

FEDERAL ENERGY REGULATORY COMMISSION
WASHINGTON, D.C. 20426

In Reply Refer To:
Office of Enforcement
Docket No. FA11-17-000
January 26, 2012

Merrill Lynch Commodities, Inc.
ATTN: Mr. Rhys Roberts
Senior Vice President
20 East Greenway Plaza
Houston, TX 77046

Dear Mr. Roberts:

1. The Division of Audits in the Office of Enforcement (OE) has completed an audit of Merrill Lynch Commodities, Inc. (Merrill Lynch) for the period of January 1, 2009 through December 31, 2010. The audit evaluated Merrill Lynch's compliance with the Commission's filing requirements for the annual report of natural gas transactions under 18 C.F.R. Part 260.401 (2010), and the Commission's FERC Form No. 552 instructions.¹ The audit also included selective tests of Merrill Lynch's physical natural gas transactions to validate the accuracy of the information filed with the Commission in its FERC Form 552 report.
2. On December 21, 2011, you notified us that Merrill Lynch agrees with audit staff's conclusions and has no further comments regarding the audit report. The enclosed report identifies that the audit did not result in any findings or recommendations that require Merrill Lynch to take corrective actions at this time. We included a copy of your response as an appendix to the audit report. Docket No. FA11-17-000 is now closed.
3. The Commission delegated authority to act on this matter to the Director of OE under 18 C.F.R. § 375.311 (2011). This letter order constitutes final agency action. Merrill Lynch may file a request for rehearing with the Commission within 30 days of the date of this order under 18 C.F.R. § 385.713 (2011).

¹ *Transparency Provisions of Section 23 of the Natural Gas Act*, Order No. 704, 121 FERC ¶ 61,295 (2007), *order on reh'g*, Order No. 704-A, 124 FERC ¶ 61,269 (2008), *order on reh'g*, Order No. 704-B, 125 FERC ¶ 61,302 (2008), *order on reh'g*, Order No. 704-C, 131 FERC ¶ 61,246 (2010).

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4. This letter order is without prejudice to the Commission's right to require hereafter any adjustments it may consider proper from additional information that may come to its attention. In addition, any instance of non-compliance not addressed herein or that may occur in the future may also be subject to investigation and appropriate remedies.

5. I appreciate the courtesies extended to the auditors. If you have any questions, please contact Mr. Bryan K. Craig, Director and Chief Accountant, Division of Audits, at (202) 502-8741.

Sincerely,

Norman C. Bay
Director
Office of Enforcement

Enclosure



Federal Energy Regulatory Commission

**Audit of FERC Form No. 552
for Merrill Lynch
Commodities, Inc.**

Docket No. FA11-17-000
January 26, 2012

Office of Enforcement
Division of Audits

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I. Executive Summary

A. Overview

The Division of Audits within the Office of Enforcement has completed an audit of Merrill Lynch Commodities, Inc. (Merrill Lynch). The audit evaluated Merrill Lynch's compliance with the Commission's filing requirements for the annual report of natural gas transactions under 18 C.F.R. Part 260.401 (2010), and FERC Form No. 552 instructions.¹ The audit covered the period January 1, 2009 through December 31, 2010.

B. Merrill Lynch Commodities, Inc.

Merrill Lynch is a wholly-owned subsidiary of Bank of America Corporation that transports, delivers, markets, and trades power, natural gas, and other energy-related commodities. In its 2009 FERC Form No. 552 Merrill Lynch reported physical natural gas purchase volumes of 485 trillion British thermal unit (TBtu) and sales volumes of 397 TBtu. Merrill Lynch ranked 26th and 37th, respectively, for total purchase and sales volumes among the 715 Respondents filing a 2009 Form No. 552. Merrill Lynch also indicated it reports natural gas transactions to price index publishers. Therefore, all of their reported transactions contribute to the formation of price indexes at hubs and city gates where they trade.

C. Conclusion

The audit did not result in any findings or recommendations that require Merrill Lynch to take corrective actions at this time. Audit staff based its conclusion on the review of material provided by Merrill Lynch in response to data requests, interviews with Merrill Lynch employees, and a review of publicly available documents.

