October 12, 2012

VIA ELECTRONIC SUBMISSION

Stacy Yochum, Acting Secretary
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Comments on Joint Final Rule and Interpretations on Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping (RIN No. 3038-AD46)

Dear Secretary Yochum:

The Interstate Natural Gas Association of America and its members (collectively, "INGAA") submit these comments in response to the Commission's request for comments relating to certain interpretive guidance in the Commission's Swap Definition Final Rule.[1] INGAA offers these comments on the Commission's interpretation in subsection II.B.2.(b)(iii) ("Certain Physical Commercial Agreements, Contracts, or Transactions") of the Swap Definition Final Rule.[2] INGAA respectfully requests that the Commission, and to the extent necessary the Securities and Exchange Commission ("SEC"),[3] confirm that the Commission will follow the standards adopted in the *1985 Interpretative Statement* concerning the characteristics of an option in determining whether a transaction will be regulated as an option subject to the swap definition.[4] Consistent with the *1985 Interpretative Statement*, INGAA requests that the

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1 *Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping; Final Rule*, 77 Fed. Reg. 48,208 (Aug. 13, 2012) (herein, "Swap Definition Final Rule").

2 Subsection II.B.2.(b)(iii), at pages 48,242-43 of the Swap Definition Final Rule, provides guidance with respect to "certain physical commercial agreements for the supply and consumption of energy that provide flexibility," including "transportation agreements on natural gas pipelines and natural gas storage agreements" (hereafter, "Facility Services Agreement Guidance").

3 INGAA's comments relate only to those aspects of the Final Swap Definition that interpret the definition of "swap" and the exclusions therefrom in respect of commodities and services, not securities. These comments do not relate to provisions of the Final Swap Definition that apply in any way to "security-based swaps," "security-based swap agreements," "mixed swaps," or "security-based swap agreement recordkeeping." Accordingly, INGAA addresses its comments to the Commission, although a copy is being provided to the SEC. Although INGAA separately has sought clarification and/or no-action relief from the Commission with respect to certain issues addressed in this letter, INGAA seeks Commission action, as opposed to action by a division of the Commission, as needed to provide for regulatory certainty.

4 *Characteristics Distinguishing Cash and Forward Contracts and "Trade" Options*, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) P 22,718 (Sept. 30, 1985) (emphasis added) ("*1985 Interpretative Statement*"). The *1985 Interpretative Statement* was issued by the Commission's General Counsel, but "has been consistently cited by both the Commission and courts as persuasive authority on the topics that it

Commission take the following specific actions concerning its Facility Services Agreement Guidance: (1) remove in its entirety or otherwise strike the three-part test on page 48,242 of the Swap Definition Final Rule (the "Three-Part Test"); (2) remove in its entirety or otherwise strike the paragraph on page 48,242 of the Swap Definition Final Rule referring to a "demand charge or reservation fee" and "usage fees" (the "However Paragraph"); and (3) as explained below, clarify that agreements for service on natural gas pipeline and storage facilities that do not have the characteristics of an option under the *1985 Interpretative Statement* and related precedent are not options subject to the swap definition and that the mere existence of a two-part fee structure is not determinative of whether a particular agreement is an option subject to the swap definition.

As explained below, the Commission's Facility Services Agreement Guidance expressly addresses natural gas transportation and storage agreements and could be applied, contrary to Commission precedent, to cause such agreements to be regulated as commodity options, despite the fact that these agreements do not contain any of the established characteristics of options and are not options under any recognized standard. In fact, natural gas transportation and storage agreements are structured to require service purchasers to carry the full risk of loss of their investments in the services to be rendered by the service provider. To the extent that the Commission intended to provide useful guidance consistent with its obligations under the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") to further define the term "swap" consistent with the Commodity Exchange Act ("CEA") definition of "swap," such guidance with respect to the characterization of certain types of facility services agreements as options is patently inconsistent with established Commission and judicial precedent. While INGAA appreciates the efforts of the Commission in the Swap Definition Final Rule to provide guidance with respect to facility service agreements for "use" of a facility, INGAA respectfully urges the Commission to adopt the recommendations set forth in these comments.

I. The Commission's Facility Services Agreement Guidance

The Commission's Facility Services Agreement Guidance sets forth the Commission's interpretation regarding "certain physical commercial agreements for the supply and consumption of energy that provide flexibility," including "transportation agreements on natural gas pipelines, and natural gas storage agreements."[5] The Commission's Three-Part Test purports to guide the industry with respect to how the Commission will interpret such agreements as options subject to the swap definition:

> The CFTC will interpret an agreement, contract or transaction not to be an option if the following three elements are satisfied: (1) The subject of the agreement, contract or

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addresses." *In the Matter of Cargill*, [2000-2002 Transfer Binder] Comm. Fut. L. Rep. (CCH) P 28,425 n.28 (Nov. 22, 2000) (citing authority), *aff'd mem*. Comm. Fut. L. Rep. (CCH) P 29,633 (Nov. 25, 2003). In determining whether an agreement is an option, the Commission has "carefully examined 'the economic reality of the transaction, not its name.'" *1985 Interpretative Statement* at P 22,718.

5 77 Fed. Reg. at 48,242.

> transaction is usage of a specified facility or part thereof rather than the purchase or sale of the commodity that is to be created, transported, processed or stored using the specified facility; (2) the agreement, contract or transaction grants the buyer the exclusive use of the specified facility or part thereof during its term, and provides for an unconditional obligation on the part of the seller to grant the buyer the exclusive use of the specified facility or part thereof; and (3) the payment for the use of the specified facility or part thereof represents a payment for its use rather than the option to use it.[6]

The Commission then provides, in its However Paragraph, additional guidance with respect to facility services agreements that employ two payments consisting of a "demand" or "reservation" charge and "usage fees, rents, or other analogous services charges not included in the demand charge or reservation fee." The "However Paragraph" reads as follows:

> However, in the alternative, if the right to use the specified facility is only obtained via the payment of a demand charge or reservation fee, and the exercise of the right (or use of the specified facility or part thereof) entails the further payment of actual storage fees, usage fees, rents, or other analogous service charges not included in the demand charge or reservation fee, such agreement, contract or transaction is a commodity option subject to the swap definition.[7]

II. Status of INGAA and INGAA's October 9, 2012 Letter for Clarification and No-Action

INGAA is a trade association and it, together with its 25 members, represents the vast majority of the interstate natural gas pipeline companies in the U.S. and comparable companies in Canada. INGAA's members operate approximately 200,000 miles of pipelines and serve as an indispensable transportation link between natural gas producers and consumers.[8]

On October 9, 2012, INGAA filed with the Commission a request for clarification and/or no-action relief ("October 9 Letter") related to the treatment of natural gas transportation and storage service agreements under the Facility Services Agreement Guidance, as written. In the October 9 Letter, INGAA requested clarification that natural gas transportation and storage agreements would not be treated as options subject to the swap definition, and also that the

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6 *Id*.

