



## **H.R. 2289, the Commodity End-User Relief Act**

***To reauthorize the Commodity Futures Trading Commission and ensure robust markets, customer protections, and a balanced approach to regulations impacting job creators.***

### **Overview**

The Commodity Futures Trading Commission (CFTC) was last reauthorized in the Food, Conservation, and Energy Act of 2008, also known as the 2008 Farm Bill, for a period of five years. The authority expired on September 30, 2013.

Derivative contracts—commodity futures, options, and swaps—are used by business owners across America to manage the risks they face and protect their companies, customers, and shareholders from unexpected changes in an uncertain global economy. These end-users, and the challenges they face managing their legitimate hedging needs, served as a backdrop for the Committee’s consideration of what changes to make when reauthorizing the CFTC.

In advance of writing legislation to reauthorize the CFTC, the House Agriculture Committee, together with its Subcommittee on Commodity Exchanges, Energy and Credit, held four hearings on the future of the Commission. The Committee heard testimony from each segment of the futures and swaps markets—from end-users to regulators—on how to make derivatives markets work better for those who need them most: businesses trying to manage their risks.

In addition, the Committee built upon the many hearings and oversight activities done in the 112<sup>th</sup> and 113<sup>th</sup> Congresses, which culminated in a bipartisan CFTC reauthorization bill. That bill, H.R. 4413, the Customer Protection and End-User Relief Act, passed the House with strong bipartisan support. The Commodity End-User Relief Act of 2015 mirrors the language in H.R. 4413.

Many of the important reforms to derivatives markets following the 2008 financial crisis have impacted end-users unintentionally, and some of the rules imposed have been implemented in unexpected ways. Despite Congress’ explicit instructions to exempt end-users from many of the costliest and complicated regulations, end-users still face unnecessary changes to customary business practices that serve little purpose but to regulate for the sake of regulating.

H.R. 2289, the Commodity End-User Relief Act, is bipartisan legislation to reauthorize and improve the operations of the CFTC, as well as improve customer protections in the wake of failures such as MF Global and Peregrine Financial. The bill was introduced by Rep. K. Michael Conaway, Chairman of the House Agriculture Committee, Rep. Austin Scott, Chairman of the Subcommittee on Commodity Exchanges, Energy and Credit, and Rep. David Scott, Ranking Member of the Subcommittee on Commodity Exchanges, Energy and Credit.

# Title I — Customer Protections

H.R. 2289, the Commodity End-User Relief Act will better protect farmers and ranchers who use the futures markets by cementing several new regulatory customer protections into law.

Added protections include mandates to:

- Require regulators to electronically confirm customer fund account balances held at depository institutions. This eliminates the flawed reporting system that allowed the management of Peregrine Financial to use forged paper documents to steal millions of dollars of customers' money.
- Require firms that move more than a certain percentage of customer funds from one account to another to follow strict reporting and permission requirements before doing so. This provides a new safeguard to prevent a firm from moving funds from one account to another, without regulators knowing about it, as happened during the MF Global bankruptcy.
- Require firms who become undercapitalized to immediately notify regulators so they can assess the firm's viability and act, if needed, to protect customer funds.
- Require firms to file an annual report with regulators from the chief compliance officer containing an assessment of a futures commission merchant's (FCM) internal compliance programs.
- Ensure farmers, ranchers, and other futures customers have a full business day to send their margin payments to an FCM, which mitigates costs of over-funding accounts.
- Provide legal clarity for futures customers that the assets of a bankrupt commodity broker would be used to help pay back any misappropriated or illegally transferred customer segregated funds.

## **Title II — Commodity Futures Trading Commission Reforms**

In the past five years, the CFTC has finalized approximately 50 rules to enforce the new law. In that time span, the CFTC has also issued an unprecedented 250 “no-action” letters, 42 exemptive letters and 42 statements of guidance, interpretation and advice in order to delay, revise, or exempt the application of these regulations upon various market participants. This haphazard patchwork of exemptions has been widely used in lieu of a thorough and well-reasoned rulemaking process. H.R. 2289 reauthorizes the CFTC through 2019 and makes reforms to CFTC operations to help ensure that all Commissioners’ voices are heard as a part of a more deliberative rulemaking process. These reforms include:

- Modifying the Commodity Exchange Act’s (CEA’s) cost-benefit analysis requirements for proposed rules, to more closely track those set forth in Executive Order 13563.
- Making the Commission’s division directors answerable to the entire Commission, not just the Chairman’s office.
- Creating a new Office of the Chief Economist, answerable to the entire Commission, to provide objective economic data and analysis.
- Enhancing the CFTC staff procedures governing the issuance of “no-action” letters to improve Commissioners’ oversight of the activities happening outside the official rulemaking process.
- Requiring the CFTC to develop a strategic technology plan every five years focused on market surveillance and risk detection, which must also include a detailed accounting of how funds provided for technology will be used.
- Requiring the Commission and the Office of the Chief Economist to develop comprehensive internal risk control mechanisms to safeguard market data.
- Ensuring that every Commissioner has a seat at the table in approving omnibus orders of investigation that authorize the issuance of subpoenas.
- Creating a judicial review process similar to that of the SEC’s for rulemakings to ensure the two regulators charged with overseeing the derivatives markets have similar procedures in place to allow market participants to challenge Commission rules.
- Prohibiting the Commission from issuing policy statements, guidance, interpretive rules, or other procedural rules that have the ultimate effect of law, without providing the public the notice and the opportunity to comment as required in the Administrative Procedure Act.
- Directing the Government Accountability Office (GAO) to conduct a study on the sufficiency of CFTC resources and examine prior expenditures of funds on market surveillance and market data collection, standardization, and harmonization. The study will also explore areas where self-regulatory organizations could reduce the CFTC’s workload.

## Title III — End-User Relief

Title III of the Commodity End-User Relief addresses the concerns shared with the Committee by many end-users over the past four years. These market participants are not investors, speculators or risk-takers, yet they have borne the brunt of many of the consequences of our new regulations. Agricultural producers, manufacturers, electric and gas utilities, and pension plans have each testified about how their business are facing new barriers to entering these markets—from increased transaction costs, to increased compliance burdens, to fewer trading partners.

Title III addresses the following concerns:

- Companies using centralized treasury units to manage and offset the risk of their affiliates will no longer be subject to burdensome and unnecessary clearing requirements.
- Trusted foreign regulators should not—and often cannot—be required to indemnify the CFTC for costs associated with the loss of data from a U.S. Swap Data Repository. The legal concept of indemnification does not exist within the tort law of all foreign jurisdictions. The bill removes that unworkable provision of the CEA, while maintaining the requirement for written confidentiality agreements.
- Government-owned utilities should not be deterred from entering into swaps with non-financial counterparties, such as natural gas producers and independent power generators, in order to hedge against operational risk. The bill codifies municipal utility companies' cost-effective access to the customized, non-financial commodity swaps that utility special entities have used for years.
- Commercial end-users should not be classified and treated like banks, and the bill fixes the definition of “financial entity” to ensure that they are not.
- Non-financial end-users should not be disadvantaged in the marketplace if they use contracts that trade so infrequently that other market participants can identify them through the new public reporting requirements. The bill would ensure that end-users hedging in thinly-traded markets are provided adequate time between completing and reporting a transaction to protect their position.
- Grain elevators, farmers, agriculture counterparties, and commercial market participants should not be subject to overreaching recordkeeping rules that require the recording of all forms of communication that may possibly lead to a trade. The bill specifies that keeping written records of the final material economic terms of an agreement will be sufficient for market participants who are only managing their own money.

- Contracts that contain an option to change the amount of a commodity delivered, but result in actual physical delivery of a commodity should not be regulated as swaps. This impacts utilities that use natural gas to produce electricity, in addition to millions of consumers who use natural gas to heat their homes.
- Non-bank swap dealers should not be required to hold exponentially more capital than their bank counterparts. This bill would ensure that swap dealers without a prudential regulator would be able to use workable capital requirement formulas.
- On December 31, 2017, the *de minimis* exception from the swap dealer definition will be reduced by \$5 billion because several years ago, the Commission arbitrarily decided it should. The bill will require a vote on a new regulation to change the current threshold, after the Commission completes a planned study on the issue.
- An oversight in the JOBS Act should not prohibit funds also registered as Commodity Pools from soliciting certain potential new investors. The bill makes a conforming change to CFTC regulations to bring them in line with the JOBS Act.
- End-users' ability to hedge against anticipated business risks should not be limited by the CFTC's arbitrary narrowing of acceptable hedging activities. The bill provides a more workable definition of *bona fide* hedging as it relates to position limits.
- In 50 rulemakings, the Commission still has not set out a rule that defines who is subject to U.S. rules, who is not subject to U.S. rules, and what to do when international rules conflict. The bill would require the CFTC to finally put in place a comprehensive plan for how to address the international nature of swaps trading and to determine how to share regulatory obligations over transactions that cross international boundaries.

