



| asset management group

February 10, 2014
Melissa Jurgens
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington DC 20581

Re: Notice of Proposed Rulemaking – Position Limits for Derivatives (RIN 3038-AD11)

The Asset Management Group (the “AMG”)¹ of the Securities Industry and Financial Markets Association (“SIFMA”) appreciates the opportunity to provide the Commodity Futures Trading Commission (the “CFTC” or the “Commission”) with our comments and recommendations relating to the Commission’s “Position Limits for Derivatives” proposed rules (“2013 NPRM”) promulgated under section 4a of the Commodity Exchange Act (“CEA” or the “Act”), as amended by section 737 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”). The AMG recognizes that regulatory action may be appropriate under certain circumstances in order to achieve the goals set forth in the CEA for setting position limits, namely to prevent market manipulation, protect against excessive speculation, ensure sufficient market liquidity for bona fide hedgers, and deter disruption to price discovery, including preventing price discovery from moving to foreign boards of trade (“FBOTs”), but continues to question whether position limits would achieve these goals, particularly as proposed under the 2013 NPRM.

AMG agrees that the Hunt brothers and Amaranth’s speculative trading should “inform” a consideration of position limits rulemaking, but finds that many aspects of the Commission’s proposal do little to directly address these two actors’ manipulative activities while resulting in serious negative consequences for the commodity markets, AMG members, and our “Main Street” customers. We believe that under the CEA, the Commission must find that speculative position limits are “necessary” and “appropriate” and balance several countervailing statutory factors on a contract-by-contract basis before promulgating position limits rules. The Commission has not met these statutory requirements in promulgating the 2013 NPRM. We believe the Commission should therefore withdraw this proposal to make the needed findings. Nevertheless, if the Commission determines to proceed with the proposal, then it can better effectuate the goals of CEA section 4a by making the following changes:

¹ The AMG’s members represent U.S. asset management firms whose combined assets under management exceed \$20 trillion. The clients of AMG member firms include, among others, registered investment companies, ERISA plans, and state and local government pension funds, many of whom invest in commodity futures, options, and swaps as part of their respective investment strategies.

- modifying the proposed spot-month limits and withdrawing or increasing the non-spot-month position limit levels;
- provide designated contract markets (“DCMs”) and swap execution facilities (“SEFs”) more discretion with respect to aggregation requirements and other rules related to position limits;
- preserving the risk management exemption from speculative positions consistent with the terms of the CEA, as informed by administrative precedent and legislative history;
- granting counterparties to “commodity index contracts” an exemption for managing price risk associated with “commodity index contract” positions;
- exempting registered investment companies and ERISA accounts from speculative position limits; and
- extending grandfather relief to pre-existing positions.

1. *Background on the AMG members’ interest in speculative position limits regulations.*

The AMG’s members represent U.S. asset management firms whose customers include, among others, registered investment companies, private funds, institutional accounts, ERISA plans and state and local government pension funds, many of whom invest in commodity derivatives as part of their investment strategies. Many of the funds and accounts that AMG members manage generally track a commodity index (*e.g.*, the Dow Jones-UBS commodity index). In addition to managing funds that specialize in commodities-related investments, many AMG members manage asset allocation funds that invest in the commodity markets, thereby enabling investors to obtain exposure to an asset class other than equities and bonds within one balanced and diversified portfolio.

Commodities represent a very small portion of assets under management by AMG members. Nevertheless, commodities represent an important asset class to investors. Through these funds and accounts that invest in commodity derivatives, AMG members offer a convenient, well-established mechanism for individuals, pension funds, retirement plans and other investors to diversify their overall investment portfolios with exposure to the commodity markets. Commodity-linked derivatives also allow prudently managed funds and accounts to mitigate economic risk, such as inflation and foreign exchange movements, and increase overall purchasing power.

Accordingly, members of the AMG have a strong interest in the proper functioning of commodity derivatives and commodities markets without undue restriction. The ability of AMG members to provide investor exposure to commodities as an asset class through these funds and accounts will be directly affected by any position limits rules adopted by the Commission. Any rules that are overly restrictive could adversely affect not only AMG members and the “Main Street” investors that invest in the products they manage, but also the U.S. commodity markets generally, potentially impairing price discovery and liquidity, which in turn could result in increased prices for all participants in the commodity derivatives market. In particular, restrictive limits could harm commodity producers and end-users who rely on these funds and accounts to take the other side of risk-reducing trades and provide a stable pool of liquidity. As the Commission determines whether and at what levels to set position limits, the AMG respectfully

submits that it consider the important portfolio diversification mechanism that AMG members provide to investors seeking diversified exposure to commodities, and the adverse impact that position limits may have on AMG members and investors that invest in the products they manage.

2. *The Commission should make findings of necessity and appropriateness of its position limits regime based on a fact-intensive, contract-by-contract analysis.*

The Dodd-Frank Act placed several constraints on the Commission’s exercise of CEA section 4a(a)(2) authority to impose position limits designed to ensure that position limits are imposed only when “necessary” and “appropriate” and that they strike an optimal balance among a series of factors.² With respect to the requirements to impose position limits when they are “necessary” and “appropriate” we refer to, and agree with, the joint International Swaps and Derivatives Association (“ISDA”) and SIFMA comment letter submitted on the 2013 NPRM.³ With respect to the statutory factors, the CEA requires that the Commission address six countervailing factors or goals as it promulgates position limit rules (the “Six Factors”).⁴ The Commission must strive to meet the “goals” of CEA section 4a(a)(2)(C) by “striv[ing] to ensure” that (Factor 1) “trading on foreign boards of trade in the same commodity will be subject to comparable limits” and that (Factor 2) “any limits to be imposed by the Commission will not cause price discovery in the commodity to shift to trading [to FBOTs].”⁵ CEA section 4a(a)(3)(B) directs the Commission to balance four additional factors when exercising its CEA section 4a(a)(2) authority:

- (Factor 3) to diminish, eliminate, or prevent excessive speculation causing sudden or unreasonable fluctuations or unwarranted changes in price;
- (Factor 4) to deter and prevent market manipulation, squeezes, and corners;
- (Factor 5) to ensure sufficient market liquidity for bona fide hedgers; and
- (Factor 6) to ensure that the price discovery function of the underlying market is not disrupted.⁶

In order to establish speculative position limits that address these factors “to the maximum extent practicable,” the Commission would need to consider each commodity

² See also CEA section 4a(a)(1) and *ISDA v. CFTC*, No. 11-cv-2146 at 15 (D.D.C. Sept. 28, 2012), available at http://www.futuresindustry.org/downloads/USDC-DC_Position-Limits-Rule-Injunction_092812.pdf (“The precise question, therefore, is whether the language of Section [4a(a)(1)] clearly and unambiguously requires the Commission to make a finding of necessity prior to imposing position limits. The answer is yes.”).

³ See Letter to CFTC from ISDA and SIFMA Re: Notice of Proposed Rulemaking – Position Limits for Derivatives (RIN 3038-AD99) (Feb. 10, 2014), available at <http://comments.cftc.gov/PublicComments/ViewComment.aspx?id=59611&SearchText=>.