7 *Id*.

8 INGAA's members are Alliance Pipeline Ltd., Boardwalk Pipelines, Carolina Gas Transmission Corporation, CenterPoint Energy, Cheniere Energy, Inc., Dominion Transmission, Inc., DTE Energy, Enbridge Energy Company, Inc., Energy Transfer, EQT Corporation, Iroquois Pipeline Operating Company, Kinder Morgan, National Fuel Gas Supply Corporation, National Grid, New Jersey Resources, NiSource Gas Transmission & Storage, ONEOK, Inc., Pacific Gas & Electric, Questar Pipeline Company, Sempra Pipelines and Storage, Southern Star Central Gas Pipeline, Inc., Spectra Energy Corp, TransCanada Corporation, WBI Energy Transmission, Inc., and Williams Gas Pipeline Company, LLC.

Commission would not look merely at whether an agreement has a two-part fee structure to determine whether an agreement is an option. A copy of the October 9 Letter is attached to these comments and incorporated herein.

III. INGAA's Recommendations

A. The Commission Should Remove the Three-Part Test in its Entirety

Under the CEA, as amended by the Dodd-Frank Act, the term "swap" is defined to include a "put, call, cap, floor, collar or similar option of any kind."[9] It therefore is clear that Congress intended that agreements considered to be options subject to the swap definition must, in fact, have the characteristics of options: namely characteristics, such as premium-based limited-risk elements, that distinguish agreements such as puts, calls, and "similar" elements from agreements that unconditionally bind one party to transfer goods or provide services and also unconditionally bind the other party to pay the full purchase price for those goods or services. The CEA, as amended by the Dodd-Frank Act, does not give the Commission authority to regulate as options subject to the swap definition, physical commercial agreements, including those for the supply and consumption of physical energy that have deliverability "flexibility" but that do not have the characteristics of, and are not known in the trade as, an option.

The *1985 Interpretative Statement* provides a straightforward test for determining whether an agreement has the characteristics of, and should be treated as, an option. As explained in *In the Matter of Cargill*:

> The *1985 Interpretative Statement* identifies three criteria indicative of an option. First, the instrument gives the buyer the right to take or make delivery of the commodity but does not obligate him to do so. Second, the buyer's losses are limited to a premium paid as consideration for the option seller's performance. Third, the instrument is purchased by offering a premium as opposed to a down payment on the eventual delivery price.[10]

The Commission should clarify that the industry should use this test in determining whether natural gas transportation and storage agreements are options subject to the statutory swap definition. Thus, in examining the "economic reality" of natural gas transportation and storage agreements, the test for whether an agreement is an option is whether (1) the instrument contains the right, but not the obligation, to acquire the subject of the agreement (in this case, the transportation or storage services), (2) the buyer's losses are limited to a premium paid as consideration for the option seller's performance, and (3) the instrument is purchased by offering a premium, as opposed to a down payment, on the eventual delivery price (in this case, the price for the transportation and storage services).[11] The Commission should use this longstanding test

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9 Dodd-Frank Act § 721(a)(2)(47)(A)(i), 7 U.S.C. § 1a (47)(A)(i) (2011).

10 *In the Matter of Cargill* at P 28,425 (citing *1985 Interpretative Statement*).

11 *Id*.

in determining whether natural gas transportation and storage agreements are options subject to the statutory swap definition.

In light of the statutory swap definition, and because there is established precedent setting forth the characteristics of options, INGAA submits that the Three-Part Test is not needed, is unnecessarily confusing, and should be removed in its entirety. First and foremost, natural gas transportation and storage agreements clearly are not options under longstanding Commission precedent. The reason that such agreements have never been considered as options historically is not due to the fact that they would pass the Three-Part Test, but simply because they do not contain any of the characteristics that the Commission has relied upon to define options subject to its jurisdiction since at least 1985. As stated in *In the Matter of Cargill*, an option establishes a right, but not an obligation to acquire the item specified of the agreement, "the buyer's losses are limited to a premium paid as consideration for the option seller's performance," and the instrument "is purchased by offering a premium as opposed to a down payment on the eventual delivery price."[12] As explained in detail in INGAA's October 9 Letter, natural gas transportation and storage services do not contain premiums, the buyer's losses are not limited to the premium paid, and the obligations of both service providers and service purchasers become legally binding at the time the agreements are entered into by the parties. For the sake of brevity, INGAA will not repeat the arguments in the October 9 Letter that establish that natural gas transportation and storage agreements are not options under the Commission's standards, but rather incorporates the October 9 Letter herein.

Furthermore, the first two prongs of the Three-Part Test limit the test's application to certain types of transactions, namely agreements for the use of a facility and not for the underlying commodity (prong 1), and agreements providing for the exclusive use of a facility or part thereof (prong 2). These first two prongs limit the applicability of the test without any explanation as to why the Commission believes such factors are needed to determine that an agreement is not an option. Nor is there any explanation as to how such factors are to be applied in the context of energy transportation and storage agreements. INGAA questions the purpose of these first two prongs when there is clear Commission and judicial precedent that, to be an option, a transaction *must* have the characteristics of an option. In fact, various agreements, regardless of whether they fit within the first two prongs of the Three-Part Test, should not be treated as options if they do not have the distinctive characteristics of options. INGAA thus questions the utility of providing such limited and unsupported guidance.

Similarly, the third prong of the Three-Part Test, that "the payment for the use of the specified facility or part thereof represents a payment for its use rather than the *option* to use it,"[13] does not appear to provide any guidance beyond what already is established law. If the payment under an agreement is for the services rendered or to be rendered, and is not a premium-type payment for the right, but not the obligation, to acquire the services, the instrument is not an

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12 *Id*.

13 77 Fed. Reg. at 48,242 (emphasis added).

option. This third prong thus must be read merely to affirm established precedent under the *1985 Interpretative Statement*. The Commission's explanation immediately following the Three-Part Test re-affirms this point. Explaining the Three-Part Test, the Commission stated as follows: "In such agreements, contracts and transactions, while there is optionality as to whether the person uses the specified facility, the person's right to do so is legally established, does not depend upon any further exercise of an option and merely represents a decision to use that for which the lessor already has paid."[14] Thus, the Commission reasoned, "[i]n this context, [it] would not consider actions such as scheduling . . . gas transportation or injection of gas into storage to be exercising an option if all three elements of the interpretation above are satisfied."[15] INGAA agrees that if an agreement establishes the legal right to use something for which the lessor has paid, and the use does not depend upon the further exercise of an option, it is not an option. However, the agreement is not an option because the agreement does not meet the definition of the term "option" in the CEA, as that term is interpreted by clear, established precedent, not because the agreement passes or fails the Three-Part Test. Likewise, INGAA agrees that scheduling gas to be transported on a facility, where the lessor already has contracted to pay for the service, is not exercising an option, regardless of whether the Three-Part Test has been met.[16] Such agreements are not options because they do not bear any of the characteristics of options.

