AGA American Gas Association

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Submitted electronically

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Re: De Minimis Exception to the Swap Dealer Definition RIN 3038-AE68

Pursuant to the De Minimis Exception to the Swap Dealer Definition Notice of Proposed Rulemaking ("NOPR") published in the Federal Register on June 12, 2018,[1] by the Commodity Futures Trading Commission ("CFTC" or "Commission"), the American Gas Association ("AGA") respectfully submits these comments. AGA believes that the regulations implementing the Dodd-Frank Wall Street Reform and Consumer Protection Act (''Dodd-Frank Act'')[2] should ensure that the financial markets related to energy commodities function efficiently and protect the ability of commercial hedgers to engage in risk management activities for the benefit of American energy consumers at a reasonable cost. For the reasons discussed below, AGA: (1) supports setting the aggregate gross notional amount ("AGNA") threshold for the *de minimis* exception at $8 billion in swap dealing activity entered into by a person over the preceding twelve months; (2) supports the addition of a hedging exception to *de minimis* calculations for swaps that hedge either physical or financial positions; and (3) urges the Commission to reconsider its delegation of authority for determining the methodologies for calculating notional amounts for purposes of determining whether a person exceeds the AGNA *de minimis* threshold because the process does not provide an opportunity for public notice and comment.

I. IDENTITY AND INTERESTS

The American Gas Association, founded in 1918, represents more than 200 state-regulated and municipal natural gas utility companies that deliver clean natural gas to more than 177 million Americans. AGA also advocates for the more than 73 million residential, commercial and industrial natural gas customers in the U.S., of which 95 percent – more than 69 million customers – receive their gas from AGA members. Today, natural gas meets more than one-fourth of the United States' energy needs.[3] AGA member companies provide natural gas service to retail customers under rates, terms, and conditions that are regulated at the local

[1] *De Minimis Exception to the Swap Dealer Definition*, 82 Fed. Reg. 27444 (June 12, 2018).
[2] Public Law 111–203, 124 Stat. 1376 (2010).
[3] For more information, please visit www.aga.org.

level by a state commission or other regulatory authority with jurisdiction. AGA's member companies engage in financial risk management transactions in markets regulated by the Commission. Many gas utilities use a variety of financial tools, such as futures contracts traded on CFTC-regulated exchanges and over-the-counter energy derivatives, to hedge the commercial risks associated with providing natural gas service, including volatility in natural gas commodity costs. As such, AGA's members are directly affected by the Commission's regulations promulgated under the Dodd-Frank Act.

II. COMMENTS

A. Background

Commodity Exchange Act ("CEA") section 1a(49) defines "swap dealer" as someone who (1) holds themselves out as a dealer in swaps; (2) makes a market in swaps; (3) regularly enters into swaps with counterparties as an ordinary course of business for its own account; or (4) engages in any activity causing the person to be commonly known in the trade as a dealer or market marker in swaps.[4]

The Dodd-Frank Act directed the CFTC and the U.S. Securities and Exchange Commission to further define the term "swap dealer" and to exempt from designation as a swap dealer a person that engages in a *de minimis* quantity of swap dealing.[5] In 2012, the Commission issued an adopting release further defining, among other things, the term "swap dealer" in § 1.3 of the Commission's regulations, and providing for a *de minimis* exception, which stated that a person shall not be deemed to be a swap dealer unless its swaps connected with swap dealing activities exceed an AGNA threshold of $3 billion, subject to a phase-in period during which the AGNA threshold is set at $8 billion.[6] The phase-in period was originally scheduled to end on December 31, 2017; however, the Commission issued two successive orders to set new termination dates, and the phase-in period is currently scheduled to terminate on December 31, 2019.[7]

The additional time allowed the Commission to study the swap market as it has evolved and to consider new information about the swap market that became available through swap data reporting.[8] In November 2015, the Commission issued a Preliminary Report,[9] which analyzed swap data to assess the $8 billion AGNA *de minimis* threshold and potential alternatives to the AGNA *de minimis* exception, and provided an opportunity for public input. The Commission then issued a Final Staff Report[10] in August 2016, which refreshed the

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[4] 7 U.S.C. 1a(49)(A).
[5] NOPR at 27445.
[6] *Id.*
[7] *Id.*
[8] *Id.*
[9] *See* Swap Dealer De Minimis Exception Preliminary Report (Nov. 18, 2015).
[10] *See* Swap Dealer De Minimis Exception Final Staff Report (Aug. 15, 2016).

analysis from the Preliminary Report and considered the $8 billion *de minimis* threshold in light of the improved data and comments received.[11]

Based on data analysis and public input, the NOPR proposes to amend various aspects of the *de minimis* threshold, such as maintaining the AGNA threshold at $8 billion in swap activity.[12] The NOPR seeks comments, *inter alia*, on whether an $8 billion *de minimis* threshold is appropriate.

