



December 22, 2014

VIA ONLINE SUBMISSION

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

RE: Forward Contracts with Embedded Volumetric Optionality (RIN 3235-AK65)

Dear Mr. Kirkpatrick:

By this letter, the National Corn Growers Association (“NCGA”) and the Natural Gas Supply Association (“NGSA”) respectfully submit these comments in response to the U.S. Commodity Futures Trading Commission’s (the “CFTC’s” or “Commission’s”) Proposed Interpretation, Forward Contracts with Embedded Volumetric Optionality, 79 Fed. Reg. 69073 (Nov. 20, 2014) (the “Proposed Interpretation”). References herein to the Commodity Exchange Act (“CEA”) refer to that statute as amended by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the “Dodd-Frank Act” or “Act”).

Founded in 1957, the NCGA represents more than 40,000 dues-paying corn farmers nationwide. NCGA and its 48 affiliated state organizations work together to create and increase opportunities for their members and their industry.

Established in 1965, NGSA represents integrated and independent companies that produce and market approximately 30 percent of the natural gas consumed in the United States. NGSA encourages the use of natural gas within a balanced national energy policy and promotes the benefits of competitive markets to ensure reliable and efficient transportation and delivery of natural gas and to increase the supply of natural gas to U.S. customers.

Because of the potential for the Dodd-Frank Act to impede what are and have been healthy, competitive, and resilient corn and natural gas markets, NCGA and NGSA played an active role in shaping the Act during its passage and have continued to play an active role with respect to related CFTC rulemakings, to ensure the Act’s successful implementation.

COMMENTS

The CFTC's final rule regarding definition of the term "swap"¹ set forth a seven-element interpretive test (the "2012 Interpretation") for determining whether forward contracts with embedded volumetric optionality fall within the CEA's forward contract exclusion from the definition of the term "swap." The 2012 Interpretation—particularly the seventh element but also the fourth and fifth elements—have been viewed by many as problematic, and NCGA, NGSAs and numerous other industry trade groups and market participants have submitted comments on multiple occasions regarding necessary clarifications to the interpretation.

The CFTC's Proposed Interpretation would clarify the seven-element interpretation as follows (deleted text ~~stricken~~, added text underlined):

[A]n agreement, contract, or transaction falls within the forward exclusion from the swap and future delivery definitions, notwithstanding that it contains embedded volumetric optionality, when:

1. The embedded optionality does not undermine the overall nature of the agreement, contract, or transaction as a forward contract;
2. The predominant feature of the agreement, contract, or transaction is actual delivery;
3. The embedded optionality cannot be severed and marketed separately from the overall agreement, contract, or transaction in which it is embedded;
4. The seller of a nonfinancial commodity underlying the agreement, contract, or transaction with embedded volumetric optionality intends, at the time it enters into the agreement, contract, or transaction to deliver the underlying nonfinancial commodity if the embedded volumetric optionality is exercised;
5. The buyer of a nonfinancial commodity underlying the agreement, contract or transaction with embedded volumetric optionality intends, at the time it enters into the agreement, contract, or transaction, to take delivery of the underlying nonfinancial commodity if ~~it exercises~~ the embedded volumetric optionality is exercised;
6. Both parties are commercial parties; and
7. The ~~exercise or non-exercise of the~~ embedded volumetric optionality is ~~based primarily on~~ intended, at the time that the parties enter into the

¹ Final Rule, Further Definition of "Swap," et al., 77 Fed. Reg. 48,208 (Aug. 13, 2012) ("Swap Definition Rule")

agreement, contract, or transaction, to address physical factors, or regulatory requirements, ~~that are outside the control of the parties and are influencing that reasonably influence~~ demand for, or supply of, the nonfinancial commodity.

NCGA and NGSAs support the Proposed Interpretation's clarification to the seventh element and the fourth and fifth elements, as both sets of changes will substantially improve market participants' regulatory certainty regarding categorization of forward contracts with embedded volumetric optionality and their determination of related compliance obligations.