In short, it is not clear how the Commission intends to apply the Three-Part Test, or why, and if so, how, it differs from established precedent or how the Three-Part Test will be harmonized with the statutory definition of the term "option" and existing precedent. INGAA submits that the Commission must act within the bounds of the statutory definition of swap and option, and the established characteristics of options as defined by the Commission and the courts. Furthermore, under the Administrative Procedure Act ("APA"), the Commission may not change its prior policy without providing adequate notice and opportunity for comment on the issue under consideration and supplying a reasoned analysis for departing from its prior policy.[17] In this case, the definition of option is established by statute, and the characteristics defining options have been established by the Commission and the courts. Under the circumstances, the simplest way to remedy the unnecessary and unduly confusing Three-Part Test is to remove it in its entirety.

If the Commission nevertheless decides to keep in place the Three-Part Test, it should, at a minimum, state affirmatively that the Three-Part Test is not intended to override the *1985 Interpretative Statement* and is only intended to provide *additional* guidance that is consistent with the *1985 Interpretative Statement*. According to the Swap Definition Final Rule, the Three-

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14 *Id*.

15 *Id*.

16 To use the service it has reserved, a pipeline or storage customer need only nominate gas to be scheduled for transportation on the pipeline or for injection/withdrawal from storage, in accordance with industry protocols, and in no manner does that change the contractual relationship between the service provider and its customer or relate to any form of a premium payment.

17 5 U.S.C. § 553 (2011).

Part Test may only be used to determine that a service agreement is *not* a swap or option. If a service agreement does not satisfy the Three-Part Test, it will not, without further analysis under the statute and the *1985 Interpretative Statement*, be considered a swap or option. In order to provide regulatory certainty to the industry, if the Commission retains the Three-Part Test, the Commission should clarify how the test will be applied in conjunction with the statutory definition of swap and option and the *1985 Interpretative Statement*.

While INGAA believes that it is simpler to apply the standards established in the *1985 Interpretative Statement* and subsequent cases, if the Commission seeks to provide any guidance concerning facility services agreements at all, its guidance should be supplemental, and conform to the standards of the *1985 Interpretative Statement*. This approach is consistent with the guidance given with respect to forward contracts in the Swap Definition Final Rule. In discussing its guidance on whether a contract is a forward contract excluded from the swap definition, the Commission re-affirms its precedent that a multi-factor, "facts and circumstances" test should be applied.[18] The Commission has consistently assessed the facts and circumstances and "economic reality" of an agreement when determining whether an agreement is an option, rather than applying a strict three-part or bright-line test focused on the structure of the agreement or its fee structure.[19] Thus, in this case, regardless of whether a particular agreement satisfies the Three-Part Test, if, under the facts and circumstances, it does not have the characteristics of an option, it should not be regulated as an option subject to the swap definition.

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[18] 77 Fed. Reg. at 48,237, n.333 ("This facts and circumstances approach to determining whether a particular embedded option takes a transaction out of the forward contract exclusion for nonfinancial commodities is consistent with the CFTC's historical approach to determining whether a particular embedded option takes a transaction out of the forward contract exclusion from the definition of the term 'future delivery' in the CEA. *See id*. at *5 ('As we have held since *Stovall*, the nature of a contract involves a multi-factor analysis * * *.')"); *see also id*. at 48,228, n.214 (quoting *In re Wright*, CFTC Docket No. 97–02, 2010 WL 4388247: "[i]n distinguishing futures from forwards, the [CFTC] and the courts have assessed the transaction as a whole with a critical eye toward its underlying purpose. Such an assessment entails a review of the overall effect of the transaction as well as a determination as to what the parties intended.").

[19] In *In re Wright*, the CFTC affirmatively rejected the Division of Enforcement's request for a bright-line test for hedge-to-arrive contracts, a type of forward contract. *See Wright* at *10 ("In assessing the parties' expectations or intent regarding delivery, the Commission applies a 'facts and circumstances' test rather than a bright-line test focused on the contract's terms"); *id*. at *18, n.13 ("The Division argues that a bright-line test based on the terms of the contract is necessary to avoid legal uncertainty, i.e., to avoid the prospect of 'a single contract starting out as a forward contract, but winding up as a futures contract if the signer changed his or her mind and cancelled the contract,' or the same contract being a future for one signer and a forward for another, depending on how each intends to use it. *Id*. The Division argues that this situation 'would create legal uncertainty throughout the life of the contract as to what regulatory framework will apply at any given moment.' . . . We acknowledge the importance of avoiding legal uncertainty. The Division's bright-line test, however, is an approach we affirmatively rejected in our other cases. Our views of the appropriateness of a multi-factor analysis remain unchanged. The Division's approach, strictly applied, potentially may undermine the usefulness of HTA contracts to the agricultural industry and may hamper innovation.").

B. The Commission Should Remove the However Paragraph in its Entirety; Clarify that Natural Gas Transportation and Storage Agreements Are Not Options; and Clarify that the Mere Existence of a Two-Part Fee Structure Is Not Determinative of Whether an Agreement Is an Option

As explained in detail in the October 9 Letter, fees for natural gas transportation and storage services represent nothing more than compensation solely for the services being rendered by the pipeline or storage company. Often natural gas transportation and storage fees have two components: a reservation fee and a usage fee. The fees compensate the pipeline or storage operator for services rendered and to establish the customer's right to use the facility. No part of these fees provides any type of risk premium (i.e., payment for an independent option to contract for or otherwise obtain service at a future date). Regardless of the fee structure, under natural gas transportation and storage agreements, the obligations of both service providers and service purchasers become legally binding at the time the agreements are entered into by the parties.

As noted above, INGAA will not repeat the arguments in the October 9 Letter that natural gas transportation and storage agreements are not options under the Commission's standards, but rather incorporates its arguments herein. INGAA submits that the best way to remedy the inconsistencies between the However Paragraph and historical Commission precedent concerning options is to remove the However Paragraph in its entirety, as noted in note 31 of the October 9 Letter. The However Paragraph, as written, is unnecessary and conflicts with the statutory definition of a swap and an option, the established characteristics of an option, and the Commission's approach of analyzing the nature of contracts based on the "economic reality" of a transaction. While the Commission could attempt to remedy the However Paragraph by revising it or further describing what is meant by "demand charge," "reservation fee," and "usage fee" in that context, such actions likely would create further confusion, particularly for market participants who use such terms in agreements that bear no resemblance to instruments historically understood to be options.[20] As INGAA explained in the context of the Three-Part Test, the statute does not authorize the Commission to modify established standards, nor could it do so without supplying notice and opportunity for comment and a reasoned analysis for departing from its prior policy. In that regard, since the However Paragraph conflicts with the long-established test in the *1985 Interpretative Statement* for determining whether an agreement has the characteristics of an option, INGAA similarly asks the Commission to strike the However Paragraph in its entirety.

