



National Grain and Feed Association

1250 Eye St., N.W., Suite 1003, Washington, D.C. 20005-3922, Phone: (202) 289-0873, FAX: (202) 289-5388, Web Site: www.ngfa.org

March 28, 2011

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

RE: "Position Limits for Derivatives," (Federal Register Vol. 76, No. 17, January 26, 2011)

Dear Mr. Secretary:

The National Grain and Feed Association (NGFA) appreciates the opportunity to provide input to the Commodity Futures Trading Commission (CFTC) on this very important proposed rule. For bona fide hedgers who are hedging physical commodity risk and depend on futures markets for price discovery and risk management, the outcome of this rulemaking is extremely important.

The NGFA is the national non-profit trade association representing more than 1,000 companies that operate an estimated 7,000 facilities nationwide in the grain, feed and processing industry. Member firms range from quite small to very large; privately owned, publicly traded and cooperative; and handle or process well in excess of 70% of all U.S. grains and oilseeds annually. Companies include grain elevators, feed mills, flour mills, oilseed processors, biofuels producers/co-product merchandisers, futures commission merchants and brokers, and related commercial businesses.

A common thread for NGFA-member firms is that they rely on convergence of cash and futures in enumerated agricultural futures markets in order to facilitate risk management for U.S. agricultural producers and in their own physical commodity operations. In the following comments, we will limit our input on the Commission's proposal as to how it will impact enumerated agricultural commodities. In that context, our primary points will be:

- 1) Convergence matters – and retaining spot-month and all-months-combined legacy position limits for enumerated agricultural commodities, as proposed by the CFTC, absolutely is the appropriate step for the Commission in its efforts to continue encouraging convergence. Before adjustments to current position limit levels are

considered, more information will be needed concerning impacts of other elements of Dodd-Frank, the scope and size of the swap marketplace and impacts of those factors on convergence. Doing otherwise could jeopardize contract performance and the viability of enumerated agricultural futures contracts as effective hedging tools.

- 2) Relative to the definition of bona fide hedging, the NGFA strongly supports the Commission's proposal to provide hedge exemptions for non-bona fide swap participants only if such swap transactions or positions represent cash market transactions and offset a bona fide counterparty's cash market risks.
- 3) The process by which bona fide hedgers apply for hedge exemptions and report cash positions needs to be simple and straightforward. There is no demonstrated need for more frequent or more onerous procedures than currently exist. We see no reason to impose additional requirements on bona fide hedgers who are hedging physical commodity risk and pose no systemic risk.

Importance of Convergence

It has been well documented in recent years that enumerated agricultural commodities – in particular, Chicago Board of Trade (CBOT) and Kansas City Board of Trade (KCBT) wheat contracts – have faced challenges to contract performance and have exhibited lack of convergence. That lack of convergence at times has contributed to severe financial stress on first-purchasers and end-users of wheat as they seek to assist producers with risk management and merchandising strategies, and as they manage their own price and inventory risk. We believe strongly that the vastly increased participation of investment capital in these markets has been a factor in lack of convergence – not the only factor, but an important one.

Today, both CBOT and KCBT have made or are making changes to their wheat contracts to help re-establish convergence. The NGFA was involved in the process of considering and providing input on those contract revisions, and we support the exchanges in this important effort. It may be too early to draw final conclusions, but performance of the CBOT contract seems to be improved. We also are hopeful that revisions to the KCBT contract that will take effect in the fall will lead to improved convergence.

The NGFA believes strongly that these contract changes need to be allowed to take full effect and that time be allowed to thoroughly evaluate their impacts on contract performance before additional major changes to these and other enumerated commodity markets are made. Certainly, increasing position limits in the current volatile market environment would be a significant change that could make it difficult to evaluate the effectiveness of recent and coming changes on enumerated agricultural futures contracts.

Enumerated Agricultural Commodities' Unique Characteristics

The NGFA is appreciative of the difficult task facing the Commission as it seeks to establish reasonable position limits for a number of diverse commodities and markets. We believe strongly that identifying a “one size fits all” approach is unlikely to provide the right

solution for commodities as diverse as energy, metals, financial products and agricultural commodities – and even within the agricultural commodities, the enumerated commodities display characteristics different from other agricultural commodities. We believe strongly that a final rule will need to recognize the unique characteristics – functionally and in terms of size of the market – of enumerated agricultural commodities. The Commission appropriately has recognized such differences in its proposed rule.

We understand the position of some who would contend that position limits should be increased for the simple reason that limits on enumerated agricultural commodities have not been raised in several years and that open interest has increased. In fact, the NGFA historically has been mostly supportive of exchange petitions to increase position limits. However, given dramatic changes in our markets in recent years – including very large increases of nontraditional investment capital that have threatened to overwhelm some markets – we believe increases are not merited at this time.

The measure of whether position limit changes are appropriate now should not be based solely on higher open interest levels – driven in part by new investment capital participation, which itself has contributed to impaired performance and lack of convergence. The truly appropriate question is this: Are we sure that futures markets for enumerated agricultural commodities are performing their price discovery and risk management roles adequately for traditional market participants, the bona fide commercial hedgers? Position limits should not be increased from current levels until the Commission and the industry are convinced this is the case.

Regarding the Commission’s proposal to establish position limits for other commodities based on open interest levels and deliverable supplies, we will comment only that such formulas applied to the enumerated agricultural commodities would result in huge position limit increases of at least several multiples of current levels. Clearly, the Commission has recognized that approach as unworkable for the enumerated agricultural commodities, a position with which the NGFA agrees strongly.

