6351-01-P

COMMODITY FUTURES TRADING COMMISSION

17 CFR Part 1

RIN 3038-AE19

Exclusion of Utility Operations-Related Swaps with Utility Special Entities from De Minimis Threshold for Swaps with Special Entities

AGENCY: Commodity Futures Trading Commission.

ACTION: Proposed rule.

SUMMARY: The Commodity Futures Trading Commission (Commission or CFTC) is proposing to amend its regulations (Proposal) to permit a person to exclude utility operations-related swaps with utility special entities in calculating the aggregate gross notional amount of the person's swap positions solely for purposes of the de minimis exception applicable to swaps with special entities.

DATES: Comments must be received on or before **[INSERT DATE 30 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER]**.

ADDRESSES: You may submit comments, identified by RIN number 3038-AE19, by any of the following methods:

- Agency website: http://comments.cftc.gov;
- Mail: Secretary of the Commission, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581;
- Hand delivery/courier: Same as Mail, above.
- Federal eRulemaking Portal: http://www.regulations.gov. Follow instructions for submitting comments.

All comments must be submitted in English, or if not, accompanied by an English translation. Comments will be posted as received to www.cftc.gov. You should submit only information that you wish to make available publicly. If you wish the Commission to consider information that is exempt from disclosure under the Freedom of Information Act, a petition for confidential treatment of the exempt information may be submitted according to the procedure established in CFTC Regulation 145.9.[1]

The Commission reserves the right, but shall have no obligation, to review, pre-screen, filter, redact, refuse or remove any or all of your submission from www.cftc.gov that it may deem to be inappropriate for publication, such as obscene language. All submissions that have been redacted or removed that contain comments on the merits of the rulemaking will be retained in the public comment file and will be considered as required under the Administrative Procedure Act and other applicable laws, and may be accessible under the Freedom of Information Act.

FOR FURTHER INFORMATION CONTACT: Gary Barnett, Director, (202) 418-6700, gbarnett@cftc.gov; Erik Remmler, Deputy Director, (202) 418-7630, eremmler@cftc.gov; Christopher W. Cummings, Special Counsel, (202) 418-5445, ccummings@cftc.gov; or Israel Goodman, Special Counsel, (202) 418-6715, igoodman@cftc.gov, Division of Swap Dealer and Intermediary Oversight, Commodity Futures Trading Commission, 1155 21st Street, NW, Washington, DC 20581.

SUPPLEMENTARY INFORMATION:

I. Background

A. De Minimis Exception from Swap Dealer Definition

[1] The Commission's regulations are found at 17 CFR Ch. I (2013) and can be accessed through the Commission's Web site.

Section 1a(49)[2] of the Commodity Exchange Act (CEA or Act) defines the term "swap dealer." CEA Section 1a(49)(D) requires the Commission to exempt from swap dealer designation an entity that engages in a de minimis quantity of swap dealing, and to promulgate regulations to establish factors for making a determination to so exempt such entities. Pursuant to this mandate, on April 27, 2012, the Commission adopted Regulation 1.3(ggg), which further defines the term "swap dealer."[3] Regulation 1.3(ggg) became effective on July 23, 2012, and registration as a swap dealer was required beginning October 12, 2012.[4]

Regulation 1.3(ggg)(4) includes an exception from the swap dealer definition for a person that has entered into swap positions connected with its swap dealing activities that, in the aggregate, do not exceed, during the preceding twelve-month period, either of two aggregate gross notional amount thresholds. The two aggregate gross notional amount thresholds are: (i) $3 billion, subject to a phase in level of $8 billion[5] (General De Minimis Threshold), and (ii) $25 million with regard to swaps in which the counterparty is a "special entity" (Special Entity De Minimis Threshold). CEA Section 4s(h)(2)(C) and Regulation 23.401(c) define the term "special entity" to include: a Federal agency; a State, State agency, city, county, municipality, or other political subdivision of a State; any employee benefit plan as defined under the Employee Retirement Income Security Act of 1974 (ERISA); any government plan as defined under

[2] 7 U.S.C. 1a(49) (2012). The CEA can be accessed through the Commission's Web site.
[3] See 77 FR 30596 (May 23, 2012) (Swap Dealer Definition Adopting Release).
[4] The further definition of the term "swap" is found in Regulation 1.3(xxx), which became effective October 12, 2012. See 77 FR 48208 (Aug. 13, 2012). See also Regulation 3.10(a)(1)(v)(C), which establishes that each person who comes within the swap dealer definition from and after the effective date of that definition is subject to registration as a swap dealer with the Commission.
[5] The Commission set the General De Minimis Threshold at an initial phase-in level of $8 billion as of July 23, 2012**,** the effective date of the Swap Dealer Definition Adopting Release. Upon termination of the phase-in period this amount will decrease to $3 billion (or such alternative amount as the Commission may adopt by rulemaking) in accordance with the phase-in procedure outlined in Regulation 1.3(ggg)(4)(ii).

ERISA; and any endowment. Regulation 23.401(c) adds "any instrumentality, department, or a corporation of or established by a State or subdivision of a State" to the definition.

B. Petition for Rulemaking

On July 12, 2012, the Commission received a petition for rulemaking that sought an amendment of Regulation 1.3(ggg)(4) (Petition).[6] The Petition requested that the regulation be amended to exclude from consideration, in determining whether a person has exceeded the Special Entity De Minimis Threshold, swaps to which the Petitioners and certain other special entities (collectively defined in the Petition as "utility special entities"[7]) are counterparties and that relate to the Petitioners' and other utility special entities' utility operations (defined in the Petition as "utility operations-related swaps").[8]

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[6] Petition for Rulemaking to Amend CFTC Regulation 1.3(ggg)(4), dated July 12, 2012. The Petition was filed by the American Public Power Association, the Large Public Power Council, the American Public Gas Association, the Transmission Access Policy Study Group and the Bonneville Power Administration (Petitioners). The Petition and the comment letters that were submitted in support of it are available at http://sirt.cftc.gov/sirt/sirt.aspx?Topic=PendingFilingsandActionsAD&Key=23845.

[7] The Petition defined the term "utility special entity" to mean a government special entity that –

> owns or operates electric or natural gas facilities or electric or natural gas operations (or anticipated facilities or operations), supplies natural gas and/or electric energy to other utility special entities, has public service obligations (or anticipated public service obligations) under Federal, State or local law or regulation to deliver electric energy and/or natural gas service to utility customers, or is a Federal power marketing agency as defined in Section 3 of the Federal Power Act (16 U.S.C. 796(19)).

[8] The Petition defined the term "utility operations-related swap" to mean any swap that a utility special entity enters into "to hedge or mitigate commercial risks" (as that phrase is used in CEA Section 2(h)(7)(A)(ii)) –

> intrinsically related to the electric or natural gas facilities that the utility special entity owns or operates or its electric or natural gas operations (or anticipated facilities or operations), or to the utility special entity's supply of natural gas and/or electric energy to other utility special entities or to its public service obligations (or anticipated public service obligations) to deliver electric energy or natural gas service to utility customers.