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[20] A fundamental requirement of the APA is that interested persons be given notice of proposed substantive regulations and an opportunity to comment. *See* 5 U.S.C. § 553. If the Commission decides to alter the However Paragraph, it must provide adequate notice and opportunity for comment. Here, the However Paragraph was added to the final rule without any notice or opportunity for comment. Parties had no notice, in any of the proposed rulemakings or at any other step of the rulemaking process, that the Commission would provide specific guidance regarding the issue of whether two-part fee agreements would be commodity options subject to the definition of a "swap." Because the addition of the However Paragraph violated the core tenants of the APA, the Commission should simply strike the paragraph.

In addition, for the reasons stated in the October 9 Letter, INGAA requests that the Commission affirmatively make the following clarifications requested in the October 9 Letter:

- The Commission should clarify that agreements for service on natural gas pipeline and storage facilities or parts thereof (i.e., as distinct from sales or purchases of the gas commodity itself) do not have the characteristics of options and hence are not options subject to the swap definition; and

- The Commission should clarify that it will use its historical approach for determining whether an agreement has the characteristics of an option, rather than the mere existence of a two-part fee structure in the agreement, to determine whether a particular natural gas transportation or storage agreement is an option subject to the swap definition.

IV. The Commission and SEC Should Accept These Comments

INGAA recognizes that the Commission has solicited comments by October 12, 2012, on the guidance regarding forward contracts with embedded volumetric options.[21] For the following reasons, good cause exists to accept these comments. First, in connection with its comment request, the Commission asked the following question: "Is the interpretation sufficiently clear with respect to capacity contracts, transmission (or transportation) services agreements, peaking supply contracts, or tolling agreements? Why or why not?"[22] Because the Facility Services Agreement Guidance provides *additional* guidance relating to transportation services agreements such as natural gas transportation and storage agreements, these comments are directly related and inextricably linked to the subject of the Commission's comment request. Indeed, both subsections (ii) and (iii) of Section II.B.2.(b) relate to guidance concerning whether or not agreements, including those for the supply of energy, contain embedded commodity options, and it would be arbitrary to disregard directly relevant comments simply because the Commission chose to provide *additional* guidance on transportation services agreements in a separately titled sub-section.

In addition, both the Facility Services Agreement Guidance and the section on forward contracts with embedded volumetric options contain *new* multi-factor guidance tests that were *not included* in the proposed rulemaking and have never previously been published, announced

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21 77 Fed. Reg. at 48,208, 48,241.

22 *Id*. at 48,242.

or used by the Commission.[23] If the Commission considered it necessary to solicit additional comments on the novel Seven-Factor Test, it is also necessary to solicit additional comments on the equally novel Three-Part Test, as well as comments specifically on the However Paragraph, which can be read to establish yet another bright-line test. In fact, INGAA had no notice in the proposed rule that the Commission would provide specific guidance in the form of the Three-Part Test, let alone the However Paragraph that, as written, could be applied, contrary to precedent, to treat natural gas transportation and storage agreements with two-part fee structures as options; such application would treat natural gas transportation and storage agreements inconsistently with the way other contracts are viewed with respect to Commission jurisdiction and could be read, in effect, to overturn longstanding Commission precedent. Moreover, the Commission's Facility Services Agreement Guidance is not a logical outgrowth of prior proposed rules or prior proposed interpretations of Dodd-Frank Act section 721(a)(21) (defining the term "swap"). Neither the advance notice of proposed rulemaking nor the notice of proposed rulemaking discussed potentially regulating transactions involving two-part fee structures as swaps, and the Swap Definition Final Rule does not provide any explanation as to why the Commission is treating agreements with two-part fee structures differently from any other contracts.

Finally, these comments are based on the statutory definition of "swap" and "option," which includes "puts, calls," etc., as well as on longstanding Commission and court precedent regarding what distinguishes an option under the CEA from a non-option. The Commission does not have the authority to change the statutory definition of swap or option, nor does it have discretion to depart from its historic interpretation of, and long-standing precedent regarding, what characterizes an option without providing interested parties notice and an opportunity to comment, and without providing adequate justification for the departure. INGAA does not believe the Commission intended its Facility Services Agreement Guidance to vary from or in any way contradict the *1985 Interpretative Statement* and its progeny. Accordingly, the Commission should accept these comments.

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[23] The Commission proposes a new seven-part test in subsection II.B.2.(b)(ii) regarding forward contracts with embedded volumetric options. *Id*. at 48,238 (hereafter, "Seven-Factor Test"); *see also id*. at 48,239 n. 344 (focusing on these factors because "the CFTC has not previously expressed the view that an agreement, contract, or transaction with embedded volumetric optionality which affects the delivery term may qualify as a forward contract if these [intent to deliver and ability to make or take delivery] facts and circumstances are present"); *see Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping*, Proposed Rule, 76 Fed. Reg. 29,818 (May 23, 2011) ("Proposed Rule").

V. Conclusion

INGAA therefore respectfully requests that the Commission accept these comments and make the recommendations as detailed above.

If the Commission or its staff would like any additional information, please do not hesitate to contact me at the address and telephone number set out in this letter.

Respectfully submitted,

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Cc: Secretary, Securities and Exchange Commission
Honorable Gary Gensler, Chairman
Honorable Jill E. Sommers, Commissioner
Honorable Bart Chilton, Commissioner
Honorable Scott D. O'Malia, Commissioner
Honorable Mark P. Wetjen, Commissioner
Dan Berkovitz, General Counsel

Attachment

October 9, 2012

VIA ELECTRONIC SUBMISSION

Stacy Yochum
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Commodity Futures Trading Commission
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Richard Shilts
Acting Director, Division of Market Oversight
Commodity Futures Trading Commission
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Re: Request for Clarification and No-Action Relief Regarding Commission Interpretive Guidance on Transportation and Storage Agreements with Two-Part Fee Structures Set Forth in the Commission's Swap Definition Final Rule

Dear Ms. Yochum and Mr. Shilts:

The Interstate Natural Gas Association of America and its members (collectively, "INGAA")[1] hereby respectfully request that the Commodity Futures Trading Commission (the "Commission") provide clarification and no-action relief concerning certain interpretive guidance in the preamble to the Commission's final rule further defining the term "swap"[2] in accordance with section 712(d)(1) of the Dodd-Frank Wall Street Reform and Consumer Protection Act.[3] Specifically, INGAA requests clarification and no-action relief in connection with specific interpretive guidance provided on pages 48,242-43 of the Swap Definition Final Rule.[4]

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1 INGAA's members are Alliance Pipeline Ltd., Boardwalk Pipelines, Carolina Gas Transmission Corporation, CenterPoint Energy, Cheniere Energy, Inc., Dominion Transmission, Inc., DTE Energy, Enbridge Energy Company, Inc., Energy Transfer Partners LP, EQT Corporation, Iroquois Pipeline Operating Company, Kinder Morgan, National Fuel Gas Supply Corporation, National Grid, New Jersey Resources, NiSource Gas Transmission & Storage, ONEOK, Inc., Pacific Gas & Electric, Questar Pipeline Company, Sempra Pipelines and Storage, Southern Star Central Gas Pipeline, Inc., Spectra Energy Corp, TransCanada Corporation, WBI Energy Transmission, Inc., and Williams Gas Pipeline Company, LLC.

