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Secretary of the Commission
Commodity Futures Trading Commission ("CFTC" "Commission")
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Notice of Proposed Rulemaking ("NPRM"): De Minimis Exception to the Swap Dealer Definition[1]

Submitted electronically to https://comments.cftc.gov

The Institute for Agriculture and Trade Policy ("IATP")[2] appreciates this opportunity to comment on this NPRM. IATP last wrote to the Commission on March 29, 2018 in response to a request for nominations and topics to discuss at the Market Risk Advisory Committee. We took that occasion to urge the Commission to propose a robust rule on automated trading systems, the topic of our letter to the Commission in May 2017. IATP attended the April 2018 CFTC conference "Protecting America's Agricultural Markets." Agricultural commodity derivative traders there contended that automated trading systems were impeding their price risk management ability, despite CFTC and academic presentations that attempted to persuade participants of the liquidity benefits of automated trading, including High Frequency Trading.[3]

The following comment comprises five parts: 1) introduction; 2) legal authorities cited in the NPRM; 3) IATP's number one priority for the Commission to delete from the proposed rule; 4) responses to a few of the NPRM's many questions and 5) a short conclusion.

***Introduction: The de minimis, deregulation and the financial situation of farmers and ranchers***

IATP is not a market participant, but nonetheless has a public interest in many of the provisions recommended and questions posed. This interest is partly outlined by the NPRM's "swap dealer policy considerations" and "de minimis policy considerations" but extends further to the relation between the swaps market and the futures market. Futures prices are the benchmark from which forward contracting prices in agricultural commodities are derived, e.g. at country elevators.

In aggregate, the proposed exemptions and exclusions from de minimis quantification—particularly the NPRM proposal to allow swaps dealers (SDs) to develop their own methodologies for calculating the de minimis—are tantamount to SD self-regulation. A return to SD self-regulation is not an isolated de minimis accounting exercise, but one that will serve as a risk multiplier, particularly if the foreign affiliate and subsidiary swaps of U.S. persons are likewise excluded from the de minimis.[4]

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If finalized in the rule, the exemptions would help to fulfill Chairman Christopher Giancarlo's promise to the Futures Industry Association (FIA) of "right-sizing the CFTC's regulatory footprint after years of expansive Dodd Frank rule making."[5] However, what is "right-sizing" for the SDs is wrong sizing for farmers, agricultural cooperatives and rural communities. Following a short-term boom in agricultural prices and income in the so-called "golden period during 2011 through 2014" of still unregulated swaps markets[6], many farmers took on more debt to buy land and machinery. In today's bust market, "On average, bankers across the [10th] District [of the Federal Reserve System] reported that nearly 30 percent of the dollar volume of their farm loan portfolios was experiencing at least minor repayment problems (Chart 6)", with the majority of those repayment problems characterized as "severe."[7] IATP would be very surprised if these farm loan repayment difficulties were confined to the 10th District. An increasingly dire agricultural credit situation will be exacerbated by the greater farm operation debt that often follows the boom years of the boom bust cycle.

Agricultural swaps perform a minute fraction of agricultural price risk management, but swaps deregulation affects a broad array of financial instruments used in farm operations and by farm families. In the very incompletely reported agricultural swaps market of late 2013 to 2014, one study stated that the estimated "swaps volume was consistently less than 10%, and typically less than 1%, of the volume for the comparable exchange-traded instrument" among 22 agricultural commodities.[8] Because the prices agribusiness traders and processors pay framers and ranchers for their raw materials are usually below the cost of production,[9] in 2017, only about 18 percent of farm household income came from farm production activities (including government payments), according to the USDA Economic Research Service. The remainder is "earned off farm. The share of farm income derived from off-farm sources had increased steadily for decades but peaked at about 95% in 2000."[10] Since cash receipts are a small fraction of farmer and rancher income, the greater impact of SD self-regulation will be in the foreign exchange and interest rate swaps that will affect respectively, agricultural export sales and a broad array of individual farm household investments, including servicing debt for farm machinery, residential home and out building mortgages, credit card debt and student loan debt.