I. NCGA and NGSAs Support the Proposed Clarification to the Seventh Element of the Interpretation.

NCGA and NGSAs support the proposed clarification to the seventh element of the interpretation, which appropriately removes reference to the "exercise or non-exercise" of embedded volumetric optionality and focuses on contracting parties' intent regarding embedded volumetric optionality at the time of contract initiation. NCGA and NGSAs believe that the proposed clarification will greatly improve the regulatory certainty of end users entering into forward contracts with embedded volumetric optionality at the time when certainty is most critical—*i.e.*, at execution of each contract, when the decision is made whether or not to enter into such contract. NCGA and NGSAs welcome the appropriate emphasis on the parties' intent at the time of contract initiation, as well as the related clarification that parties may reasonably rely on their counterparties' representations regarding such intent. In addition, NCGA and NGSAs welcome the Proposed Interpretation's further clarifications regarding: (i) the scope of the term "physical factors," (ii) the ability of parties to satisfy the interpretation despite having some level of influence over factors affecting their demand or supply or having price considerations, and (iii) the acceptability of price considerations under the interpretation if they arise subsequent to execution or are motivated by an applicable regulatory requirement. Each of these clarifications will facilitate market decisions and compliance efforts by eliminating unnecessary uncertainty regarding the scope of the forward contract exclusion.

This is a vast improvement over the unworkable 2012 Interpretation's seventh element. As NCGA and NGSAs pointed out in its joint comments responding to the Commission's April 3, 2014 Public Roundtable,² by focusing on the "exercise or non-exercise" of embedded volumetric optionality, the 2012 Interpretation raises severe compliance problems and potentially distorts market behavior because of: (i) difficulty in crafting adequate representations in contracts to address compliance concerns, (ii) disagreement among parties as to how to categorize transactions, (iii) potentially shifting regulatory categorization of transactions after execution because of *ex post facto* developments, and (iv) avoidance of otherwise well-suited transactions or counterparties because of such practical difficulties.

By focusing on intent at the time of contract initiation, the Proposed Interpretation brings the seventh element substantially in line with the language of the forward contract exclusion

² Letter to CFTC from Commodity Markets Council, National Corn Growers Association, and Natural Gas Supply Association, dated April 17, 2014.

itself. The forward contract exclusion excludes from the definition of the term “swap” any “sale of a nonfinancial commodity or security for deferred shipment or delivery *so long as the transaction is intended to be physically settled.*”³ Consistent with other CFTC interpretations concerning the intent of contracting parties,⁴ the construction of this exclusion only makes sense if the intent of contracting parties is analyzed as of the time of contract execution.

II. NCGA and NGSAs Request Expedited Approval of the Proposed Interpretation to Facilitate Compliance with the 2014 Form TO Reporting Obligation.

As discussed above, the Proposed Interpretation provides much needed certainty regarding the categorization of numerous forward contracts that make use of embedded volumetric optionality to address commercial uncertainty with respect to the quantity of a commodity that may become needed or available for commercial purposes. Application of the seven-element interpretation is often critical in determining whether individual forward contracts should be included or excluded from Form TO under Section 32.3(b)(2) of the CFTC’s regulations. Continued applicability of the 2012 Interpretation is highly problematic in this regard because the intractable associated uncertainties cause both: (i) compliance problems for market participants (including incurrence of substantial and unnecessary compliance costs due to the need to employ costly professional and legal advisors to analyze and categorize transactions); and (ii) the data supplied to the CFTC on Form TO to be of questionable value. For these reasons, NCGA and NGSAs request that the CFTC provide expedited approval of the Proposed Interpretation at least **six (6)** weeks prior to the March 1, 2015 deadline for filing Form TO for 2014 transactions, so that market participants have adequate time to analyze such transactions under the applicable interpretation. Alternatively, NCGA and NGSAs request that the CFTC extend the March 1, 2015 Form TO deadline itself to provide a similar **six (6)**-week buffer.

CONCLUSION

NCGA and NGSAs support the Proposed Interpretation. NCGA and NGSAs welcome the opportunity to discuss these comments with the Commission. If we can provide any additional information, please do not hesitate to contact us. Correspondence regarding this submission should be directed to:

³ CEA § 1(a)(47)(B)(ii) (emphasis added).

⁴ See, e.g., Swap Definition Rule at 48230 (recognizing that a netting agreement’s reduction of offsetting delivery obligations to a net delivery amount would not alter the forward contract nature of affected transactions “provided that the parties had a bona fide intent, *when entering into the transactions*, to make or take delivery” (emphasis added)); *id.* at 48230 (recognizing that, with respect to termination rights in excluded forward contracts, “a bona fide termination right must be triggered by something *not expected by the parties at the time the contract is entered into*” (emphasis added)); *id.* at 48228.

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Respectfully submitted,

National Corn Growers Association
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