2 *Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Record Keeping; Final Rule*, 77 Fed. Reg. 48,208 (Aug. 13, 2012) (hereafter, "Swap Definition Final Rule").

3 Pub. L. 111-203, 124 Stat. 1376 (2010) (hereafter, "Dodd-Frank Act").

4 These pages, titled as subsection (iii), "Certain Physical Commercial Agreements, Contracts, or Transactions," provide guidance with respect to "certain physical commercial agreements for the supply and consumption of energy that provide flexibility," including "transportation agreements on natural gas pipelines, and natural gas storage agreements" (hereafter, "Facility Services Agreement Guidance").

INGAA appreciates the Commission's efforts to provide guidance on the definition of a "swap" with respect to facility services agreements for the "supply and consumption of energy." However, the Facility Services Agreement Guidance makes the application of longstanding Commission precedent concerning the characteristics of options more confusing, not less, in the facility services agreement context. One paragraph in particular in the Facility Services Agreement Guidance raises concern as to the application of the Commission's guidelines regarding facility usage agreements that employ "two-part" rate structures consisting of a "demand" or "reservation" charge and "usage fees, rents, or other analogous services charges not included in the demand charge or reservation fee."[5] As applied to natural gas transportation and storage agreements, contracts or transactions that use two-part rates, the However Paragraph is contrary to the Commission's intent and historic approach to determining whether an agreement, contract or transaction (collectively "agreement") is an option.

For the reasons explained below, INGAA respectfully requests the Commission clarify:

(1) that agreements for service on natural gas pipeline and storage facilities or parts thereof (i.e., as distinct from sales or purchases of the gas commodity itself) do not have the characteristics of options and hence are not options subject to the swap definition; and

(2) that the Commission will use its historical approach of determining whether an agreement has the characteristics of an option, rather than the mere existence of a two-part fee structure, to determine whether a particular natural gas transportation or storage agreement is an option subject to the swap definition.

Providing natural gas transportation and storage providers and their customers with the requested certainty concerning the definition of "swap" is critical prior to the rule's effective date of October 12, 2012, or as soon thereafter as reasonably possible. INGAA therefore respectfully urges the Commission, the Commission's General Counsel, or an appropriate Division of the Commission to issue no-action relief stating that the Commission will not take, or such Division of the Commission will not recommend, any enforcement action if the members of INGAA (and parties to facility agreements with INGAA's members) do not treat such facility agreements, including but not limited to natural gas transportation and storage agreements, as swaps or commodity options subject to the swap definition, for purposes of complying with the provisions of Title VII of the Dodd-Frank Act and the rules thereunder, solely because such agreements provide for a two-part fee structure. The requested no-action relief should be provided at least until such time as the Commission issues a final clarification, interpretation, rule revision, or

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[5] The paragraph, which will hereafter be referred to as the "However Paragraph," reads as follows:

> However, in the alternative, if the right to use the specified facility is only obtained via the payment of a demand charge or reservation fee, and the exercise of the right (or use of the specified facility or part thereof) entails the further payment of actual storage fees, usage fees, rents, or other analogous service charges not included in the demand charge or reservation fee, such agreement, contract or transaction is a commodity option subject to the swap definition.

Id. at 48,242.

response to comments concerning the Swap Definition Final Rule and its applicability to such agreements.[6]

INGAA respectfully asks the Commission to issue the requested clarification and no-action relief on an expedited basis before October 12, 2012, or as soon thereafter as reasonably possible.[7]

I. Executive Summary

INGAA members provide natural gas transportation and storage services under agreements that do not meet the definition of an option under the Commodity Exchange Act, the Dodd-Frank Act, and Commission precedent and therefore should not be regulated as swaps. INGAA had understood, and continues to believe, that neither the Commission nor Congress intended to include natural gas transportation and storage service agreements as "swaps" or as "commodity options subject to the swap definition." These agreements do not contain the historical characteristics of options and they are not options under any recognized standard. In fact, these agreements are structured to require service purchasers to carry the full risk of loss of their investments in the services to be rendered by the service provider. Moreover, as explained below, the fee structures utilized in natural gas transportation and storage agreements are designed simply to compensate the pipeline and storage operator for the service rendered. Natural gas transportation and storage charges are not designed to be limited risk, premium-based fees that allow buyers to shift risk and give buyers the right, but not the obligation, to acquire service, which the Commission and the courts have held characterize options.

INGAA understands that the Facility Services Agreement Guidance is intended to be read consistently with the Commission's precedent, including its *1985 Interpretative Statement* and subsequent precedent setting forth the characteristics of an option.[8] Indeed, INGAA interprets

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6 INGAA intends to submit comments on October 12, 2012, suggesting revisions to the Facility Agreement Guidance, as well as seeking clarifications consistent with this letter.

7 INGAA is aware that Edison Electric Institute ("EEI"), the American Gas Association ("AGA"), and the Electric Power Supply Association ("EPSA") (collectively the "Joint Associations") have filed a request for extension of the compliance dates or, in the alternative, for no-action relief with respect to Dodd-Frank regulations impacting non-swap dealer and non-major swap participants in the energy markets. INGAA supports the Joint Associations' position and believes that their request is fully consistent with the requested clarification and no-action relief sought herein. However, the relief requested by INGAA is critical and necessary even if the Commission grants the relief sought by the Joint Associations. Thus, notwithstanding the relief sought by the Joint Associations, INGAA respectfully asks the Commission for prompt consideration of its request.

8 *Characteristics Distinguishing Cash and Forward Contracts and "Trade" Options*, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) P 22,718 (Sept. 30, 1985) (emphasis added) (hereafter, "*1985 Interpretative Statement*"). The *1985 Interpretative Statement* was issued by the Commission's General Counsel, but "has been consistently cited by both the Commission and courts as persuasive authority on the topics that it addresses." *In the Matter of Cargill*, [2000-2002 Transfer Binder] Comm. Fut. L. Rep. (CCH) P 28,425 n.28 (Nov. 22, 2000) (citing authority), *aff'd mem.* Comm. Fut. L. Rep. (CCH) P 29,633 (Nov. 25, 2003).

the Facility Services Agreement Guidance as incorporating this precedent, particularly since the Commission acknowledged that it would not interpret "actions such as scheduling" gas transportation and storage on facilities on which a customer has reserved capacity as equivalent to exercising an option.[9]

The Commission's Facility Services Agreement Guidance, however, includes one paragraph of interpretive language that could be read as contradicting the *1985 Interpretative Statement* to the extent it deems that natural gas transportation and storage agreements are commodity options, subject to regulation as swaps, solely because they employ a two-part fee structure.

