



AMERICAN PUBLIC GAS ASSOCIATION

September 15, 2009

The Honorable Blanche Lincoln
Chairman
Committee on Agriculture, Nutrition and Forestry
U.S. Senate
Washington, D.C. 20510

Dear Chairman Lincoln:

On behalf of the American Public Gas Association (APGA), I want to congratulate you on your recent appointment as Chairman of the Senate Agriculture, Nutrition and Forestry Committee. We look forward to working with you on a number of important issues over the coming session.

I also want to express our strong concerns on an issue that the Committee may be working on later this year as part of over-the-counter (OTC) derivatives reform legislation. Specifically, we are extremely concerned about certain proposals that would require public gas systems to clear their OTC derivatives transactions and the impact those proposals would have on their consumers. Not all proposals would mandate clearing of all OTC transactions. Some might exclude transactions between a dealer and non major customers, such as APGA members. Others, however, would mandate clearing for all standardized OTC transactions regardless of the nature of the customer.

APGA is the national association for publicly-owned natural gas distribution systems. There are approximately 1,000 public gas systems in 36 states and over 720 of these systems are APGA members. Publicly-owned gas systems are not-for-profit, retail distribution entities owned by, and accountable to, the citizens they serve. They include municipal gas distribution systems, public utility districts, county districts, and other public agencies that have natural gas distribution facilities.

Public gas systems depend upon both the physical commodity markets as well as the markets in OTC derivatives to meet the natural gas needs of their consumers. Together, these markets play a critical role in these utilities securing natural gas supplies at stable prices for their communities. Specifically, natural gas distributors purchase firm supplies in the physical delivery market at prevailing market prices, and enter into OTC derivative agreements customized to meet their specific needs, reduce their consumers' exposure to future market price fluctuations and stabilize rates.

By using both markets, these public gas systems are able to purchase firm deliveries of natural gas from a diverse set of suppliers while hedging the risk of future market price fluctuations. For these reasons, APGA has pushed for the passage of legislation and regulations that increase transparency and help ensure that the OTC markets are an accurate reflection of supply and demand conditions for natural gas.

However, proposals that would require all standardized OTC derivatives transactions to be cleared would significantly impair the financial ability of public gas systems to engage in these gas supply strategies. Under current practices in the OTC markets, many APGA members are not required to pledge collateral for transactions above agreed upon levels based upon their very-high credit worthiness. Moreover, adjustments to collateral levels are made on a pre-defined, periodic basis. In contrast, the mandated clearing of all OTC transactions would require public gas systems to post initial margin for all transactions and to meet potential margin calls whenever required on little notice. This would constitute a significant financial and operational burden on these systems, their communities and their consumers.

It has been suggested that the clearing requirements would be less burdensome if some end-users are given the option of posting non-cash collateral. Unfortunately, the alternative of using non-cash collateral would not provide any relief to public gas systems. Non-cash collateral would entail the deposit of liquid assets and public gas systems simply do not maintain such liquid assets in the quantity necessary to meet the requirements associated with clearing. And maintaining this level of liquid assets doing so would be at odds with the routine funding and fee collection practices of public natural gas distribution systems.

APGA understands that provisions that require the clearing of all OTC transactions are intended to address issues related to systemic risk. However, the hedging of natural gas supply purchases by public natural gas systems using non-cleared bi-lateral OTC derivatives do not present the types of systemic risks posed by some dealers of credit-default swaps, which is the impetus behind the proposed clearing mandate. Moreover, the proposed mandate to clear all standardized OTC derivatives transactions would increase costs for public gas systems and their municipalities; an increase which would be borne 100% by their consumers. I look forward to working with you and others towards protecting consumers from these cost increases.

Sincerely,

A handwritten signature in black ink, appearing to read "Bert Kalisch". The signature is fluid and cursive, with a prominent initial "B" and a long, sweeping underline.

Bert Kalisch
President & CEO