November 24, 2014

***VIA ELECTRONIC SUBMISSION***

Office of the Comptroller
of the Currency
250 E Street, SW, Mail Stop 2-3
Washington, DC 20219

Board of Governors
of the Federal Reserve System
Attn.: Robert deV.Frierson, Secretary
20th Street and Constitution Avenue, NW
Washington, DC 20551

Federal Deposit Insurance Corporation
Robert E. Feldman, Executive Secretary
Attn.: Comments
550 17th Street, NW
Washington, DC 20429

Federal Housing Finance Agency
Alfred M. Pollard, General Counsel
Attn.: Comments/RIN 2590-AA45
Constitution Center
400 7th St., SW
Washington, DC 20024

Farm Credit Administration
Barry F. Mardock, Deputy Director
Office of Regulatory Policy
1501 Farm Credit Drive
McLean, VA 22102-5090

**Re: Comments on the Proposed Rule on Margin and Capital Requirements for Covered Swap Entities (RIN 1557-AD43,7100-AD74, 3064-AE21, 3052-AC69, 2590-AA45)**

Dear All:

The American Gas Association ("AGA"), the American Public Power Association ("APPA"), the Edison Electric Institute ("EEI"), the Electric Power Supply Association

("EPSA"), the Large Public Power Council ("LPPC"), and the National Rural Electric Cooperative Association ("NRECA") (hereafter "Joint Associations") respectfully submit these comments in response to the proposed rule ("Proposed Rule" or "2014 Proposal") issued by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Federal Housing Finance Agency, and the Farm Credit Administration (collectively, the "Prudential Regulators") regarding capital and margin requirements for swap dealers ("SDs") and major swap participants ("MSPs").[1] The Joint Associations have been active participants in the many aspects of the Dodd-Frank Wall Street Reform and Customer Protection Act ("Dodd-Frank Act") implementation process and previously filed comments on the proposed rules addressing capital and margin requirements for SDs and MSPs, issued by the Prudential Regulators in April 2011 ("2011 Proposal")[2]. The Joint Associations appreciate the Prudential Regulators proposal to not require a covered swap entity ("CSE") to impose margin thresholds on non-financial end users and welcome the opportunity to continue to discuss commercial end user-related issues with the Prudential Regulators and their staffs.

## I. Description of the Joint Associations and their Interest in the Proposed Rule

AGA is the national trade association representing U.S. shareholder-owned natural gas distribution companies. There are more than 71 million residential, commercial and industrial natural gas customers in the U.S., of which 94 percent — over 68 million customers — receive their gas from AGA members. AGA is an advocate for natural gas utility companies and their customers and provides a broad range of programs and services for member natural gas pipelines, marketers, gatherers, international natural gas companies and industry associates. Today, natural gas meets more than one-fourth of the United States' energy needs. AGA's members engage in financial risk management transactions with counterparties that may be considered swap dealers or major swap participants that are regulated by the CFTC. As such, AGA's members will be directly affected by regulations promulgated under the Dodd- Frank Act.

APPA is the national service organization representing the interests of publicly-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 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 publicly-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. Public power utilities are accountable to elected and/or appointed officials and, ultimately, the American public. The focus of a public power utility is to provide reliable and safe electricity service, keeping costs low and predictable for its customers, while practicing good environmental stewardship.

---

[1] Margin and Capital Requirements for Covered Swap Entities, 79 Fed. Reg. 57,348 (September 24, 2014) ("NOPR").

[2] Margin and Capital Requirements for Covered Swap Entities, 76 Fed. Reg. 27,564 (May 11, 2011)

EEI is the association of U.S. shareholder-owned electric companies. EEI's members serve 99 percent of the ultimate consumers in the shareholder-owned segment of the U.S. electricity industry, and represent approximately 70 percent of the U.S. electric power industry. EEI also has more than 65 international electric companies as Affiliate members, and more than 170 industry suppliers and related organizations as Associate members.

EPSA is the national trade association representing leading competitive power suppliers, including generators and marketers. These suppliers, who account for nearly 40 percent of the installed generating capacity in the United States, provide reliable and competitively priced electricity from environmentally responsible facilities. EPSA seeks to bring the benefits of competition to all power customers.