¹ *Transparency Provisions of Section 23 of the Natural Gas Act*, Order No. 704, 121 FERC ¶ 61,295 (2007), *order on reh'g*, Order No. 704-A, 124 FERC ¶ 61,269 (2008), *order on reh'g*, Order No. 704-B, 125 FERC ¶ 61,302 (2008), *order on reh'g*, Order No. 704-C, 131 FERC ¶ 61,246 (2010).

II. Background Information

A. Regulatory Overview

On December 26, 2007, the Commission issued a final rule in Order No. 704, which amended Part 260 of its regulations to require the annual submission of a new form, the FERC Form No. 552.² The order has its genesis from the Energy Policy Act of 2005, which added section 23 of the Natural Gas Act (NGA).³ Section 23 of the NGA, among other mandates, directs the Commission “to facilitate price transparency in markets for the sale or transportation of physical natural gas in interstate commerce, having due regard for the public interest, the integrity of those markets, and the protection of consumers.”⁴ Accordingly, Order No. 704 required natural gas wholesale market participants, including a number of entities that may not otherwise be subject to the Commission’s traditional NGA jurisdiction, to report certain information concerning their natural gas sales and purchases annually.

This information includes an annual requirement for certain buyers and sellers of natural gas to report whether or not they report transactions to index publishers and volumes of relevant transactions for the previous calendar year.⁵ The annual reporting requirement allows the Commission and the public to assess the importance of index pricing in the natural gas markets, and to determine the size of the fixed-price transactions that contribute to or may contribute to formation of price indexes.

B. FERC Form No. 552

The Commission requires natural gas market participants subject to the Commission’s reporting requirements to file the FERC Form No. 552 annually, unless the Commission has exempted a participant or granted it a waiver. Specifically, 18 C.F.R. § 260.401 (a) requires participants to file the FERC Form No. 552 for the calendar year ending December 31, 2008 and each calendar year from then on. Under 18 C.F.R. § 260.401 (b)(1), unless the Commission has exempted a participant or granted it a waiver by rule or order, each participant (i.e., any buyer or seller engaged in physical natural gas transactions the previous calendar year), must prepare and file with the Commission a FERC Form No. 552, under the form’s definitions and general

² *Transparency Provisions of Section 23 of Natural Gas Act*, Order No. 704, 73 Fed. Reg. 1,014 (Jan. 4, 2008), FERC Stats. & Regs. ¶ 31,260 (2007) (Final Rule).

³ Energy Policy Act of 2005, Pub. L. No. 109-58, 119 Stat. 594 (2005).

⁴ 15 U.S.C. § 717t-2(a)(1) (2006).

⁵ *Transparency Provisions of Section 23 of the Natural Gas Act*, 72 Fed. Reg. 20,791 (Apr. 26, 2007), FERC, Stats. & Regs. ¶ 32, 614 (2007).

instructions. However, during the time this audit was conducted, a participant was exempted from this filing requirement if it engaged in reportable physical natural gas sales or purchases amounting to less than 2.2 TBTu for the previous calendar year. Also, 18 C.F.R. § 260.401 (b)(2) requires participants to file the FERC Form No. 552 by May 1 of each year, unless otherwise instructed by the Commission, and prepare it so it conforms with Commission software and guidance posted on FERC's web site.

The basic purpose of reporting physical natural gas sales and purchases is to provide greater transparency over the use of indexes to price physical natural gas. FERC Form No. 552 also informs the Commission and the public on what volumes contribute to, or may contribute to the formation of a price index during the subject calendar year. Many market participants rely on daily and monthly indexes as a way to reference market prices without taking on the risks of active trading. During the time of this audit, Order No. 704, and Order Nos. 704-A, 704-B, and 704-C required market participants to report physical natural gas purchases or sales that used a natural gas index and, contributed to, or could contribute to the formation of a price index in the FERC Form No. 552, page 4, lines 1-9, as reflected below.⁶

1. Total volume of the respondent's reportable physical sales and purchases.
2. Quantities contracted at fixed prices for next-day delivery.
3. Quantities contracted at prices at published daily gas price indices.
4. Quantities contracted at fixed prices for next-month delivery.
5. Quantities contracted at prices at published monthly gas price indices.
6. Quantities contracted under trigger agreements (e.g., NYMEX Plus contracts).
7. Quantities contracted as physical basis transactions.
8. Difference between respondent's purchases reported on line 1 and the sum on lines 2, 3, 4, 5, 6, and 7.
9. Difference between respondent's sales reported on line 1 and the sum on lines 2, 3, 4, 5, 6, and 7.