The Petition defined the term "intrinsically related" to include all transactions related to:

> (i) the generation or production, purchase or sale, and transmission or transportation of electric energy or natural gas, or the supply of natural gas and/or electric energy to other utility special entities, or delivery of electric energy or natural gas service to utility customers, (ii) all fuel supply for the utility special entity's electric facilities or operations, (iii) compliance with electric system reliability obligations applicable to the utility special entity, its electric facilities or operations, (iv) compliance with energy, energy efficiency, conservation or renewable energy or environmental statutes,

The amendment requested by the Petition would have the effect of allowing a person, in any rolling twelve-month period, to deal in utility-related swaps with utility special entities up to an aggregate gross notional amount not to exceed (together with other swaps in which the person was engaged) the General De Minimis Threshold (currently $8 billion) without being required to register as a swap dealer. In support of this amendment, the Petition claimed that:

> The rule amendment is necessary in order to preserve uninterrupted and cost-effective access to the customized, nonfinancial commodity swaps that Petitioners and other Utility Special Entities [as defined in the Petition] use to hedge or mitigate commercial risks arising from their utility facilities, operations and public service obligations.

The Petition explained that this amendment was necessary in order to increase the number of counterparties available to utility special entities to enter into swaps that are necessary for the efficient conduct of the businesses and operations of utility special entities.

C. CFTC Staff Letter No. 12-18[9]

As the October 12, 2012, effective date for Regulation 1.3(ggg) and the other regulations announced in the Swap Dealer Definition Adopting Release approached, Petitioners submitted to the Commission and several of its divisions a letter requesting

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> regulations or government orders applicable to the utility special entity, its facilities or operations, or
> (v) any other electric or natural gas utility operations-related swap to which the utility special entity is a party.

Finally, the Petition stated that a "utility operations-related swap" did not include:

> a swap based or derived on, or referencing, commodities in the interest rates, credit, equity, or currency asset classes, or a product type or category in the 'other commodity' asset class that is based or derived on, or referencing, metals, or agricultural commodities or crude oil or gasoline commodities of any grade not used as fuel for electric generation.

[9] [2012-2013 Transfer Binder] Comm. L. Fut. Rep. (CCH) ¶32,409 (October 12, 2012). (Staff Letter 12-18). The letter can be accessed on the Commission's Web site at http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/12-18.pdf.

no-action relief from the de minimis threshold for swaps with certain special entities.[10] In Staff Letter 12-18, the staff of the Commission's Division of Swap Dealer and Intermediary Oversight (Division),[11] concluded that, in light of the representations made in support of the request and in view of the impending effective date for the swap dealer registration requirement, it was appropriate to provide temporary, limited no-action relief with respect to the Special Entity De Minimis Threshold for persons dealing in utility related swaps with utility special entities. Staff Letter 12-18 stated that the Division would not recommend that the Commission commence an enforcement action against a person for failure to apply to be registered as a swap dealer, if:

> (1) the Utility Commodity Swaps connected with the person's swap dealing activities into which the person – or any other entity controlling, controlled by or under common control with the person – enters over the course of the immediately preceding 12 months (or following October 12, 2012, if that period is less than 12 months) have an aggregate gross notional amount of no more than $800 million;
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> (2) the person is not otherwise within the definition of the term "swap dealer," as provided in 17 CFR 1.3(ggg) (i.e., the person – or any other entity controlling, controlled by or under common control with the person – has not entered into swaps as a result of its swap dealing activities in excess of the General De Minimis Threshold or (not counting Utility Commodity Swaps) the Special Entity De Minimis Threshold);[12] and
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> (3) the person is not a "financial entity," as defined in section 2(h)(7)(C)(i) of the CEA.

[10] This letter was received on October 8, 2012.
[11] The Division is responsible for, among other things, overseeing compliance with the registration requirements applicable to swap dealers.
[12] Division staff emphasized that the aggregate gross notional amount of a person's utility commodity swaps would reduce the $8 billion aggregate gross notional amount General De Minimis Threshold for that person.

For purposes of Staff Letter 12-18, Division staff defined the term "utility commodity swap"[13] to mean a swap where: (1) a party to the swap is a utility special entity;[14] (2) a utility special entity is using the swap in the manner described in Regulation 1.3(ggg)(6)(iii);[15] and (3) the swap is related to an exempt commodity in which both parties to the swap transact as part of the normal course of their physical energy businesses.[16]

The Division selected the $800 million aggregate gross notional amount threshold, which is ten percent of the current General De Minimis Threshold of $8 billion, based on suggestions made by certain of the Petitioners and other commenters responding to the Commission's proposed further definition of the term "swap dealer." In a joint comment letter on that proposed definition, two persons recommended a de minimis threshold for swaps with special entities that would be one-tenth of the General De Minimis Threshold for exclusion from the "swap dealer" definition.[17] Another joint

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[13] Based on conversations with industry participants, Division staff decided to use a definition for "utility commodity swap" that encompassed the transactions that utility special entities believed were necessary to their business, while avoiding an over-expansive application of the relief.

[14] Either or both parties to the swap could be a utility special entity. For purposes of Staff Letter 12-18, Division staff employed the definition of "utility special entity" set forth in the Petition.

[15] That is, the utility special entity is using the swap to hedge a physical position, as described in Regulation 1.3(ggg)(6)(iii).

[16] As defined in CEA Section 1a(20), an "exempt commodity" is one that is neither an agricultural commodity, nor an "excluded commodity" as defined in CEA Section 1a(19) (which encompasses interest rates, exchange rates, and other instruments, indices and measures of a generally financial nature). At the time Staff Letter 12-18 was issued, Division staff believed it was necessary to limit the relief the Division was providing to situations involving an exempt commodity in which both parties transact as part of the normal course of their physical energy businesses.

[17] Those commenters stated that the Commission should:

> set the threshold for the [general] de minimis exception at 1/1,000th of a percent of the aggregate gross notional size of the U.S. swap market over the preceding 12 months, or 1/10,000th of a percent of the aggregate gross notional size of the U.S. swap market over the preceding 12 months for swaps in which the counterparty is a 'special entity.' This level of swap dealing activity more accurately corresponds to an amount that arguably could pose a potential risk to the stability of the financial system.

Joint comment letter from the Edison Electric Institute and Electric Power Supply Association dated Feb. 22, 2011, at pages 10-11. The letter can be accessed at the Commission's web site. See http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=27918.

comment letter on the proposed further definition of the term "swap dealer" (whose signatories included two of the Petitioners) concurred with this recommendation.[18]

The relief made available by Staff Letter 12-18 was not self-executing. Rather, to claim the relief, a person was required to file with the Division a notice [19] that, among other things, identified each utility special entity with which the person has entered into utility commodity swaps connected with the person's swap dealing activities, and that stated with respect to each such utility special entity the total gross notional amount of such utility commodity swaps.

Division staff based its decision to provide relief on several reasons. For one, the Petitioners had represented that that commodity and swap markets are likely to be local and particularized for utility special entities (as opposed to other special entities that do not provide public utility services). Pricing and other terms of electricity and natural gas swaps may vary significantly from region to region so that only market participants active in the physical energy markets in a particular region are able to enter into swaps with the utility special entities. Thus, staff also understood that the counterparties to the utility special entities for hedging swaps were generally other non-financial entities that are active in the physical markets for these products. As a result, the number of counterparties available to the utility special entities is likely to be limited.

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[18] See joint comment letter from the National Rural Electric Cooperative Association, the American Public Power Association and the Large Public Power Council dated Feb. 22, 2011, at 18. The letter can be accessed at the Commission's web site. See http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=27917. Four other comment letters on the Commission's proposed further definition of the term "swap dealer" from energy market participants also recommended that the overall de minimis threshold be set at 1/1,000th of a percent of the aggregate gross notional size of the U.S. swap market and that the de minimis threshold for swaps with special entities be set at 1/10,000th of a percent of the aggregate gross notional size. See the Swap Dealer Definition Adopting Release, 77 FR at 30627, n.390.

