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Via On-line Submission

Mr. David A. Stawick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street, N.W.
Washington, DC 20581

February 22, 2011

Re: Proposed Rules – Further Definition of “Swap Dealer,” “Security-Based Swap Dealer,” “Major Swap Participant,” “Major Security-Based Swap Participant” and “Eligible Contract Participant” (RIN 3235-AK65); End-User Exception to Mandatory Clearing of Swaps (RIN 3038-AD10)

Dear Mr. Stawick:

The Commodity Markets Council (“CMC”) appreciates the opportunity to comment on two Commodity Futures Trading Commission (the “CFTC” or “Commission”) proposed rulemakings regarding Further Definitions and the End-User Exception.

CMC is a trade association bringing together commodity exchanges with their industry counterparts. The activities of our members represent the complete spectrum of commercial users of all futures markets including agriculture. Specifically, our industry member firms are regular users of the Chicago Board of Trade, Chicago Mercantile Exchange, ICE Futures US, Kansas City Board of Trade, Minneapolis Grain Exchange, and New York Mercantile Exchange. CMC is uniquely positioned to provide the consensus views of commercial end-users of swaps and derivatives exchanges. Our comments below represent the collective view of the CMC’s members.

Congress and the President enacted The Dodd–Frank Wall Street Reform and Consumer Protection Act (the “Act”) in response to the financial crisis in 2008-09 with the purpose of establishing a regulatory framework for systemically risky financial institutions and instruments. Since 2008, CMC has advocated for increased transparency and regulation of such institutions and instruments; however, we do not believe the Act was intended to prescriptively regulate *all* firms and *all* instruments that operate in financial markets. While Congress created a regulatory framework, it provides the CFTC with flexibility to implement the law in a way that continues to promote and maintain the efficiency of US markets. CMC encourages the Commission to recognize the protections already embedded in swaps which exchanges agree to list, trade and accept for clearing. We also urge you to make the necessary distinctions as the CFTC makes decisions related to definitions.

Defining “Swap Dealers”

Cleared over-the-counter (OTC) swaps would be subject to exchange rules of credit assessment and margining. Moreover, clearing members of the exchanges are subject to a thorough credit analysis and required to provide regular financial reporting. These clearing members in turn require a margin and credit analysis of their customers. Entities that exclusively trade exchange-cleared swaps mark their positions to market and are assessed a daily margin. The clearing house also verifies the provision and maintenance of adequate liquidity buffers to cover extreme markets swings.

Despite these protections, senior CFTC officials have stated that the Commission could classify as many as 200 firms as “Swap Dealers” (“SD”), subjecting them to additional capital and margining requirements. CMC supports the Commission in its mission to curb systemically risky institutions and instruments; however, we ask the CFTC to use caution in drafting definitions so broad as to impede the creation and flow of capital and liquidity in the financial markets.

CMC recommends that the Commission exercise its definitional authority with a measure of pragmatism that reflects the market and the structure of corporations actively engaged in the underlying physical market value chains. As such, CMC believes the following should fall clearly outside the SD definition: entities which only trade exchange-cleared swaps, entities engaged in cash forward transactions with embedded derivatives and/or book-out transactions, and swaps entered into and/or offered by or among end-users. This will ensure commercial end users continue to utilize deep OTC markets with adequate liquidity to effectively hedge their risks. We are concerned increased capital and margining requirements will correspondingly increase the cost of compliance and opportunity cost of capital for entities which only trade exchange-cleared OTC swaps. These costs could result in firms ceasing or reducing their use of such instruments which would decrease the liquidity of currently robust markets.

Finally, the Act specifies that an SD or Major Swap Participant (“MSP”) designation does not apply across all asset classes. There is concern within the industry that the designation of a firm as an SD for one asset class will mean it is regulated as such for *all* asset classes. CMC urges the Commission to hew closely to the law’s intent by limiting the scope of the SD rules and would ask the Commission to clarify its position on this issue.

Defining Yield Swaps

There are market participants (e.g. reinsurance companies) that offer risk mitigant products, i.e. “swaps,” that reference “yield” (in bushels per acre on corn, soybeans, wheat and other commodities) as the underlying asset. The CMC would like to ensure that such products are included in the definition of “swaps”.

Cash Forward Contracts With Embedded Options and Certain Cash Transaction Book-outs Should Not be Treated as “Swaps”

While recognizing these trades are different, CMC believes embedded options in forward contracts and, separately, book-outs from certain cash transactions should not be treated as swaps. Each of these markets has been historically recognized by the Commission as cash and we merely seek confirmation of this from the CFTC as the proposed rules affecting agricultural and energy transactions move forward. Regardless of whether these trades are made with producers or are between commercial entities, so long as the parties to the transaction have the intention of physical delivery, they should continue to be

treated as cash and not become subject to regulation as a swap. CMC believes these transactions are significant to the cash market; any change in the characterization would reduce cash contract opportunities for producers and disrupt export markets in bulk agricultural and energy commodities.

From a producer perspective, treating embedded options as swaps would deny them access to cash contracts that allow them improved pricing opportunities. These contracts require delivery, but hold open final pricing until the producer sets his basis and/or futures component of the contract price under the terms of the contract. The CMC requests the Commission to reaffirm its position that these transactions fit within the exclusion for cash forward transactions under the Act.

Similarly, if book-outs are treated as swaps, CMC believes it could hinder the net settlement of physical transactions and place the Commission in the position of regulating what is, in fact, a vibrant piece of the cash market between commercial participants. Senators Dodd and Lincoln in their letter to the CFTC expressly excluded from the definition of swaps the situation where “commercial parties agree to book-out their physical delivery obligations under a forward contract.” Accordingly, CMC urges the Commission to grant an exclusion from rules regulating swaps for book-outs, so long as such transactions are intended to be physically settled.

Because of the importance of this distinction to the industry, CMC requests the CFTC expressly state in its rulemaking that embedded options in forward contracts and book-outs are not swaps and therefore will not be regulated as such.

A Broad End-User Exception from Mandatory Clearing of Swaps is Necessary and Beneficial for the Industry and Consumers

Many market participants rely on customized OTC swaps because they may not have volumes that are big enough to hedge with standardized contracts, their volumes may not equate precisely to one or more futures contracts, or there may be no standardized contracts available to hedge their specific commercial risks. For these reasons, it is very important that the Commission provide a broad end-user exception from mandatory clearing of swaps. Failure to do so would increase the costs associated with entering into swaps, thus reducing the benefits that producers, processors, miners, extractors and refiners can achieve through hedging. If end-users were required to conduct all of their hedging activities with cleared swaps, they would incur higher margin costs and would have less capital available to deploy towards their business operations. They also may be forced to pass the increased hedging costs along to their customers, which could negatively impact the economic recovery after the recent recession.

CMC thanks the Commission for the opportunity to comment on these matters, and we look forward to working with the Commission in the weeks and months ahead. If you should have any questions, please do not hesitate to contact me at christine.cochran@commoditymktcs.org or via phone at (202) 842-0400 – extn. 101.

Sincerely,



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Commodity Markets Council