The However Paragraph is inconsistent with the remainder of the Facility Services Agreement Guidance and it is contrary to (and neither recognizes nor incorporates) the Commission's precedent concerning the definition of an option. INGAA does not believe the Commission meant to have this limiting language apply to natural gas transportation and storage agreements, and similar facility usage agreements, which do not meet the definition of options. Because the effective dates for key swaps regulations are quickly approaching, INGAA seeks timely, near-term relief to clarify the application of this limiting language as requested herein, or, if such clarification cannot be made prior to October 12, 2012, to secure the no-action relief requested above pending removal of the However Paragraph or similarly permanent and comprehensive relief.

II. Background on INGAA and Natural Gas Transportation and Storage Services

INGAA is a trade association and it, together with its 25 members, represents the vast majority of the interstate natural gas pipeline companies in the U.S. and comparable companies in Canada. INGAA's members operate approximately 200,000 miles of pipelines and serve as an indispensable transportation link between natural gas producers and consumers.

The natural gas transportation network in the U.S. consists of approximately 300,000 miles of pipelines as well as natural gas storage facilities, which bring natural gas from producing regions to consuming regions. INGAA's members include the owners and operators of interstate pipelines and storage facilities, which are regulated by the Federal Energy Regulatory Commission ("FERC"). INGAA members own and operate approximately 200,000 miles of interstate pipeline.

Intrastate pipelines and storage facilities generally are regulated by state commissions. Some INGAA members have affiliates that own and operate intrastate pipelines and storage facilities that provide transportation and storage services that may be regulated by FERC under section 311 of the Natural Gas Policy Act or by state commissions.

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[9] 77 Fed. Reg. at 48,242.

III. Status of the Swap Definition Final Rule

Pursuant to section 712(d)(1) of the Dodd-Frank Act, and following an advance notice of proposed rulemaking,[10] a notice of proposed rulemaking regarding the Swap Definition Final Rule was published in the Federal Register on May 23, 2011.[11] The comment period closed on July 22, 2011. Neither the advance notice of proposed rulemaking nor the notice of proposed rulemaking discussed potentially regulating transactions involving two-part fee structures. On August 13, 2012, the Swap Definition Final Rule was published in the Federal Register, marking the first time the two-part fee structure issue was included in the rulemaking process. The Swap Definition Final Rule will become effective on October 12, 2012, although phasing provisions and Commission orders are delaying the dates for compliance with certain aspects of the regulations.

INGAA recognizes that the Commission has solicited comments on certain aspects of the Swap Definition Final Rule, including the interpretation regarding forward contracts with embedded volumetric optionality. These comments are due on October 12, 2012.[12] In connection with its comment request, the Commission asked the following: "Is the interpretation sufficiently clear with respect to capacity contracts, transmission (or transportation) services agreements, peaking supply contracts, or tolling agreements? Why or why not?"[13]

While INGAA intends to submit comments by October 12, 2012, INGAA's members are in the very difficult position of having to respond to a final rule that also becomes effective on October 12, 2012, while also complying with other already effective rules that have compliance dates tied to the effective date of the Swap Definition Final Rule. They must respond and comply despite having no notice, in the advance notice of proposed rulemaking, the Proposed Rule or at any other step of the rulemaking process, that the Commission would provide specific guidance that could be read to conclusively determine that certain natural gas transportation and storage agreements are commodity options subject to the definition of a "swap."

The However Paragraph could have significant regulatory impacts on all INGAA members, as well as thousands of customers who receive natural gas transportation and storage services under transportation and storage agreements employing two-part rates, if the scope and applicability of that paragraph is not clarified or addressed in advance of the October 12, 2012 public comment closing date and effective date of the Swap Definition Final Rule (or at least very shortly thereafter). For this reason, good cause exists to provide the prompt and timely clarification and no-action relief INGAA requests.

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[10] *See Definitions Contained in Title VII of Dodd-Frank Wall Street Reform and Consumer Protection Act*, 75 Fed. Reg. 51,429 (Aug. 20, 2010).

[11] *See Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping*, Proposed Rule, 76 Fed. Reg. 29,818 (May 23, 2011) (hereafter, "Proposed Rule").

[12] 77 Fed. Reg. at 48,208.

[13] *Id*. at 48,242.

IV. Legal Standards

Under the Dodd-Frank Act, a "swap" is defined to include "options," defined as "any agreement, contract, or transaction . . . that is a put, call, cap, floor, collar or similar option of any kind that is for the purchase or sale, or based on the value, of 1 or more . . . commodities . . . ."[14] Thus, to be regulated as a swap, an agreement, contract, or transaction must either be a swap as defined in the statutory swap definition, or an option as defined in the statutory swap definition, which means it must have the characteristics of an option consistent with Commission precedent (that is, must have characteristics of a "put, call, cap, floor, collar or similar option").

As set forth in the *1985 Interpretative Statement*, in determining whether an agreement is an option, the Commission and courts "have carefully examined 'the economic reality of the transaction, not its name.'"[15] As explained in *In the Matter of Cargill*:

> The *1985 Interpretative Statement* identifies three criteria indicative of an option. First, the instrument gives the buyer the right to take or make delivery of the commodity but does not obligate him to do so. Second, the buyer's losses are limited to a premium paid as consideration for the option seller's performance. Third, the instrument is purchased by offering a premium as opposed to a down payment on the eventual delivery price.[16]

Furthermore, as recognized by the Commission, "an option is a limited risk instrument. . . . [T]he option purchaser will benefit from a favorable price move and will not be liable for any other losses beyond the premium or other payment that the purchaser pays for the option."[17] The Commission's glossary recognizes the limited risk nature of options, defining an option as "[a] contract that gives the buyer the right, but not the obligation, to buy or sell a specified quantity of a commodity or other instrument at a specific price within a specified period of time, regardless of the market price of that instrument."[18]

In sum, the statutory language (i.e., "put, call, cap, floor, collar or similar option"), together with this longstanding Commission and judicial precedent, makes it clear that options subject to Commission swaps jurisdiction must have characteristics of options, including the right, but not the obligation, to obtain the subject of the option (in this case, the transportation or storage service), that the buyer's losses are limited to a premium paid as consideration for the option seller's performance, and that the option is purchased by offering a premium as opposed to a down payment on the eventual delivery price (in this case, the total price for the services

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[14] Sec. 721(a)(2)(47)(A)(i).

[15] *1985 Interpretative Statement* at P 22,718.

[16] *In the Matter of Cargill* at P 28,425.

[17] *1985 Interpretative Statement* at P 22,718.