[19] The notice was required to be provided by December 31, 2012, and on a quarterly basis thereafter.

Second, staff understood that utility special entities have a unique obligation to provide continuous service to the public; moreover, this continuous service is crucial to public safety. This also may limit the availability of counterparties to utility special entities if, for example, a utility special entity must arrange hedges covering a continuous period of time without interruption. While other special entities, such as municipal governments, also serve the public interest, they do not have the same obligations to provide a continuous supply of a commodity (e.g., electricity or natural gas). Thus, the need for utility special entities to use physical commodity swaps is different from their need to use other types of swaps, and it is different from the need for other special entities to use swaps.

Finally, a significant reduction in the number of swap counterparties available to utility special entities could be especially harmful to the public interest in view of the importance of the energy services provided by the utility special entities.

D. CFTC Staff Letter No. 14-34

Subsequent to the issuance of Staff Letter 12-18, certain Petitioners acknowledged to the Commission the relief the letter had made available, but also raised concerns regarding the effects of the conditions imposed upon persons seeking to avail themselves of that relief, and regarding continuing regulatory uncertainty surrounding some transactions with utility special entities.[20] They characterized specific features of Staff Letter 12-18 (e.g., the requirement to establish that the utility special entity is using

[20] Letter from Petitioners to Gary Gensler, CFTC Chairman, dated Nov. 19, 2013 (Petitioners' Letter), available at http://sirt.cftc.gov/sirt/sirt.aspx?Topic=PendingFilingsandActionsAD&Key=23845. (One of the original Petitioners did not, however, participate in this follow up letter.) More recently, one of the Petitioners asserted to the Commission that based on an informal survey it conducted, public power utilities subject to the Special Entity De Minimis Threshold have on average lost a large percentage of their potential counterparties, and that granting the request made in the Petition would provide a substantial increase in potential counterparties to the affected utilities. See Letter from the American Public Power Association to Mark Wetjen, Acting CFTC Chairman, dated March 6, 2014.

the swap to hedge a physical position in an exempt commodity, and the requirement to establish that the counterparty seeking relief is not a "financial entity") as imposing administrative costs or creating legal uncertainty such that would-be counterparties were dissuaded from entering into relevant swaps. The Petitioners' Letter thus renewed the relief requested in the previously-filed Petition, claiming that counterparties that had become reluctant to deal with utility special entities were not taking Staff Letter 12-18 as a reason to resume entering into swaps with those entities.[21]

In response to these concerns, on March 21, 2014, the Division issued CFTC Staff Letter No. 14-34 (Staff Letter 14-34),[22] which superseded and broadened the relief provided in Staff Letter 12-18. Specifically, Staff Letter 14-34 stated that the Division would not recommend that the Commission commence an enforcement action against a person for failure to register as a swap dealer if the person – or any other entity controlling, controlled by or under common control with the person – does not include "utility operations-related swaps" in calculating whether it has exceeded the Special Entity De Minimis Threshold, provided that the person's swap dealing activities have not exceeded the General De Minimis Threshold, including utility operations-related swaps.

For purposes of Staff Letter 14-34, a swap is a "utility operations-related swap" if:

(1) A party to the swap is a utility special entity;[23]

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[21] On March 11, 2013, a bill (H.R. 1038) was introduced in the U.S. House of Representatives that would amend the CEA to require the Commission to treat a "utility operations-related swap" entered into with a "utility special entity" as though the swap were entered into with an entity that was not a special entity. The bill would add definitions for "utility special entity" and "utility operations-related swap." H.R. 1038 was passed in the House on June 12, 2013. On December 11, 2013, a companion bill with the same text as H.R. 1038 was introduced in the Senate (S. 1802), and that bill was referred to the Committee on Agriculture, Nutrition and Forestry on the same date.

[22] The letter can be accessed on the Commission's web site at http://www.cftc.gov/ucm/groups/public/@lrlettergeneral/documents/letter/14-34.pdf.

[23] For purposes of Staff Letter 14-34, Division staff continued to employ the definition of "utility special entity" set forth in the Petition.

> (2) The utility special entity has represented to the other party that it is using the swap in the manner described in 17 CFR 50.50(c); and
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> (3) The swap is either (i) an electric energy or natural gas swap; or (ii) The utility special entity has represented to the other party that the swap is associated with: (a) The generation, production, purchase or sale of natural gas or electric energy, the supply of natural gas or electric energy to a utility, or the delivery of natural gas or electric energy service to utility customers; (b) Fuel supply for the facilities or operations of a utility; (c) Compliance with an electric system reliability obligation; or (d) Compliance with an energy, energy efficiency, conservation, or renewable energy or environmental statute, regulation, or government order applicable to a utility.

The Division explained in Staff Letter 14-34 that it was revising the relief provided in Staff Letter 12-18 based on its understanding from discussions with market participants that (1) doing so would allow utility special entities to significantly increase the number of swap counterparties available to utility special entities and thereby lessen potential harm to the public interest in view of the importance of the energy services provided by utility special entities; and (2) acting to increase the volume of utility operations-related swaps between utility special entities and persons not registered as a swap dealer would likely not raise the types of risks that swap dealer registration is intended to prevent.

The Commission does not intend the Proposal to have any effect on the eligibility requirements for the relief currently available under Staff Letter 14-34. In the event the Commission adopts the regulations being proposed herein, the Commission will discuss in the adopting Federal Register release the effect of those regulations on the relief provided under Staff Letter 14-34.

II. The Proposal

The Commission recognizes that utility special entities have a specialized purpose – they provide electricity and natural gas production and/or distribution to their customers. Utility special entities have a unique obligation in that the services they provide must be continuous and are important to public safety. Furthermore, the Commission is of the view that utility operations-related swaps have become an integral part of providing continuous service and managing costs in connection therewith.

The specialized nature of utility special entities distinguishes them from other types of special entities (e.g., public pension plans or municipal governments) in that the conduct of their business routinely involves, and indeed often depends upon access to, specific types of swap transactions that permit them to manage the risks of their businesses and to be able to provide electricity and natural gas consistently. As a consequence, they not only need regular access to swaps that directly affect the smooth operation of their business activities, but also are more likely to have developed expertise with swaps directly related to their operations. While the Special Entity De Minimis Threshold may represent a reasonable protection for other types of special entities that enter into swaps intermittently and whose activities do not depend on a consistent use of particular swaps, for the reasons stated above, the Commission believes that its application to utility operations-related swaps with utility special entities is not as necessary for their regular operation.[24]

The Commission believes that it is important to address the concerns raised in the Petition regarding the ability of utility special entities to hedge the commercial risks of

[24] The Commission is not considering, as part of this proposed rulemaking, altering the Special Entity De Minimis Threshold with respect to other types of swaps or special entities.

their electric and natural gas production and delivery businesses including the availability of counterparties with whom utility special entities can enter into customized swaps. The Commission believes that, because the swaps used by utility special entities are typically conducted in localized and specialized markets and the number of available counterparties may be limited, the $25 million amount of the existing Special Entity De Minimis Threshold may deter those counterparties from engaging in utility operations-related swaps. Given the obligations of utility special entities to provide continuous service to customers, the Commission preliminarily believes that the public interest would be better served if the likely counterparties for utility operations-related swaps are able to provide liquidity to this limited segment of the market without registering as swap dealers solely on account of exceeding the Special Entity De Minimis Threshold. In addition, given the expertise utility special entities are likely to have with utility operations-related swaps, the need for a lower de minimis threshold for dealing activity in such swaps with utility special entities is reduced.