⁴ These Six Factors are separate from any other considerations, including a finding of necessity, required under CEA section 4a(a)(1) or any other consideration included in a finding of appropriateness. The Six Factors provide a purpose for the speculative position limits regime the Commission may impose under CEA section 4a(a)(2).

⁵ CEA section 4a(a)(2)(C).

⁶ CEA section 4a(a)(3)(B).

individually because the calculus required to fully maximize these factors would differ based on characteristics specific to each commodity contract market, as discussed further below.⁷ The requirement to conduct a fact-intensive contract-by-contract analysis of which contracts should be subject to position limits also is supported by administrative precedent.⁸ These factors also apply to rules that affect the efficacy of position limits. We believe the Commission must analyze each exercise of discretion it proposes to undertake in establishing position limits under these Six Factors.

2.1. The AMG agrees that the Hunt brothers and Amaranth’s speculative trading should “inform” a consideration of position limits.

While the 2013 NPRM proposes to issue position limits rules without a finding of necessity, “in an abundance of caution,” it makes a general finding of necessity citing two historic episodes: (1) Hunt brothers (1979-1980) and (2) Amaranth (2006). Amaranth and the Hunt brothers shared one important feature in common: both were “pure speculator[s]” that did not have financial or physical exposures that offset the risk exposures created by their extremely large natural gas or silver derivatives positions (respectively). The Commission claims that these two firms’ speculative trading “inform” the Commission’s proposal.¹⁰

⁷ We note that in our interpretation of CEA section 4a(a)(2)’s “as appropriate” language, the Commission must make a fact-driven interpretation that position limits are appropriate and, if so, that the limits it has selected are also appropriate, regardless of whether the Commission must make a finding of necessity before establishing position limits.

⁸ In the 2013 NPRM, the Commission cites a rulemaking from 1981 (“1981 Rulemaking”) as supporting its assertion that the Commission only has “to determine that excessive speculation is harmful to the market and that limits on speculative positions are a reasonable means of preventing price disruptions in the marketplace that place an undue burden on interstate commerce” to meet the requirements of CEA section 4a(a)(1). 78 Fed. Reg. at 75,683 at fn. 34, *citing* 46 Fed. Reg. at 50,940. The 2013 NPRM ignores, however, that the 1981 Rulemaking imposed speculative position limits only after a fact-intensive inquiry into the characteristics of individual contract markets in order to determine limits “most appropriate” for “an individual contract market.” 46 Fed. Reg. at 50,940 (“[CEA section 4a] represents an express Congressional finding that excessive speculation is harmful to the market, and a finding that speculative limits are an effective prophylactic measure.” Consistent with this, the Commission promulgated rules directing DCMs to “employ their knowledge of their individual contract markets to propose the position limits they believe most appropriate.”). In other words, DCMs’ deployment of “knowledge” of an “individual contract market” allowed DCMs to implement position limits “most appropriate” for that market. Furthermore, in the 1981 Rulemaking, the Commission found that specific speculative position limits designed to combat excessive speculation should be carefully calibrated so as not to “interfere with normal trading patterns or significantly impact market liquidity or pricing efficiency... [or] cause [the preponderance] of speculative traders to conduct their trading in a foreign futures market.” 46 Fed. Reg. at 50,940-50,941 (“The Commission is aware that speculation is often an important contributing factor to market liquidity and pricing efficiency. [...] In this respect, the Commission indicated that in its review of proposed [DCM] speculative limits, it will consider the historical distributions of speculative positions considering, among other things, recent trends in position patterns, the frequency of positions occurring at different levels and the levels at which occur the preponderance of speculative positions normally observed in the market.”).

⁹ *Id.* at 75,692 at note 103 (“Amaranth was a pure speculator that, for example, could neither make nor take delivery of physical natural gas.”). “The Hunt brothers were speculators who neither produced, distributed, processed nor consumed silver.” *Id.* at 75,686.

¹⁰ *Id.* at 75,685.

The Hunt brothers exemplify two forms of manipulation: cornering a physical market to benefit a large leveraged derivatives position and the short squeeze.¹¹ Amaranth is an example of “banging the close” manipulation¹² coupled with “excessive speculation” in the form of large calendar spread speculative positions that, at times, amounted to as much as 40% of all of the open interest on the New York Mercantile Exchange (“NYMEX”) for the winter months (October 2006 through March 2007).¹³

We agree that these two firms’ abusive trading could be instructive and provide commenters the ability to compare the Commission’s proposal with actual undesirable trading activity (as opposed to theoretical harms addressed by “prophylactic” limits). However, when we compare Amaranth or the Hunt brothers’ trading to the 2013 NPRM’s provisions, we find that many key aspects of the proposal go far beyond preventing such market abuse while imposing significant, real harm to the commodity and commodity derivatives markets and market participants. This harm is precisely what Congress sought to avoid in requiring the Commission to make a finding of appropriateness in support of position limits, including careful consideration of the Six Factors for each contract subject to position limits. We note, finally, that neither Amaranth nor the Hunt brothers were subject to an existing regulatory regime that aligned their incentives with investors, limited their leverage, required them to diversify their holdings, and required them to provide their investors transparency.

2.2. The Commission already has the power to address the purposes of CEA section 4a without a restrictive position limits regime.

The Commission’s exercise of its CEA section 4a authority to impose “necessary” and “appropriate” speculative position limits should take into account its ability to prevent excessive speculation and manipulation in the absence of new speculative position limits. Concerns regarding manipulation and excessive speculation are already addressed through DCMs’ and SEFs’ position limits and accountability rules.¹⁴ DCMs’ (or SEFs’) position accountability rules can prevent manipulative or potentially manipulative conduct, or “excessive speculation,” far before a position limit is reached while not imposing unneeded constraints on large positions that

¹¹ “Position limits would help to deter and prevent manipulative corners and squeezes, such as the silver price spike caused by the Hunt brothers and their cohorts in 1979–80.” 78 Fed. Reg. at 75,683. The Commission defined both manipulative corners and squeezes: “A market is ‘cornered’ when an individual or group of individuals acting in concert acquire a controlling or ownership interest in a commodity that is so dominant that the individual or group of individuals can set or manipulate the price of that commodity. In a short squeeze, an excess of demand for a commodity together with a lack of supply for that commodity forces the price of that commodity upward.” *Id.* at 75,685.

¹² *CFTC v. Amaranth*, Complaint for Injunctive and Other Equitable Relief under the Commodity Exchange Act, CA 07-CIV-6682, July 25, 2007, available at <http://www.cftc.gov/ucm/groups/public/@lrenforcementactions/documents/legalpleading/enfamaranthcomplaint072507.pdf>.

¹³ Excessive Speculation in the Natural Gas Market, Staff Report, Permanent Subcommittee on Investigations of the Senate Committee on Homeland Security and Governmental Affairs, U.S. Senate, at 6 and 51-52 (June 25, 2007), available at <http://www.levin.senate.gov/imo/media/doc/supporting/2007/PSI.Amaranth.063507.pdf> (“Amaranth Report”).