Besides this information, the FERC Form No. 552 permits the aggregation of affiliates. The respondent must complete the "Schedule of Reporting Companies", on page 3 of the FERC Form No. 552, which lists those affiliates. Further, this schedule requires the respondent to indicate whether it or any affiliate listed reported any transaction information to Price Index Publishers during the report year.

⁶ *Transparency Provisions of Section 23 of the Natural Gas Act*, Order No. 704, 121 FERC ¶ 61,295 (2007), *order on reh'g*, Order No. 704-A, 124 FERC ¶ 61,269 (2008), *order on reh'g*, Order No. 704-B, 125 FERC ¶ 61,302 (2008), *order on reh'g*, Order No. 704-C, 131 FERC ¶ 61,246 (2010).

III. Introduction

A. Objectives

The audit objectives were to evaluate Merrill Lynch's compliance with the Commission's regulations for the annual report of natural gas transactions under 18 C.F.R. Part 260.401 (2010), and determine whether the information filed in its FERC Form No. 552 was accurate. The audit covered January 1, 2009 through December 31, 2010.

B. Scope and Methodology

Audit staff performed several specific actions to conduct this audit. Audit staff first identified standards and criteria, including Commission rules, regulations, and other requirements to evaluate Merrill Lynch's compliance with the audit objectives. Audit staff then reviewed publicly available information to understand Merrill Lynch's corporate environment, business operations, customer activities, and regulatory history relevant to the FERC Form No. 552. Audit staff conducted substantive testing to determine whether Merrill Lynch reported volumes in its FERC Form No. 552 consistent with the definitions and general instructions in that form.

Audit staff performed the actions below to facilitate its testing and evaluation of compliance:

- *Gathered Relevant Data:* Audit staff issued data requests to Merrill Lynch. The information sought included internal policies and procedures, transactional data and contracts, internal and external reports, and other information relevant to the audit objectives. Audit staff used this information as support for testing and evaluating Merrill Lynch's compliance with the FERC Form No. 552 requirements. Responses to data requests also provided information about the structure and operation of Merrill Lynch's regulatory compliance program.
- *Conducted Interviews and Teleconferences:* Audit staff interviewed Merrill Lynch employees and spoke with them via teleconference to discuss administrative and technical matters, and assist in evaluating the Company's compliance with the audit objectives.
- *Met with Commission Staff:* Audit staff met with Commission staff to discuss audit developments, potential compliance issues, and ensure audit report findings were consistent with Commission precedent and policy.

Audit staff performed the actions below to evaluate Merrill Lynch's compliance with requirements relevant to the audit scope:

- *Reporting of Affiliates:* Audit staff reviewed corporate organizational charts and held discussions with Merrill Lynch to identify all affiliates that purchased or sold physical natural gas subject to the reporting requirements of the FERC Form No. 552.
- *Reporting to Price Index Publishers:* Audit staff requested supporting documentation and held discussions with employees to determine whether Merrill Lynch reported transaction information to Price Index Publishers.
- *Total Transaction Volumes:* Audit staff reviewed total reportable physical natural gas purchases and sales volumes to verify the accuracy and completeness of the FERC Form No. 552. This required audit staff to compare the FERC Form No. 552 reported volumes to transactional data the Company provided to support the accuracy of the purchases and sales associated with those volumes. Merrill Lynch provided this data on a monthly basis for January 1, 2009 through December 31, 2009.
- *Classification of Transaction Volumes:* Audit staff evaluated the physical natural gas purchases and sales volumes reported in the form to verify the accuracy of each transaction category. For example, for the "fixed price, next-day delivery" category, audit staff requested and evaluated transactional data to ensure that the transactions were completed before the NAESB nomination deadline (11:30 a.m. Central time) and were for uniform delivery over the next pipeline day. Also, for the "fixed price, next-month delivery" category, audit staff requested and evaluated transactional data to ensure that the transactions were completed in the last five business days of the month (during bidweek) and were for uniform physical delivery over the next month.
- *Reportable and Nonreportable Transactions:* Audit staff analyzed physical natural gas transactions to ensure Merrill Lynch reported all of them in the FERC Form No. 552. For example, audit staff requested a sample of all physical natural gas transactions to verify the Company reported only required transaction volumes. Audit staff also reviewed specific nonreportable transactions, such as affiliate transactions, unprocessed gas, and international transportation volumes to verify the Company did not report these types of transactions in its FERC Form No. 552.

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Besides these actions, audit staff reviewed Merrill Lynch's regulatory compliance program. Audit staff assessed the compliance program for the audit scope areas consistent with prior Commission orders and policy statements. Specifically, audit staff:

- Reviewed Merrill Lynch's regulatory compliance program structure, including its authority and responsibilities for overseeing corporate compliance and the delegation of compliance responsibilities at the department level.
- Reviewed Merrill Lynch's Internal Audit department structure, including chain-of-command and access to the Board of Directors through the Audit Committee to assess the effectiveness and independence of the audit process.
- Interviewed executives, managers, and operational employees to evaluate their knowledge and application of Merrill Lynch's compliance program.

IV. Appendix



December 21, 2011

VIA DHL Overnight Delivery

Re: Office of Enforcement, Docket No. FA11-17-000

Dear Mr. Craig:

Thank you for the draft report dated December 9, 2011 following the audit of FERC Form No. 552 for Merrill Lynch Commodities, Inc.

I note that the audit report did not result in any findings or recommendations that require Merrill Lynch Commodities, Inc to take corrective action at this time. I can confirm that we have no additional comments to make to the draft report.

Pursuant to Section 8 and 8(a) of the Commodity Exchange Act, as amended, ("CEA") and Commission Regulation § 145.9, Merrill Lynch requests confidential treatment of the enclosed materials on the ground that disclosure of such material would reveal trade secrets or confidential commercial or financial information of Merrill Lynch, or protected personal information. Furthermore, the disclosure of the enclosed materials may not only violate Merrill Lynch's proprietary rights, but may also grant competitors an unfair competitive advantage or compromise competitive advantages possessed by Merrill Lynch. Merrill Lynch also requests that this letter requesting confidential treatment not be disclosed for the aforementioned reasons. We reserve all rights with respect to inadvertent disclosures.

Pursuant to 28 C.F.R. § 16.8(c), Merrill Lynch further requests that this letter and the enclosed materials not be disclosed in response to any request under the Freedom of Information Act, 5 U.S.C. § 552. In the event that this letter and/or the enclosed materials are the subject of a Freedom of Information Act request, please inform me, and I will provide further substantiation of Merrill Lynch's request for confidential treatment.

Merrill Lynch Commodities, Inc. is a subsidiary of Bank of America Corporation and is not covered by the FDIC or SIPC.

Tel: 832.681.2100 • Fax: 832.681.7217 • 877.699.7400

MERRILL LYNCH COMMODITIES, INC.
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The information and data provided herewith are expressly subject to, and without waiver of, any objections that MLCI may have to the request, including but not limited to objections based upon the Commission's assertion of jurisdiction over any matter covered by the request or other procedural or substantive objections related to the content, scope, timing, burdensomeness, interpretation or application of any part of the request, including each question, the instructions or definitions.

If you have any questions, please contact either Rhys Roberts at (832) 681-5359 or Kelly Funderburk at (832) 681-5262. Thank you for your cooperation in this matter.

Kind Regards,

A handwritten signature in blue ink that reads "Rhys Roberts". The signature is written in a cursive style.

Rhys Roberts

Document Content(s)

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