Accordingly, the Proposal would permit a person to exclude specified swaps (i.e., utility operations-related swaps) entered into with a defined subset of special entities (i.e., utility special entities) when calculating whether the person has exceeded the Special Entity De Minimis Threshold. In light of the foregoing and the Commission's further deliberations in this area, the Commission is now proposing to amend its regulations in order to permit persons engaging in utility operations-related swaps with utility special entities (as these terms are defined in the Proposal) to exclude such swaps solely for purposes of calculating whether such persons' swap dealing activities have exceeded the Special Entity De Minimis Threshold.

A. Adding an Exclusion for Utility Operations-Related Swaps with Utility Special Entities

Regulation 1.3(ggg) defines the term "swap dealer." Currently, Regulation 1.3(ggg)(4)(i) provides for a de minimis exception from the swap dealer definition, under either the General De Minimis Threshold or the Special Entity De Minimis Threshold. The Proposal would amend Regulation 1.3(ggg)(4)(i) to permit persons engaging in utility operations-related swaps with utility special entities to exclude such swaps solely for purposes of determining whether they have exceeded the Special Entities De Minimis Threshold. This would be done by redesignating current Regulation 1.3(ggg)(4)(i) as Regulation 1.3(ggg)(4)(i)(A), placing the text "In General" before the redesignated regulation and adding a new Regulation 1.3(ggg)(4)(i)(B), captioned "Utility Special Entities."

Regulation 1.3(ggg)(4)(i)(B)(1) would provide that solely for purposes of determining whether a person's swap dealing activity has exceeded the $25 million aggregate gross notional amount threshold set forth in Regulation (ggg)(4)(i)(A) for swaps in which the counterparty is a special entity, a person may exclude utility operations-related swaps in which the counterparty is a utility special entity. Proposed Regulation 1.3(ggg)(4)(i)(B)(1) would not, however, permit a person to exclude the gross notional amount of such utility operations-related swaps in determining whether the person has exceeded the General De Minimis Threshold. In other words, a person would add the aggregate gross notional amount of the utility operations-related swaps it enters into with utility special entities to the gross notional amount of any other swaps entered

into by it during the preceding twelve months in determining whether the person has exceeded the General De Minimis Threshold.[25]

As is the case for other swaps, in calculating the gross notional amount of utility operations-related swap positions entered into with utility special entities, a person must also include swap positions entered into by any entity controlling, controlled by or under common control with the person, and if a stated notional amount of a swap is leveraged or enhanced by the structure of the swap, the threshold calculation would be required to be based "on the effective notional amount of the swap rather than on the stated notional amount."

Under the Proposal, a person would be required to file a one-time notice to rely on the exclusion provided by the new rule.[26] Specifically, the notice would be required to be filed electronically with the National Futures Association (NFA),[27] to provide such information as the person's name, address, and a contact, and to contain a representation that the person meets the criteria of the exclusion for utility operations-related swaps with utility special entities in Regulation 1.3(ggg)(4)(i)(B). Congress has determined that special entities merit additional protections when engaging in swap transactions, and has adopted, for example, heightened business conduct requirements on swap dealers

[25] A person likewise would include the aggregate gross notional amount of swaps entered into with other types of special entities to the same extent required for swaps generally in determining whether the person's swap dealing activity has exceeded the General De Minimis Threshold.

[26] See proposed Regulation 1.3(ggg)(4)(i)(B)(4).

[27] NFA is a futures association registered as such with the Commission pursuant to CEA Section 17. Although persons relying on the exclusion in Regulation 1.3(ggg)(4)(i)(A) would be outside the swap dealer definition and therefore not subject to the requirement in Regulation 170.16 that a swap dealer must become an NFA member, a requirement to file a notice with NFA would be consistent with past action the Commission has taken with regard to requiring other persons seeking to rely on an exception or exclusion from a term defined in the Act – i.e., by requiring such persons to file a notice with NFA. See, e.g., 62 FR 52088 (Oct. 6, 1997), authorizing NFA to process notices of eligibility for exclusion from the definition of the term "commodity pool operator" under Regulation 4.5, and 72 FR 1658 (Jan. 16, 2007), establishing that a person seeking an exclusion under Regulation 4.5 must file its claim with NFA electronically. In the event the Commission adopts the proposing filing requirement, it will concurrently delegate to NFA the authority to accept the filing.

advising and dealing with special entities.[28] Because the Proposal, if adopted, would permit persons to engage in a greater aggregate gross notional amount of swaps with utility special entities, who Congress has determined warrant additional protections under the CEA, without registering as swap dealers (and becoming subject to corresponding business conduct standards), it is important that the Commission be able to know who the persons are that rely on the exclusion under the Proposal. The proposed notice filing will help the Commission to monitor compliance with the swap dealer registration requirement, and better ensure that the exclusion under the Proposal serves the intended purpose of enabling utility special entities to manage operational risks in a cost-effective way.

Additionally, a person relying on the exclusion under the Proposal would be required to maintain in accordance with Regulation 1.31 books and records that substantiate its eligibility to rely on this exclusion.[29]

B. New Definitions

1. "Utility Special Entity"

Proposed Regulation 1.3(ggg)(4)(i)(B)(2) would define the term "utility special entity" to mean a special entity[30] that owns or operates electric or natural gas facilities, electric or natural gas operations or anticipated electric or natural gas facilities or operations; supplies natural gas or electric energy to other utility special entities; has public service obligations or anticipated public service obligations under Federal, State or

[28] See CEA Sections 4s(h)(4) and 4s(h)(5).
[29] This requirement is consistent with other similar Commission regulations, such as the requirement in Regulation 4.7 that commodity pool operators and commodity trading advisors claiming relief under that regulation maintain books and records relating to their eligibility to claim that relief.
[30] As noted above, the term "special entity" is defined in CEA Section 4s(h)(2)(c) and Regulation 23.401(c).

local law or regulation to deliver electric energy or natural gas service to utility customers; or is a Federal power marketing agency as defined in Section 3 of the Federal Power Act, 16 U.S.C. 796(19). This definition is essentially identical to the definition of "utility special entity" in the Petition.

2. "Utility Operations-Related Swap"

Proposed Regulation 1.3(ggg)(4)(i)(B)(3) would define the term "utility operations-related swap," to mean a swap to which at least one of the parties is a utility special entity that is using the swap to hedge or mitigate commercial risk, and that is related to an exempt commodity. In addition, the swap must be an electric energy or natural gas swap, or associated with the operations or compliance obligations of a utility special entity in a manner more fully set forth in Regulation 1.3(ggg)(4)(i)(B)(3)(iv).

In this regard, the Commission notes that, in determining whether a person may rely on the proposed exclusion for utility operations-related swaps with utility special entities, it may not always be possible for the person to establish with absolute certainty that a counterparty is a utility special entity, that the counterparty is using a swap to hedge or mitigate commercial risk, that the swap is related to an exempt commodity, or that the swap meets the other requirements to come within the definition of a utility operations-related swap. Therefore, the Commission intends to take the position that a person seeking to rely on the (proposed) exclusion may reasonably rely upon a representation by the utility special entity that it is a utility special entity and that the swap is a utility operations-related swap, as such terms are defined in proposed

Regulation 1.3(ggg)(4)(i)(B), so long as the person was not aware, and should not reasonably have been aware, of facts indicating the contrary.[31]

III. Request for Comments

The Commission seeks comments regarding the nature and application of an exclusion for utility operations-related swaps with utility special entities for purposes of calculating whether a person's swap dealing activities have exceeded the Special Entity De Minimis Threshold, as provided for in the Proposal. Set forth below, then, is a non-exclusive list of questions to which the Commission seeks responses.