¹⁴ *Speculative Position Limits-Exemptions From Commission Rule 1.61; Comex Proposed Amendments to Rules 4.47 and 4.48*, 57 Fed. Reg. 29,064, 29,065-29,066 (June 30, 1992). See also e.g., CME Rulebook, Rule 560, available at <http://www.cmegroup.com/rulebook/CME/I/5/5.pdf>.

pose no risk.¹⁵ Violations of these position limits are violations of federal law under CEA section 4a(e). The Commission also has surveillance capabilities (e.g., large futures and swaps trading reports,¹⁶ swap data reporting and recordkeeping requirements,¹⁷ “special call” authority,¹⁸ etc.) that provide it granular visibility into the commodity derivatives and cash market activities (upon special call) of all market participants to prevent manipulation and detect excessive speculation. This increased visibility is augmented by automated surveillance systems,¹⁹ the Commission’s emergency powers under CEA section 8a(9), new Dodd-Frank anti-manipulation and disruptive trade practices authority,²⁰ and the Commission’s whistleblower program – all of which vastly increase the probability of detecting, preventing, and taking effective action against manipulative or potentially disruptive speculative activity.

3. Comments on specific aspects of the Commission’s proposal

If, notwithstanding our comments above, the Commission adopts speculative position limits, then it should make significant changes to the rulemaking in order to better address the CEA’s Six Factors. Below, we provide comments aimed at achieving the goals embodied in CEA section 4a in light of Amaranth and the Hunt brothers. Our suggestions, if implemented, form an alternative to the Commission’s proposal that would be less costly in terms of compliance costs, result in less negative consequences on liquidity and price discovery, and provide the same benefit in terms of reduced likelihood for excessive speculation and manipulation.

3.1. The proposed spot-month position limits are inappropriate because they fail to take into account the characteristics of each contract and should therefore be withdrawn or significantly altered.

3.1.1. The Commission’s spot-month limit formula is arbitrary and the Commission should adopt an approach that takes into account the characteristics of each commodity market or defer to DCMs and their knowledge of individual markets to determine appropriate spot-month position limit levels.

¹⁵ See e.g., CBOT Rulebook, Rule 560, available at <http://www.cmegroup.com/rulebook/CBOT/I/5/5.pdf>.

¹⁶ See 17 CFR parts 15, 16, 17, 18, and 20.

¹⁷ See 17 CFR part 45.

¹⁸ See e.g., 17 CFR 18.05 and 17 CFR 20.6.

¹⁹ See CFTC Market Surveillance Program, <http://www.cftc.gov/IndustryOversight/MarketSurveillance/CFTCMarketSurveillanceProgram/tradepacticesurveillance> (last visited Jan. 26, 2013) (“Trade violation detection software will perform sophisticated pattern recognition and data mining to automate basic trade practice surveillance. Among other things, TSS will provide Commission staff with the necessary tools to conduct inter-exchange and cross border surveillance of related contracts; to detect novel and complex abusive practices in today’s high-speed, high volume global trading environment; and to perform timely and customized analyses of all trading activity as well as complex, value-added surveillance in significant cases.”).

²⁰ See CEA section 4c.

The Commission proposes to set spot-month position limits at 25% of estimated deliverable supply under proposed 150.2(e)(3). If a commodity market has consistently liquid cash markets, greater storage capacity, and more reliable supply, it would be unlikely to be subject to a short squeeze or susceptible to cornering, even with position limits set at higher than 25% of estimated deliverable supply.²¹ We encourage the Commission to provide a means by which more appropriate spot-month position limit levels may be established. We therefore recommend the Commission either adopt an approach that takes into account the characteristics of each commodity market or, consistent with the terms of CEA section 4a and administrative precedent, that the Commission defer to DCMs and their knowledge of individual markets to determine appropriate spot-month position limit levels.

3.1.2. The Commission’s spot-month limit determination process should be explained further in order to avoid arbitrary and potentially harmful outcomes.

Under proposed 150.2(e)(3), DCMs listing physical-delivery referenced contracts would be required to submit, every two years, estimates of deliverable supply. The Commission indicates that it will defer to DCMs’ estimate of deliverable supply unless it “determines to rely on its own estimate.”²² The Commission gives no indication as to when or under what standard it will determine to “rely on its own estimate,” leaving open the possibility of arbitrary determinations that could be harmful to the markets. We recommend the Commission provide specific criteria both for when it determines not to rely on the DCMs’ estimate and as to how it will formulate its own estimates of deliverable supply in such circumstances. We also recommend that the Commission estimates be subject to notice and comment.

3.1.3. Market participants should be permitted to net their cash-settled and physically-settled positions in a spot month in order to accurately reflect their aggregate spot-month positions.

Under proposed 150.2(a), the Commission proposes separate federal physical-delivery spot-month position limits and aggregate cash-settled position limits. The Commission has not demonstrated that these separate limits are necessary. We understand one motivation behind this proposal is a theoretical concern that a market participant could establish an unrestricted long position in the physical-delivery contract held through the end of the spot month resulting in a delivery obligation for its counterparties that is offset with a cash-settled position. Market discipline is generally sufficient to deter such trading behavior. While maintaining the long physical-delivery position could be used to effect a short squeeze, the trader in this scenario would not benefit from any price spike caused by a short squeeze – indeed, their short positions would result in substantial losses. More importantly, the danger to market integrity under this scenario is adequately addressed by DCMs’ and futures commission merchants’ rules and by procedures designed to ensure that market participants that hold a long or short position into a

²¹ See 17 CFR 1.61(a)(2)(1991).

²² 78 Fed. Reg. at 75,728; proposed 150.2(a)(3)(i).

delivery period actually have the ability to take or make delivery.²³ Conversely, allowing market participants to net physically-settled and cash-settled contracts would more accurately reflect net positions. We see no reason why such netting should not be permitted.

3.2. The Commission’s non-spot-month limit formula is arbitrary and the Commission should adopt an approach that takes into account the characteristics of each commodity market or defer to DCMs and their knowledge of individual markets to determine appropriate non-spot-month position limit levels.