The Large Public Power Council is an organization representing twenty-six of the largest locally owned and operated public power systems in the nation. LPPC members own and operate over 75,000 megawatts of generation capacity and nearly 34,000 circuit miles of high voltage transmission lines. Collectively, LPPC members own nearly ninety percent of the transmission investment owned by non-federal public power entities in the U.S. LPPC member utilities supply power to some of the fastest growing urban and rural residential markets in the country. Members are located in eleven states and Puerto Rico and provide power to some of the largest cities in the country, including Los Angeles, Seattle, Omaha, Phoenix, Sacramento, Jacksonville, San Antonio, Orlando, and Austin.

Formed in 1942, NRECA is the national service organization for more than nine hundred not-for-profit rural electric utilities and public power districts that provide electric energy to approximately forty-two million consumers in forty-seven states or twelve percent of the nation's population. Kilowatt-hour sales by rural electric cooperatives account for approximately eleven percent of all electric energy sold in the United States. Because its members are customers of the cooperative, all the costs of the cooperative are directly borne by its consumer-members.[3]

The Joint Associations' members are not financial entities. Rather, they are physical commodity market participants that rely on swaps primarily to hedge and mitigate commercial risk. Regulations that make effective risk management options more expensive for commercial end users of swaps (like electric companies) will likely lead to higher energy prices if the costs

---

[3] 13 C.F.R. §121.201, n.1. The vast majority of NRECA's members meet the definition of "small entities" under the Small Business Regulatory Enforcement Fairness Act ("SBREFA"). Only four distribution cooperatives and approximately twenty-eight G&Ts do not meet the definition. The RFA incorporates by reference the definition of "small entity" adopted by the Small Business Administration (the "SBA"). The SBA's small business size regulations state that entities which provide electric services are "small entities" if their total electric output for the preceding fiscal year did not exceed four million megawatt hours.

associated with new regulations are passed through to retail energy consumers and commercial, and industrial electric customers, or will result in more volatile prices if commercial end users decide to hedge a smaller portion of their commercial risk. Accordingly, as end users of commodity swaps to hedge commercial risk, the Joint Associations' members have a direct and significant interest in rules affecting margin requirements. .

## II. Summary of the Joint Associations' Comments

The Joint Associations are appreciative and supportive of the Prudential Regulator not to require a covered swap entity ("CSE") to impose margin thresholds on non-financial/commercial end users[4]. Joint Associations believe that this is consistent with congressional intent under the Dodd-Frank Act. While generally supportive of the Proposed Rule, the Joint Associations respectfully request that the Prudential Regulators provide the following clarifications to provide additional regulatory certainty.

- Provide certainty by clarifying that non-financial/commercial end users cannot be re-classified as financial end-users under subpart (xiii) of the proposed definition;
- Explicitly state in the regulatory text that non-financial/commercial end users are permitted to continue to use a wide variety of non-cash collateral consistent with the plain language of the Dodd-Frank Act and well-established commercial practice
- Revise the proposed timing requirement for posting margin since non-financial/commercial end users may not be able to meet the T + 1 business process for posting margin.

## III. COMMENTS

### A. Not Requiring Margin and Collateral Requirements for Non-Financial End Users is consistent with Congressional intent and helps avoid ambiguous regulatory treatment by bringing the Prudential Regulator and CFTC rules into closer agreement.

The Joint Associations appreciate the Prudential Regulators acknowledgement in the Proposed Rule that "... application of margin requirements to non-cleared swaps with non-financial end users could be viewed as lessening the effectives of the clearing requirement exemption for these non-financial end users[5] and that unlike the 2011 Proposal, the Proposed

---

[4] FN 58 states "Although the term "commercial end user" is not defined in the Dodd-Frank Act, it is generally understood to mean a company that is eligible for the exception to the mandatory clearing requirement for swaps under section 2(h)(7) of the Commodity Exchange Act and section 3C(g) of the Securities Exchange Act, respectively. This exception is generally available to a person that (i) is not a financial entity, (ii) is using the swap to hedge or mitigate commercial risk, and (iii) has notified the CFTC or SEC how it generally meets its financial obligations with respect to non-cleared swaps or security-based swaps, respectively. *See* 7 U.S.C. 2(h)(7) and 15 U.S.C. 78c–3(g)." NOPR at 57,357.

[5] *Id.* at 57,358.

Rule, consistent with the Dodd-Frank Act, does not require a CSE to impose a margin threshold on non-financial end users.