## **Title IV — Technical Corrections**

Working with the CFTC, House Legislative Counsel, and market participants, the Committee has prepared a section of technical edits and changes to the Commodity Exchange Act which correct references, remove obsolete terms, comport ambiguous text to existing practices, fix formatting errors, and remove a study due to Congress in 1986.

## Past Committee Activity

Many of the policy objectives within Title III were set forth in the following measures that passed the House Agriculture Committee and/or the U.S. House of Representatives with overwhelming bipartisan support in the 113<sup>th</sup> Congress:

- An amended bipartisan version of H.R. 677, the Inter-affiliate Swap Clarification Act, which originally was passed by House Agriculture Committee on March 20, 2013 by voice vote and by the Financial Services Committee on May 7, 2013, by a vote of 50-10.
- H.R. 742, the Swap Data Repository and Clearinghouse Indemnification Act that passed the House on June 12, 2013, by a vote of 420-2.
- H.R. 1038, the Public Power Risk Management Act that passed the House on June 12, 2013, by a vote of 423-0.
- H.R. 1256, the Swap Jurisdiction Certainty Act that passed the House on June 12, 2013, by a vote of 301-124.
- H.R. 4413, the Customer Protection and End-User Relief Act that passed the House on June 24, 2014, by a vote of 265-144.
- H.R. 5471, To amend the Commodity Exchange Act and the Securities Exchange Act of 1934 to specify how clearing requirements apply to certain affiliate transactions, and for other purposes, passed by the House on December 2, 2014, by voice vote.

During the 113<sup>th</sup> Congress, the House Agriculture Committee also held four hearings to gather input from CFTC Commissioners, end-users, and a variety of market participants in preparation for legislation to reauthorize the CFTC. The Committee also held a legislative hearing to examine seven legislative proposals to improve Title VII of the Dodd-Frank Act. Two of those measures were eventually signed into law and the remaining five were individually passed by the House with bipartisan support, and/or were included in H.R. 4413, the Customer Protection and End-User Relief Act which also passed the House with bipartisan support.

In the 112<sup>th</sup> Congress, the Committee also considered a variety of bills addressing concerns similar to those addressed in the Commodity End-User Relief Act of 2015. Those bills included:

- H.R. 1573, To facilitate implementation of title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, promote regulatory coordination, and avoid market disruption, that was ordered reported out of Committee on May 4, 2011.
- H.R. 1840, To improve consideration by the Commodity Futures Trading Commission of the costs and benefits of its regulations and orders, that was ordered reported out of Committee on January 25, 2012.
- H.R. 2682, the Business Risk Mitigation and Price Stabilization Act of 2012, that was ordered reported out of Committee on January 25, 2012.
- H.R. 2779, To exempt inter-affiliate swaps from certain regulatory requirements put in place by the Dodd-Frank Wall Street Reform and Consumer Protection Act, that passed the House on March 26, 2012, by a vote of 357-36.

- H.R. 2586, the Swap Execution Facility Clarification Act, that was ordered reported out of Committee on January 25, 2012.
- H.R. 3336, the Small Business Credit Availability Act, that passed the House on April 26, 2012, by a vote of 312-111.
- H.R. 3527, the Protecting Main Street End-Users From Excessive Regulation, was ordered reported out of Committee on January 25, 2012.

During the 112<sup>th</sup> Congress, the Committee was the first to hear testimony from Jon Corzine following the collapse of MF Global, and later heard the views of foreign regulators regarding the cross-border application of U.S. swaps rules. The Committee held an additional 10 hearings regarding derivatives markets, end-users, and the implementation of Title VII of the Dodd-Frank Act.