1. Will the Proposal enable utility special entities to adequately hedge their operational risks in a cost-effective manner by entering into utility operations-related swaps? If not, explain why, and indicate ways in which the Proposal could be modified in order to accomplish this goal.

2. Are there factual errors or omissions in the Commission's understanding and analysis of the issues faced by utility special entities and the efforts to date to resolve those issues?

3. Is it appropriate to treat utility operations-related swaps with utility special entities differently than other swaps with special entities for purposes of determining whether a person is a swap dealer?

4. Does the definition of utility operations-related swap in proposed Regulation 1.3(ggg)(i)(4)(B)(3) adequately encompass the range of swap transactions with respect to which it is appropriate to, in effect, set a higher de minimis threshold in the context of

[31] This position is consistent with the Commission's approach to permitting reliance on representations for other purposes, such as the requirement in Regulation 50.50(b)(3) that a reporting party have a reasonable basis to believe that its counterparty meets the requirements for the exception to the clearing requirement for end-users. See 77 FR 42560, 42570 (July 19, 2012).

persons dealing with utility special entities? If not, in what way(s) should the definition be expanded or narrowed and why? More specifically, should the scope of the swaps identified in Regulation 1.3(ggg)(i)(4)(B)(3)(iv) be expanded or narrowed? Are there swaps that would meet the requirements of Regulation 1.3(ggg)(i)(4)(B)(3)(i), (ii) and (iii), but not of Regulation 1.3(ggg)(i)(4)(B)(3)(iv) that should be included? Is Regulation 1.3(ggg)(i)(4)(B)(3)(iv) too restrictive or not restrictive enough?

5. One of the conditions to coming within the definition of the term "utility operations-related swap" is that the party to the swap that is a utility special entity is using the swap in the manner prescribed in Regulation 50.50(c) – i.e., to hedge or mitigate commercial risk. What issues might there be in determining whether a swap constitutes hedging activity for purposes of complying with this proposed rule? Is reference to Regulation 50.50(c) for defining hedging activities appropriate? Are there alternative definitions that should be considered (e.g., Regulation 1.3(ggg)(6)(iii))? Should the definitions for hedging activities in Regulation 50.50(c) and Regulation 1.3(ggg)(6)(iii) be harmonized? If so, how (e.g., by following Regulation 50.50(c) or Regulation 1.3(ggg)(6)(iii) or some iteration of both) and why? Please provide any estimates of costs of compliance with any proposed alternative as compared to the cost of compliance with Regulation 50.50(c).

6. Another condition to coming within the proposed definition of the term "utility operations-related swap" is that the swap be related to an exempt commodity (as defined in CEA Section 1a(20)). Is this condition appropriate? If not, why not and/or how and why should it be modified?

7. Should the definition of utility operations-related swap be limited to swaps in which both parties to the swap transact as part of the normal course of their physical energy businesses?

8. The Proposal would allow persons to, in effect, treat utility operations-related swaps in which the counterparty is a utility special entity like swaps with a counterparty that is not a special entity in determining whether the person has exceeded a de minimis threshold under Regulation 1.3(ggg)(4)(i)(A). Thus, utility operations-related swaps with utility special entities would be subject to the General De Minimis Threshold under Regulation 1.3(ggg)(4)(i), which is currently set at the $8 billion phase in level. Is that an appropriate threshold, or should the de minimis threshold for such swaps be higher or lower? What considerations support using a different amount? Should the de minimis threshold for utility operations-related swaps be set at $3 billion, the level of the General De Minimis Threshold without application of the $8 billion phase-in level, in light of the special protections afforded to special entities under the CEA? Should the threshold be set at an amount equal to a percentage of the gross notional amount of the General De Minimis Threshold, such that an increase or decrease in the gross notional amount of the General De Minimis Threshold would result in a proportionate change in the de minimis threshold for utility operations-related swaps?

9. Should the nature of the person entering into swaps with a utility special entity determine whether the person can rely on the exclusion for utility operations-related swaps under the Proposal (e.g., by limiting the exclusion to persons who are not "financial entities," as Staff Letter 12-18 limited relief to such persons)? If so, what characteristics or factors should be considered?

10. Should the Commission specify the books and records a person must maintain to substantiate that the person may rely on the (proposed) exclusion for utility operations-related swaps?

11. Would the Proposal impact the Commission's ability to carry out its market oversight responsibilities with regard to the overall derivatives market? If so, how?

12. To what extent, if any, would the Proposal reduce transparency with regard to utility operations-related swaps, counterparties to such transactions or the broader derivatives market?

13. Does the Proposal serve the public interest? In what ways? How could the Proposal be improved to better serve the public interest?

14. How should the Commission balance the public interest in having the additional protections that a de minimis threshold for transactions with utility special entities that is lower than the General De Minimis Threshold would afford, versus the public interest in maintaining the ability for utility special entities to enter hedging transactions?

15. As noted above, it is important that the Commission be able to know who the persons are that rely on the exclusion under the Proposal to monitor compliance with the swap dealer registration requirement, and better ensure that the exclusion under the Proposal serves the intended purpose of enabling utility special entities to manage operational risks in a cost-effective way. Will the notice requirement in proposed Regulation 1.3(ggg)(4)(i)(B)(4) enable the Commission to achieve these objectives? If not, why? Is there an alternative method for the Commission to obtain the relevant information and achieve the stated objectives without requiring a notice filing?

16. Are there any special entities (or types of special entities) who come within the proposed definition of "utility special entity" (as set forth in proposed Regulation 1.3(ggg)(4)(i)(B)(2)), but are not likely to have expertise in utility operations-related swaps? If yes, describe those entities. Should persons dealing in swaps with those entities be treated differently than persons dealing with other utility special entities under the Proposal?

17. Should the description of swap dealing activity in the swap dealer definition be more specifically described for the purposes of defining swap dealing with utility special entities? What specific dealing or non-dealing activities should be taken into account given the nature of utility special entities? Have any compliance issues arisen with respect to the description of swap dealing activity in the swap dealer definition? If so, how should the Commission clarify the description?

18. Will utility special entities benefit if the Commission revised its interpretation regarding forward contracts with embedded volumetric optionality as described in the swap definition adopting release?[32] If so, how? Is the seven element interpretation appropriate for determining whether a forward contract with volumetric optionality qualifies for the forward contract exclusion from the definition of a swap? If not, should the Commission revise the interpretation or adopt an alternative standard? If so, what should the revised interpretation or standard be?

19. Regulation 1.3(ggg)(6)(iv) provides that swaps entered into by a floor trader who meets certain conditions do not need to be counted in determining whether the floor trader is a swap dealer. Should the Commission afford similar treatment to swaps entered into with utility special entities by their counterparties? For purposes of the de minimis

[32] See 77 FR 48238 (Aug. 13, 2012).

calculation under the swap dealer definition, why should the Commission hold floor traders and entities dealing with utility special entities to different standards?

The Commission welcomes comments on any other issues concerning the subject matter of this Federal Register release and the de minimis exception from the swap dealer definition for persons engaging in swap transactions with special entities, in general.

