MEMO

TO: MGEX Members and Market Participants

FROM: Athena R. Elias, Associate Corporate Counsel

DATE: February 4, 2014

SUBJECT: CFTC Notice of Proposed Rulemaking on Position Limits for Derivatives

Introduction

On December 12, 2013, the Commodity Futures Trading Commission ("CFTC") published the Position Limits for Derivatives Notice of Proposed Rulemaking ("Position Limits NOPR") in the Federal Register.[1] The public comment period on the proposal ends February 10, 2014.[2] MGEX is drafting a comment letter which will be submitted by the February 10 deadline, and asks for your support in drafting and submitting additional comment letters illustrating the negative effects this proposed rule could have on MGEX market users.

MGEX is issuing this fact sheet as a reference in regards to the Position Limits NOPR and the key points on which MGEX is focusing its comments, and encourages its Members, market participants and other interested parties to submit their own comments.

Rule Summary

The CFTC's Position Limits NOPR sets limits on speculative positions in 28 core commodity contracts and their economically equivalent futures, options and swaps contracts ("referenced contracts"). MGEX Hard Red Spring Wheat is one of the three wheat contracts included as core futures referenced contracts in the rule.

The proposed limits are divided into two categories; spot-month and non-spot month.

Spot-month position limits would initially be based on the spot month position limit levels currently in place, and later would be based on estimates of deliverable supply. Subsequent levels would be adjusted at least every two years, and would be based on the CFTC's determination of deliverable supply. Generally, spot-month position limits levels are set at 25% of estimated deliverable supply.

Non-spot month position limits would be based on open interest and would also be adjusted at least every two years. Non-spot month position limits are set using a 10/2.5% formula, meaning 10% of the contracts first 25,000 of open interest and 2.5% thereafter. Open interest used in determining subsequent non-spot month position limits will be the larger of the prior two years

[1] Full text of the proposed rule can be found at the following link: http://www.cftc.gov/ucm/groups/public/@lrfederalregister/documents/file/2013-27200a.pdf

[2] Public comments can be submitted by any of the following methods: online at http://comments.cftc.gov; by mail to Secretary of the Commission, CFTC, Three Lafayette Centre, 1155 21st Street NW, Washington, DC 20581; or via the Federal eRulemaking Portal at http://www.regulations.gov.

annual average of the sum of futures and options open interest, cleared swaps open interest and uncleared swaps open interest on a futures equivalent basis.

The Position Limits NOPR narrows the current definition of a bona fide hedge, and also includes amendments to the current account aggregation standards.[3]

Key Points for Comment

Currently, all three domestic wheat contracts are treated equally as to position limits. Under the Position Limits NOPR however, the current HRSW spot-month speculative limit of 600 contracts could drop as a result of lower stocks at delivery locations in prior years. The current non-spot month MGEX HRSW speculative limit of 12,000 contracts would decrease to just **3,300** contracts, while the KC HRW limit would decrease to 6,500 contracts, and the CBOT SRW limits would actually increase to 16,200 contracts. This results in different position limits for all three wheat contracts.

Market Participants have long appreciated the position limit parity among the three wheat contract markets, particularly as it relates to non-spot months. Having the same limits makes cross-hedging and spread trading easy to monitor and is a legitimate risk management tool. In the event position limits are set at different levels for each of the three wheat contracts as proposed in the Position Limits NOPR, price volatility or concentration in one contract may unduly affect the price of the others. The value and certainty that parity presents to the marketplace has resulted in historically effective and efficient markets for all wheat contracts. Without it, inequities are introduced into the marketplace which could result in market distortion and arbitrage.

The formulaic approach of the NOPR inhibits growth in HRSW just when activity is increasing. This approach is backwards looking, not forward thinking, and simply does not allow for growth or participation by liquidity providers in the same way they can participate in the other wheat contracts.

The definition of bona fide hedging and the related examples would still be too narrow. In practice, the effect upon commercial end users of this narrowing will be profound. The CFTC should listen carefully to the real life examples market participants provide.

Conclusion

The CFTC has indicated that specific examples and proposed solutions are most persuasive in public comment letters and as such, MGEX is working to incorporate detail regarding the need for continued parity of position limits among the three wheat contracts into its comment letter. Specifically, that a lack of parity could significantly and negatively impact volume, liquidity and open interest in our market.

MGEX requests that MGEX Members, market participants and interested parties submit additional public comment letters to the CFTC which highlight concerns and explain the potential impact this proposed rule, if made final as it is currently written, would have on them and on the industry as a whole.

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[3] Additional information on the proposed changes, including changes to the bona fide hedge definition and account aggregation standards can be found at: http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/pl_150_factsheet.pdf