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September 21, 2010

Chairman Gary Gensler
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Dear Chairman Gensler:

Thank you for taking the time to meet with us and our members last week. We certainly appreciated having the opportunity to visit with you about some of the issues surrounding implementation of the Dodd-Frank Act that may impact farmer cooperatives and their members.

For your reference, I've attached comments NCFC submitted yesterday in response to the Commodity Futures Trading Commission's request for comments on some of the definitions contained in the Dodd-Frank Act.

Again, the time you took to meet with us is greatly appreciated. We look forward to providing further input to CFTC throughout the rule-writing process.

Sincerely,

Charles F. Conner
President & CEO

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Eric
Tim
Megan

NCFC®
NATIONAL COUNCIL OF FARMER COOPERATIVES

September 20, 2010

Mr. David A. Stawick
Secretary
Commodities Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW.
Washington, DC 20581

RE: Advance notice of proposed rulemaking; request for comments: Definitions Contained in Title VII of Dodd-Frank Wall Street Reform and Consumer Protection Act (Federal Register/Vol. 75, No. 161)

Dear Mr. Stawick:

On behalf of the more than two million farmers and ranchers who belong to one or more farmer cooperative(s), the National Council of Farmer Cooperatives (NCFC) submits the following comments in response to the Commodity Futures Trading Commission's (CFTC) request for comments: Definitions Contained in Title VII of Dodd-Frank Wall Street Reform and Consumer Protection Act (17 CFR Part 1).

Since 1929, NCFC has been the voice of America's farmer cooperatives. Our members are regional and national farmer cooperatives, which are in turn composed of over 2,500 local farmer cooperatives across the country. NCFC members also include 21 state and regional councils of cooperatives.

Farmer cooperatives – businesses owned and controlled by farmers, ranchers, and growers – are an important part of the success of American agriculture. These farmer cooperatives allow individual farmers the ability to own and lead organizations that are essential for continued competitiveness in both the domestic and international markets. In all cases farmers are empowered, as elected board members, to make decisions affecting the current and future activities of their cooperative. Earnings derived from these activities are returned by cooperatives to their farmer-members on a patronage basis thereby enhancing their overall farm income.

America's farmer-owned cooperatives provide a comprehensive array of services for their members. These diverse organizations handle, process and market virtually every type of agricultural commodity produced. They also provide farmers with access to infrastructure necessary to manufacture, distribute and sell a variety of farm inputs.

Congress recognized the unique status of farmer cooperatives with enactment of the Capper-Volstead Act in 1922. The Act gives agricultural producer organizations limited antitrust immunity "in collectively processing, preparing for market, handling, and marketing" their products and permits such organizations to have "marketing agencies in common." [1] Other indications of Congressional support for cooperatives, include the Agricultural Marketing Act of 1929; the Agricultural Marketing Agreement Act of 1937; and the Agricultural Fair Practices Act of 1967, which states: "the marketing and bargaining position of individual farmers will be adversely affected unless they are free to join together voluntarily in cooperative organization..."[2]

Although farmer co-ops have unique status in federal and state law, they still face many challenges. Farmer cooperatives themselves face practical constraints that place them in a more challenging situation than non-farmer owned businesses. Because agricultural cooperatives are grower-owned and consist of a limited number of grower-investors, they typically do not seek capital from outside investors and their ability to raise additional capital from their grower-members is limited.

Such practical limitations on access to capital pose a major impediment to the activities of most agricultural cooperatives and make it difficult for cooperatives to expand and bargain on an equal footing. This is particularly acute for advance planning by cooperatives that requires substantial capital investment or commitment of resources, such as planning for operating and expansion expenses, environmental compliance or expansion into the global market. Therefore, farmer-owned cooperatives will be very sensitive to any additional margin, capital, reporting and other regulatory requirements that may be imposed due to the Dodd-Frank Act.

Farmer-owned Cooperatives' Use of Swaps

As processors of commodities and suppliers of farm inputs, farmer cooperatives are commercial end-users of over-the-counter (OTC) derivatives. Farmer cooperatives use swaps to effectively minimize risks associated with price movements in commodities, including (but not limited to) grain, milk products, energy, and fertilizer. Due to market volatility, cooperatives use swaps to better manage their exposure by customizing their hedges and accessing risk management alternatives in otherwise illiquid markets. This practice increases the effectiveness of risk mitigation and can reduce the costs of those activities. In addition, swaps give cooperatives the ability to offer customized products to producers to help them better manage their risk and returns and, ultimately, provide more predictable profitability. Outlined below are how co-ops in different sectors of agriculture participate in this market to provide valuable risk management services to their farmer members.

- **Dairy:** Co-ops provide customized hedging solutions to dairy farmers, allowing them to lock in margins to help ensure future profitability. The co-ops, in turn, offset that risk by buying financial futures on corn and soybean meal, while selling class III milk futures.

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[1] 7 U.S.C. § 291.

[2] 7 U.S.C. §§ 2301-2305.