IV. Related Matters

A. Regulatory Flexibility Act

The Regulatory Flexibility Act[33] requires that Federal agencies consider whether the rules they propose will have a significant economic impact on a substantial number of small entities and, if so, they must provide a regulatory flexibility analysis respecting the impact. Whenever an agency publishes a general notice of proposed rulemaking for any rule, pursuant to the notice-and-comment provisions of the Administrative Procedure Act[34] a regulatory flexibility analysis or certification typically is required.[35] The Proposal, if adopted, will not have a significant economic impact on affected persons because the Proposal will primarily relieve them from regulatory obligations that would otherwise apply to them. That is, the (proposed) exclusion for utility operations-related swaps will permit counterparties to engage with utility special entities in utility operations-related swaps to a degree that would, absent the proposed exclusion, require them to register with the Commission as a swap dealer, and to comply with regulations applicable to swap dealers.[36] While the Proposal does require a notice filing in order to rely on the (proposed) exclusion for utility operations-related swaps, to the extent that

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[33] 5 U.S.C. 601 et seq.
[34] 5 U.S.C. 553. The Administrative Procedure Act is found at 5 U.S.C. 500 et seq.
[35] See 5 U.S.C. 601(2), 603–05.
[36] See, e.g., Part 23 of the Commission's regulations, which establishes, among other things, reporting, recordkeeping and business conduct requirements for swap dealers.

any small entities opt to rely on the exclusion, the notice requirement will not have a significant economic impact on those entities.[37] Moreover, the number of potential counterparties seeking to rely on the (proposed) exclusion may be limited, given the local nature of the relevant markets.

Accordingly, the Chairman, on behalf of the Commission, hereby certifies pursuant to 5 U.S.C. 605(b) that the Proposal will not have a significant economic impact on a substantial number of small entities.

B. Paperwork Reduction Act

The Paperwork Reduction Act (PRA)[38] provides that an agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid control number from the Office of Management and Budget (OMB). This rulemaking contains notification and recordkeeping requirements that are collections of information within the meaning of the PRA. Accordingly, the Commission will submit the required information collection requests to OMB.

1. Collections of Information

This rulemaking contains two elements that would qualify as collections of information. First, proposed Regulation 1.3(ggg)(4)(i)(B) would create an exclusion from the Special Entity De Minimis Threshold with regard to specified swaps (utility operations-related swaps) entered into with a defined subset of special entities (utility special entities). As proposed, a person seeking to rely on the exclusion would be required to file a one-time notice. Specifically, and as explained above, the notice would

[37] See 77 FR 2613, 2620 (Jan. 19, 2012), wherein the Commission stated that in the experience of the Commission, complying with the registration process regulations – a far more burdensome process than the notice filing that would be required under the Proposal – has not had a significant economic effect on a substantial number of small entities.
[38] 44 U.S.C. 3501 et seq.

be required to be filed electronically with NFA, to provide such information as the person's name, address, and a contact, and to contain a representation that the person meets the criteria of the exclusion for utility operations-related swaps in Regulation 1.3(ggg)(4)(i)(B). Based upon the information currently available to the Commission, an accurate estimate of the persons who may rely on the exclusion under the Proposal, if adopted, cannot be made. Nevertheless, the Commission is preliminarily using a conservative estimate of 100 potential counterparties of utility special entities. The Commission invites comments regarding whether this is a reasonable estimate to use for PRA paperwork burden calculations.

Commission staff estimates that ascertaining whether a person is eligible to rely on the exclusion for utility operations-related swaps under the Proposal will take no more than one hour. Because the information required for the notice is readily known to the person, staff estimates that preparing and filing the notice will take no more than one-half hour. The notice will be filed only once, but a person who has filed a notice will periodically check to ensure that it remains eligible. Staff estimates that because such verification will be based on information within the person's control, it will not require more than an hour annually.

Consequently, the Commission preliminarily estimates the burden associated with the required notice filing would be as follows:

Number of Respondents: 100

Frequency of Response: Annually (initial filing and ongoing compliance)

Average Burden Hours per Response: 1.2

Estimated gross annual reporting burden: $79,680

On this basis, the Commission will request a new collection of information control number from OMB.

Proposed Regulation 1.3(ggg)(4)(i)(B) would also require a person seeking to rely on the proposed exclusion for utility operations-related swaps to maintain books and records in accordance with Regulation 1.31 that substantiate its eligibility. The Commission notes that it has previously requested and obtained OMB Control Number 3038-0090 pertaining to Regulation 1.31. The Commission preliminarily believes that each person claiming the proposed exclusion will need to establish a procedure to maintain the necessary books and records substantiating ongoing eligibility with for reliance on the proposed exclusion. In addition, each such person will incur some burden to create and maintain relevant records. As noted above, the Commission preliminarily estimates 100 persons may seek to rely on the exclusion for utility operations-related swaps under the Proposal, if adopted. Although the books and records required to substantiate initial and ongoing eligibility to rely on the exclusion will be books and records that the person has already prepared in the course of engaging in utility operations-related swaps, Commission staff estimates that the person will incur an hour of burden initially and an hour annually thereafter as a result of consulting and reviewing those books and records. Consequently, the Commission preliminarily estimates the recordkeeping burden associated with the proposed Regulation 1.3(ggg)(4)(i)(B) would be as follows:

Number of Respondents: 100

Frequency of Response: Annually

Average Burden Hours per Response: 1

Estimated gross annual reporting burden: $16,100

On this basis, the Commission will submit a request to amend OMB Control Number 3038-0090. The Commission preliminarily believes that the persons who are likely to rely on the exclusion for utility operations-related swaps may already have procedures in place to comply with this requirement so that actual burdens may be less – and possibly much less – for those persons.

2. Information Collection Comments

The Commission invites comment on any aspect of the proposed information collection requirements discussed above. Pursuant to 44 U.S.C. 3506(c)(2)(B), the Commission will consider public comments on such proposed requirements in:

- Evaluating whether the proposed collection of information is necessary for the proper performance of the functions of the Commission, including whether the information will have a practical use;

- Evaluating the accuracy of the Commission's estimate of the burden of the proposed collection of information, including the validity of the methodology and assumptions used;

- Enhancing the quality, utility, and clarity of the information proposed to be collected; and

- Minimizing the burden of collection of information on those who are to respond, including through the use of appropriate automated, electronic, mechanical, or other technological information collection techniques.

Copies of the submission from the Commission to OMB are available from the CFTC Clearance Officer, 1155 21st Street NW, Washington, DC 20581, (202) 418–5160

or from http://RegInfo.gov. Persons desiring to submit comments on the proposed information collection requirements should send those comments to:

- The Office of Information and Regulatory Affairs, Office of Management and Budget, Room 10235, New Executive Office Building, Washington, DC 20503, Attn: Desk Officer of the Commodity Futures Trading Commission;
- (202) 395–6566 (fax); or
- OIRAsubmissions@omb.eop.gov (email).

Please provide the Commission with a copy of submitted comments so that all comments can be summarized and addressed in the final rulemaking, and please refer to the **ADDRESSES** section of this rulemaking for instructions on submitting comments to the Commission. OMB is required to make a decision concerning the proposed information collection requirements between thirty (30) and sixty (60) days after publication of the Proposal in the Federal Register. Therefore, a comment to OMB is best assured of receiving full consideration if OMB (as well as the Commission) receives it within thirty (30) days of publication of the Proposal. The time frame for commenting on the PRA does not affect the deadline established by the Commission on the Proposal, provided in the **DATES** section of this rulemaking.

