INTERNATIONAL ENERGY CREDIT ASSOCIATION

Be Informed.
Stay Connected.

Final

October 7, 2022

Christopher Kirkpatrick, Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Comments Submitted via CFTC Comments Portal: https://comments.cftc.gov

Re: Request for Information on Climate-Related Financial Risk, 87 Fed. Reg. 34856, published June 8, 2022 ("Climate-Related Financial Risk RFI")

Dear Mr. Kirkpatrick:

The International Energy Credit Association ("**IECA**") appreciates the opportunity to submit these comments ("**IECA Comments**") to the Commodity Futures Trading Commission ("**CFTC**" and "**Commission**") regarding the CFTC's above-captioned *Request for Information on Climate-Related Financial Risk* ("**Climate-Related Financial Risk RFI**" or "**RFI**").

We appreciate that the CFTC is seeking responses to this Climate-Related Financial Risk RFI to "better inform its understanding and awareness of climate-related financial risk as pertinent to the derivatives markets and underlying commodities markets," which will "help to inform the Commission's next steps in furtherance of its purpose to, among other things, promote responsible innovation, ensure the financial integrity of all transactions subject to the Commodity Exchange Act, and avoid systemic risk." We also understand that our comments and those of others responding to this Climate-Related Financial Risk RFI will "inform the Commission's response to the recommendations of the Financial Stability Oversight Council 2021 Report on Climate-Related Financial Risk and inform the ongoing work of the Commission's Climate Risk Unit."

In that light, we respectfully offer these IECA Comments, which will focus on the "transition risks" portion of the Commission's consideration of Climate-Related Financial Risks. As explained below, we recommend that the CFTC recognize that this transition to a clean energy economy will, by necessity, involve a prolonged transition period of many years during which the U.S. economy will consume significant quantities of fossil fuels.

I. IECA Comments.

The Commission recognized in its RFI that Climate-Related Financial Risks can be divided into two categories, Physical Risks and Transition Risks. On page 34857 of its RFI, the CFTC offered the following description of "*Climate-Related Financial Risks:"*

> The effects of climate change and the transition to a low-carbon economy present emerging climate-related financial risks, which fall into two broad categories: Physical risks and transition risks.2 Physical risks generally are characterized by harm caused by acute, climate-related events such as hurricanes, wildfires, floods, and heatwaves; and chronic shifts in precipitation patterns, sea level rise, and ocean acidification.3 These extreme weather events and natural disasters, especially as they increase in frequency and/or intensity, can damage assets, disrupt operations, and increase costs.4 Transition risks generally are characterized by stresses to certain financial institutions or sectors that result from shifts in policy, regulations, customer and business preferences, technology, credit or insurance availability, or other market or social forces that can affect business operations.5" (Emphasis added.)

These IECA Comments are intended to focus the CFTC's attention on "Transition Risks."

A. Energy Transition Period Defined.

The entire global community is in the process of a global "energy transition," which, we hope, will lead to a global economy powered by cleaner sources of energy with zero, or at least "net zero," emissions of GHGs by 2050, possibly a little sooner or a little later. By definition then, the global economy faces a transition period of approximately 28 years.

The primary reason the transition will take 28 years is the enormous scale of the global use of energy. Much of the equipment and infrastructure used to produce and distribute GHG emitting fuels has a useful life of 20-30 years and much of the equipment used to consume GHG emitting fuels, such as automobiles, have a useful life of 10 years. Replacing all of that equipment would, by itself, take many years to accomplish.

But the task is complicated beyond the sheer size of the equipment and systems that need to be replaced, by the additional fact that significant technological innovations need to be invented, tested, and scaled-up to commercial operation levels, before those technologies can take on the role of providing the type of clean, affordable, plentiful, and reliable energy on which our modern economy depends. Since many of those innovations have yet to be invented and proven at commercial scale, we cannot know for certain which technological innovations will ultimately be the choice of the clean-energy future.

As a result, the amount of time required for our energy transition is actually increased by the fact that numerous technological innovations remain to be invented before the use of cleaner sources of energy can be achieved.

IECA • 1120 Route 73, Suite 200, Mt. Laurel, NJ 08054 USA • Ph 856-380-6854 • Fax 856-439-0525

For example, there are many technological innovations still waiting to be created. Just to name a few: the development of long-duration batteries; the production of clean electric vehicles (EVs) to replace the existing millions of fossil fuel vehicles (FFVs); the creation of quick-recharging technologies to recharge those EVs in the mere minutes now required to refuel FFVs; the installation of EV-recharging facilities across the U.S. to allow drivers to use EVs to travel across the wide expanse of land in the U.S.; the mining of enormous quantities of lithium required for all the new batteries that will be required by EVs and preferably that lithium can be sources in countries not hostile to the U.S.; the development of electrolytic or other clean production means of producing massive quantities of clean-burning hydrogen needed to decarbonize those industries that cannot be decarbonized using batteries, such as airlines, shipping, steel-making, and cement-making.

