



April 1, 2011

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

Re: Commodity Options and Agricultural Swaps, RIN 3038-AD21

Dear Mr. Stawick:

The Futures Industry Association (the “FIA”)<sup>1</sup> and the International Swaps and Derivatives Association, Inc. (“ISDA”)<sup>2</sup> submit these comments in response to the proposed rule on Commodity Options and Agricultural Swaps (the “Proposed Rule”)<sup>3</sup>, in which the Commodity Futures Trading Commission (the “CFTC”) solicited comments on the regulation of commodity options and agricultural swaps under Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”). FIA and ISDA appreciate the opportunity to provide their comments on the Proposed Rule, building on FIA’s and ISDA’s respective October 2010 comment letters to the advanced notice of proposed rulemaking regarding agricultural swaps<sup>4</sup> (the “ANPR Comment Letters”). We are pleased that, if enacted,

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<sup>1</sup> FIA is a principal spokesman for the commodity futures and options industry. FIA’s regular membership is comprised of approximately 30 of the largest futures commission merchants (“FCMs”) in the United States. Among its associate members are representatives from virtually all other segments of the futures industry, both national and international. Reflecting the scope and diversity of its membership, FIA estimates that its members effect more than eighty percent of all customer transactions executed on United States designated contract markets.

<sup>2</sup> ISDA, which represents participants in all aspects of the derivatives industry, is among the world’s largest global financial trade associations as measured by the number of member firms. ISDA was chartered in 1985, and today has over 800 member institutions from 54 countries on six continents. These members include most of the world’s major institutions that deal in privately negotiated derivatives, as well as many of the manufacturers, governmental entities and other commercial interests that rely on listed and over-the-counter derivatives to manage efficiently the financial market risks inherent in their core economic activities. Information about ISDA and its activities is available on the Association’s web site: [www.isda.org](http://www.isda.org).

<sup>3</sup> Commodity Options and Agricultural Swaps, 76 Fed. Reg. 6095 (Feb. 3, 2011).

<sup>4</sup> Agricultural Swaps, 75 Fed. Reg. 59670 (Sept. 28, 2010).

the Proposed Rule would revise existing CFTC regulations in order to treat agricultural commodity swaps as “swaps,” subjecting them to the same regulatory regime as all other commodity swap transactions under Dodd-Frank.<sup>5</sup>

### Agricultural Swaps

If enacted, the Proposed Rule, adopted pursuant to Section 4(c) of the CEA, will permit swap transactions in agricultural commodities, subject to all provisions of the CEA, and any rule, regulation, or order applicable to all other swaps. According to the proposing release to the Proposed Rule (the “Release”), the intention of the proposed new Part 35 is to remove any need for distinguishing between an agricultural commodity and a non-agricultural commodity for the purpose of identifying the law applicable to a swap transaction.<sup>6</sup> The Release states that “permitting agricultural swaps to trade under the same terms and conditions as other swaps should provide greater certainty and stability to existing and emerging markets so that financial innovation and market development can proceed in an effective and competitive manner. Treating all swaps, including agricultural swaps, in a consistent manner should provide greater certainty to markets.”<sup>7</sup> The Release also notes that the vast majority of commenters to the ANPR supported the equal treatment of agricultural swaps (including trade options) under the same regulatory scheme as other categories of swaps.<sup>8</sup>

As stated in the ANPR Comment Letters, we firmly agree with these conclusions. Agricultural swaps are important hedging and risk management vehicles for a wide variety of agricultural entities, including farmers, processors, manufacturers, storage facilities and distributors and these entities have long depended on agricultural swaps to meet their hedging needs. The markets for these instruments have become highly developed and efficient and have functioned without significant problems. In addition, agricultural products are not limited to U.S. markets and exchanges. They are widely sold and traded by U.S. and non-U.S. market participants in a global commodity marketplace. We do not believe that more stringent restrictions are needed with respect to such instruments relative to other categories of swaps.

