December 11, 2023

The Honorable Michael S. Barr
Vice Chairman for Supervision
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue NW
Washington, DC 20551

The Honorable Martin J. Gruenberg
Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20499

Mr. Michael J. Hsu
Acting Comptroller of the Currency
The Office of the Comptroller of the Currency
400 7th Street, SW
Washington, DC 20219

Re: Comments on Regulatory Capital Rule: Large Banking Organizations and Banking Organizations with Significant Trading Activity, Docket ID OCC–2023–0008, Fed: Docket No. R–1813, RIN 7100–AG64, FDIC: RIN 3064–AF29, 88 Fed. Reg. 64028 (2023) and Regulatory Capital Rule: Risk-Based Capital Surcharges for Global Systemically Important Bank Holding Companies; Systemic Risk Report (FR Y-15), Docket No. R–1814, 88 Fed. Reg. 60385 (2023)

Dear Vice Chair Barr, Chairman Gruenberg, and Acting Comptroller Hsu:

Well-functioning derivatives markets are critical for hedging price risks in the agricultural supply chain. We are concerned that recent bank capital proposals will have unintended consequences for the health of US derivatives markets and make hedging significantly more expensive for all market participants. We urge you to reconsider the proposal and avoid taking actions that will harm end-users in the real economy.

Farmers, ranchers and other agricultural producers use derivatives such as futures and options to make sure that they cover their costs of production. On the other side of the market, companies that process agricultural products into food, fiber and biofuels use derivatives to protect their profit margins from a steep increase in their input costs. Both sides depend on well-functioning derivatives markets to hedge their risks.

Central clearing is a core component of derivatives markets. Central clearing reduces counterparty risk and allows end-users to trade these contracts without fear of loss if their counterparty defaults. Central clearing has been a mainstay of the agricultural futures markets for more than a century, and its importance to financial stability and market functioning was validated by the G20 leaders in the aftermath of the financial crisis of 2008.

The strength of central clearing depends, however, on the participation of banks and other institutions as members of clearinghouses. They provide the majority of the financial resources that support the clearing system, and they guarantee the performance of the trades they clear. This is an expensive business, and we are concerned that two recent capital proposals will make it even more expensive.

For agricultural end-users, hedging is like insurance – it is a cost they are willing to pay for protection against price volatility. But not at any price. If the cost of using cleared derivatives rises too high, they will switch to using uncleared derivatives, or simply abandon hedging. Furthermore, there is already a shortage of firms available to provide clearing services to agricultural end-users, and these proposals could reduce the number even more.

According to data from the Commodity Futures Trading Commission, the number of futures commission merchants that clear exchange-traded derivatives for clients has fallen by 50% over the past 20 years. We see a similar trend in the more specialized business of clearing interest rate swaps and other over-the-counter derivatives. In 2014, there were 22 firms clearing these contracts for clients. Today there are 12.

The two recent capital proposals -- the US Federal Reserve GSIB Surcharge Proposal and the US Basel III Endgame Proposal – are likely to have a significant impact on the availability of clearing services in the US. Although the proposals only affect banking organizations – and there are some non-bank financial institutions that provide clearing services – the majority of the clearing firms in the US are banks. According to CFTC data, two thirds of all customer funds in the US clearing system are held by US banks.

There are many types of commercial entities that use derivatives, including asset managers, pension funds, insurance companies, energy producers and auto manufacturers. We are very concerned that any contraction in the availability of clearing services will have a disproportionate impact on agricultural end-users that are far outside the major financial centers, especially smaller entities such as grain elevators and family farms. We urge you to modify the proposals so that they do not disincentivize banks from providing this important service to their customers.

Sincerely,

National Council of Farmer Cooperatives
Commodity Markets Council
National Cattlemen's Beef Association
National Grain and Feed Association
American Farm Bureau Federation
National Milk Producers Federation
National Pork Producers Council
American Cotton Shippers Association
Farm Credit Council