C. Cost-Benefit Considerations

CEA Section 15(a) requires the Commission to consider the costs and benefits of its actions before promulgating a regulation under the CEA or issuing certain orders. CEA Section 15(a) further specifies that the costs and benefits shall be evaluated in light of five broad areas of market and public concern: (1) protection of market participants and the public; (2) efficiency, competitiveness and financial integrity of futures markets;

(3) price discovery; (4) sound risk management practices; and (5) other public interest considerations. The Commission considers the costs and benefits resulting from its discretionary determinations with respect to the Section 15(a) factors, and seeks comments from interested persons regarding the nature and extent of such costs and benefits.

1. Background. The Commission is proposing to amend its regulations to permit a person to exclude utility operations-related swaps with utility special entities (as such terms are defined in the Proposal) in calculating the aggregate gross notional amount of the person's swap positions for purposes of the Special Entity De Minimis Threshold.

As discussed above, CEA Section 1a(49) defines the term "swap dealer," and Regulation 1.3(ggg) further defines that term. A person who comes within the swap dealer definition is subject to registration as such with the Commission and the regulatory requirements applicable to swap dealers.[39] Regulation 1.3(ggg)(4)(i) provides an exception from the swap dealer definition for persons who engage in a de minimis amount of swap dealing activity. Currently, under Regulation 1.3(ggg)(4)(i) persons who engage in swap dealing activity with special entities are excepted from the swap dealer definition so long as the swap positions connected with those dealing activities into which the person enters over the course of the immediately preceding 12 months have an aggregate gross notional amount of no more than $25 million (i.e., the Special Entity De Minimis Threshold). These regulatory provisions set the baseline for the Commission's consideration of the costs and benefits of the Proposal. That is, the Commission considers the costs and benefits that would result from allowing persons to exclude utility operations-related swaps with utility special entities from the Special Entity De Minimis

[39] See, e.g., Part 23 of the Commission's regulations.

Threshold ($25 million), such that the de minimis threshold with respect to such swaps would the same as for swaps not involving a special entity (i.e., the General De Minimis Threshold, currently set at $8 billion), subject to the requirements set forth in the Proposal.[40]

2. Costs. As noted by the Commission in the Swap Dealer Definition Adopting Release, "a de minimis exception, by its nature, will eliminate key counterparty protections provided by Title VII for particular users of swaps . . . [and] [t]he broader the exception, the greater the loss of protection."[41] In adopting the Special Entity De Minimis Threshold, the Commission explained that the $25 million threshold was "appropriate in light of the special protections that Title VII affords to special entities." The Commission also recognized the "serious concerns raised by commenters" regarding the application of the de minimis exception to swap dealing with special entities in light of losses that special entities have incurred in the financial markets.[42]

Under the Proposal, a greater quantity of swap dealing with utility special entities would potentially be undertaken without the benefits to utility special entities of that dealing activity being subject to swap dealer regulation.[43] In addition, the Proposal will impose costs associated with ascertaining whether a person is eligible to rely on the proposed exclusion for utility operations-related swaps and the preparation and submission of the notice required to rely on the exclusion under proposed Regulation

[40] While Staff Letter 14-34 currently provides no-action relief in circumstances, and subject to requirements, that are substantially similar to those of the Proposal, the Commission preliminarily believes that Staff Letter 14-34 should not set or affect the baseline from which the Commission considers the costs and benefits of the Proposal. This is because, as it indicates, Staff Letter 14-34 does necessarily represent the position or view of the Commission or any other office or division of the Commission.
[41] See 77 FR at 30596, 30627-30628 (May 23, 2012).
[42] See Id. at 30633.
[43] See Id. at 30707 (stating that the benefits of swap dealing regulation include customer protection, market orderliness and market transparency).

1.3(ggg)(4)(i)(B)(2). Finally, to the extent that a person relying on the exclusion under the Proposal would be required to keep books and records it would not otherwise keep, in order to substantiate its eligibility for the exclusion, that represents another potential cost. Comments are invited regarding the extent of all of these costs, and any other costs that would result from adoption of the Proposal, including estimates of monetary or other measurements thereof.

3. Benefits. With respect to benefits, the Commission preliminarily believes that the Proposal will benefit utility special entities and the public by encouraging a greater number of prospective counterparties to engage with utility special entities in utility operations-related swaps.[44] Because of the local and particularized nature of the electric and natural gas production and distribution, the number of potential swap counterparties for utility special entities seeking to hedge commercial risk is more limited than for other special entities seeking to hedge non-physical commodities. The number of counterparties to utility special entities may be further limited due to the unique obligation of utilities to provide continuous service to the public. These considerations may be more critical given the important role energy services play in public safety and commerce. Thus, limiting the number of counterparties to utility special entities could be counter to the public interest.

Accordingly, increasing the number of potential counterparties available to utility special entities will enable utility special entities to practice sound, cost-effective risk management and to efficiently operate and conduct their business. This will, in turn, help

[44] The Commission explained in the Swap Dealer Definition Adopting Release that "[i]n principle, a higher [de minimis] threshold would promote a larger pool of swap-dealing entities (since entities with swap dealing activity below the threshold need not incur costs to comply with swap dealer regulations), meaning more potential counterparties available to swap users." See Id.

utility special entities meet their obligations to provide continuous services to the public in a cost-effective manner, and will help protect the public interest and safety that is dependent on such energy services. Comments are sought regarding these benefits and any other benefits resulting from adoption of the Proposal, and to the extent they can be quantified, estimates of the monetary or other value thereof.

4. Section 15(a). Section 15(a) of the CEA requires the Commission to consider the effects of its actions in light of the following five factors:

a. Protection of Market Participants and the Public. The Proposal will allow utility special entities to engage in certain swaps to a greater extent than other special entities, without the protections of swap dealer registration and regulation. However, given the limited circumstances for which the proposed exclusion would apply, and the requirements persons must meet to rely on the exclusion, the Commission preliminarily believes the costs to the affected utilities, market participants and the public will be limited. Moreover, these costs will be counteracted by the benefits the Proposal will provide to utility special entities and the public, namely, enabling utility special entities to efficiently hedge and manage risk, and to meet their obligations to provide vital energy services to the public in a consistent and cost-effective manner.

b. Efficiency, Competitiveness, and Financial Integrity of Markets. The Commission preliminarily believes that the Proposal will enhance efficiency and competitiveness in the electricity and natural gas markets by encouraging prospective counterparties to engage in swap transactions with utility special entities. The availability of additional swap counterparties in these markets will enhance competition

between counterparties, which will, in turn benefit utility special entities by lowering transaction costs for utility special entities.

c. Price Discovery. It is unlikely that facilitating more counterparties for utility special entities to trade with will have a significant impact on price discovery. Price discovery is the process by which prices for underlying commodities may be determined or inferred through market prices. The addition of more counterparties willing to trade with utility special entities may improve, but not necessarily adversely impact, the prices that the utility special entities receive on their swap contract transactions, but the overall effect on the determined or inferred prices for the underlying commodities is indeterminate. Interested persons are invited to comment on this conclusion.

d. Sound Risk Management. The Commission preliminarily believes that if counterparties refrain from transacting in swaps with utility special entities because of the regulatory costs associated with swap dealer registration and regulation, the ability of utility special entities to hedge commercial risks will be impaired, particularly in cases for which the number of counterparties available becomes very limited. Mitigating the costs and regulatory concerns of potential counterparties by permitting them to transact with utility special entities without being subject to swap dealer registration and regulation will enable utility special entities to better manage their commercial risk.

e. Other Public Interest Considerations. As discussed above, the Commission preliminarily believes the proposed rule will enable utility special entities to practice sound, cost-effective risk management and to more effectively operate and conduct their business. This may, in turn, help utility special entities meet their obligations to provide continuous services to the public in a more cost-effective manner.