The Dodd-Frank Act directs the Prudential Regulators and the CFTC to establish margin requirements for swap dealers and MSPs in order "[t]o offset the greater risk to the swap dealer or [MSP] and the financial system arising from the use of swaps that are not cleared."[6] In particular, CEA Section 4s(e)(2)(A) authorizes the Prudential Regulators to adopt margin requirements for swap dealers and MSPs that are banks, whereas CEA Section 4s(e)(2)(B) authorizes the CFTC to adopt margin requirements for swap dealers and MSPs that are not banks.[7] Notably, the Dodd-Frank Act does not authorize the Prudential Regulators or the CFTC to adopt margin requirements that apply to commercial end users. On the contrary, by their own terms these provisions apply only to swap dealers and MSPs and, in particular, to non-cleared swaps entered into between swap dealers and MSPs. CEA Section 4s(e)(3)(D) provides that the Prudential Regulators and the CFTC must adopt margin requirements applicable to swap dealers and MSPs that are "comparable" to the maximum extent practicable.[8]

Joint Associations believe that, despite the use of different terms, both the Prudential Regulator and the CFTC Proposed Rules[9] have the effect of not requiring non-financial end users to post margin which means that the counterparties are able to negotiate the terms and conditions that they feel are necessary to address credit risk. The Proposed Rule states that: Under the Proposal, a covered swap entity's collection of margin from ''other counterparties'' that are not swap entities or financial end users (e.g.,nonfinancial or ''commercial'' end users that generally engage in swaps to hedge commercial risk, sovereigns, and multilateral developments banks), is subject to the judgment of the covered swap entity. That is, under the proposed rule, a covered swap entity is not required to collect initial and variation margin from these ''other counterparties'' as a matter of course."[10] This is consistent with the lesser risk posed by nonfinancial end users. It is entirely appropriate for *both* the Prudential Regulators and the CFTC to exempt such counterparties from margin requirements that would frustrate the effectiveness of other provisions of the Dodd Frank Act and of rules promulgated thereunder. This consistent approach by all covered agencies also poses less risk of confusion from inconsistent approaches by CSEs.

---

[6] CEA Section 4s(e)(3)(A)

[7] CEA Section 4s(e)(3)(A)-(B).

[8] CEA Section 4s(e)(3)(D). CEA Section 4s(e)(3)(D) requires the CFTC and Prudential Regulators "to the maximum extent practicable, [to] establish and maintain comparable . . . minimum initial and variation margin requirements, including the use of non-cash collateral."

[9] Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants: Proposed Rule, 79 Fed. Reg. 59,898 (October 3, 2014) ("CFTC Proposed Rule").

[10] NOPR at 57,354.

### B. Prudential Regulators Should Clarify that Commercial End Users Cannot be Re-characterized as Financial End Users Under Subpart (xiii) of the Proposed Definition

The Proposed Rule sets forth a list of entities that would be financial end users as well as a list of entities excluded from the definition. The Proposed Rule indicates that this "approach would mean that covered swap entities would not need to make a determination regarding whether their counterparties are predominantly engaged in activities that are financial in nature, as defined in section 4(k) of the Bank Holding Company Act of 1956, as amended (the BHC Act)"[11] The last category in the list of enumerated financial end users states that notwithstanding the specified exclusion any other entity can be designated as a financial end user.[12] It appears that the Commission included this provision due to concerns that the list may not capture a particular entity where it may be useful to treat the counterparty as a financial end user "for safety or soundness purposes or to address systemic risk."[13] Joint Associations believe that this vague and standardless provision, which potentially allows for arbitrary categorization of non-financial commercial end users as financial end users, brings unnecessary uncertainty to commercial end users accessing swaps markets to hedge risk.

The Joint Associations request that the Prudential Regulators delete this provision from the Proposed Margin Rule or in the alternative clarify that commercial end users are exempt from this provision. Implementing such a vague requirement would not serve the intended purpose of providing greater safety to the market. The proposal only adds another layer of uncertainty to the rules as exercise of the provision would have a material economic impact on the commercial end user affected. The Prudential Regulators provide no parameters, objective standards, or procedural protections for how such a decision to treat non-financial end users as financial end users for margin purposes would be made. The Prudential Regulators proposed no specific metrics, either on a quantitative or qualitative basis, outlining how it would make such a determination. Additionally, such a proposal lacks a method for sufficient notice and comment to be made to the affected non-financial end user. The Prudential Regulators fail to describe how requiring such treatment of non-financial end users under such vague circumstances would enhance the safety of the marketplace or otherwise further the stated goals of the statute to increase the stability of the swaps market or the broader financial system.

