). Each commercial end-user has valuation and pricing methodologies tied to the underlying commodity markets and to the specific operational or commercial risks being hedged. Delivery location and other aspects are key to value in the underlying commodity transaction or asset (power delivered in California has no value in Massachusetts). Unique commercial pricing contingencies and permutations (based on transmission/transportation constraints, available storage assets, weather, economic conditions) and the long-term commercial relationship between the parties, as well as particular creditworthiness characteristics of the commercial end-user counterparty, are all important, customized terms of a bilateral Utility Operations-Related Swap.

For Utility Operations-Related Swaps, there are also unique and unusual commercial end-user market participants, such as state utility-regulated and/or FERC-regulated counterparties, as well as not-for-profit utilities, such as NFP Electric Associations' members, with public service obligations and that *only* enter into such swaps to hedge commercial risks arising from ongoing utility operations in a particular geographic region.

Each of the NFP Electric Associations' members use Utility Operations-Related Swaps to hedge or mitigate the commercial risks arising from such member's unique ongoing electric operations. Every member is exposed to different, but identifiable, "commercial risks" arising from, and in many respects unique to, such member's ongoing electric operations and assets: fuel supply risk, location risk, delivery risk, weather risk, time risk, execution risk, political risk, counterparty risk, market risk, regulatory risk, and other operational risks. Each member makes ongoing business judgments about the best and most cost-effective way to either manage, hedge or mitigate each of the unique commercial risks that arise from its particular electric operations.

An NFP Electric Association member typically enters into a Utility Operations-Related Swap with another NFP Electric Entity⁴³ or with another commercial energy company with assets or businesses in the same geographic region— a commercial end-user rather than a financial institution or financial entity. Such a commercial end-user may either (a) conducts energy commodity swap activity as an ancillary business to its principal commercial business in natural gas production or transportation, or as a utility, merchant generator or energy marketer, where

⁴³ The "between NFP Electrics" transaction would be exempt from DFA Swap Reporting Rules and most other Dodd-Frank Act swap regulations under the Order Exempting Certain Transactions [Between NFP Electrics], 78 Fed. Reg. 19.670 (April 2, 2013).

dealing activity is below the threshold requiring registration as a “swap dealer” or (b) is itself entering into the Utility Operations-Related Swap to hedge or mitigate commercial risks arising from the counterparty’s own business operations (in either case, another “commercial end-user”). All these unique features of the narrow sector of the global swaps market in which the NFP Electric Association members participate makes the one-size-fits-all DFA Swap Transaction Data Reporting Rules, with unlimited data elements including several asking the reporting party to add any other material terms, difficult to interpret for Utility Operations-Related Swaps.

ATTACHMENT C - MARKET STRUCTURE DEVELOPMENT CHARACTERISTICS BY SWAP ASSET CLASS

