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May 1, 2013

The Honorable Debbie Stabenow
Chairwoman
Committee on Agriculture, Nutrition and
Forestry
United States Senate
Washington, D.C.20510

The Honorable Thad Cochran
Ranking Member
Committee on Agriculture, Nutrition and
Forestry
United States Senate
Washington, D.C.20510

Dear Chairwoman Stabenow and Ranking Member Cochran:

The Los Angeles Department of Water and Power (LADWP) appreciates this opportunity to provide input to the Agriculture Committee about the reauthorization of the Commodity Futures Trading Commission (CFTC) and the implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (Dodd-Frank Act). Specifically, we are concerned that the CFTC's interpretation and implementation of the Dodd-Frank Act unnecessarily hampers the ability of public power utilities to use swaps to hedge commercial risk. As the nation's largest municipal water and power utility, LADWP depends on the ability to use swaps to procure fuel and provide reliable electric energy at reasonable and stable prices in order to fulfill our public service obligations to our over 4 million consumers.¹

Under the Dodd-Frank Act, entities that are defined as swap dealers or major swap participants are subject to a myriad of CFTC regulations such as registration requirements, business conduct standards, clearing and exchange trading, capital and margin requirements, position limits, and various reporting and recordkeeping duties (collectively "swap regulations"). The Dodd-Frank Act also imposes certain requirements on swap dealers and major swap participants transacting with "special entities," which are defined in the statute to include among other entities, a State, State agency, city, county, municipality, or other political subdivision of a State. As a municipally-owned utility, LADWP is considered a special entity under the Dodd-Frank Act.

The CFTC provided that anyone entering into more than a de minimis amount of transactions with special entities (currently \$800 million per year, but it was set in the final rule as \$25 million) will be subject to the swap dealer regime. A different and much higher de minimis threshold (currently \$8 billion per year), however, was set as the "swap dealer" trigger for transactions with entities that are not special entities, such as

¹ LADWP was established more than 100 years ago to deliver reliable, safe water and electricity to 4 million residents and businesses in the City of Los Angeles. LADWP provides its 666,000 water customers and 1.4 million electric customers with quality service at competitive prices. A five-member Board of Water and Power Commissioners establishes policy for the LADWP, which is a revenue-producing proprietary department of the City of Los Angeles.

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privately-owned utilities and cooperatives. While LADWP understands the general motivation behind a policy to protect special entities, in this case, the differentiation between special entities that are public power utilities and other utilities - both of which have public service obligations - is not justified, increases operational risks, and imposes economic disadvantages.

LADWP is governed by a Board of Commissioners, a 15-member full-time City Council and a Mayor. The governance oversees a strong Risk Management Policy and independent auditor review. As a utility with jointly-owned generating and transmission facilities in seven western states, and one of the most aggressive renewable energy programs in the country, the annual fuel and purchased power budget exceeds \$1.5 billion. Many of these utility facilities are jointly-owned with Investor-Owned Utilities (IOUs) that are not special entities. LADWP and the IOUs (collectively, the "Parties") enter Inter-Party agreements to manage operations and hedge risks. Having a different regulatory paradigm for hedging creates the potential for violations and is now limiting the Inter-Party and joint transaction options that previously existed between the Parties. The special entity sub-threshold is stranding some of the value of these historical investments and relationships between LADWP and the IOUs because IOUs working with LADWP do not want to have to register or risk registering as swaps dealers.

LADWP maintains that municipally-owned utilities have the same expertise in hedging price risks as other utilities, and therefore should be treated the same when it comes to swaps. Many of our current counterparties are nonfinancial entities (such as IOUs, independent producers, and natural gas suppliers) engaged in the electric and natural gas industry in the same geographic area as we are. These counterparties have indicated that they want to avoid the risk of tripping over the special entity sub-threshold and having to register as a "swap dealer." These counterparties can rely on a much higher safe harbor threshold of \$8 billion (which eventually will phase down to \$3 billion) when transacting with IOUs or cooperative utilities than with special entities. The protection intended by the CFTC in establishing the lower, currently \$800 million sub-threshold in fact puts special entity utilities at a competitive disadvantage to other utilities by hindering our ability to hedge operational risks.

The lower de minimis sub-threshold will make it harder for special entity utilities to find willing nonfinancial counterparties that can provide needed market competition and highly customized and regional products that "Wall Street" firms are unable or unwilling to provide. If we cannot cost-effectively hedge our commercial risks, consumers will confront more volatile and higher rates for energy or, even worse, face risks to their electric grid reliability.

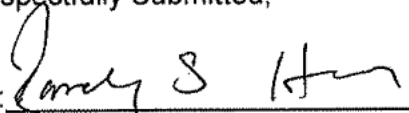
The comments submitted to this Committee by the American Public Power Association (APPA) and Large Public Power Council (LPPC), groups of which LADWP is a member, outline the efforts that have been undertaken to petition the CFTC to amend the swap-dealer rule to exclude utility special entities' utility operations-related swap transactions from counting towards the special-entity threshold. The CFTC's response to these efforts was an October, 12, 2012, no-action letter that allows a counterparty to deal in up to \$800 million in swaps (instead of \$25 million) with government-owned utilities without being required to register as a swap dealer. While we appreciate the CFTC's attempt to address the problem, the solution provided in the October 2012 no-action letter has proven insufficient.

On November 19, 2012, APPA and LPPC submitted a letter to the CFTC explaining our concerns with the no-action letter fix and reiterating the need for effective relief as requested in our July 12, 2012, petition.² Although some of the CFTC commissioners have voiced agreement that more effective relief is appropriate, it has become apparent that without a legislative fix there may be no real relief for public power entities like LADWP.

LADWP strongly encourages the Senate Agriculture Committee to include a legislative solution to address the utility special entity sub-threshold problem as part of CFTC reauthorization or as a stand-alone bill. The Committee may wish to consider the Public Power Risk Manage Act of 2013 (H.R. 1038), which was introduced by Congressmen Doug LaMalfa (R-CA), Jim Costa (D-CA), Jeff Denham (R-CA), and John Garamendi (D-CA) and House Financial Services Committee member Blaine Luetkemeyer (R-MO) and reported out by the House Agriculture Committee on March 20, 2013, as a framework for its solution. .

Without a legislative fix, the current \$800 million sub-threshold will leave government-owned utilities, which need to hedge commercial risks of their energy operations in the same way as other utility providers, as hostage counterparties to large financial institutions, or in some cases without any available counterparties. We appreciate your consideration of our concerns and look forward to working with you to ensure an effective solution.

Respectfully Submitted,

By: 

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²November 19, 2012 Letter available at:

http://www.lppc.org/issues/cftc/LPPC_CFTC_Letter_to_Chairman_Gensler_November_19_2012.pdf