[18] *CFTC Glossary: A Guide to the Language of the Futures Industry*, CFTC.GOV, http://www.cftc.gov/ucm/groups/public/@educationcenter/documents/file/cftcglossary.pdf (last visited Oct. 8, 2012) (hereafter, "CFTC Glossary").

rendered). In its Facility Services Agreement Guidance, the Commission sets forth a three-part test to guide the industry as to how the Commission will interpret agreements, contracts and transactions for the "use" of a facility, but not for the purchase or sale of the commodity used, transported or stored in the facility (the "Three-Part Test"):

> The CFTC will interpret an agreement, contract or transaction not to be an option if the following three elements are satisfied: (1) The subject of the agreement, contract or transaction is usage of a specified facility or part thereof rather than the purchase or sale of the commodity that is to be created, transported, processed or stored using the specified facility; (2) the agreement, contract or transaction grants the buyer the exclusive use of the specified facility or part thereof during its term, and provides for an unconditional obligation on the part of the seller to grant the buyer the exclusive use of the specified facility or part thereof; and (3) the payment for the use of the specified facility or part thereof represents a payment *for its use rather than the option to use it*.[19]

The Commission then explained further: "In such agreements, contracts and transactions, while there is optionality as to whether the person uses the specified facility, the person's right to do so is legally established, does not depend upon any further exercise of an option and merely represents a decision to use that for which the lessor already has paid."[20] Thus, the Commission states, "[i]n this context, [it] would not consider actions such as scheduling . . . gas transportation or injection of gas into storage to be exercising an option if all three elements of the interpretation above are satisfied."[21]

Nevertheless, despite adopting guidance that distinguishes agreements in which the buyer pays for the use of a facility from agreements that depend upon the "further exercise of an option," the Commission proceeds to set out the However Paragraph, which, on its face is inconsistent with the *1985 Interpretative Statement* and the further guidance immediately preceding it in the Facility Services Agreement Guidance.

V. Request for Clarification and No-Action

A. Natural gas transportation and storage services are for the "usage" of the facility and are not commodity options

In the natural gas industry, transportation and storage fees pay for the service being rendered by the pipeline or storage company. Often the fee has two components: a reservation fee and a usage fee. The fees are designed to compensate the pipeline or storage operator for services rendered and to establish the customer's right to use the facility. These fees do not provide any type of risk premium (i.e., an independent option to contract for or otherwise obtain

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19 77 Fed. Reg. at 48,242 (emphasis added).

20 *Id*.

21 *Id*.

service at a future date). Regardless of fee structure, under natural gas transportation and storage agreements, the obligations of both service providers and service purchasers become legally binding at the time the agreements are entered into by the parties.

With respect to agreements with reservation fees and usage fees, such agreements legally obligate the customer to pay the reservation fee for the duration of the agreement, regardless of whether the customer uses the service on any particular day. Consistent with the Commission's position on the nature of these agreements in the Facility Services Agreement Guidance, "while there is optionality as to whether the person uses the specified facility, the person's right to do so is legally established, does not depend upon any further exercise of an option and merely represents a decision to use that for which the lessor already has paid."[22] The customer need only nominate gas to be scheduled for transportation on the pipeline or for injection/withdrawal from storage, in accordance with industry protocols.

As the Commission correctly notes, "actions such as scheduling" natural gas transportation and storage are not exercising an option. If scheduling gas under a transportation or storage agreement is not exercising an option, then the underlying agreement and collecting payment for services rendered under the agreement cannot be an option.

Natural gas transportation and storage agreements, on their face, are materially different from options. Unlike an option:

- Once entered into, transportation and storage agreements containing reservation and usage fees obligate the buyer (shipper) to pay the reservation fee for the amount of reserved capacity for the duration of the agreement, regardless of the shipper's actual use of the reserved capacity;

- The reservation fee in a transportation and storage agreement is not a limited-risk premium, nor does it constitute consideration for the purchase of a right or option to later purchase a specified amount of capacity; rather, it is the payment for the service;

- The right to use the specified amount of capacity for the term of the agreement is legally established upon signing the agreement, and the use of the facility does not depend on the further exercise of an option;

- The usage fee, together with the reservation fee, compensates the pipeline for the full costs of providing the buyer the service which the buyer has committed to pay for, and does not constitute a "strike" price or similar fee that is characteristic of an option; rather, the usage fee is in the nature of a reimbursement for the variable costs incurred by the operator in rendering the service; and

- The reservation and usage fees are payments for transportation and storage service and do not give the buyer the right to buy or sell a specified quantity of a commodity.

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22 *Id*.

Furthermore, the "economic reality" of natural gas transportation and storage agreements distinguishes them from commodity options. The fees for these services are designed solely to compensate the transportation or storage provider for the services that were sold to the customer. These fees are not designed or used to shift economic risk to the pipeline or to provide a limited-loss instrument to the customer. With an option, the option buyer is obligated only to pay the premium and has the right, but not the obligation, to acquire the service.[23] Thus, if the economics are unfavorable to the option buyer (e.g., the option is not at- or in-the-money),[24] the option buyer can walk away from the contract without further obligation, losing only the premium paid.[25] By contrast, in a natural gas transportation or storage agreement with a reservation fee and a usage fee, the customer commits to pay the reservation fee for the duration of the agreement, and the pipeline commits to provide the service up to the amount of reserved capacity; no matter how much the North American natural gas markets may change, both the service provider and the customer remain obligated under the agreement as originally agreed.

The economic reality of these agreements is starkly different from that of an option. Upon entering such a facility agreement, the operator sells the right to the service to the customer in consideration for the fixed obligation of the customer to pay the fees for the service; unlike as is the case with an option, the operator has not sold to the customer, upon the customer's payment of a limited-risk premium, any option-like right to buy a service from the operator that the customer may or may not exercise by paying an additional, more substantial fee to the operator.

The Commission's Facility Services Agreement Guidance appears to recognize that natural gas transportation and storage agreements do not have option-like features. In explaining the Three-Part Test, the Commission noted that in such facility agreements a person's right to use the facility "is legally established, [and] does not depend upon any further exercise of an option."[26] The Commission also states, "[i]n this context, [it] would not consider actions such as scheduling . . . gas transportation or injection of gas into storage to be exercising an option."[27] Because the However Paragraph could incorrectly be interpreted to hold that a natural gas transportation or storage agreement with a two-part fee structure is a commodity option, regardless of whether such agreement has the characteristics of an option, the Commission should clarify that agreements for service on natural gas pipeline and storage facilities or parts thereof (i.e., as distinct from sales or purchases of the gas commodity itself) do not have the characteristics of options and hence are not options subject to the definition of a "swap."

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23 *See In the Matter of Cargill* at P 51,217.

24 *See* CFTC Glossary ("At-the-Money: When an option's *strike price* is the same as the current trading price of the underlying commodity, the option is at-the-money"; "In-The-Money: A term used to describe an option contract that has a positive value *if exercised*") (emphasis added).