Farmers and ranchers, even those who now service their debt with little difficulty, cannot afford another "commodity boom/bust" deregulatory failure like the one enabled by regulations authorized by the Commodity Futures Modernization Act of 2000.[11] The next financial crisis likely will be one triggered not by mortgage values, portfolio compression failure and SD under-capitalization, but by a source of systemic risk that farmers and ranchers know all too well—climate change. A senior official of the Bank of England, who played a role in the 2008-2010 SD bailouts, wrote last year, "new risks are emerging around climate change that are poorly understood, hard to manage and, at the extreme, pose threats to the financial system not unlike those we faced in 2008."[12] Although, 160 financial firms have indicated their support for the voluntary recommendations of the Financial Stability Board on climate-related financial risk disclosure,[13] scenario analysis of climate-related financial risk impacts should include the Business As Usual scenario that a very lightly regulated swaps market represents.

At a time when the budget and staff of the federal office that maps the "hot spots" of the financial system is being cut,[14] it is the height of hubris to introduce dozens of "flexibilities" to help SDs try to recapture their former share of the derivatives market and ignore the systemic financial risks posed by those "flexibilities," including those for de minimis

calculation. Artificial intelligence bots applied, whether by SDs or the Commission, to those calculations cannot anticipate financial system default cascades any more than the best super-computer modeling has been able to anticipate the myriad instances of climate change intensification all around the world.[15]

***Legal authority for the de minimis exception to the swap dealer definition***

The de minimis exception to the swap dealer definition in the Dodd Frank Wall Street Reform and Consumer Financial Protection Act ("Dodd Frank Act") authorizes a quantitatively defined rule for who must register and be subject to Dodd Frank Act requirements stipulated for SDs: "The Commission shall exempt from designation as a swap dealer an entity that engages in a de minimis quantity of swaps dealing in connection with transactions with or on behalf of its customers. The Commission shall promulgate regulations to establish factors with respect to the determination to exempt."[16] The NPRM however, proposes to interpret the establishment of "factors" in such a way as to greatly increase the number and kind of swaps dealer transactions and activities that would be exempted from the de minimis calculation.

It is not clear throughout the NPRM when the legal authority for the provisions proposed are industry responses to the Project KISS [Keep It Simple Stupid] Request for Information and when they derive from Dodd Frank or Commodity Exchange Act authorities. For example, concerning the Commission deliberations about whether to lower the threshold for the de minimis exception to register as a SD, the NPRM stated that "A number of Project KISS suggestions addressed these policy related concerns." (Federal Register ("FR") June 12, 2018, p. 27454) Chairman Giancarlo was careful to emphasize to FIA that "Project KISS is not about changing policy. It's designed to simplify and make our rules and regulations less complex, less costly, less burdensome."

However, industry respondents to Project KISS proposed dozens of major policy changes to the Commission. For example, the International Swaps and Derivatives Association prefaced its 43-page list of changes by stating: "In some cases, this letter will recommend changes to CFTC rules, no-action relief, and guidance to resolve instances where those rules or interpretations are ambiguous or otherwise incomplete and unclear in a way that places an unnecessary element of uncertainty on businesses, transactions and markets without promoting any corresponding regulatory or policy goals."[17] The NPRM's response would change policy through the aggregation of exemptions and changes of definitions, e.g. to exclude non-commercial risk hedging from the definition of "swaps dealing activities," (FR 27462-27463) to make Dodd Frank rule-making— in this case the calculation and application of the de minimis to the swaps dealer registration requirement— less burdensome and costly to industry.