- **Grain:** Local cooperative elevators offer crop farmers a guaranteed price for future deliveries of a specific volume of a commodity and offset that risk by entering into swaps with cooperatives in a regional or federated system.
- **Fertilizer:** Large inventories of fertilizer are necessary to provide farmers with timely service as fertilizer is produced year round and there are only seasonal applications. A growing OTC market for fertilizer helps co-ops hedge away inventory/price risk during volatile times.
- **Fuel:** Customized solutions are developed by the co-op to assist individual farmers with their fuel hedging needs as individual farmers do not have the fuel demands necessary to consume a standard 42,000-gallon monthly NYMEX contract.
- **Small Producers:** A cooperative can aggregate its members' small volume swaps or forward contracts and transfer that risk to a swap partner. The swap partner would otherwise not have the interest in servicing so many small producers.

Agricultural cooperatives are "natural" end users and have used swaps as an extension of their risk mitigation business, as was intended when futures and options markets were implemented. Agricultural cooperatives are not a cause of systemic risk. In fact, cooperatives' swap transactions seek to hedge commercial risk and support the viability of their members' farms and cooperatively owned facilities. As such, agricultural cooperatives should be treated as end users. We believe this was the intent of Congress when writing the Dodd-Frank Act.

In order to provide risk mitigation services to their farmer-members, a local cooperative must have the ability to enter into swaps with a member of its cooperative federation (or its subsidiary). In addition, the cooperative must have affordable access to the OTC market with other commercial counterparties. This allows the cooperative to aggregate the risk of offering forward contracts to farmers and swaps with its members.

For example, a local co-op may buy grain from farmers using a forward contract that has a guaranteed minimum price. These contracts can range in size from a truck load to barge load. By offering these contracts, local co-ops are exposed to higher prices, yet must guarantee a minimum price to the farmer if prices fall. To manage this risk local co-ops enter into swap contracts with its regional or federated cooperatives that aggregate quantities for volume discounts and favorable terms. The cooperatives in turn may use swaps with swap dealers to transfer their price risk and lock in their margins; effectively reducing the exposure of price risk from the entire supply chain of farmer to the regional or federated cooperative.

Agricultural cooperatives that enter into swaps with third parties (or members) in the course of marketing their member's agricultural products should be treated as end-users because any swaps they enter into are for the purpose of hedging the physical product that the cooperative is marketing on behalf of its members. An affiliate of an agricultural cooperative also should be entitled to rely on the end-user exemption to the extent it is executing swaps with third parties (or members) to hedge risks associated with products marketed by the cooperative.

Definitions of Swap Dealer and Major Swap Participant

As the Dodd-Frank Act is implemented, the regulations should clarify that, as end-users, farmer cooperatives are not captured under the rules as swap dealers or major swap participants (MSP). Not only are farmer cooperatives end-users for their primary business activities, but they are also end-users for the transactions that are used to offset the risk of aggregating producers' and member cooperatives' hedges.

Several factors making farmer-owned cooperatives swap end-users include:

- As with bona fide hedge exemptions, where the CFTC looks through the cooperative to the member's underlying physical position, the CFTC should treat both the member and the cooperative as end-users for purposes of derivatives regulation (cooperatives are considered bona fide hedgers on the Chicago Mercantile Exchange and are not subject to speculative trading limits).

- Our members enter into OTC swaps to hedge the price risk of the commodities they supply, process or handle; i.e. have a physical interest in the underlying asset. For example, swaps are entered into to hedge the price risk generated by cooperatives' clients forward pricing of sales.

- By entering into swaps to offset risk of aggregating member hedges, cooperatives are providing a service to their owner-members and not operating on a "for-profit" basis. Existing law requires cooperatives to distribute any positive net margins to back to their owner members in a fair and equitable manner.

- While cooperatives need to locate counterparties to take the other side of a swap, they are doing so to hedge commercial risk of their members, either directly at the farm or to help protect their investment in their cooperatively-owned businesses.

- A reasonable amount of agricultural inputs and products are not traded in a volume to meet the levels necessary for conventional futures market contracts. Swaps are often the only risk management option for those inputs and products.

- Entities that have a physical interest in the underlying commodity and that utilize swaps as a minority percentage of their total derivates portfolio should fall under the de minimus exception.

Eligible Contract Participant

The current CFTC definition of Eligible Contract Participant (ECP) as outlined in section 1a(18)(A)(v) "a corporation, partnership, proprietorship, organization, trust, or other entity--" of the Commodity Exchange Act should be retained in the new regulations.

Conclusion

Farmer cooperatives are a critical component of U.S. agriculture, providing supply, processing, and marketing services to their farmer-members. Increasingly, producers depend on their cooperatives to provide them with the tools to manage price risk as volatility in commodity markets has increased. Derivatives not only allow cooperatives to hedge the commercial risk in their operations, these tools allow them to offer customized risk management tools to their member-owners. As the CFTC drafts regulations to implement the Dodd-Frank Act, we strongly encourage you take into account the unique nature of cooperatives and their future ability to provide risk management services to their producer-members.

We appreciate your consideration of the above points in drafting a proposed definitions rule.

Sincerely,

Charles F. Conner
President & CEO