25 *See In the Matter of Cargill* at P 51,217 ("the buyer's losses are limited to a premium paid as consideration for the option seller's performance").

26 77 Fed. Reg. at 48,242.

27 *Id*.

B. The Commission should clarify that it will use its historical approach of determining whether the agreement has the characteristics of an option, rather than the mere existence of a two-part fee structure, to determine whether a particular natural gas transportation or storage agreement is an option subject to the swap definition

For the reasons discussed above, natural gas transportation and storage agreements are not options subject to the Swap Definition Final Rule. Indeed, INGAA does not believe the Commission intended its Facility Services Agreement Guidance to vary from or in any way contradict the *1985 Interpretative Statement* and its progeny. Nowhere does the Commission discuss changing its precedent, nor does the Commission announce or provide a reasoned analysis supporting any departure from its precedent in the case of facility services agreements. Elsewhere in the Swap Definition Final Rule, the Commission re-affirms its precedent when discussing how to characterize forward contracts.[28] In fact, because the term "swap" is defined to include a "put, call, cap, floor, collar or similar option of any kind," it is clear that Congress intended that options subject to the definition of a "swap" in fact have the recognized characteristics of options, namely, premium-based, limited-risk characteristics common to puts, calls, and "similar" options. Simply put, natural gas transportation and storage agreements do not have the characteristics of options as historically interpreted by the Commission and the courts.

In reviewing the Commission's Facility Services Agreement Guidance, INGAA believes that the Commission intended to incorporate the above-cited precedent into the further interpretive guidance the Commission provided. For example, the third part of the Three-Part Test states that "the payment for the use of the specified facility or part thereof represents a payment for its use rather than the *option* to use it."[29] The Commission further explained that in such agreements, "while there is optionality as to whether the person uses the specified facility, the person's right to do so is legally established, *does not depend upon any further exercise of an option* and merely represents a decision to use that for which the lessor already has paid."[30] This guidance appears to make it clear that if the agreement does not have the recognized characteristics of an option, as established by Commission precedent, the agreement will not be regulated as an option.

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28 *Id*. at 48,237, n.333 ("This facts and circumstances approach to determining whether a particular embedded option takes a transaction out of the forward contract exclusion for nonfinancial commodities is consistent with the CFTC's historical approach to determining whether a particular embedded option takes a transaction out of the forward contract exclusion from the definition of the term 'future delivery' in the CEA. *See id*. at *5 ('As we have held since *Stovall*, the nature of a contract involves a multi-factor analysis * * *.')"); *see also id*. at 48,228, n.214 (quoting *In re Wright*, CFTC Docket No. 97–02, 2010 WL 4388247: "[i]n distinguishing futures from forwards, the [CFTC] and the courts have assessed the transaction as a whole with a critical eye toward its underlying purpose. Such an assessment entails a review of the overall effect of the transaction as well as a determination as to what the parties intended.").

29 *Id*. at 48,242 (emphasis added).

30 *Id*. (emphasis added).

Nevertheless, despite providing guidance that incorporates the historically recognized characteristics of an option, the However Paragraph could be applied to conclude that natural gas transportation and storage agreements with two-part rates are options, a result directly contrary to Commission precedent, the Three-Part Test set forth in the Facility Services Agreement Guidance, and the Commission's traditional approach of analyzing the nature of contracts based on the "facts and circumstances" and the "economic reality" of the transaction. Unfortunately, the However Paragraph was never discussed prior to issuance of the Swap Definition Final Rule, so INGAA had no notice that the Commission would provide guidance regarding two-part rate structures that raises questions about its application to natural gas transportation and storage agreements.

Because the However Paragraph could result in misapplication of Commission guidance and precedent, INGAA respectfully asks the Commission, in addition to or in the alternative to the clarification in part V.A. above, to confirm that it will use its historical approach of determining whether the agreement has the characteristics of an option, rather than the mere existence of a two-part fee structure, to determine whether a particular natural gas transportation or storage agreement is an option subject to the swap definition.[31]

C. At a minimum, the Commission, the Commission's General Counsel or an appropriate Division of the Commission should issue no-action relief prior to October 12, 2012, or as soon thereafter as reasonably possible

INGAA respectfully asks that, at a minimum, the Commission, the Commission's General Counsel or an appropriate Division of the Commission issue no-action relief stating that the Commission will not take, or that such Division of the Commission will not recommend that the Commission take, any enforcement action if the members of INGAA and the other parties to facility agreements with INGAA's members do not treat such facility agreements, including but not limited to natural gas transportation and storage agreements, as "swaps" as defined in Section 1a(47) of the Commodity Exchange Act, as amended, and 17 C.F.R. § 1.3(xxx), or as commodity options subject to the swap definition, in each case, for purposes of complying with the provisions of Title VII, Part II of Dodd-Frank and the rules of the Commission adopted pursuant thereto, solely because such agreements provide for a two-part fee structure. The requested no-action relief should be provided at least until such time as the Commission issues a final clarification, interpretation, rule revision, or response to comments concerning the Final Swap Definition and its applicability to such agreements.

Based on the discussion above, the However Paragraph could result in misapplication of Commission guidance and precedent at a time when market participants require clarity in order to plan for overall compliance with the Dodd-Frank regulatory reforms. As explained in detail in the Joint Associations' request for extension and no-action relief, energy market participants face uncertainty because of numerous pending petitions for exemptive relief from various regulations

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[31] INGAA notes that a straightforward way to achieve this result would be to strike the However Paragraph in its entirety.

that have not yet been published for public comment or granted; ambiguous provisions and unresolved material issues in final and interim final rules that prevent market participants from developing, testing and implementing policies to comply with the Commission's new regulations; numerous rules, or portions thereof, that have been issued as interim final rules without further guidance (an unclear status as "interim" final rules); and proposed rules that have not yet been finalized. It would be contrary to the public interest to impose new and unsupported obligations on natural gas transportation and storage providers, in a manner contrary to the Commission's own historical interpretation of option agreements, when the Commission, in INGAA's view, did not intend to construe all two-part fee agreements as options. Accordingly, good cause exists to issue timely and prompt no-action relief.

VI. Conclusion

INGAA therefore respectfully requests that the Commission, the Commission's General Counsel, or an appropriate Division of the Commission provide the above clarifications and no-action relief pursuant to Commission Rule 140.99, 17 C.F.R. § 140.99, or any other appropriate provision, prior to October 12, 2012, or as soon thereafter as reasonably possible.

If the Commission or its staff would like any additional information, please do not hesitate to contact me at the address and telephone number set out in this letter.

Respectfully submitted,

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cc: Honorable Gary Gensler, Chairman
Honorable Jill E. Sommers, Commissioner
Honorable Bart Chilton, Commissioner
Honorable Scott D. O'Malia, Commissioner
Honorable Mark P. Wetjen, Commissioner
Dan Berkovitz, General Counsel

Attachment