As the Commission deliberates exemptions from which swaps will be counted towards the quantitative threshold of the de minimis exception from SD registration, it should keep in mind this legal analysis in a Better Markets comment letter on Project KISS:

> And even the exemptive authority of the Commission is bounded by the public interest: "The Commission may grant exemptions to futures market participants only if it finds the exemptions are in the public interest." [(7 U.S.C. § 5 (2012)] Nowhere in these [Dodd Frank] guides to Congress's intent is there a concern for protecting the profits of banking entities, sparing them compliance costs, or

> otherwise accommodating their preferences in a regulatory model. Any changes to the Commission's rules or practices that cannot be reconciled with the statutory provisions of the Commodity Exchange Act and the Dodd-Frank Act and their protective purposes must be rejected.[18]

The NPRM outlines the public interest requirements of the CEA (FR, 27474-27478) and then argues that the proposed exemptions and exclusions serve the realization of these requirements. For example, consider the rationale for the fit between the NPRM and the price discovery public interest requirements of the CEA:

> All else being equal, the Commission preliminarily believes that price discovery will not be harmed and might be improved if there are more entities engaging in ancillary dealing due to increased competitiveness among swap counterparties. The Commission is preliminarily of the view that, as compared to a $3 billion threshold, an $8 billion de minimis threshold would encourage participation of new SDs and promote ancillary dealing because those entities engaged in swap dealing activities below the threshold would not need to incur the direct costs of registration until they exceeded a higher threshold. (FR 27475)

There is no economic or business model equality among SDs, nor among the bank holding company parents of the SDs, nor among Major Swaps Participants, nor among the exchanges and Swaps Execution Facilities. For example, the addition of a staff-estimated 13 Likely SDs by adopting the NPRM proposed $8 billion de minimis would increase by .01 percent the estimated aggregated gross notional amount of (ANGA) coverage, by .06 percent of the estimated swaps transaction coverage and 2.05% of the estimated counterparty coverage. (FR 27452, Table 3) Even a 2.05 percent increase in counterparty coverage for 13 Likely SDs hardly points to a significant increase in competition, much less a marked improvement in swaps price discovery, particularly among agriculture and energy commodity swaps for which trading data is largely dark to the public.

The idea that more "ancillary dealing" would promote greater competition and thus more efficient and transparent price discovery as swaps data reporting to the CFTC eventually improves, is highly conjectural at best. The conjecture is not well supported by any data in a NPRM that purports to be data driven. The beating heart of the NPRM argument that proposed swaps dealing exemptions and exclusions promote improved price discovery, however, is the "not need to incur the direct costs of registration until they [the SDs] exceeded a higher threshold." The beating heart is not a public interest objective of the CEA, but the regulatory compliance cost and burden reduction objective of Project KISS.

Another illustration of the shaky legal ground of the NPRM is its proposal that swaps included in multilateral portfolio compression exercises be categorically exempted from the de minimis quantity because these exercises, according to the Commission's interpretation of Staff Letter 12-62,

> generally do not involve any of the attributes the Commission has identified as indicative of swap dealing activity. [footnote 146] Further, the Commission notes that counting such swaps towards a person's de minimis threshold could discourage participation in multilateral portfolio compression exercises, reducing the market benefit of the risk reduction such exercises provide. (FR 27464)

The Commission's interpretation assumes that SDs are not engaging in multilateral portfolio compression exercises because of the purported threat of including swaps in those exercises in the SDs' de minimis calculation. The Commission's argument is flawed on at least two counts.

First, the overwhelming driver for the reduction in the global ANGA of swaps is not the purported regulatory "risk" of the de minimis, but the implementation of swaps centralized clearing requirements in the jurisdictions of Financial Stability Board members. According to a June 2016 *Financial Times* article, if that reduction is to be reversed from the lowest global swaps ANGA since 2007, it will be because of product innovation and lessons learned from futures market operations.[19] Exempting swaps in portfolio compression from the de minimis will not "resist the future," to cite part of the *FT* article's title, that is centralized clearing. The systemic use by SDs of centralized clearing platforms is a well-documented way to achieve the CEA's public interest requirements of "protection of market participants and the public" and enhancing the "efficiency, competitiveness and financial integrity of the markets."