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<sup>5</sup> The ANPR Comment Letters urged the CFTC to confirm that all agricultural swaps (including options on agricultural commodities) would be within the definition of “swaps” for purposes of the Commodity Exchange Act, as amended by Dodd-Frank (the “CEA”). The ANPR Comment Letters also encouraged the CFTC to not impose additional capital or financial requirements on agricultural swaps or agricultural options that are not imposed on other commodity swap transactions.

<sup>6</sup> However, we question the need for proposed Part 35, if agricultural swaps are to be treated as other swaps. We believe that it might be more efficient and provide greater regulatory certainty to eliminate the proposed Part 35.

<sup>7</sup> 76 Fed. Reg. 6103.

<sup>8</sup> 76 Fed. Reg. 6099.

As a general matter, the Release requests comment on whether agricultural commodities swaps should be subject to the same legal requirements as swaps in other commodities. As stated in the ANPR Comment Letters, we continue to strongly believe that agricultural commodities swaps should be subject to the same legal requirements as swaps in other commodities. In addition, the Release queries whether reducing systemic risk and increasing innovation and competition by permitting agricultural swaps to trade under the same terms and conditions as other swaps would be consistent with Section 4(c)(2) of the CEA,<sup>9</sup> the general purposes of the CEA, and the public interest. For the reasons discussed above, we believe that it would be consistent with the general purposes of the CEA, and the public interest to permit agricultural swaps to trade under the same terms and conditions as other swaps.

### Agricultural Options

In addition, if enacted, the new part 32 of CFTC regulations would no longer require market participants to distinguish between a trade option (under existing CFTC Regulation § 32.4) and an agricultural trade option (existing CFTC Regulation § 32.13) for the purpose of identifying the law applicable to a particular transaction. Rather, all agricultural option transactions (except for options on a future) will be subject to the same laws and rules as any other commodity option transactions.<sup>10</sup>

As noted in the ANPR Comment Letters, we recommended that agricultural options be regulated in the same manner as options on other types of commodities, for the reasons noted above. We believe that options are an important and essential component of the hedging vehicles that should be available to any commercial entities that qualify as eligible contract participants (“ECPs”), as well as to non-ECPs. Options are a more efficient manner to accomplish certain hedging objectives that cannot be satisfied by swaps and we believe that all market participants should have access to options; and we believe that the regulatory regime that will be applicable to all market participants under Dodd-Frank should be more than sufficient to protect market participants entering into agricultural options. Therefore, we agree that the CFTC should treat options on agricultural commodities in the same manner as options on other

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<sup>9</sup> Section 4(c)(2) of the CEA provides that the Commission may grant exemptions only when it determines that the requirements for which an exemption is being provided should not be applied to the agreements, contracts or transactions at issue; that the exemption is consistent with the public interest and the purposes of the CEA; that the agreements, contracts or transactions will be entered into solely between appropriate persons; and that the exemption will not have a material adverse effect on the ability of the Commission or Commission-regulated markets to discharge their regulatory or self-regulatory responsibilities under the CEA.

<sup>10</sup> In doing so, the Proposed Rule would eliminate CFTC Regulations § 32.12 and § 32.13. We believe this would be appropriate. As noted by the Release, the dealer option business has not existed since the early 1990s and only one market participant registered as an Agricultural Trade Option Merchant, and they subsequently withdrew their registration.

commodities and not subject parties entering into agricultural swaps to greater capital requirements than parties to other types of swaps.

Commodity Options and Forward Contracts

The Release raises two additional issues, which as the Release notes are beyond the scope of the Proposed Rule. While we briefly raise these points in this comment letter, FIA and ISDA will address these issues in the appropriate rulemakings. First, we believe that the CFTC should defer any final rulemaking on whether agricultural options should be treated as swaps to the joint proposed rulemaking with the Securities and Exchange Commission to further define the term “swap.” This new rulemaking is the proper place to address whether physical commodity options of any kind, including agricultural commodity options, should be treated as swaps. Second, the Release notes that commenters to the ANPR requested that certain types of transactions (embedded options in forward contracts and book-outs) fall within the definition of an excluded forward contract rather than the definition of a “swap.” We agree and, consistent with comments we have made in the past, we will seek confirmation that the CFTC will continue to endorse the treatment of these transactions as forward contracts.<sup>11</sup>

We appreciate the opportunity to comment on the Proposed Rule, and would be pleased to discuss any questions either regulator may have with respect to this letter.