The Joint Associations argue that the other elements of the existing proposal contain sufficient rules and safeguards that avoid the need for any perceived "safety" that such a vague provision as that proposed herein would achieve. As such, the Joint Associations request that the Prudential Regulators delete this provision from the regulations.

---

[11] NOPR at 57,360.

[12] *Id.* at 57,361.

[13] *Id.*

### C. Permitting the Use of a Wide Variety of Non-Cash Collateral is Consistent with the Plain Language of the Dodd-Frank Act and Well-Established Commercial Practice.

CEA Section 4s(e)(3)(C) provides that "[i]n prescribing margin requirements . . . the prudential regulator . . . shall permit the use of noncash collateral, as [it]. . . determines to be consistent with . . . (i) preserving the financial integrity of markets trading swaps; and (ii) preserving the stability of the United States financial system."[14] The Joint Associations commend the Prudential Regulators for expanding the list of acceptable securities, in response to comments received on the 2011 Proposal, but believe that the list remains unnecessarily restrictive and should be expanded to include a wider array of conventional credit support instruments.

The Proposed Rule states that a CSEs can collect initial and variation margin "...at such times and in such forms and amounts (if any) as the covered swap entity determines would appropriately address the credit risk posed by swaps entered into with "other counter parties."[15] Despite the use of the phrase "if any", the Prudential Regulator's proposal does not allow a covered swap entity to fulfill the minimum margin requirements with any forms of non-cash collateral not included in the list of liquid and readily marketable assets that are found in §_.6 Eligible collateral.[16] However, the Prudential Regulators state that differential treatment of "other counterparties" is consistent with the Dodd-Frank Act's risk-based approach to establishing margin requirements. The Joint Associations request that the Prudential Regulators should explicitly state in the regulation that non-financial end users are permitted to use all forms of collateral as appropriate to their industry's practice. This would be consistent with the statement in the preamble section that margin collected by a covered swap entity in connection with a non-cleared swap with an "other counterparty" can be in any form of collateral including forms other than the types of collateral specified in the rule.[17]

Any requirement that non-financial end users to post substantial cash collateral with swaps clearing houses would harm liquidity and significantly impair non-financial end user's ability to efficiently deploy capital. The narrow list of acceptable collateral proposed by the Prudential Regulators may inadvertently create significant cash flow and operational challenges for commercial end users that use swaps to hedge commercial risk. Many commodity market participants rely on a wide range of credit support, such as mortgages and other liens on physical assets, letters of credit, pledges of stock, payment guarantees, deposit accounts or cash management agreements, and other arrangements, to provide credit support for their swap transactions. In the electric and natural gas industries, swaps (and the physical commodity transactions they hedge) often are unsecured or secured by collateral that would not satisfy the Prudential Regulators' narrow requirements. Such credit support arrangements are not

---

[14] CEA Section 4s(e)(3)(C).

[15] NOPR at 57,358.

[16] *Id.* at 57,392-57,393

[17] *Id.* at 57,371.

analogous to the dollar-for-dollar margin commonly used in transactions between financial entities. For example, utilities and other energy market participants often rely on their highly-reliable source of cash flow (*i.e.*, rate payers) and valuable tangible assets (*i.e.*, natural gas plants or power plants) as much as or more than formal credit support arrangements to support their payment obligations on swaps. Commercial end users use this combination of unsecured credit and diverse collateral responsibly and in a manner that reduces commercial risk and promotes the stability of the United States financial system.[18]

As such, the Prudential Regulators should explicitly state in the regulation that commercial end users counterparties may rely on any form of non-cash collateral that is mutually agreeable to it and its CSE/covered swap counterparty. Joint Associations would propose inserting the language found on page 57371 of the Proposed Rule to sections §_.3 (d) Initial margin and §_.4 (c) Variation margin as follows:

> §_.3 (d), A covered swap entity is not required to collect initial margin with respect to any non-cleared swap or non-cleared security-based swap with a counterparty that is neither a financial end user with material swaps exposure nor a swap entity but shall collect initial margin at such times and in such forms, **including forms other than the types of collateral specified in the rule (*e.g.*, letters of credit or credit support agreements)** and such amounts (if any), that the covered swap entity determines appropriately address the credit risk posed by the counterparty and the risks of such non-cleared swaps and non-cleared security-based swaps.
>
> §_.4 (c) A covered swap entity is not required to collect variation margin with respect to any non-cleared swap or non-cleared security-based swap with a counterparty that is neither a financial end user nor a swap entity but shall collect variation margin at such times and in such forms, **including forms other than the types of collateral specified in the rule (*e.g.*, letters of credit or credit support agreements)** and such amounts (if any), that the covered swap entity determines appropriately address the credit risk posed by the counterparty and the risks of such non-cleared swaps and non-cleared security-based swaps.