The second flaw in the Commission's argument is that merely engagingly in portfolio compression exercises, without documenting and reporting to the CFTC the results of those exercises, should categorically qualify a SD to receive regulatory relief from de minimis inclusion. Granting such regulatory relief to SDs must not be granted apriori to all SDs, when SDs are just beginning to run successful compression exercises that meet clearing house requirements.[20] If the CFTC is to grant regulatory relief from inclusion of a SD's swaps in the de minimis exception, it must not be based on the attributes of portfolio compression exercises outlined in Staff Letter 12-32, but on the basis of well-documented and successful, (i.e. completely reconciled swaps) reportable compression portfolio exercise performance for each SD on centralized clearing platforms. The clearing industry hopes that someday Digital Ledger Technology will find a way to reconcile the values of even swaps with very large numbers of data elements, if the relentless pressure for short term profits allows financial institutions to make the long term and sustained investment in computer technology required for long term data integrity and control.[21] In IATP's view, that's a big "if" question that will not likely be answered in favor of long term data integrity and control by all Commission identified 108 Likely SDs.

If the Commission grants SDs de minimis exemptions for swaps in compression exercises, regardless of their performance, the CEA public interest objectives are not achieved. The sole legal justification for portfolio compression triggered de minimis exemption seems to be that "adding this proposed exception to the regulatory text would be consistent with the goals of Project KISS." (FR 27464) In anticipation of portfolio compression exercise failure, particularly for uncleared swaps, "the proposed rule includes an anti-evasion provision" (FR 27464). However, enforcement of that provision puts the burden on the under-resourced Commission to show that a SD intended to evade the de minimis exception in its portfolio compression activities.

Finally, the Commission is aware that the presidential Executive Order that authorized Project KISS is currently the subject of an ongoing lawsuit in the U.S. District of Colombia Court.[22] The Commission should not finalize the de minimis exception or, indeed, other swaps-related rulemaking in terms of being consistent with the realization of Project KISS objectives. Project KISS is based on an Executive Order that could be modified or even

annulled in a Court order as violating the Administrative Procedures Act, which would subject any rulemaking based on achieving Project Kiss objectives subject to annulment.

***Allowing SDs to propose their own de minimis calculation methodology: a NPRM proposal for the Commission to reject before all others***

The public interest concerns of the Commodity Exchange Act, according to which each proposed exemption from the de minimis exception to SD registration must be justified, are the following:

(A) considerations of protection of market participants and the public;
(B) considerations of the efficiency, competitiveness, and financial integrity of futures markets;
(C) considerations of price discovery;
(D) considerations of sound risk management practices;
and (E) other public interest considerations[23]

Among the proposals and "related matters" in the NPRM, the Commission outlines a framework according to which each SD could propose its own "methodology to be used to calculate the notional amount for any group, category, type or class of swaps. The Commission is also proposing to delegate authority to the Director of DSIO [Division of Swap Dealer and Intermediary Oversight] to make such determinations" (FR 27465) as to whether the proposed SD methodology for calculating its notional amounts is "economically reasonable" and "analytically supported." (FR 27465) This propose-your-own-swaps-calculation methodology is an exemption multiplier to the de minimis exception for SD registration. This section of the comment letter is a global response to questions 1-7, (FR 27465).

> (1) Is the proposed process to determine the methodology to be used to calculate the notional amount for any group, category, type, or class of swaps appropriate? Why or why not?
> (2) Is the proposed process too narrowly or broadly tailored?
> (3) Is the restriction that a methodology be economically reasonable and analytically supported appropriate? Why or why not? What other standards may be appropriate for this purpose?
> (4) How will the proposed process impact persons that enter into swaps where notional amount is not a stated contractual term?
> (5) Is the proposed delegation of authority too narrowly or broadly tailored?
> (6) How will the proposed delegation of authority impact persons that enter into swaps where notional amount is not a stated contractual term?
> (7) Is there a better alternative to this proposed process? If so, please describe.

In theory, each of the staff estimated 108 Likely [to register] SDs (Table 7, FR 27453) would be authorized to submit a methodology for each "group, category, type or class of swaps." (FR 27448) The Director of DSIO and the staff would have to analyze these hundreds of calculation methodologies for the 108 Likely SDs and determine which of them were "economically reasonable" and "analytically supported." Furthermore, the DSIO would have to establish a common metric for aggregating swap positions across the "group, category, type or class of swaps," if, as suggested, the CFTC might, under a modification to the proposed rule-making, develop a metric to replace the AGNA.

