98-6

COMMENT 2

The Andersons

The Andersons, Inc.
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March 13, 1998

Ms. Jean Webb
Secretary of Commission
Commodity Futures Trading Commission
Three Lafayette Center
1155 21st Street, N. W.
Washington, D.C. 20581

Dear Jean:

The following is the response of The Andersons, Inc. to the Federal Register dated January 28, 1998, requesting information relative to exchanges of futures for physicals.

This response is directed to the agriculture markets only. As the Commission knows, EFP activity as a share of trading volume has been relatively stable in the agriculture markets. This has not been the case in financial futures markets where EFP activity continues to increase, dramatically in some cases. Again, it should be noted that our comments are related exclusively to the agriculture markets only, as that is our primary area of expertise.

The following is a list of responses to several of the questions asked by the Commission:

1. *Question:* How should the "strong price correlation standard" articulated in the EFP report be implemented?

   Answer: The report states that the cash commodity should have a reliable and demonstrable price relationship with the futures contract. The cash leg should exhibit price movement that historically has paralleled the price movement of the futures contract. To the degree this paralleled price movement is present, we believe that a futures exchange to price a transaction in an underlying physical commodity is acceptable if done within the price range established during the life of the futures contract. Exchanging futures at any price level before or after the life of the cash contract is a violation of the intent of the rule.

2. *Question:* Should the Commission require contract markets to adopt a minimum statistical correlation coefficient to be used in assessing the acceptability of a particular cash commodity for use as the cash leg of the EFP report?

   Answer: No.

3. *Question:* Should the Commission address string trading as that practice is described in the EFP report?

   Answer: No.

4. ***Question***: What Criteria is appropriate for judging whether the futures leg of an EFP is bona fide?

   Answer: For an EFP to be a bona fide exchange for physicals, a cash contract transaction must occur simultaneously with the exchange of futures.

5. ***Question***: Should the Commission require both the futures and the cash leg of an EFP to be priced within the daily range of their current respective markets?

   Answer: We have answered this question in our first response by stating that we believe exchanges of futures to price cash transactions should be at a price level that falls within the life of the futures contract.

6. ***Question:*** Should the Commission require contract markets to obtain documentation regarding the business purpose underlying an EFP?

   Answer: We believe that requiring contract markets to obtain documentation of the business purpose underlying an EFP transaction would be unnecessary and additive to costs. The cost to the exchanges and market participants in collecting this documentation would be unnecessarily burdensome relative to the benefits that such a collection of data would provide to the market as a whole. We also believe that disclosure of all cash transactions in such a fashion could lead to misuses of this information within the trade. The current system of spot checking these transactions to ensure proper cash reasons for the EFP is the most prudent path of oversight.

7. ***Question:*** Are the current reporting and record keeping requirements related to EFP's adequate?

   Answer: Yes.

8. ***Question:*** What should be the form and content of risk disclosure concerning EFP's?

   Answer: Commercial participants who engage in cash commodity transactions as a regular course of business should be exempt from unnecessary regulation.

9. ***Question:*** What internal controls are appropriate for the Commission registrants to insure compliance with regulatory requirements concerning the essential element of bona fide EFP reporting, record keeping and disclosure?

   Answer: Today's rules call for diligent supervision of the handling by its partners, officers, employees and agents of all commodity interest accounts carried, operated, advanced or introduced by the Commission registrants. We believe this to be sufficient.

10. ***Question:*** Do existing price reporting standards provide adequate transparency concerning EFP's to the marketplace and if not are there alternative methods of achieving improve price transparency?

    Answer: Exchange of futures is part of a private cash transaction and should not be disclosed to the public. This is part of our concern stated above in answering the Commission's question regarding mandatory documentation of cash transactions involving an EFP. The disclosure of private cash transactions beyond the participating parties would not be in the best interest of the trade as a whole.

11. Question: The Commission has a number of questions about the exchange of options for physicals, block trades and swaps as a new area that ESP's may be used.

Answer: The Andersons, Inc has had very limited use of option and swaps. However, I might leave this introductory comment out of the response. We cannot see any reasons why the use of options, block trades or swaps would distort the marketplace. As a matter of fact we believe it could, and should, add value. We believe the over-the-counter activity, for example, has added volume to the regulated exchange volume.

12. Question: Should exchange options for physicals be permitted?

Answer: Yes. A market participant may begin a pricing strategy with the use of an option position. Later the participant may enter into a cash commitment for delivery to another market participant. Then the participant may want to exchange his option position to the cash participant holding the cash commitment to establish a minimum pricing strategy or other pricing strategies which incorporates pricing flexibility into the formula pricing mechanism for the cash contract.

13. Question: Should alternative, non-competition executive procedures be permitted?

Answer: We do not believe that this approach is necessary for the agricultural markets. Price discovery, liquidity, manipulation, mis-pricing, and front-running are all areas of concern.

The Andersons, Inc. has chosen not to address all of the questions posed by the Commission in the January 28, 1998 Federal Register's request for comment on this topic. Rather, we have chosen to provide the Commission with feedback on the particular questions, which specifically impact the agricultural markets. We are hopeful that our answers provide insight for the Commission in dealing with the (re)definition of EFP procedures.

Sincerely,
The Andersons, Inc.

William A. Dodds
Merchandising Manager
Grain Division

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