The Commission proposes under 150.2(e)(4) to use the same formula (“open interest formula”) regardless of the characteristics of the market.²⁴ The Commission first proposed the open interest formula in 1992 for “legacy” agricultural commodities subject to federal speculative position limits.²⁵ Because the Commission has not undertaken an analysis of the individual referenced contract commodity markets, its proposed non-spot-month position limits would be inappropriate for all referenced contracts. In the same 1992 rulemaking the Commission stated that the “fundamental tenet in the Commission’s setting of speculative position limits is that such limits must ‘be based upon the individual characteristics of a specific contract market.’”²⁶ The Commission also noted that “the limits which are appropriate for certain types of commodities, such as agricultural commodities, may [not] be appropriate for other tangible or intangible commodities.”²⁷ The Commission suggested different limits might be appropriate for non-agricultural commodities because of the “depth of the underlying cash market and ease of arbitrage [that] differ from agricultural markets.”²⁸ For example, with respect to energy and metals commodities, the Commission found in 1992 that because these commodities generally exhibited “a high degree of liquidity,” position accountability rules – rather than limits - would be adequate to address concerns relating to excessive speculation.²⁹

Notwithstanding these countervailing considerations, the Commission now proposes to apply the same open interest formula to all 28 referenced contract commodities. It is unclear how the misgivings the Commission had in 1992 have been overcome. If anything, the agricultural markets now resemble the energy and metals markets of 1992 in terms of greater liquidity, which would provide support for a less restrictive formula under Commission

²³ See e.g., NYMEX Rulebook, Rule 716, available at <http://www.cmegroup.com/rulebook/NYMEX/1/7.pdf> (“each clearing member shall be responsible for assessing the account owner’s ability to make or take delivery for each account on its books with open positions in the expiring contract. Absent satisfactory information from the account owner, the clearing member is responsible for ensuring that the open positions are liquidated in an orderly manner prior to the expiration of trading.”).

²⁴ The formula would set single-month and all-months position limits at 10% of open interest for the first 25,000 contracts in a referenced contract market and 2.5% thereafter. Proposed 150.2(e)(4).

²⁵ See Revision of Federal Speculative Position Limits, Proposed Rules, 57 Fed. Reg. 12,766 (Apr. 13, 1992).

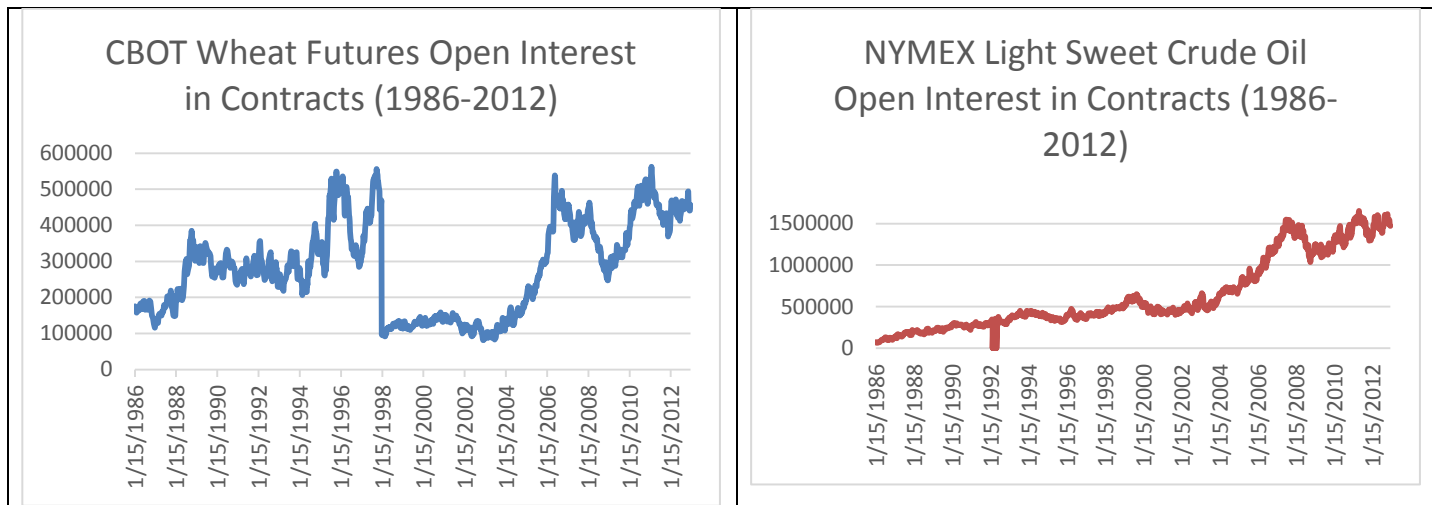
²⁶ *Id.* at 12,770, citing 52 Fed. Reg. at 6,815.

²⁷ *Id.*

²⁸ *Id.* at n. 14.

²⁹ 57 Fed. Reg. at 29,065-29,066 (June 30, 1992) (also finding that speculative position limits are not necessary in commodities that “have substantial forward markets that readily are arbitrated with the futures of [sic] option markets.”).

administrative precedent. Take, for example, the following levels of open interest (indicative of liquidity) in the CBOT Wheat and NYMEX Light Sweet Crude Oil futures contracts:³⁰



We note further that the Commission’s proposed non-spot-month position limit formula results in a disparate impact that demonstrates this formula is wholly inappropriate. The limits the Commission is proposing would have widely different effects on different commodities. For example, Table 11 to the 2013 NPRM shows that in COMEX Copper referenced contracts, 16 unique enterprises would have been over the Commission’s speculative position limit levels in 2011-2012. In contrast, in many other referenced contract markets, the number of overages is few. Is this because there is more “excessive speculation” in COMEX Copper than in NYMEX Henry Hub Natural Gas, for example (which Table 11 describes as having zero non-spot-month overages)? It does not attempt to explain that there is any rationale behind this disparate impact. The Commission does not explain whether any, all, or some of the overages it has indicated in Table 11 result from speculative positions or from bona fide hedging positions or from a combination of the two. Essentially, what Table 11 indicates is that the impact of the Commission’s non-spot-month position limits is random – demonstrating that the non-spot-month formula and the limits that result from it are entirely arbitrary and have no relationship to preventing excessive speculation or manipulation. If the Commission is to set non-spot-month limits at arbitrary levels, it should do so at very high levels in order to prevent the types of harms unduly restrictive position limits can have, as reflected in the statutory Six Factors.

Finally, the Commission’s proposed non-spot-month position limits do not increase the likelihood of preventing the excessive speculation or manipulative trading exemplified by Amaranth or the Hunt brothers relative to the status quo. We note that the large non-spot-month positions of Amaranth and the Hunt brothers could have been addressed by DCMs and SEFs under position accountability rules.³¹ In the case of Amaranth, NYMEX did, in fact, cap

³⁰ Data taken from the CFTC’s Historical Compressed Commitment of Traders Report, <http://www.cftc.gov/MarketReports/CommitmentsofTraders/HistoricalCompressed/index.htm> (last visited Jan. 26, 2014).

³¹ CEA sections 5(d)(5)(A) and 5h(f)(6)(A) (“To reduce the potential threat of market manipulation or congestion, especially during trading in the delivery month,” a DCM or SEF shall adopt for each contract, “as is necessary and appropriate, position limitations or position accountability for speculators.”).