For an adequately funded and staffed agency, these calculations, their implementation and adjustment to swap innovation and grouping, would be a monumental and perhaps insuperable task, even with the addition of the three quantitative analyst positions that Chairman Giancarlo hopes to fill with a more robust budget, as he told the House of Representatives Agricultural Committee on July 25. Given the federal fiscal austerity that is very likely to result at non-military and security agencies from the $1.5 trillion tax cut,[24] it is hard to imagine that the Commission's budget will be adequate to implement and enforce this atomized approach to calculating the de minimis exception.

Even if that budget were applied to hiring more quantitative analysts to assist the Director of DSIO in evaluating each of the 108 Likely SD proposed calculation methodologies, the inadequate capacity default would be to concede that each methodology was "economically reasonable" and "analytically supported," according to the information supplied by the Likely SDs. Even a CFTC converted from being an "analogue regulator" of rules to a "digital regulator" of data, in the futuristic vision Chairman Giancarlo bruited in his oral testimony to the House agricultural committee on July 25, will be no match for the possibilities of regulatory and data arbitrage if each Likely SD is allowed to propose its own methodology for calculating its de minimis. In effect, the NPRM has migrated the Commission's "regulatory sandbox" approach to unregulated FinTech entities to the de minimis exception rule required by the Dodd Frank Act.

With reference to the CEA's public interest considerations, how are market participants, specifically swaps participants and the public that relies on them, e.g. municipal governments with Collateralized Debt Obligations, protected by allowing each Likely SD to propose its own methodology for calculating the notional value for each of its "group, category, type or class of swaps," for exemption from the de minimis calculation? More broadly, how will swaps participants and the public they serve be better protected by having fewer SDs register with the CFTC and be subject to SD registration requirements because of exemptions from SD registration created by the profusion of methodologies to calculate the de minimis? IATP could continue to ask such questions for each category of public interest concern outlined in the CEA.

IATP agrees with Commissioner Rostin Benham's dissent that

> There is not any controversy as to how notional amount is calculated. Giving the Director of DSIO broad authority to determine how this calculation is made for all categories of swaps is a remedy that is not commensurate to the limited issue of how to determine the notional value of commodity swaps. It also provides an opportunity for mischief. This provision could subsume the entire de minimis threshold by giving the Director of DSIO broad authority to determine what swaps count toward the threshold—and perhaps more importantly, what swaps do not. I'm concerned that the Commission is proposing to both establish its authority and immediately delegate such authority without any internal discussion, without any public deliberation, and within this Proposal. (Appendix 4—Dissenting Statement of Commissioner Rostin Benham, FR 24783)

The Director of DSIO could reduce the "opportunities for mischief," i.e. regulatory arbitrage in methodologies to exempt ever greater amounts of swaps activity from the de minimis. The Director could reduce the number of calculation methodologies and/or the classes or

grouping of swaps to which the methodologies could apply. Or the DSIO could take a first-come, first serve approach to calculation methodology proposals, regardless of their aggregate impact on market integrity. But the brunt of Commissioner Benham's dissent is that the NPRM, if finalized by the Commission, would fast-track a radical methodological departure in the calculation of notional value, when the current calculation of notional value, the spot price multiplied by the contract units of swaps transacted, has not been controversial within the industry until very, very recently.

However, notional value as the metric for calculating the swaps positions that trigger SD registration if not below the de minimis, is controversial for Commissioner Brian Quintenz. He characterizes notional value as a "poor measure of activity and a meaningless measure of risk and therefore, by itself, is a deficient metric by which to impose large costs [of SD registration] and achieve substantial policy objectives." (Appendix 3—Supporting Statement of Commissioner Brian D. Quintenz, FR 27480) Commissioner Quintenz wants to minimize the regulatory costs of SD registration and the number of swaps dealers who must register as SDs. He implies that achieving the public interest policy objective of sound risk management is better served by adding to the notional value metric "additional measures (such as dealing counterparty count and dealing transaction count) to determine what constitutes a de minimis quantity of swaps dealing activity" (FR 27481).

