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Autorité des marchés financiers
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Manitoba Securities Commission
New Brunswick Securities Commission
Nova Scotia Securities Commission
Ontario Securities Commission

c/o:

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c/o:

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Dear Sirs/Mesdames:

RE: Comment Letter to CSA Staff Consultation Paper 91-405 – *Derivatives: End-User Exemption*

Capital Power Corporation (“**CPC**”), CP Energy Marketing LP (“**CPEM**”) and CP Energy Marketing (US) Inc. (“**CPEMUS**”) and their other affiliates and subsidiaries (collectively, “**Capital Power**”) make this submission to comment on Consultation Paper 91-405 - *Derivatives: End-User Exemption* (“**CSA Paper 91-405**”), which outlines an exemption (the “**End-User Exemption**”), for businesses who utilize over-the-counter derivatives (“**OTC Derivatives**”) to manage and mitigate the risks related to their operations, from a number of the proposed requirements the Committee is recommending for the regulation of OTC Derivatives.

Capital Power appreciates the opportunity to comment on the CSA paper 91-405 and is supportive of the efforts of the CSA to exempt such “eligible market participants” from many of the proposed regulatory requirements with respect to OTC Derivatives, such as the central clearing or registration requirement, but not from the requirement to report trading activity to a trade repository (“**TR**”). We would also like to thank the Alberta Securities Commission (the “**ASC**”) for providing an extended opportunity for us to comment on the proposed regulatory

requirements contained in CSA Paper 91-405 in conjunction with providing comments on *CSA Staff Consultation Paper 91-407- Derivatives Registration* (“**CSA Registration Paper 91-407**”) although the comment period for CSA Paper 91-406 closed in September 2012.

Capital Power is an independent power producer that owns more than 3600MW of power generation capacity across 15 facilities in Canada and the United States, with an additional 595MW of generation currently under construction or in advanced development. Capital Power operates and optimizes power generation from a variety of fuel sources including coal, natural gas, bio-waste and wind. In Alberta, Capital Power’s portfolio, including interests in joint venture facilities, comprises approximately 1000MW of merchant generation capacity. Assuming an Alberta electricity pool price of \$60/MWh, Capital Power’s Alberta portfolio represents an annual notional value of approximately half a billion dollars for which the commodity price exposure is actively managed and optimized. Capital Power optimizes and hedges its portfolio using physical forward contracts for electricity, natural gas, environmental commodities and USD/CDN currency exchange, and financial derivative transactions based on those same commodities. Capital Power’s trading counterparties include other independent power producers, utility companies, banks, hedge funds and other energy industry market participants. Trading activities take place through electronic exchanges, such as ICE (Intercontinental Exchange) and NGX (Natural Gas Exchange), brokered transactions and directly with counterparties. Approximately 90% of Capital Power’s energy commodity derivatives trading take place through regulated exchanges.

GENERAL COMMENTS

Capital Power notes that although the Committee sets out the CSA’s position that the rationale behind the End-User Exemption is to prevent hardship, to businesses that utilize OTC Derivatives to manage and mitigate risks related to their operations, that may be caused by some of the new regulatory requirements such as registration, the Committee does not propose an End-User Exemption for “eligible market participants” from the registration requirement in CSA Registration Paper 91-407.

One of the factors listed by the Committee in CSA paper 91-405 to be considered as a criterion for eligibility for the End-User Exemption is “hedging to mitigate commercial risks related to the operation of a market participant’s business”. The Committee considers the term “hedging” in this instance to include End-Users who trade in OTC Derivatives for the purposes of mitigating risk related to the operation of business. The Committee stated that market participants who trade OTC Derivatives to generate profit will not be considered End-Users for the purposes of the exemption and may be required to meet registration requirements. The position taken by the CSA in CSA Paper 91-405 with respect to hedging is contrary to the position taken in CSA Registration Paper 91-407, in which the Committee has not proposed to exclude entities that predominantly use OTC derivatives to hedge and mitigate commercial risks that arise out of their operations from the proposed registration requirements.

CAPITAL POWER’S RESPONSE TO CERTAIN QUESTIONS IN CSA PAPER 91-405

Capital Power has the following responses to questions raised by the Committee in CSA Paper 91-405:

Q1: Do reporting obligations create any barriers to participation in the derivatives market that would be unique to the end-users or category of end-users?

Capital Power does not believe that reporting obligations, per se, would create any barriers to participation in the derivatives market for end-users, however we submit that, after having reviewed the first proposed model rules with respect to reporting obligations contained in CSA Paper 91-301, Capital Power (potentially eligible for the End-User Exemption), remains concerned about uncertainty surrounding the pending final rules regarding the reporting obligations, including what kind of reporting infrastructure we would need to build and the costs attached thereto.

Q2. Are the end-user eligibility criteria proposed by the Committee appropriate?

For the most part Capital Power believes that the proposed end-user eligibility criteria are appropriate. We submit however that the proposed disqualification, from “end-user” status, of market participants who trade to generate profit through speculative derivatives trading is not appropriate. Capital Power strongly disagrees with the statement that: “*Speculation does not involve mitigating a commercial risk related to the operation of the business because it is based on a trading strategy independent of other aspects of the business*”. Speculative trading for one’s own account, along with hedging, are both risk mitigation and asset optimization tools that allow derivatives market participants to manage commercial risks associated with their business and to optimize asset value through gathering of market intelligence, including commodity price discovery. These activities, and the strategies behind them, are inextricably and directly linked to optimizing shareholder value, which is the paramount objective of any business enterprise. Speculative trading in the derivative end-user context does not pose systemic risk to Canada’s financial system.

Q3: Should alternative or additional criteria be considered?

See Capital Power’s response to question 2 above.

Q4. Are the Committee’s recommendations to exclude the specified end-user eligibility criteria from consideration appropriate?

Capital Power submits that it is not appropriate for the Committee to recommend excluding the specified end-user eligibility criteria because doing so causes legal uncertainty for entities in their determination of eligibility for the End-User Exemption. The U.S. agencies under the Dodd-Frank Act regulatory regime have specified eligibility criteria for various exemptions such as the end-user exception from the clearing requirement, the de minimis exemption, the exclusion of “swaps” used for hedging and mitigating of commercial risks and the exclusion of “forward contracts” and foreign exchange forwards and swaps, to name a few. Providing eligibility criteria has provided market participants certainty in their assessment for eligibility for the exemptions provided to implement the Dodd-Frank Act.

Q5. Is the Committee’s proposal that the market participant itself determines its qualification for an exemption and provide notice to the regulator of its intention to rely on the exemption appropriate?

See Capital Power's response to question 4 above.

CONCLUSION


Capital Power continues to support the Committee and the CSA's efforts to regulate the OTC derivatives market in Canada, but would strongly urge the Committee to provide clarity as it continues to consider the regulatory tools at its disposal. Capital Power also urges the CSA to continue to strive for uniformity in the development and application of all rules and regulations with similar rules in the US that affect the same OTC derivative transactions. A coordinated approach to implementation of reform efforts will be the most effective and least onerous for Canadian market participants in terms of minimizing incremental compliance costs and putting Canadian market participants at a competitive disadvantage compared to their foreign counterparts.

Capital Power respectfully requests that the Committee consider its comments. Capital Power looks forward to further consultation papers and model rules prior to the creation of legislation and regulations to govern the Canadian OTC derivatives markets. If you have any questions, or if we may be of further assistance, please contact either the undersigned at 403-717-4622 (znagy-kovacs@capitalpower.com).

Yours Truly,

"CAPITAL POWER"

Per:



Zoltan Nagy-Kovacs
Senior Legal Counsel