Support for CFTC Proposal on Treatment of Swap Dealers

The NGFA does not seek to exclude investment participation, swap dealer participation or any other participant from the enumerated agricultural futures markets. However, reasonable limits on such participation are needed to ensure that markets function properly for U.S. agricultural producers and bona fide hedgers. For that reason, application of position limits to all non-bona fide hedge participants, as in the proposed rule, is appropriate. This includes application of position limits to swap dealers who previously have enjoyed an exemption from position limits and, consequently, virtually unlimited direct access to futures markets. The Commission rightly proposes that non-bona fide swap participants will qualify for hedge exemptions only to the extent the transaction involves a bona fide hedger as counterparty, a position strongly supported by the NGFA. The Commission will need to be vigilant in enforcing its account ownership and control procedures to ensure that non-bona fide investment and other financial entities do not act in ways that circumvent the intent of the rule.

Position Limit Parity

Traditionally, the industry, the Commission and the commodity futures exchanges have advocated parity in position limits across the exchanges that offer enumerated agricultural futures contracts. For example, the position limits for wheat currently are identical for the Kansas City Board of Trade, the Chicago Board of Trade and the Minneapolis Grain Exchange. We believe that parity needs to be maintained and serves as additional justification for adopting legacy position limits for the spot month and all-months-combined.

Clearly, basing position limits on open interest levels or deliverable supplies inherently would lead to widely varying levels. Further, establishing disparate position limits could have unintended and deleterious effects in terms of competition among exchanges for growth and liquidity; impacts on risk management strategies across exchanges in terms of intermarket spreading or arbitrage opportunities; and potentially harmful disparate concentrations of non-commercial open interest that could impede contract performance. Position limit parity across exchanges would help avoid these pitfalls, and we believe legacy limits are the appropriate level to enhance performance and avoid inequities.

Bona Fide Hedging

Various types of firms in the grain, feed and processing industry utilize a wide range of hedging and risk management strategies to manage a broad and diverse portfolio of risk. The NGFA urges the Commission not to take the overly narrow or simplistic approach of covering only “hedge and hold” strategies. Doing so could introduce a lack of clarity for many bona fide hedgers managing physical commodity risk.

In proposed Section 151.5(a)(2)(C), a literal reading could indicate that operators of commodity handling and merchandising assets not engaged in “...processing, manufacturing, or feeding...” might not be able to hedge their risk with spreads. For example, a grain elevator, which may be engaged in handling and transporting commodity, without processing, manufacturing or feeding that commodity, may not be afforded that opportunity. Often, the elevator’s economic hedging requirements are the same as those of a processor. We urge the Commission to clarify that the same bona fide hedging treatment will exist for such physical commodity merchants.

Filing for Hedge Exemption

In Section 151.5(i), the Commission proposes to establish a new requirement that bona fide hedgers file a report with the CFTC every day they enter into or maintain a position in excess of position limits. This report would take the place of an annual submission by bona fide hedgers to the relevant commodity exchange. If adopted, this would have the practical effect of increasing the frequency of filing for a hedge exemption by 365 times!

The NGFA urges the Commission to take into account that participants subject to this proposed requirement are not large financial entities that pose systemic risk – nor are they

investors or speculators that merit added oversight by the Commission. Rather, they are bona fide hedgers managing physical commodity risk.

Certainly, one of the reasons Congress passed the Dodd-Frank law was to strengthen oversight and help ensure that another financial crisis is averted. However, Congress also recognized that imposing overly restrictive reporting, recordkeeping, clearing and other requirements on bona fide hedgers and end-users would serve only to increase costs on the system and ultimately to consumers.

Without additional justification, we are unable to see why such a huge increase in reporting for bona fide hedgers is merited. Therefore, we respectfully urge the Commission in its final rule to revert back to a system that has worked well; that is, annual submissions to the exchange as application for hedge exemptions.

Reporting of Cash Positions

Similarly, in Section 151.10, the Commission proposes reporting requirements under its position visibility regulations. Under this proposal, bona fide hedgers that are hedging physical commodity risk would be required to file reports of their cash positions every day they carry a position in excess of position limits. These reports currently are required on a monthly basis. Again, we can see no justification for increasing the reporting frequency and the related cost burdens that such daily reporting would impose on bona fide hedgers. The NGFA urges that the Commission in its final rule retain the current monthly reporting requirement.

Deliverable Supply Estimate

Even though the NGFA supports adoption of CFTC-proposed legacy limits, there is one additional issue we would like to address concerning the use of deliverable supply estimates to facilitate annual calculations of spot-month position limits. The proposed rule stipulates that supply that is committed to long-term agreements would not be available to fulfill delivery obligations and, therefore, would not be included in an estimate of deliverable supply. For the enumerated agricultural commodities, this is not necessarily the case.

A long-term commitment does not imply that grains and oilseeds are committed forever and at any price. Often, such agreements are renegotiated or commodity is bought back for delivery, sometimes during expiration in the spot month. Especially now that shipping certificates generally have been adopted as the delivery mechanism for grains and oilseeds, such supplies regularly are available to the market. For these reasons, we would recommend to the Commission that supplies of enumerated commodities committed to long-term agreements not be excluded from deliverable supply estimates.

Conclusion

The NGFA deeply appreciates the work of the Commission and the opportunity to comment on the proposed rule. We would be happy to provide any additional information that

might be helpful to the Commission as it considers the above comments and other input on the rule.

Sincerely,

A handwritten signature in black ink that reads "Matt Bruns". The signature is written in a cursive style with a large, sweeping initial "M" and a distinct, sharp hook at the end of the name.

Matt Bruns, Chair
Risk Management Committee