July 13, 2016

The Honorable Tim Massad, Chairman
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

RE: "Position Limits for Derivatives: Certain Exemptions and Guidance," RIN 3038-AD99

To Chairman Massad:

Americans for Financial Reform ("AFR") appreciates this opportunity to comment on the above-referenced Supplemental Notice of Proposed Rulemaking (the "Proposal") by the Commodity Futures Trading Commission (the "Commission"). AFR is a coalition of more than 200 national, state, and local groups who have come together to advocate for reform of the financial industry. Members of AFR include consumer, civil rights, investor, retiree, community, labor, faith based, and business groups.[1]

AFR and other public interest groups have been long time supporters of the swaps position limits mandated by the Dodd-Frank Act. The Dodd-Frank Act required that these positions be established within six to nine months of the passage of the legislation. However, the Commission's completion and implementation of these position limits has been significantly delayed, first by a lawsuit, and then by a lack of Commission action since the re-proposal of the rule in 2013. Indeed, the delay since the 2013 re-proposal rule that complied with the conditions laid out by Judge Wilkins in the lawsuit is approaching three years.

In this Proposal, the Commission suggests the following changes to the 2013 re-proposal of the rule:

1) A broadening of the general definition of "bona fide hedges" to remove the longstanding requirement that hedges be "incidental" to commercial activity and replace it with a more general standard that they be "economically appropriate" to the reduction of commercial risk. The "incidental" test has been a part of the bona fide hedge definition since 1975.

2) An exemption for any Designated Contract Market (DCM) or Swaps Execution Facility (SEF) from compliance with position limits if that SEF lacks sufficient information on

[1] A list of AFR member organizations is available at http://ourfinancialsecurity.org/about/our-coalition/.

total customer swaps positions to determine if trading activity would violate position limits. The Proposal implies that this exemption would currently apply to most exchanges with regard to swaps position limits.

3) Delegating the authority to DCMs and SEFs to recognize non-enumerated and anticipatory bona fide hedges as exempt from position limits. This would be based on an exchange-designed and managed application and approval system and subject to possible, but not necessarily required, review by the Commission.

We are deeply concerned that these changes could further weaken a rule that already contains numerous exemptions and has been greatly delayed.

As pointed out in the comment letter by the Institute for Agriculture and Trade Policy (IATP), the elimination of the longstanding requirement that hedges be incidental to commercial activity could open the door to the use of "economically appropriate" hedges by purely financial entities, such as swap dealers. The requirement that hedged risks are incidental to commercial activity served to better limit the use of hedge exemptions to companies whose main business was producing a non-financial product. The "incidental" requirement also offered a narrower and clearer test for the appropriateness of hedges than the vaguer standard that hedges simply be "economically appropriate". We urge the Commission to either retain the "incidental" test or to find a better way to retain these strengths in the final rule.

The exemption of DCMs and SEFs that lack sufficient data to implement position limits is a serious threat to the effectiveness of position limits. It raises questions about the Commission's broader implementation of swaps data reporting requirements, questions that go beyond the scope of this comment. Given that the Commission seems to admit in this Proposal that the lack of swaps market transparency is preventing full implementation of position limit mandates that are already long overdue, we would expect to see a plan for addressing these issues that goes beyond simply exempting affected exchanges.

The Proposal also grants authority to exchanges to expand the list of hedges that qualify as exemptions to position limits. This step appears deeply inappropriate given that exchanges have a direct economic interest in increasing trading volume, including speculative trading. Exchanges are for-profit enterprises that charge fees based on trading volume. They have a clear economic motivation to increase trading volumes and face a conflict of interest in making decisions that directly affect trading volume, such as whether trading qualifies for a hedge exemption from position limits. This interest is clearly in conflict with Congressional intent to limit excessive speculation in derivatives markets.

The Proposal explains that specific hedges granted by DCMs and SEFs would be subject to review by the Commission and could potentially be reversed by Commission action. However, if Commission review is discretionary and new hedge exemptions are allowed to take effect without an explicit requirement for Commission review and approval, we are concerned that such reviews will be inconsistent and uncertain. Given resource limitations at the Commission there will be a tendency to cede the central role in approval of new hedge exemptions to the exchanges themselves.

We would strongly oppose such an outcome. The role played by exchanges in the approval of hedge exemptions should be ***fundamentally advisory***, with a clear expectation and indeed requirement that the Commission review any hedge approved by an exchange before that hedge can be used to exempt swaps from position limits.

By a "fundamentally advisory" role, we mean that the exchange could appropriately play a role in taking applications for new hedge exemptions, gathering supporting data, and providing a recommendation as to whether such an application should be approved. But the Commission must review any such application and make the final decision as to whether to reject it, approve it, or simply not to act on it due to lack of information or lack of available resources to address the application. No new hedge exemption should be used in trading without review and approval by the Commission itself, not an exchange.

It would be deeply inappropriate to instead grant exchanges approval powers that go beyond an advisory capacity. The Commission has already established a robust and extensive set of enumerated hedges. The decision as to whether to approve or reject hedges that go beyond this list, or to approve anticipatory hedges, is critical to the position limits regime. The Commission, not conflicted for-profit exchanges, should make the decision on such requests.

Commission oversight of the broad approval process used by exchanges to review new hedge applications does not provide adequate control. Such a general approval process is essentially procedural and leaves too many questions unanswered as to what specific hedges would be approved or denied.

We are further concerned that in the absence of regular and routine Commission review of specific hedges, the Commission will eventually lose important experience and analytic capacity related to regular monitoring of hedge claims in the market. Without regularly performing de novo analysis and review of new requests for hedge exemptions, the Commission will become inappropriately dependent on conflicted self-regulatory organizations to perform core oversight functions for the position limits regime. This could lead the Commission to lose touch with the range of activities and trading exemptions being permitted in the market.

It is true that Congress granted extensive exemption authority to the Commission with respect to position limits. But the use of such authority must not compromise the clear Congressional directive that the Commission establish *specific* limits on swaps positions and reduce excessive speculation to the *maximum extent practicable*. If the Commission chooses to delegate a central element of its authority concerning the scope of position limits exchanges or the corresponding self-regulatory bodies, these goals are likely to be compromised. We urge the Commission not to fully cede such authority and to limit exchanges to an advisory role.

Thank you for the opportunity to comment on this Proposal. Should you have any questions, please contact Marcus Stanley, AFR's Policy Director, at marcus@ourfinancialsecurity.org or (202) 466-3672.

Sincerely,

Americans for Financial Reform