Amaranth's speculative positions on its exchange. Amaranth responded by taking advantage of a regulatory arbitrage opportunity: "[i]n August 2006, Amaranth traded natural gas on [the then unregulated InterContinental Exchange ("ICE") OTC platform] rather than NYMEX so that it could trade without any restrictions on the size of its positions."³² The Amaranth Report recommended therefore, most pertinently, that: (1) the Congress should give the Commission authority to regulate electronic OTC markets (e.g., ICE at the time)³³ and (2) the Commission "should monitor aggregate positions on NYMEX and ICE for all of the months in which contracts are traded, not just for contracts near expiration."³⁴ This concern from 2006 would not exist under today's rules. Under the Commission's part 37 rules relating to SEFs it now has authority over all multilateral derivatives trading platforms (ICE would have been a SEF) and the Commission's expanded part 20 and its part 45 reporting rules now enable it to monitor all futures and swaps positions. Notably, the Amaranth Report did not recommend that the Commission establish non-spot-month position limits for natural gas, the 28 referenced contract commodities, or all physical commodity derivatives.

In order to ensure that the Commission's speculative position limits "to the maximum extent practicable" achieve the goals of CEA section 4a, AMG recommends therefore that the Commission take one of three non-exclusive actions: (1) decline to adopt non-spot-month position limits; (2) set non-spot month limits at levels where they are unlikely to affect any persons until the Commission is able to develop a factual record to justify restrictive limit levels under the Six Factors and other purposes of CEA section 4a; or (3) re-propose its speculative position limits proposal after utilizing the expertise and resources of DCMs and SEFs to determine "appropriate" non-spot-month position limit levels as the Commission has done traditionally.³⁵

3.3 DCMs and SEFs should be given more discretion to determine appropriate aggregation and other requirements relating to speculative position limits.

The 2013 NPRM proposes to limit the discretion of DCMs and SEFs ("exchanges" collectively) in their administration of speculative position limits in two important ways including:

- (1) under proposed 150.5(a)(5), aggregation requirements must "conform to" those of the Commission under proposed 150.4; and

³² Amaranth Report at 6.

³³ *Id.* at 8.

³⁴ *Id.* Significantly, the Amaranth Report did not recommend changes to the Commission's position limits regime. Its recommendation that the Amaranth problem be addressed, in part, by statutory authority for the Commission to regulate electronic OTC markets was achieved through the enactment in 2008 of the Food, Conservation and Energy Act of 2008, Public Law 110-246, 122 Stat. 1624 (June 18, 2008).

³⁵ In 1981, the Commission finalized rules directing DCMs to "employ their knowledge of their individual contract markets to propose the position limits they believe most appropriate." Establishment of Speculative Position Limits, 46 Fed. Reg. 50,938, 50,940. In other words, DCMs' deployment of "knowledge" of an "individual contract market" enabled DCMs to implement position limits "most appropriate" for that market. *Id.* The Commission also stated that it "endorse[d]" the "concept" that "the exchanges are in the best position to determine the most efficacious level at which position limitations may be established." *Id.* at n. 5. *See also* 17 CFR 1.61(a)(2) (1981).

- (2) under proposed 150.5(a)(2)(i), limiting their discretion to defining the scope of hedge and other exemptions to those that conform to the Commission's definitions.

As discussed above, the Commission has traditionally followed the principle that exchanges have superior knowledge of individual contract markets enabling them to implement position limits and related aggregation requirements and exemptions "most appropriate" for that market.³⁶ Consistent with this principle, we urge the Commission to provide exchanges broader discretion in determining aggregation rules and exemptions, subject to Commission oversight. Providing the exchanges this broader discretion would enable them to more effectively and efficiently further the purposes of CEA section 4a by tailoring these requirements to the individual commodity contract markets. The need for broader exchange discretion is particularly warranted in the non-referenced contracts, including excluded commodities, that the Commission has not considered in any depth in this rulemaking. We note finally that the Commission has not considered the costs borne by exchanges and market participants from the prescriptive approach to exchange-administered position limits, including exchange aggregation notice filing and application requirements conforming to proposed 150.4(c)(1) and (c)(2). For example, under proposed 150.4(c), the Commission would require notice and application filings for market participants seeking an aggregation exemption. The Commission should allow and encourage exchanges to tailor such requests for aggregation relief to the markets they regulate.³⁷

3.4 Bona fide hedging exemption.

3.4.1. The Commission should preserve the risk management exemption.

Commission staff historically provided a bona fide hedging exemption for positions that offset risks related to swaps or similar OTC positions involving both individual commodities and commodity indexes ("risk management exemption").³⁸ These exemptions were subject to specific conditions to protect the market, including: (1) the futures positions must offset specific price risk; (2) the dollar value of the futures positions must be no greater than the dollar value of the underlying risk; and (3) the futures positions must not be carried into the spot month.³⁹

³⁶ In 1981, the Commission finalized rules directing DCMs to "employ their knowledge of their individual contract markets to propose the position limits they believe most appropriate." 46 Fed. Reg. at 50,940. This included aggregation and exemption rules. See 17 CFR 1.61 (1982).

³⁷ AMG is commenting separately on the Commission's aggregation proposal, Aggregation of Positions, 78 Fed. Reg. 68,946 (Nov.15, 2013).

³⁸ "Position Limits and the Hedge Exemption, Brief Legislative History," Testimony of General Counsel Dan M. Berkovitz, Commodity Futures Trading Commission, July 28, 2009, available at <http://www.cftc.gov/PressRoom/SpeechesTestimony/berkovitzstatement072809>.

³⁹ *Id.* See also CFTC Form 40, Part B, Item 3 and Schedule 1 (defining "hedging" as including "asset/liability risk management, security portfolio risk, etc.").

The Commission proposes to eliminate the risk management exemption on the basis of CEA section 4a(c)(2)'s definition of a "bona fide hedging transaction or position" ("statutory definition"), which was added by Dodd-Frank. CEA section 4a(c)(2) was modeled on 17 CFR 1.3(z) ("regulatory definition") with one important difference: the statutory definition of a "bona fide hedging transaction or position" did not include the term "normally" in presenting the "temporary substitute criterion," which provides that a bona fide hedge position should "normally represent[] a substitute for transactions made or to be made or positions taken or to be taken at a later time in a physical marketing channel." (emphasis added) The Commission proposes to interpret this omission as meaning that a bona fide hedging position must represent a "substitute for transactions made or to be made in a physical marketing channel."⁴⁰ In other words, the hedge position is "a temporary substitute for a cash transaction that will occur later."⁴¹

By eliminating the risk management exemption, the Commission's speculative position limits rules would go beyond deterring excessive speculation and manipulation and would have the effect of deterring and constraining liquidity by market participants with non-speculative positions in commodity derivatives – essentially deterring non-speculative, prudent risk management. Commodity funds and asset allocation funds, for example, utilize commodity derivatives in active or passive management strategies in order to provide diversified, commodity-based returns to their clients and to mitigate economic risk. Reduced liquidity would also result in increased prices for all participants in the commodity derivatives market.

We urge the Commission to reconsider eliminating the risk management exemption. A risk management position represents a non-speculative, flat-risk position and should therefore be exempt from speculative position limits. The risk management exemption also encourages the provision of liquidity across financial and physical markets and therefore furthers the goals of promoting liquidity for bona fide hedgers and price discovery. We note that neither Amaranth nor the Hunt brothers used the risk management exemption and therefore its elimination is not warranted if those two actors' trading activity is to provide any guidance to the Commission as to the regulatory changes that it should implement. Indeed, speculative position limits under CEA section 4a are intended to target excessive speculation and manipulation,⁴² and risk management positions present zero risk of either. As discussed below, we do not believe the elimination of the risk management is compelled by CEA section 4a(c)(2) and the Commission has ample authority to exempt risk management positions under CEA section 4a(a)(7).