Toward minimizing the number of swaps dealers who must register and pay the regulatory costs of SD registration, Quintenz states, "an entity would have to surpass all three hurdles collectively in order to lose the de minimis exception's safe harbor" (FR 27481) from the requirements and costs of SD registration. IATP does not believe that the addition of two hurdles to trigger SD registration will achieve the public interest objectives of the CEA, even the objective of sound risk management, because counterparty count and transaction count are subsumed in what notional value reports.

It is highly unusual for a CFTC Commissioner to repudiate a swaps metric relied upon by the industry and the Commission itself[25] to measure swaps activity, and<u>, in concert with prudential regulator metrics</u>, such as the leveraged risk ratio, to measure and manage swaps dealing risk. (Nobody claims that notional value is, by itself, a robust indicator of risk.) Only on May 25, about three weeks before the posting of the NPRM for comment, the International Swaps and Derivatives Association announced that it was considering changing its thirty-year reliance on notional value in a research note about a new metric explored for interest rate swaps in a paper by the CFTC's Chief Economist and Chairman Giancarlo.[26]

Commissioner Quintenz's proposed three-pronged hurdle to SD registration, when combined with the proposal to allow each of 108 Likely SDs to present to the Director of DSIO methodologies for determining how to "calculate the notional amount for any group, category, type or class of swaps," would radically reduce the number of swaps dealers required to register and be subject to SD requirements. The reduction would be all the greater, if the de minimis quantity were raised to $20 billion, as Commissioner Quintez, suggests (FR 27481). But how would such a reduction better protect market participants or the financial integrity of markets, to reference just two CEA public interest criteria?

Commissioner Benham reports in his dissent that his office received the three-pronged hurdle to SD registration proposal championed by Commissioner Quintenz on "May 31, 2018, providing my office less than 17 hours to respond before DSIO intended to submit

final voting copy to the Commission's Office of the Secretariat." (FR 27483) Whatever the reason for this last-minute provision to Commissioner Benham of a major and radical proposed change to the method for calculating the "de minimis quantity of swaps dealing," above which SD registration is required, the process of drafting, reviewing and voting on this crucial provision in the NPRM appears to be hasty and even heedless of Dodd Frank and CEA policy objectives.

The purpose of the NPRM fast-tracking is apparently to fulfill Chairman Giancarlo's commitment, announced to FIA in March, that "This year we will complete rules on de minimis levels for swap dealer registration." If the Commission votes to do so, IATP urges the Commission to delete the provision that would delegate its authority to the Director of DSIO to determine SD's proposed methodologies for calculating swaps to count towards the de minimis exception. Additionally, the Commission should delete the proposed three-pronged hurdle to SD registration, to allow a full public discussion of the elements of and rationale for the hurdle, as recommended by Commission Benham. This is a crucial rule and one that a full five-member Commission, and not just the present three-member Commission, should discuss and vote on.

***Responses to questions posed in the NPRM***

Most of the questions to which the NPRM request answers largely are directed to market participants. Questions are prefaced with this request, "To the extent possible, please quantify the impact of issues discussed in comments, including costs and benefits, as applicable." (FR 27458) However, under the reduce regulatory costs and burdens order of Project KISS, the questions are not framed to elicit comments about the benefits for the financial system and it's participants of a robust regulation of SDs.

Regarding the quantity of de minimis swaps activity before SD registration is required, the Commission asks

> (1) Based on the data and related policy considerations, is an $8 billion de minimis threshold appropriate? Why or why not?
> (2) Should the de minimis threshold be reduced to $3 billion? Why or why not?
> (3) Should the de minimis threshold be increased? If so, to what threshold? Why or why not?
> (4) Are the assumptions discussed above regarding a $3 billion de minimis threshold, an $8 billion de minimis threshold, or a higher de minimis threshold accurate, including, but not limited to, compliance costs and market liquidity assumptions?
> (5) As an alternative or in addition to maintaining an $8 billion threshold, should the Commission consider a tiered SD registration structure that would establish various exemptions from SD compliance requirements for SDs whose AGNA of swap dealing activity is between the $3 billion and $8 billion?
> (6) What is the impact of the de minimis threshold level on market liquidity? Are there entities that would increase their swap dealing activities if the Commission raised the de minimis exception, or decrease their swap dealing activities if the Commission lowered the threshold? How might these changes affect the swap market?
> (7) Are there additional policy or statutory considerations underlying SD regulation or the de minimis exception that the Commission should consider? (FR 27458)