Plus, renewable sources of electricity generation, such as solar and wind, are only available during certain hours of each day, this intermittency means that some other source of clean, affordable, and reliable electricity generation must be supplied during the hours that intermittent renewable energy is unavailable, if our global economy is going to rely on cleaner sources of electric energy to achieve our aspirational level of "net zero" or actual zero emissions of GHGs by 2050. Conceptually, that clean, affordable and reliable electricity during the hours each day (or night!) that renewable energy is unavailable could come from larger, long-duration, and more plentiful batteries, or perhaps from nuclear power, or from hydrogen fueled combustion turbines, or from fossil-fuel fired generators with carbon capture and storage.

In other words, some form of technology-neutral solution must yet be chosen and developed, to fill the gap left by intermittent renewable energy sources, if our global economy is going to have clean, affordable, plentiful and also RELIABLE energy resources on which our global economy and our standard of living can rely and grow.

It cannot be forgotten that there remain many people in the world still without access to basic electricity supplies. Their impoverished standard of living is abysmal by any measure. Any climate-change responsive energy transition policy that pretends to be "sustainable," must be capable of the kind of scale necessary to ensure that all global inhabitants have access to clean, affordable, reliable and also PLENTIFUL sources of energy.

So each of these vital steps of the "energy transition" still require technological innovations that have not yet been invented, let alone tested and scaled-up to a commercial level. That will take years to accomplish.

Fortunately, the recently enacted Bipartisan Infrastructure Act and the Inflation Reduction Act have put in place many of the technology-neutral financial incentives necessary to fund the above-listed climate-change responsive innovations that are required to achieve the transition to a clean-energy future. This we see as a very good thing and policy leaders are to be applauded for laying the groundwork for the kind of

IECA • 1120 Route 73, Suite 200, Mt. Laurel, NJ 08054 USA • Ph 856-380-6854 • Fax 856-439-0525

energy transition which, we hope, will address the existential risk presented by climate change and still provide clean, affordable, plentiful and reliable sources of energy.

But, even with the recently enacted legislation, for all the reasons noted above, that energy transition period will still take many years to achieve.

B. Transition Period Risks Defined.

The energy transition will take many years to achieve and the U.S. and the global economy will continue using significant quantities of fossil fuels for at least the next ten years and likely beyond the next ten years. Ignoring that fact will not make it disappear and making policy decisions that penalize companies in the fossil fuel industries or financial institutions providing financing to fossil fuel industries will be contrary to our national security interests and will increase the risks to our financial system.

We suggest that policies related to financing of fossil fuel industry participants, in addition to considering climate change and environmental impacts, should also consider national security interests during the transition period. The failure to consider national security risks would leave our financial system and our global economy exposed to potentially unmanageable risks.

Policy makers who exclusively focus on pursuing GHG emissions policies that rely on reducing funding to the fossil fuel industry risk overlooking the transition period risks to our financial system and our global economy that will, in fact, be compounded by such policy maker's decisions to frustrate funding of the fossil fuel industry.

For example, penalizing banks or other financial institutions for providing loans or other capital to companies that are still in the fossil fuel industry are likely to reduce the liquidity of transition risk management tools that companies providing petroleum-based fuels, plastics, and other products, as well as natural gas and liquified natural gas (LNG) for export to other countries, need and will continue to need for many more years during the "transition period."

History will tell us the various drivers for the current global economic crisis, spiking crude oil, motor fuels, and natural gas prices and rapidly rising inflation rates, but there seems to be no escaping that the current global energy and economic crisis is an energy transition period risk to our financial system.

C. Market tools required during energy transition.

In some ways the two broad categories of Physical Risk and Transition Risk are also related. Currently, market participants in US energy infrastructure and related industrial complexes can manage climate related risks such as worsening storm-related physical damages with available risk management tools like casualty insurance and weather derivatives. As pressures mount from regulatory authorities and ESG motivated investors cause insurers and re-insurers to exit these markets, market participants may be unable to access these risk management tools, magnifying the effects to the economy and markets of climate related hazards.

IECA • 1120 Route 73, Suite 200, Mt. Laurel, NJ 08054 USA • Ph 856-380-6854 • Fax 856-439-0525

Fewer interested insurers, which creates capacity and pricing issues for fossil fuel related industries including generators necessary to maintain the electricity grid is a common complaint of risk managers at these companies. The Commission should also be studying the role of insurers in the energy transition and their impact on market participants.