3.4.1.1. The Commission has ample authority under CEA section 4a(a)(7) to exempt risk management positions.

Representative Lucas, the Ranking Member of the House Agriculture Committee that authored CEA section 4a(c)(2)'s bona fide hedging language strongly cautioned against overly

⁴⁰ 78 Fed. Reg. at 75,709.

⁴¹ *Id.* at 75,686 at fn. 70.

⁴² CEA section 4a(a)(1). CEA sections 4a(a)(4) and 4a(a)(5) provide further evidence that Congress wanted to ensure that market participants could net price risk in related products, "significant price discovery function" and "economically equivalent" swaps, with futures price risk.

strict position limits with overly narrow exemptions.⁴³ Representative Lucas urged the Commission to “make use of the exemptive authority granted by the [CEA] to avoid establishing position limits which would force widely-held funds or firms to divest their current holdings in highly regulated products.”⁴⁴ Congress did not intend, he continued, that the Commission establish speculative position limits in a manner that “impair[s] price discovery for commercial producers and their counterparties, and cause unnecessary harm to the futures markets and small investors.”⁴⁵

Under CEA section 4a(a)(7), the Commission may exempt any persons or transactions from position limits. Proposed 150.3(e)(2) provides that the Commission “may request” relief from the Commission for “risk-reducing practices commonly used in the market.” The Commission does not explain specifically under what circumstances this relief may be granted.

We believe the Commission should provide for a means to obtain reliable and predictable relief for risk management positions under the Commission’s CEA section 4a(a)(7) authority. The Commission should provide for a risk management position exemption under the conditions of the Commission’s past risk management exemption, i.e., (1) the exempted positions must offset specific price risk; (2) the dollar value of the futures positions must be no greater than the dollar value of the underlying risk; and (3) the futures positions must not be carried into the spot month. These conditions ensure the exemption would not be abused. The Commission could grant such relief in a manner similar to the bona fide hedging exemption in proposed 150.3(a)(1)(i).

3.4.1.2. Eliminating the risk management exemption is not compelled by CEA section 4a(c)(2).

The Commission’s rationale in proposing to eliminate the risk management exemption is based on the omission of a single word in CEA section 4a(c)(2)’s “bona fide hedging transaction or position” definition. We urge the Commission to reconsider its interpretation of the omission of the term “normally” in CEA section 4a(c)(2)’s temporary substitute clause and to interpret that clause as it has been traditionally interpreted under applicable administrative precedent: as a non-restrictive condition providing further indication that the risks being hedged under the exemption arise from operation of a commercial enterprise.

In the Commission’s 1987 “Clarification of Certain Aspects of the Hedging Definition,” (“1987 Clarification”), the Commission provided background on the meaning of the temporary substitute criterion of 17 CFR 1.3(z).⁴⁶ In the 1987 Clarification, the Commission pointed out

⁴³ Letter dated December 16, 2010 from Congressman Spencer Bachus and Congressman Frank Lucas to the Honorable Timothy Geithner, the Honorable Gary Gensler, et al. (the “Bachus/Lucas Letter”), available at <http://online.wsj.com/public/resources/documents/bachus.pdf> (“Overly prescriptive position limits would drain existing liquidity from the capital markets, impair price discovery for commercial producers and their counterparties, and cause unnecessary harm to the futures markets and small investors.”).

⁴⁴ *Id.*

⁴⁵ *Id.*

⁴⁶ Clarification of Certain Aspects of the Hedging Definition, 52 Fed. Reg. 27,195, 27,196 (July 20, 1987).

that in first proposing a definition of bona fide hedging position in 1977, the Commission did not include the term “normally.”⁴⁷ The Commission added the term “normally” in response to commenters to “provide *further* indication” that the temporary substitute criterion was *not* to be “construed as a restrictive, *necessary condition* for the bona fide hedging” exemption (emphasis added). In 1977, the Commission explained that the intention behind the proposed definition of bona fide hedging position was “to set out the basic conditions which must be met by a bona fide hedging transaction or position; i.e. that it must be economically appropriate to risk reduction, such risks must arise from operation of a commercial enterprise, and the price risk fluctuations of the futures contract used in the transaction must be substantially related to fluctuations of the cash market value of the assets, liabilities, or services being hedged.”⁴⁸ The Commission has not, until 2011, intended to make the temporary substitute criterion a necessary requirement for the bona fide hedging exemption.

Similarly, in its 1987 “Guidelines for Risk Management Exemptions,” the Commission noted that the concerns it sought to address with speculative position limits related primarily to “derivative market positions lacking an offsetting cash or derivative market position.” For market participants claiming a risk management exemption, they have an offsetting derivatives position and should be able to claim an exemption for managing these risks.

3.5 The AMG welcomes exclusion of “commodity index contracts” but recommends that counterparties to “commodity index contracts” be provided an exemption for managing commodity index contract position risks.

3.5.1. “Commodity index contract” exclusion.

We welcome the exclusion of “commodity index contracts”⁴⁹ from the proposed definition of “referenced contract.” We agree with the Commission’s rationale for this exclusion. Commodity index contracts do not “involve a separate and distinct exposure to the price of a referenced [] contract’s commodity” price.⁵⁰ This provision benefits many asset managers and their customers who invest in such products in order to gain price exposure to a diversified array of commodities over a diverse set of maturities. The liquidity added to commodity markets by these investments is particularly beneficial in longer dated maturities where liquidity can be scarce. Commercial, bona fide hedgers that might use long-dated commodity derivatives can more cost-effectively establish long-term hedges because of the liquidity that commodity index contracts provide.

3.5.2. The Commission should provide a risk management exemption for positions hedging the price risk of “commodity index contracts.”

⁴⁷ *Id.* citing 42 Fed. Reg. at 14,833.

⁴⁸ *Id.*

⁴⁹ “Commodity index contract means an agreement, contract, or transaction that is not a basis or any type of spread contract, based on an index comprised of prices of commodities that are not the same or substantially the same.” Proposed 150.1.

⁵⁰ Federal Speculative Position Limits for Referenced Energy Contracts and Associated Regulations, 75 Fed. Reg. 4,144, 4,153 (Jan. 26, 2010).

As discussed above in section 3.4, we urge the Commission to reinterpret its bona fide hedging exemption to include risk management positions, inclusive of price risk associated with commodity index contract positions. If it declines to do so, we urge the Commission to extend a risk management exemption for the limited purpose of managing the price risk associated with commodity index contract positions, consistent with the intention behind excluding commodity index contract positions. We note that currently, counterparties to commodity index swaps can remain in compliance for exceeding a position limit based on a position hedging “commodity index contract” price risk under DCM risk management exemptions. We believe that counterparties to commodity index swaps should be able to manage the risk of these contracts without these positions counting against their limits.