The Commission analysis for these questions is framed by thirteen tables derived from a preliminary and final staff report analyzing non-public swaps data to argue for maintaining the $8 billion de minimis. That threshold that was set provisionally in 2012 before SDs were required to report their swaps to swaps data repositories. As we contended above, IATP does not believe that the de minimis threshold or the lack of exemptions to calculating that threshold, which are now proposed in the NPRM, are the main drivers in the shrinkage of the swaps market ANGA.

The clearing of swaps on centralized platforms and the migration of swaps to the futures market are the main drivers, not avoidance of the swaps market by potential counterparties due to regulatory compliance costs of SD registration. IATP does not have a data-based argument for changing the current swaps de minimis of $8 billion. However, maintaining the $8 billion threshold because of "potential administrative burdens" (FR 27457) to lowering it is a poor, Project KISS-based rationale that once again does not consider the benefits of SD registration for the financial integrity and price discovery of the swaps market.

The seven questions above are difficult to answer for a public interest participant in CFTC activities and particularly, as the NPRM notes in several places, because Non-Financial Commodity (NFC) swaps data are not reported to the CFTC with the data integrity required for inclusion in the CFTC's Weekly Swaps report (Fr 27457 and elsewhere). As a result, the NPRM makes its arguments for maintaining the $8 billion de minimis threshold for SD registration based on staff analysis of proxy data of ANGA for the Financial Commodity swaps reported in the Weekly Swaps Report. NFC swaps (agriculture, energy, environmental goods, and base and precious metals) are a very small ANGA fraction, perhaps one percent according to the Bank for International Settlement and agriculture swaps a small fraction of that one percent.

As IATP wrote in 2012, agriculture swaps are "A tiny boat on the vast financial data sea."[27] Like the Commission, IATP "does not believe decreasing or increasing the de minimis threshold would have much benefit for the NFC swap market" (FR 27457) since that market is far too small, relative to Financial Commodity swaps, to be impacted by an increase or decrease. We are perplexed by the Commission summary of market participants' views: "Rather there is a concern that a change in the threshold would cause harm to that market," since that concern is based on conjecture about who, e.g. small-town bankers, would avoid the swaps market if the de minimis were lowered to $3 billion (FR 27457).

Perhaps banker preference for the greater data and price formation transparency of regulated futures and options markets, rather than conjecture about reduced swap market participation alleged if the de minimis were reduced to $3 billion, is a better explanation for the lack of smaller bank participation in swaps markets. The CFTC could put a survey in the field to find out why smaller banks are shunning swaps, rather than speculate about why. Or the Commission could ask the Federal Reserve to add such a question to its regular surveys of smaller banks. Where there is a strong demand for the risk management products that the swaps market is innovating, such as to package soaring U.S. corporate debt[28] into tradeable assets, the regulatory costs and obligations of SD registration will not decrease activities in those products, e.g. credit default swaps.

In the very incompletely reported agricultural swaps market of late 2013 to 2014, one study reported, "the total dollar value of agricultural swaps activity for the 13-month period covered by this study was valued at more than $51 billion,"[29] small change compared to agricultural futures activity during that period. The study's author noted, "Of greater concern, from a data integrity standpoint, are the transactions that were eliminated because the underlying commodities could not be identified or because the reported data contained various errors. For example, two soybean swaps were deleted from this study because the reported notional quantity for each transaction was roughly equal to the size of the entire U.S. soybean crop. These types of reporting errors are not uncommon, both in the context of this study and for the swaps market in general."[30]

Since this 2014 analysis, because of the implementation of Dodd Frank Act authorities, CFTC swaps reporting has shown great improvement in financial commodities swaps trade data reporting. However, NFC swaps reporting, continue to suffer from data integrity challenges that impede realization of CEA public interest objectives, particularly in market participant protection, price discovery and market integrity.[31]