D. Reduced capital impacts.

Public policy and ESG investor directed reductions of capital available to fossil fuel related industries also impact the functioning of physical and financial markets regulated by the Commission. As the market discovered during Winter Storm Uri, climate can have a severe impact on physical energy markets. Combined with the Commission's focus on moving transactions to central clearing counterparties, these climate events create severe and immediate liquidity stress, and without capital resources particularly from the banking sector, participants may be forced to exit cleared markets creating market instability or worse forced liquidations of positions, which may cause a volatility spiral. Compounding the liquidity issue is the fact that many, if not all, central clearing counterparties do not have access to the Fed window, rather they rely on the credit support of their members.

At the time, the market became concerned about the health of major commodity merchants, who are key to the health of commodity market functioning, and the possible need for public support, similar to what recently occurred with Uniper SE in Germany, but the commodity banking sector quickly responded making capital available to participants and averting a market collapse. Continued capital capacity to fossil fuel industries is therefore critical to market function during the energy transition.

Physical market participants may also experience dislocations from a lack of credit capacity and inability to purchase required supplies in spot markets without trade finance support from the banking sector. The bankruptcy of Brazos Municipal Cooperative is now a cautionary tale for credit managers, who may restrict future availability to key providers of utility services to consumers and commercial customers causing financial stress to become a human calamity without banking support for collateral.

And since foreign banks have traditionally played such a large role in the commodity banking sector and therefore commodity markets, the Commission cannot ignore the impact of global regulations, particularly the impacts of contradictory regulatory guidance. Coordination with other international regulators would therefore be helpful to commodity markets.

The Commission should look for input from market participants and the banking sector to ensure adequate capital availability for standard market stress scenarios. A few years ago, spurred by NSRO's who required rated issuers to consider standard commodity price increase and decrease scenarios and its impact on the issuer's business and liquidity, credit managers began to evaluate these scenarios for their unrated as well as rated portfolios. So development of stress testing standards by the Commission would help market participants anticipate and plan for these climate related market stresses and help the banking sector anticipate and plan ahead to support related capital requirements.

IECA • 1120 Route 73, Suite 200, Mt. Laurel, NJ 08054 USA • Ph 856-380-6854 • Fax 856-439-0525

II. Conclusion.

The CFTC's RFI outlines the FSOC's recommendations in response to President Biden's Executive Order 14030 as follows (on page 34857):

> "(1) Build capacity and expand efforts to address climate-related financial risks;
> (2) fill climate-related data and methodological gaps;
> (3) enhance public climate-related disclosures; and
> (4) assess and mitigate climate-related risks that could threaten the stability of the financial system."

The IECA supports focusing on the "Physical Risks" to our economy and our financial system as a result of climate change. Seeking to ensure that incentives are available for climate-change responsive technological innovations, and seeking to "enhance public climate-related disclosures" are conducive policies to incentivize the successful achievement of total zero or net zero emissions of GHG by 2050.

However, it is essential that the CFTC and other financial system regulators are simultaneously mindful that physical risk often translates into financial risk, which really is manifested as credit risk. Such could become systemically important risks to our financial system arising from our continued need to not only consume fossil fuels, but also to financially support the existing businesses required to successfully transition the country during the next ten years, and possibly longer if the various technological innovations required to implement alternative clean energy resources are not invented as quickly as developers may hope.

We ask that as you assess climate-related financial risks from the energy transition, that you ask: "What could go wrong?" during the energy transition period and then ensure that the policies adopted by the CFTC will ensure that companies, governments, and individuals have the tools, the financing and the liquidity available to them to manage and mitigate those risks, which we see as the CFTC's primary purpose.

The IECA appreciates the opportunity to submit these comments to the CFTC. We welcome the opportunity to discuss these comments further should you require any additional information.

Yours truly,
INTERNATIONAL ENERGY CREDIT ASSOCIATION

/s/ Phillip G. Lookadoo	*/s/ Jeremy D. Weinstein*
Phillip G. Lookadoo, Esq.	Jeremy D. Weinstein, Esq.
Haynes and Boone, LLP	Law Offices of Jeremy Weinstein

IECA • 1120 Route 73, Suite 200, Mt. Laurel, NJ 08054 USA • Ph 856-380-6854 • Fax 856-439-0525

Please direct correspondence concerning these comments to:

Phil Lookadoo, Esq.
Haynes and Boone, LLP
800 17th Street, NW, Suite 500
Washington, DC 20006
Phone: 202-654-4510
Email: phil.lookadoo@haynesboone.com

Jeremy Weinstein, Esq.
Law Offices of Jeremy Weinstein, PC
1512 Bonanza Street
Walnut Creek, CA 94596
Phone: 925-943-2708
Email: jweinstein@jweinsteinlaw.com