February 10, 2014

Ms. Melissa D. Jurgens
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Via Online Submission

SUBJECT: RIN 3038-AD99 Position Limits for Derivatives

Dear Secretary Jurgens:

The Minneapolis Grain Exchange, Inc. ("MGEX" or "Exchange") would like to thank the Commodity Futures Trading Commission ("CFTC" or "Commission") for the opportunity to respond to the Commission's request for comment on the above referenced Notice of Proposed Rulemaking entitled "Position Limits for Derivatives" published in the December 12, 2013 Federal Register Vol. 78, No. 239 ("Proposed Rule").

MGEX is both a Designated Contract Market ("DCM") and a Derivatives Clearing Organization ("DCO") and appreciates the continued efforts the Commission has put forth to address the requirements placed upon it by Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act").

<u>Spot-Month Wheat Contract Position Limits</u>

Since its inception in 1881, MGEX has been the principle market for Hard Red Spring Wheat ("HRSW"). Millers, exporters, elevators, farmers and speculators look to MGEX when they trade HRSW wheat via the cash market, futures and options. Upon review of the Proposed Rule, MGEX has several concerns, particularly with regard to the new and different position limits among the three domestic wheat contracts: MGEX HRSW, the Kansas City Board of Trade Hard Red Winter Wheat ("HRW") and the Chicago Board of Trade Soft Red Winter Wheat ("SRW").

Currently, all three domestic wheat contracts are treated equally as to position limits, with the same spot-month limit of 600 contracts and the same single/all months combined limit of 12,000 contracts. Under the Proposed Rule, however, the current spot-month speculative limit of 600 contracts could drop as a result of lower stocks at delivery locations, if based upon estimates using prior period inventories which may not represent future activity. Furthermore, estimates based on anticipated production or inventory are going to be just that, estimates. Inventory is based upon many factors besides domestic production, including world supply and demand, logistics, tariffs, prices and competition. Therefore, the greatest latitude possible must be provided to DCMs to establish and modify spot-month limits. The current maximum of 600 contracts should not be lowered based upon assumptions of circumstances that could quickly change, but rather upon real

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situations and when the DCM itself determines necessary to prevent potential market disruption. If such determinations are made and the DCM believes the spot month limits should be lowered, it should be permitted to implement the reduction even if the current or future delivery month has open interest.

MGEX strongly urges the Commission to consider that it is the DCMs that are in the best position to monitor and appropriately adjust (lower) these limits. Therefore, MGEX supports changing the spot-month limit only when there is actual evidence of the need to do so. However, should the CFTC proceed with the adoption of the Proposed Rule as it is currently written, MGEX hopes and expects the CFTC to give great deference to a DCMs estimate of deliverable supply and the methodology used to arrive at that number.

Non-Spot Month Wheat Contract Position Limits

Of greatest concern to MGEX is that the current non-spot month MGEX HRSW speculative limit of 12,000 contracts would decrease a staggering **72.5%** to just **3,300** contracts, while the HRW limit would decrease to 6,500 contracts, and the SRW limit would actually increase to 16,200 contracts. Based on the examples in the Proposed Rule, this would result in different position limits for all three wheat contracts which will impede growth and limit the potential for the use of risk management strategies between the wheat markets. Furthermore, these numbers derive from 2011 and 2012 data which becomes less relevant each passing day.

Wheat market participants have long appreciated the position limit parity among the three wheat contract markets, particularly as it relates to non-spot months. This parity approach has been followed by the three wheat contract markets since 1938 and has also been followed by the CFTC since its inception. Having the same limits makes the legitimate risk management tools of cross-hedging and spread trading possible and easy to monitor. In the case of wheat, this is particularly critical given the nature of the three wheat varieties. Having three varieties not only provides additional opportunities for cross-hedging and spread trading as mentioned above, but also allows for hedging and trading strategies between markets in response to economic factors that could result in varying impacts on the differing varieties of wheat.

