March 18, 2019

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Re: Comment to Notice of Proposed Rulemaking – Standardized Approach for Calculating the Exposure Amount of Derivative Contracts:
OCC, Capital Adequacy: Standardized Approach for Calculating the Exposure Amount of Derivative Contracts, Docket ID OCC-2018-0030;
Federal Reserve Docket No. R-1629 and RIN 7100-AF22;
FDIC Docket No. RIN 3064-AE80

The Central Plains Energy Project ("CPEP"), a separate legal entity and a public body corporate and politic and an instrumentality of its members, organized under the laws of the State of Nebraska, appreciates the opportunity to provide comments in response to the Notice of Proposed Rulemaking regarding proposed revisions to the standardized approach for calculating the exposure amount ("SA-CCR") of derivatives contracts of large banks (the "Proposed Rule"). The Proposed Rule, issued jointly by the Office of the Comptroller of the Currency ("OCC"), the Board of Governors of the Federal Reserve System (the "Board"), and the Federal Deposit Insurance Corporation (the "FDIC", and together with the OCC and the Board, the "Prudential Regulators")[1], threatens to result in significant and unnecessary costs for CPEP and other end-user companies and governmental organizations. Specifically, CPEP is most concerned that large banks acting in the role of prepaid gas supplier or commodity swap counterparty in natural gas prepayment

[1] Prudential Regulators, Notice of Proposed Rulemaking, *Standardized Approach for Calculating the Exposure Amount of Derivative Contracts*, 83 Fed. Reg. 64660 (Dec. 11, 2018), available at https://www.federalregister.gov/documents/2018/12/2018-24924/standardized-approach-for-calculating-the-exposure-amount-of-derivative-contracts [hereinafter, the "Proposed Rule"].

transactions will be required, or will interpret the rule as requiring, capital set asides beyond those that currently exist, if any, under current statutory and regulatory standards.

1. <u>Introduction – CPEP's Participation in Derivatives Markets</u>

CPEP's members are the Metropolitan Utilities District of Omaha, Nebraska; the City of Hastings, Nebraska d/b/a Hastings Utilities; and the Municipal Gas Utility of the City of Cedar Falls, Iowa. CPEP is a governmental entity. Its Board of Directors is comprised of appointed representatives of it members.

CPEP is a joint action gas supply agency that provides wholesale sales service to municipal gas systems. It is an end user that benefits from the statutory end user exception from mandatory clearing and the exemption from margining requirements.

CPEP is a continuous participant in the municipal gas marketplace, including the marketplace for long-term gas supplies, and is a participant in derivatives transactions. Long-term gas supplies are essential to enable CPEP to meet the needs of its customers for reliable, secure, firm natural gas deliveries at reasonable and competitive prices. One of the primary strategies to meet these needs which CPEP has pursued in recent years, is pursuing today, and intends to pursue in the years to come is the purchase of natural gas supplies through gas prepayment transactions under Internal Revenue Code Section 148(b)(4) and Treasury Regulations. Large banks and their commodities affiliates are among the primary participants in this marketplace as gas suppliers and/or as commodity swap counterparties. As such they provide an essential service to the municipal gas industry, one that we believe could not and would not be replicated or replaced by other industry participants, at least not under market conditions that have prevailed over at least the past 12 years.

Gas prepayment transactions contain matched, customized commodity swaps as essential components. These are so-called "tear up" swaps. There is no mark-to-market exposure to either counterparty upon early termination of the swaps, only exposure for accrued but unpaid amounts owed by one party or the other.

CPEP completed its first gas prepayment transaction in 2007 and its fourth and most recent such transaction in the Fall of 2018. Through its active participation in this marketplace, it has saved its members, other participating municipalities, and the gas consuming public millions of dollars in the price of gas for space heating, cooking, water heating and industrial applications.

2. The SA-CCR NOPR's Effect and Potential Effect

The Prudential Regulators have proposed a new methodology for measuring derivatives counterparty credit risk known as the "Standardized Approach for Counterparty Credit Risk" or "SA-CCR". As proposed, large banks would be required to adopt SA-CCR by July 2020.

As proposed, the SA-CCR methodology would significantly raise banks' capital requirements for natural gas derivatives, with the largest impacts being on derivatives executed with end users, like CPEP. While banking organizations may absorb some of these increased capital costs, CPEP fears, and believes, that the potential magnitude of the increase will result in the following:

(1) the transfer of all or a significant portion of the increased cost to end users, including CPEP, which will have a direct effect on our costs, leading in turn to higher prices for natural gas service for our customers and the consumers they serve, and a negative impact on local economies, and potentially making gas prepayment transactions uneconomic for us;

(2) increased pressure on banking organizations to collect margin from end users or submit transactions to exchanges for clearing, notwithstanding the hard-fought efforts by end users, including CPEP, to be exempted from mandatory margin and clearing requirements; and

(3) a decrease in the overall liquidity in natural gas derivatives markets, as some banking organizations may choose to exit the market due to higher transaction costs, resulting in increased concentration risk and the lack of access to unique transactions such as gas prepayments and their customized commodity swaps.

3. CPEP End User Perspective

SA-CCR proposes increases in capitalization requirements that will increase the cost of doing business for banks participating in the natural gas markets as prepaid gas suppliers and as commodity swap counterparties. This would have the result of increasing the cost of natural gas prepayments for CPEP and therefore for consumers served by our municipal gas system customers. The economics of gas prepayments in the marketplace that have prevailed over the last several years make the successful completion of such projects difficult. Any increase in the cost to prepaid gas suppliers of providing the supply and/or on counterparties to participate in matched commodity swaps has a negative effect on our ability to close those transactions. We fear that if implemented, the SA-CCR could convince some banks to withdraw from the physical gas markets and commodity swap markets as it becomes more difficult to operate profitably in them. A reduction in the number of prepaid gas suppliers in the market will be detrimental to municipal gas systems.

In sum, we are concerned that significant capital requirements for commodity derivatives with end users, including municipalities, may significantly affect the ability of municipal organizations such as CPEP to obtain reliable access to natural gas supplies through gas prepayment transactions, as well as frustrate the policy goals of exempting end users, including municipalities, from mandatory clearing and margin requirements, ultimately resulting in increased costs to the consumer.

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4. Conclusion

For the foregoing reasons, CPEP respectfully requests that the proposed SA-CCR NOPR should not be applied to banks' commodities transactions with end users, including governmental end users such as CPEP who utilize supply contracts and commodity swap contracts in the natural gas industry for long-term supply reliability, price competitiveness, and price protection for the consumers they serve.

Respectfully submitted,

[redacted]

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