3.5.3. Benefits arising from commodity index investment and the costs borne by deterring commodity index investment.

AMG believes that evidence supports the many benefits offered to commodity markets by commodity index funds and accounts, whose long-term diversified investments enhance stability, price discovery and producer hedging. Recognizing these benefits, Senator Blanche Lincoln stated in a July 16, 2010 Senate Colloquy that commodity index participation, in addition to the benefits it provides investors, may “also serve to provide agricultural and other commodity contracts with the necessary liquidity to assist in price discovery and hedging for the commercial users of such contracts.”⁵¹

These considerable benefits will be significantly reduced if the Commission determines not to grant the relief we have requested. Our members noted that leading up to the effective date of the Commission’s vacated part 151 position limits rules (a rulemaking that also excluded “commodity index contracts” and also did not provide for an exemption for positions offsetting commodity index contract price risk), our members noticed less liquidity and noticeably worse pricing for commodity index swaps. These results were due to the expectation of counterparties that our members trade with that their ability to manage the risk offsetting commodity index swaps would be hindered under the anticipated part 151 rules. Our members would expect to incur similar costs under the Commission’s new proposed rules. Furthermore, during the run-up to the effective date of the Commission’s vacated part 151 position limits rules, our members were finding that they needed to transact with additional counterparties in order to trade commodity index swaps as their counterparties were concerned with hitting limits. As a result, many of our members were preparing to initiate trades with less creditworthy counterparties in order to source liquidity.

We note finally that neither Amaranth nor the Hunt brothers were in any way involved in commodity index swaps. Reducing the ability of commodity index swap counterparties to

⁵¹ Blanche Lincoln, Senate Colloquies, July 16, 2010: “I wish to also point out that section 719 of the conference report calls for a study of position limits to be undertaken by the CFTC. In conducting that study, it is my expectation that the CFTC will address the soundness of prudential investing by pension funds, index funds and other institutional investors in unleveraged indices of commodities that may also serve to provide agricultural and other commodity contracts with the necessary liquidity to assist in price discovery and hedging for the commercial users of such contracts.”

manage the risk associated with their swap positions therefore would present no beneficial effect on the Commission's ability to prevent the type of trading conducted by these two bad actors.

3.6. The Commission should exempt registered investment companies and ERISA accounts from speculative position limits.

Registered investment companies ("RICs") and ERISA accounts are subject to stringent regulatory requirements that ensure that the incentives of the investment adviser are aligned with those of the customers.⁵² These rules and regulations ensure that RICs and ERISA accounts do not engage in the kind of "excessive speculation" or manipulative trading exemplified by Amaranth or the Hunt brothers. Unlike RICs and ERISA accounts, Amaranth was an unregulated private fund.⁵³ Amaranth had a leverage ratio that ranged from five to eight times capital, which resulted in more market pressure when Amaranth was forced to unwind positions.⁵⁴ Being unregulated, Amaranth's investors had little transparency in how dangerously exposed Amaranth was to natural gas prices.⁵⁵ Not subject to diversification requirements, Amaranth had extreme exposures to just a few natural gas settlement prices.⁵⁶

In contrast to Amaranth and the Hunt brothers, RICs and ERISA accounts are subject to existing regulatory regimes that align their incentives with investors, limit their leverage, require them to diversify their holdings, and require them to provide transparency to their investors. RICs are required to comply with all regulations and related guidance under the Investment Company Act of 1940 (the "Investment Company Act"), including those regarding counterparty limits, liquidity and asset coverage and the use of leverage. The Investment Company Act limits the amount of leverage that a RIC may obtain, including through the use of derivatives, by requiring the fund to segregate liquid assets or hold offsetting positions on its books in an equivalent amount.⁵⁷ Unleveraged funds significantly reduce market pressure in the event of any forced unwinding of positions, and are substantially less likely to liquidate due to market movements than leveraged funds like Amaranth.

⁵² See letter dated December 16, 2010 from Congressman Spencer Bachus and Congressman Frank Lucas to the Honorable Timothy Geithner, the Honorable Gary Gensler, et al. (the "Bachus/Lucas Letter"), available at <http://online.wsj.com/public/resources/documents/bachus.pdf> ("We hope that the [CFTC] will make use of the exemptive authority granted by the [CEA] to avoid establishing position limits which would force widely-held funds or firms to divest their current holdings in highly regulated products. Overly prescriptive position limits would drain existing liquidity from the capital markets, impair price discovery for commercial producers and their counterparties, and cause unnecessary harm to the futures markets and small investors.").

⁵³ Amaranth Report at 57.

⁵⁴ *Id.* at 58.

⁵⁵ See The Amaranth Debacle: A Failure of Risk Measures or a Failure of Risk Management?, Ludwig B. Chincarini, *Journal of Alternative Investment* (2007), available at <http://pages.pomona.edu/~lbc04747/pubs/pub10.pdf>.

⁵⁶ See e.g., Amaranth Report at 60-64.

⁵⁷ Section 18(f) of the Investment Company Act; see also Securities Trading Practices of Registered Investment Companies, Investment Company Act Release No. 10666 (Apr. 18, 1979); Merrill Lynch Asset Management, L.P., SEC No-Action Letter (July 2, 1992); Dreyfus Strategic Investing & Dreyfus Strategic Income, SEC No-Action Letter (June 22, 1987).

RICs electing to be “diversified companies” under the Investment Company Act are required to follow strict diversification requirements, including restrictions against investing more than 5% of total capital in any single issuer, and requirements to invest at least 75% of total assets in cash and securities.⁵⁸ In addition, RICs must maintain at least 85% of their assets as liquid investments, are required to calculate and publish net asset values and disclose substantial information about their investments, and are obligated to maintain comprehensive compliance programs. All of these requirements help assure that RICs do not engage in manipulative practices, become too heavily concentrated in any one investment, or create systemic risk.

Additionally, under Subchapter M of the Internal Revenue Code of 1986, at least 90% of the annual gross income of a RIC must be so-called “qualifying income” in order for the RIC to maintain its tax status as a “regulated investment company.” Commodities and derivatives referencing commodities generally do not produce qualifying income under current law. As a result, some RICs use wholly-owned unregistered subsidiaries to invest in commodity derivatives transactions; each subsidiary is included within the regulatory limitations applicable to its registered parent.⁵⁹ Nevertheless, any RIC’s investment in such a subsidiary, and therefore its investment in commodities or commodity-related instruments, is limited to no more than 25% of a RIC’s assets under the tax diversification provisions of the Internal Revenue Code.⁶⁰

Investment advisers to ERISA accounts are subject to strict fiduciary obligations, including the duty to discharge their duties under a stringent prudence test,⁶¹ the duty to diversify the investment of an account’s assets so as to minimize the risk of large losses⁶² and the duty of loyalty, which requires each adviser to discharge its duties solely in the interest of the account and for the exclusive purpose of providing benefits to participants and beneficiaries.⁶³ Similarly, the Investment Company Act requires advisers to RICs and other vehicles to be registered

⁵⁸ Section 5 of the Investment Company Act.