The value and certainty that parity presents to the marketplace has resulted in historically effective and efficient markets for all wheat contracts. If position limits are set at different levels for each of the three wheat contracts, price volatility or concentration in one contract may unduly affect the price of the others. Additionally, without parity among the wheat contracts, inequities will be introduced into the marketplace which could result in market distortion and arbitrage.

In the absence of any evidence over the last 75 years that parity among the three wheat contract markets is not working or harms users, there is absolutely no need to change this practice. Rather, a practice that has worked efficiently and effectively for so many years should be applauded and retained. As such, MGEX strongly urges the Commission to carefully consider these comments and the comments of market participants using wheat futures as a legitimate hedging tool, and to maintain the historically proven, effective and efficient parity of limits among the wheat contract markets.

Formulaic Approach

The proposed formulaic approach of the Proposed Rule in calculating non-spot month position limits is too slow, in that it does not allow for timely adjustment of the limits to account for growth in market activity and open interest. Per the Proposed Rule a DCM can, at best, only adjust on a yearly basis. Market growth can quickly outpace this yearly adjustment timeframe. For example, month end open interest in HRSW futures during calendar year 2013 averaged over 43,000 contracts. As of late, MGEX has experienced dramatic volume and open interest growth; from the end of August 2013 through the end of January 2014, HRSW futures open interest has increased

from 32,355 to 69,000 contracts. This is a more than **113%** increase. The slow, annual application of the formula in the Proposed Rule cannot adjust for this increase in a timely manner, which is unacceptable.

Both the 10% baseline and the 2.5% increase of the proposed formula fail to adequately account for volume and open interest growth. To further illustrate this point, a doubling of open interest from 35,000 to 70,000 contracts would only increase the speculative position limit by 2.5% over 25,000 contracts, or a minimal increase in the limit of just 875 contracts, which is hardly reflective of what may actually be occurring in the marketplace.

Of particular concern for MGEX is that the formulaic approach inhibits growth in HRSW at a time when activity is actually increasing. Limiting growth and participation runs counter to the very principles of price discovery and risk protection. This approach is backwards looking rather than forward thinking, and simply does not allow for growth or participation by liquidity providers in the HRSW market in the same way that it does in the other two wheat markets. This effectively would work to drive activity away from the MGEX wheat market. Establishing position limits based on a formula that does not account for real world situations without strong evidence that reveals a benefit to the market is simply not good policy.

Bona Fide Hedge Definition

Narrowing the current definition and use of a bona fide hedge does not appear to provide the marketplace any better protection from perceived or potential speculation than exists currently. Rather, numerous end users of the physical product may be forced to curtail legitimate futures activity for fear of a potential rule violation, or otherwise be forced to go through the burdensome process of seeking hedge exemptions. In this respect, the Proposed Rule appears discriminatory to end users. The Proposed Rule indicates that a hedger may have to apply to both a DCM and the Commission for exemptions based on the type of hedge they need to employ. This seems an unnecessary recordkeeping burden for the hedger, as well as an inefficient use of resources for the hedger, the DCM and the CFTC. The practical resolution would be to maintain the current definition and create a dual exemption application process.

The futures markets were developed for use by hedgers, and they should not now be forced to endure multiple and more complex hurdles just to continue to use and operate within the futures marketplace as they have done for many years. As such, MGEX strongly encourages the Commission to listen to end users, particularly hedgers, as to their concerns with the Proposed Rule.

Conclusion

MGEX appreciates the work the Commission is doing to properly incorporate and implement the requirements of the Dodd-Frank Act. However, promulgating rules or adjusting long standing market practices without any evidence indicating a need to do so is not sound rulemaking policy. Speculation alone is not an inappropriate or manipulative practice, and is actually necessary in that it provides liquidity in any derivatives market. Furthermore, the formulaic approach used to establish non-spot month position limits will not itself prevent excessive speculation in the marketplace. The formulaic approach of the Proposed Rule is both slow and inadequate in addressing real market growth situations, which supports MGEX' argument that parity among the three wheat contracts must be maintained.

Regards,

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Associate Corporate Counsel