B. The *De Minimis* Threshold Should Remain at $8 Billion

In previous comments on the Preliminary Staff Report,[13] AGA explained that an important consideration in any determination to change the current threshold is whether doing so would reduce the number of swap market participants willing to engage in swap transactions in the energy commodity markets. AGA, in its previous comments, raised concerns that a reduction in the *de minimis* threshold may have the unintended result of reducing the availability of potential swap counterparties, result in a reduction in the level of swap activity of existing swap counterparties, and/or cause some current or potential swap counterparties to exit the space in the face of being required to register and comply with costly swap dealer regulations.[14]

AGA appreciates the CFTC's careful consideration of the potential impacts of reducing the current *de minimis* threshold. As the Commission stated in the NOPR, its analysis indicates that at a lower threshold of $3 billion there would only be a small amount of additional AGNA and swap transactions subject to swap dealer regulation, and there would be potentially reduced liquidity in the swap market, as compared to the current $8 billion threshold.[15] Further, the Commission's analysis indicates that a lower threshold could lead to reduced liquidity for non-financial commodity ("NFC") swaps, negatively impacting end-users and commercial entities who utilize NFC swaps for hedging purposes.[16]

AGA supports the Commission's proposal to set the AGNA threshold for the *de minimis* exception at $8 billion. The available data, related policy considerations, and comments from market participants submitted concerning this issue demonstrate that maintaining an $8 billion threshold is appropriate.[17] This proposal will provide efficiency, clarity, and certainty in the application of the swap dealer definition. As explained by the Commission, the policy objectives underlying swap dealer regulation (reducing systemic risk,

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[11] NOPR at 27446.
[12] *Id.* at 27448.
[13] *See* Comments of the American Gas Association on the Swap Dealer De Minimis Exception Preliminary Report at p. 2 (Jan. 19, 2016), available at https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=60604&SearchText=.
[14] *Id.*
[15] NOPR at 27450.
[16] *Id.*
[17] *See, e.g.,* NOPR at 27457.

increasing counterparty protections, and increasing market efficiency, orderliness, and transparency) would not be significantly advanced if the threshold were to decrease to $3 billion.[18] Furthermore, the policy objectives furthered by a *de minimis* exception (increasing efficiency, allowing limited ancillary dealing, encouraging new participants, and focusing regulatory resources) would not be significantly advanced if the threshold were to be lowered.[19]

The Commission's own analysis supports maintaining the $8 billion *de minimis* threshold for three reasons. First, an $8 billion threshold subjects almost all swap transactions to the swap dealer regulations.[20] Second, at a lower threshold of $3 billion, there would only be a small amount of additional AGNA and swap transactions subject to the swap dealer regulations. Third, a lower threshold could lead to reduced liquidity for swaps, negatively impacting end-users and commercial entities who utilize swaps for hedging purposes.[21]

It is important for AGA members, that use commercial risk hedging activities to reduce natural gas price volatility for their end-use customers, to have counterparties that are available and willing to engage in swaps. AGA supports the $8 billion threshold because, *inter alia*, a lower threshold could reduce liquidity for swaps and negatively impact end-users such as AGA members, and their customers. AGA believes that the Commission's proposal, as stated in the NOPR, regarding the *de minimis* threshold provides stability to market participants and increases the efficient application of the swap dealer definition.[22]

AGA also supports the Commission's proposal to add a hedging exception in new paragraph (4)(i)(D) of the swap dealer definition, to permit entities to not count towards their *de minimis* calculations swaps entered into to hedge financial or physical positions, *i.e.*, hedging swaps.[23] As explained by the Commission, when entering into a swap for the purpose of hedging one's own risk, an element of the swap dealer definition is absent and, therefore, the activity of entering into such swaps does not constitute swap dealing.[24] This is true whether the swap hedges physical or financial positions. The proposal, as discussed by the Commission, will help swap market participants know with greater certainty what swaps have to be counted towards the *de minimis* threshold and that swaps hedging financial or physical positions are

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[18] NOPR at 27450.
[19] *Id*.
[20] *Id*.
[21] *Id*.
[22] The Commission should consider establishing a mechanism whereby the *de minimis* threshold is automatically adjusted periodically to keep pace with potential price increases. For example, adjusting the *de minimis* threshold annually based on increases in the consumer price index would recognize the fact that as prices increase over time, a stagnant threshold may unnecessarily negatively impact end-users and commercial entities that utilize swaps for hedging purposes for the reasons discussed herein regarding the lower $3 billion *de minimis* threshold.
[23] NOPR at 27462.
[24] *See* NOPR at 27463, *citing* Further Definition of ''Swap Dealer,'' ''Security-Based Swap Dealer,'' ''Major Swap Participant,'' ''Major Security-Based Swap Participant'' and ''Eligible Contract Participant,'' 77 Fed. Reg. 30596, 30710 (May 23, 2012).

excluded, and will thereby help market participants apply the swap dealer definition more efficiently.

In the NOPR, the Commission also proposes to delegate to the Director of the Division of Swap Dealer and Intermediary Oversight the authority to approve or establish methodologies for calculating notional amounts for purposes of determining whether a person exceeds the AGNA *de minimis* threshold.[25] The methodology used to determine the AGNA is a critical component of the *de minimis* threshold because its calculation impacts the aptness of the threshold level. Accordingly, the determination of the methodology for calculating notional amounts should be made by the Commission, subject to a formal notice and comment period, and evaluated under a cost-benefit analysis. For these reasons, AGA respectfully urges the Commission to reconsider its delegation proposal.

III. CONCLUSION

Wherefore, for the reasons stated above, the American Gas Association respectfully requests that the Commission consider these comments in adopting its final rule and, *inter alia*, retain the current $8 billion *de minimis* threshold.

Respectfully submitted,

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[25] NOPR at 27464.