5. Request for Comment.

The Commission invites comments from the public on all aspects of its preliminary consideration of costs and benefits associated with the Proposal. The questions below relate to areas that the Commission preliminarily believes may be relevant. In addressing these or any other aspect of the Commission's preliminary assessment, commenters are encouraged to submit any data or other information that they may have quantifying or qualifying the costs and benefits of the Proposal.

a. What are the costs and benefits to market participants, if any, associated with the Proposal? Please explain and, to the extent possible, quantify these costs.

b. What are the costs and benefits to the public associated with the Proposal? Please explain and, to the extent possible, quantify these costs.

c. Would a de minimis threshold other than the General De Minimis threshold for transactions with utility special entities as set forth in the Proposal impact the costs and/or benefits to market participants or the public? Is there a threshold level that would be optimal, i.e., maximize net benefits?

d. Has the Commission identified all of the relevant categories of costs and benefits in its preliminary consideration of the costs and benefits associated with the Proposal? Please describe any additional categories of costs or benefits that the Commission should consider with respect to the Proposal.

e. To what extent does the Proposal protect market participants and the public? How, if at all, could the Proposal be altered to better protect market participants and the public?

f. How, if at all, does the Proposal affect the efficiency, competitiveness, and financial integrity of markets?

g. How, if at all, does the Proposal affect price discovery for utility operations-related swaps? For the swaps market more generally?

h. How, if at all, does the Proposal affect sound risk management for utility special entities? For participants in the swaps market more generally?

i. How, if at all, does the Proposal affect the public interest?

List of Subjects in 17 CFR Part 1

De minimis exception, Registration, Special Entities, Swap dealers, Swaps, Utility operations-related swaps, Utility special entities.

For the reasons discussed in the preamble, the Commission proposes to amend 17 CFR part 1 as follows:

PART 1 – GENERAL REGULATIONS UNDER THE COMMODITY EXCHANGE ACT

1. The authority citation for part 1 is revised to read as follows:

Authority: 7 U.S.C. 1a, 2, 5, 6, 6a, 6b, 6c, 6d, 6e, 6f, 6g, 6h, 6i, 6k, 6l, 6m, 6n, 6o, 6p, 6r, 6s, 7, 7a-1, 7a-2, 7b, 7b-3, 8, 9, 10a, 12, 12a, 12c, 13a, 13a-1, 16, 16a, 19, 21, 23, and 24 (2012).

2. Amend § 1.3 by revising paragraph (ggg)(4)(i) to read as follows:

§ 1.3 Definitions.

* * * * *

(ggg) * * *

(4) De minimis exception—(i)(A) In General. Except as provided in paragraph (ggg)(4)(vi) of this section, a person that is not currently registered as a swap dealer shall

be deemed not to be a swap dealer as a result of its swap dealing activity involving counterparties, so long as the swap positions connected with those dealing activities into which the person—or any other entity controlling, controlled by or under common control with the person—enters over the course of the immediately preceding 12 months (or following the effective date of final rules implementing Section 1a(47) of the Act, 7 U.S.C. 1a(47), if that period is less than 12 months) have an aggregate gross notional amount of no more than $3 billion, subject to a phase in level of an aggregate gross notional amount of no more than $8 billion applied in accordance with paragraph (ggg)(4)(ii) of this section, and an aggregate gross notional amount of no more than $25 million with regard to swaps in which the counterparty is a "special entity" (as that term is defined in Section 4s(h)(2)(C) of the Act, 7 U.S.C. 6s(h)(2)(C), and § 23.401(c) of this chapter), except as provided in paragraph (ggg)(4)(i)(B) of this section. For purposes of this paragraph, if the stated notional amount of a swap is leveraged or enhanced by the structure of the swap, the calculation shall be based on the effective notional amount of the swap rather than on the stated notional amount.

(B) Utility Special Entities. (1) Solely for purposes of determining whether a person's swap dealing activity has exceeded the $25 million aggregate gross notional amount threshold set forth in paragraph (ggg)(4)(i)(A) of this section for swaps in which the counterparty is a special entity, a person may exclude "utility operations-related swaps" in which the counterparty is a "utility special entity."

(2) For purposes of this paragraph (4)(i)(B) a "utility special entity" is a special entity, as that term is defined in Section 4s(h)(2)(C) of the Act, 7 U.S.C. 6s(h)(2)(C), and § 23.401(c) of this chapter, that:

(i) Owns or operates electric or natural gas facilities, electric or natural gas operations or anticipated electric or natural gas facilities or operations;

(ii) Supplies natural gas or electric energy to other utility special entities;

(iii) Has public service obligations or anticipated public service obligations under Federal, State or local law or regulation to deliver electric energy or natural gas service to utility customers; or

(iv) Is a Federal power marketing agency as defined in Section 3 of the Federal Power Act, 16 U.S.C. 796(19).

(3) For purposes of this paragraph (ggg)(4)(i)(B) a "utility operations-related swap" is a swap that meets the following conditions:

(i) A party to the swap is a utility special entity;

(ii) A utility special entity is using the swap in the manner described in § 50.50(c) of this chapter;

(iii) The swap is related to an exempt commodity, as that term is defined in Section 1a(20) of the Act; and

(iv) The swap is an electric energy or natural gas swap; or the swap is associated with: the generation, production, purchase or sale of natural gas or electric energy, the supply of natural gas or electric energy to a utility special entity, or the delivery of natural gas or electric energy service to customers of a utility special entity; fuel supply for the facilities or operations of a utility special entity; compliance with an electric system reliability obligation; or compliance with an energy, energy efficiency, conservation, or renewable energy or environmental statute, regulation, or government order applicable to a utility special entity.

(4) Any person relying upon the exclusion in paragraph (ggg)(4)(i)(B)(1) of this section must file electronically with the National Futures Association a Notice of Reliance on Exclusion for Utility Operations-Related Swaps with Utility Special Entities. The notice must be filed by no later than [effective date of final rule] or the date the person first engages in such swaps, whichever is later. The notice must contain: the person's name, main business address, and main telephone number; the name of a contact; and a statement signed by an individual with authority to bind the person that the person meets the criteria for the exclusion in Regulation 1.3(ggg)(4)(i)(B) (paragraph (ggg)(4)(i)(B) of this section).

(5) Each person who relies on the exclusion in paragraph (ggg)(4)(i)(B) of this section must maintain books and records, in accordance with § 1.31, that substantiate its eligibility to rely on the exclusion in paragraph (ggg)(4)(i)(B) of this section.

* * * * *

Issued in Washington, DC, on May 23, 2014, by the Commission.

Christopher J. Kirkpatrick,

Deputy Secretary of the Commission.

NOTE: The following appendix will not appear in the Code of Federal Regulations.

Appendix to Exclusion of Utility Operations-Related Swaps with Utility Special Entities from De Minimis Threshold for Swaps with Special Entities – Commission Voting Summary

On this matter, Acting Chairman Wetjen and Commissioner O'Malia voted in the affirmative. No Commissioner voted in the negative.

[FR Doc. 2014-12469 Filed 05/30/2014 at 8:45 am; Publication Date: 06/02/2014]