⁵⁹ Mutual funds utilizing this parent-subsubsidiary structure rely on IRS private letter rulings which conclude that income arising from a mutual fund’s investment in a subsidiary that invests in commodities investments constitutes qualifying income. These same private letter rulings require such subsidiaries to comply with the requirements of Section 18(f) of the Investment Company Act and all related guidance regarding asset coverage and the use of leverage by mutual funds. *See, e.g.*, I.R.S. Priv. Ltr. Rul. 201039002 (June 22, 2010); I.R.S. Priv. Ltr. Rul. 201037012 (June 4, 2010); I.R.S. Priv. Ltr. Rul. 201030004 (Apr. 28, 2010). In addition, in various SEC No-Action Letters, the SEC has permitted RICs to establish wholly-owned foreign subsidiaries for the purpose of avoiding unfavorable foreign tax treatment or foreign investment restrictions, and has acknowledged that such subsidiaries did not avoid any regulatory requirements since the parent-subsubsidiary structures were operated in accordance with the Investment Company Act. *See, e.g.*, S. Asia Portfolio, SEC No-Action Letter (Mar. 12, 1997), Templeton Vietnam Opportunities Fund, Inc., SEC No-Action Letter (Sept. 10, 1996), The Spain Fund, Inc., SEC No-Action Letter (Mar. 28, 1988) and The Scandinavia Fund, Inc., SEC No-Action Letter (Nov. 24, 1986).

⁶⁰ Section 851(b)(3) of the Internal Revenue Code.

⁶¹ ERISA § 404(A)(1)(B), 29 U.S.C.A. § 1104(A)(1)(B). This provision requires the manager to have conducted a sufficient investigation into the details and particulars of a transaction and its appropriateness for the account involved prior to engaging in a transaction.

⁶² ERISA § 404(A)(1)(C), 29 U.S.C.A. § 1104(A)(1)(C).

⁶³ ERISA § 404(A)(1)(A), 29 U.S.C.A. § 1104(A)(1)(A).

themselves under the Investment Advisers Act of 1940, which subjects advisers to rigorous fiduciary duties of loyalty and care to customers as a matter of law.⁶⁴

While RICs and ERISA accounts present virtually no risk of “excessive speculation” or manipulation, their unfettered participation in commodity markets provides valuable liquidity, particularly in long-dated maturities, that is beneficial to bona fide hedgers with long-term hedging needs. We therefore urge the Commission to exempt RICs and ERISA accounts from position limits, particularly where the risk of “excessive speculation” and manipulation is non-existent. Granting these exemptions would reduce the compliance cost associated with RIC and ERISA participation in commodity markets without any real reduction in the efficacy of position limits.

3.7. Grandfather relief.

3.7.1. Grandfather relief should not be limited to only those who do not increase their position after the effective date of a limit.

The Commission proposes at 150.2(f)(2) to exempt a referenced contract position (“a pre-existing position”) acquired by a person in good faith prior to the effective date of a non-spot-month limit, on the condition that the position is not increased after the effective date of a limit. This latter condition should be eliminated because in many scenarios it appears to be inconsistent with the purposes of CEA sections 4a(b)(2) and 4a(c)(1).

CEA section 4a(b)(2) provides that position limits “shall not apply to a position acquired in good faith prior to the effective date of such rule, regulation, or order.” CEA section 4a(c)(1) provides that “[n]o rule, regulation, or order issued under subsection (a) of this section shall apply to transactions or positions which are shown to be bona fide hedging transactions or positions as such terms shall be defined by the Commission by rule, regulation, or order consistent with the purposes of this chapter.”

Consistent with these statutory directives, we believe that the Commission should exempt all pre-existing positions established in good faith from position limits, particularly those that are pre-existing bona fide hedging positions. Doing so should not undermine the Commission’s ability to prevent another Amaranth or Hunt brothers.

3.7.2. The Commission should amend proposed 150.2 to provide for grandfather relief for positions that result from rolling forward of pre-existing positions.

AMG members’ counterparties often hedge the risk of commodity derivatives positions by holding positions in futures contracts. In order for them to effectively hedge the risk associated with a pre-existing position, they would need to be able to roll these hedges from a prompt month into a deferred contract month. The Commission should therefore amend proposed 150.2(f)(2) to cover “any commodity derivative contract position *or position that*

⁶⁴ See Sections 206(1) and (2) of the Advisers Act; *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 192-93 (1963).

results from transferring the price risk exposure created by such position into a deferred contract month acquired in good faith...”

3.7.3. The costs associated with the Commission’s narrow grandfather relief are significant.

Absent the changes we have requested above, particularly in sections 3.4.1, 3.5.1, and 3.5.2, AMG members and their customers would bear significant costs resulting from a diminished ability of AMG members to generate desired returns for customers. Without these changes, the rules as proposed would also result in diminished willingness from our counterparties to transact, resulting in unduly higher costs to enter into commodity derivatives trades. Indeed, as indicated above, AMG members witnessed a noticeable widening of the bid/ask spread, indicative of reduced liquidity, in the commodity index swaps market even before the Commission’s vacated part 151 position limits rules were to take effect in 2012, which was due in part to a similarly narrow grandfather exemption under vacated 151.9.

4. Conclusion

As discussed above, the AMG believes that before imposing speculative position limits, the Commission must and should make fact-intensive findings of necessity and appropriateness in support of its position limits regime based on an individual contract-by-contract basis. As the Commission has failed to do so with the 2013 NPRM, we believe that it should be withdrawn. Nevertheless, if the Commission determines to proceed with this rulemaking, the Commission can better effectuate the goals of CEA section 4a by making the following changes:

- modifying the proposed spot-month limits and withdrawing or increasing the non-spot-month position limit levels;
- providing DCMs and SEFs more discretion with respect to aggregation requirements and other rules related to position limits;
- preserving the risk management exemption from speculative position limits consistent with the terms of the statute, as informed by administrative precedent and legislative history;
- granting counterparties to “commodity index contracts” an exemption for managing commodity index contract position risks;
- exempting RICs and ERISA accounts from speculative position limits; and
- expanding grandfather relief available to pre-existing positions.

* * *

The AMG thanks the CFTC for the opportunity to comment on the proposed rulemaking concerning position limits. The AMG would welcome the opportunity to further discuss our comments with you. Should you have any questions, please do not hesitate to contact Matt Nevins at 212-313-1176 or Michael Loesch at Norton Rose Fulbright 202-662-4552.

Sincerely,

A handwritten signature in black ink, appearing to be 'T. Cameron', with a long horizontal flourish extending to the right.

Timothy W. Cameron, Esq.
Managing Director, Asset Management Group
Securities Industry and Financial Markets Association

A handwritten signature in blue ink, appearing to be 'Matt Nevins', with a long horizontal flourish extending to the right.

Matthew J. Nevins, Esq.
Managing Director and Associate General Counsel, Asset Management Group
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