Because of the poverty of data integrity in NFC swaps reporting, and the huge disparity between financial commodity and NFC swaps reporting, IATP believes that the Commission should propose, after further analytic work, a tiered SD registration for SDs with a certain threshold of NFC swaps activity, e.g. via commodity indexes. One basis for the tiering would be an averaging of NFC ANGA for Likely (to be registered) SDs since the beginning of CFTC NFC reporting in 2013. Rather than assuming that the $3 billion ANGA de minimis threshold would result in less NFC swap liquidity, the Commission should evaluate which of the Likely SDs has demonstrated a sustained commitment to providing "usable liquidity" to commercial hedgers of commodities, to enable realization of the CEA public interest requirements. "Usable liquidity" would require definition, but it would include a bidding process that would enable commercial hedger intra-day transaction access to swaps contracts comparable to what commercial hedgers have on futures and options markets. The intentional spoofing of bids already prohibited by Dodd Frank would, of course, continue to apply. But lack of timely access to liquidity adequate, but not excessive, for managing price risk is a rulemaking matter of automated market structure, not just of catching individual spoofers.

*Conclusion*

The NPRM proposes so many exemptions and exclusions to the de minimis as to circumvent and greatly reduce the number and kind of swaps dealing activities, including cross border ones, that are regulated under the Obama administration swaps regulatory regime. Indeed, a major failing of the NPRM discussion is lack of analysis of the impact of the proposed exemptions and exclusions from the de minimis calculations on comparability determinations of SD registration requirements with those of foreign regulatory jurisdictions. Mere deference to those jurisdictions did not enable realization of any of the CEA public interest requirements during the 2007-2010 liquidity crisis, caused in no small part by uncleared and poorly reported swaps and undercapitalized SDs.[32] The Obama administration's proposed swaps regulatory regime has been criticized by Chairman Giancarlo as being erroneously modeled on the operations of the futures market.

The ease and rapidity with which many swaps migrated to the futures market to avoid swaps regulation (a regulatory arbitrage strategy called the "futurization of swaps") is

testimony to the large degree of functional equivalency between the futures market and the swaps market.[33] Therefore, the capital efficiency, price discovery efficiency and integrity of many futures markets is not a bad model to emulate, in IATP's view.

IATP believes that Commissioner Benham, in his dissent against releasing the NPRM, has good cause to ask whether the "ancillary considerations" of the NPRM "may signify the Commission's willingness to exploit the de minimis exception to undermine the swap dealer definition and circumvent Congressional intent." (FR 27481) For example, the NPRM proposes that swaps transacted by SDs to hedge financial risk be exempt for inclusion in the de minimis exception for swaps deals. (FR 27462-27463) The definition of "major swaps participant" in Dodd Frank includes "positions held for hedging or mitigating commercial risk." By proposing that transactions to hedge financial risk be exempted from aggregation for the purpose of determining the de minimis exception, the NPRM would extend to SDs a hedging exemption Congress intended only for major swaps participants. If Commission finalizes the de minimis exception rule to extend the commercial hedging exception to the much larger entities that manage price risk in financial commodity swaps, litigation concerning the circumvention of Congressional intent via the de minimis exception's proposed exemptions and exclusion may further delay the application of that rule and leave the integrity of the swaps market again in question.

IATP hopes that these comments assist the Commission in proposing a de minimis exception rule that is consistent with its authorizing statutes, and that can be implemented and enforced with the Commission's budget constrained resources. We look forward to commenting on the draft proposed rule.

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[2] IATP is a nonprofit, 501(c)(3) nongovernmental organization, headquartered in Minneapolis, Minn., with offices in Washington, D.C. and Berlin, Germany. IATP has participated in the Commodity Markets Oversight Coalition (CMOC) since 2009, and the Derivatives Task Force of Americans for Financial Reform since 2010. IATP has submitted several comments on CFTC rulemaking, and on consultation papers of the International Organization of Securities Commissions, the European Securities and Markets Authority, and the European Commission's Directorate General for Internal Markets.

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