Joint Associations also request that beyond what is stated in §_.7 of the Proposed Rule, the Prudential Regulators clarify that nothing in this rule impacts a non-financial end users ability to negotiate the manner in which their posted initial and variation margin will be maintained. This will help ensure that non-financial end users continue to have the ability to negotiate these terms.

---

[18] CEA Section 4s(e)(3)(C).

### D. The Commission Should Revise the Proposed Timing Requirement for Posting Margin

In the Proposed Margin Rule, the Prudential Regulators propose to require each CSE to collect initial margin for every swap with a single counterparty on or before the business day following the day it enters into the transaction and ending on the date the non-cleared swap is terminated or expires.[19] The Joint Associations request that the Prudential Regulators amend this proposal to allow two business days before collection of margin is required rather than the one day as proposed, at least as it applies to non-financial counterparties. Such a change would still ensure that any necessary margin is collected within a reasonable time period, but would allow non-financial end users, that are required to post margin, sufficient time to ensure that any necessary transfer of funds can be fully implemented.

Without amending this proposal to allow for an extra day to post margin, any non-financial entities would face extreme challenges to ensure that appropriate margin is posted in a timely manner to comply with the rule since any entity would need to calculate the appropriate margin after daily close and then request from their financial institution to transfer the appropriate funds. Commercial end users that are members of the Joint Associations may utilize, for example, letters of credit (LOCs) to support their collateral posting requirements for hedging transactions. The LOCs are typically provided by financial institutions, the terms of which often require the commercial end user to notify the bank 2 days in advance in order to draw on the letter of credit to meet a collateral posting requirement. Further, a request to an entity's financial institution to draw upon funds from a line of credit facility must be made before a notification time (i.e. 11:00 a.m. Eastern Standard Time) to ensure next day availability. If the request to draw appropriate funds is received after the financial institution's notification time, the funds will not be available for a margin payment until the second business day. Therefore, amending the regulations to allow for 2 business days to post margin would ensure that all entities, regardless of their status, would have sufficient time to meet the requirement while still ensuring there is not an unreasonable time lag between the close and the posting of margin.

## IV. Conclusion

The Joint Associations' appreciate the opportunity to submit these comments and are supportive of the Prudential Regulators proposal to not require non-financial end users to post margin. This is consistent with congressional intent to ensure that commercial end users and their non-financial affiliates are exempted from regulatory requirements that Congress intended to apply only to swap dealers and MSPs. Joint Associations request that the Prudential Regulators provide additional certainty by providing the clarifications requested herein. Please contact us at the numbers listed below if you have any questions regarding our comments.

---

[19] *Id.* at 57,368.

Respectfully Submitted,

Richard F. McMahon, Jr.
Vice President
Lopa Parikh
Director, Regulatory Affairs
Edison Electric Institute
701 Pennsylvania Avenue, N.W.
Washington, D.C. 20004
Phone: (202) 508-5058
Email: lparikh@eei.org

Melissa M. Mitchell
Director of Regulatory Affairs and Counsel
Electric Power Supply Association
1401 New York Avenue, NW
Suite 1230
Washington, DC 20005
202-349-0151
mmitchell@epsa.org

Russell Wasson
Director of Tax, Finance and
Accounting Policy
National Rural Electric Cooperative
Association
4301 Wilson Blvd., EP11-253
Arlington, VA 22203
russell.wasson@nreca.coop

James C. Cater
Director of Economic and Financial Policy
American Public Power Association
2451 Crystal Drive
Suite 1000
Arlington, VA 22202-4804
jcater@publicpower.org

Noreen Roche-Carter
Chair, Large Public Power Council Tax
and Finance Task Force
6201 S St.
Sacramento, CA 95817-1899
nrochec@smud.org

Arushi Sharma Frank
Counsel, Regulatory Affairs
American Gas Association
400 N. Capitol St., NW
Washington, DC 20001
asharma@aga.org/202.824.7120