Very truly yours,



John M. Damgard  
President, FIA



Robert Pickel  
Executive Vice President, ISDA

Cc: Gary Gensler, Chairman  
Michael Dunn, Commissioner  
Jill Sommers, Commissioner  
Bart Chilton, Commissioner  
Scott O’Malia, Commissioner  
Donald Heitman, Senior Special Counsel  
Ryne Miller, Attorney Advisor

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<sup>11</sup> This result would be consistent with longstanding Commission interpretation. See Interpretative Statement on Characteristics Distinguishing Cash and Forward Contracts and “Trade” Options, 50 Fed. Reg. 39656 (Sept. 30, 1985).

### Questions from Release

1. Generally, will the rule changes and amendments proposed herein provide an appropriate regulatory framework for the transacting of (a) agricultural swaps, and (b) trade options on all commodities?

FIA and ISDA believe that the Proposed Rule will provide an appropriate regulatory regime for agricultural swaps. As stated above, FIA and ISDA do not believe that options on physical commodities should be treated as “swaps.”

2. Does the proposal for new part 35 appropriately address all outstanding issues as they relate to the transaction of swaps in an agricultural commodity?

Yes. However, if agricultural swaps are to be treated as other swaps, it might be more efficient and provide greater regulatory certainty to eliminate the proposed Part 35.

3. Regarding the proposed revisions to part 32, and specifically the revised § 32.4 trade option exemption, will such revisions significantly affect hedging opportunities available to currently active users of the trade options market? In other words, is there any reason not to revise § 32.4 as proposed? In particular, are there persons who offer to purchase trade options on non-enumerated agricultural commodities (e.g., coffee, sugar, cocoa) under current § 32.4 who would not qualify as ECPs and would therefore be ineligible to participate in such options under revised § 32.4? If so, should such participants be excepted from the general requirement that all swaps participants must be ECPs unless the transaction takes place on a DCM?

Yes. FIA and ISDA believe that the CFTC should revise CFTC Regulation § 32.4 to ensure that all market participants, even those who do not qualify as ECPs, are permitted to enter into trade options. As discussed above, we believe that options are critically important products that allow market participants to accomplish certain hedging objectives that cannot be satisfied by swaps. In addition, we believe that non-ECPs should also be permitted to enter into a transaction that takes place on a DCM or swap execution facility.

4. Regarding the proposed withdrawal of § 32.12 in its entirety, would such action (in conjunction with the adoption of the new rules proposed herein) prejudice or otherwise harm any person, group of persons, or class of transactions? In other words, is there any reason not to withdraw § 32.12 as proposed?

FIA and ISDA believe that the CFTC should withdraw CFTC Regulation § 32.12. As the Release noted, the dealer option business has not existed since the early 1990s.

5. Similarly, and regarding the proposed withdrawal of § 32.13 (the agricultural trade option provision) in its entirety, would such action (in conjunction with the adoption of the new rules proposed herein) prejudice or otherwise harm any person, group of persons, or class of transactions? In other words, is there any reason not to withdraw § 32.13 as proposed?

The CFTC should withdraw CFTC Regulation § 32.13. As the Release noted, only one market participant registered as an Agricultural Trade Option Merchant, and they subsequently withdrew their registration.

6. Do the proposals as they relate to part 33 appropriately limit the scope of part 33 to DCM-traded options on futures, leaving DCM-traded options on physical commodities subject to part 32?

Yes.

7. Do the proposals outlined herein omit or fail to appropriately consider any other areas of concern regarding agricultural swaps and options in any commodity?

No, but FIA and ISDA believe that the CFTC should not impose higher capital and margin requirements on agricultural swaps than for swaps on other physical commodities.