National Grain and Feed Association

1250 Eye St., N.W., Suite 1003, Washington, D.C. 20005-3922, Phone: (202) 289-0873, FAX: (202) 289-5388, Web Site: www.ngfa.org

TESTIMONY OF THE
NATIONAL GRAIN AND FEED ASSOCIATION
TO THE
COMMITTEE ON AGRICULTURE
U.S. HOUSE OF REPRESENTATIVES
December 8, 2011

Good morning, Chairman Lucas, ranking member Peterson, and members of the committee. My name is John Fletcher. I am General Manager of Central Missouri Agri-Service LLC in Marshall, Missouri. Our firm purchases about 15 million bushels of corn and soybenas annually from 100-150 producers in our trade territory, with whom we work closely on marketing and risk management strategies. We also provide a range of feed, fertilizer, seed and crop protection products and services to our farmer-customers. Thank you for the opportunity today to provide the NGFA's perspective on the MF Global bankruptcy and its ripple effects across agribusiness and production agriculture.

My firm is a member of the National Grain and Feed Association (NGFA), the national non-profit trade association representing agribusinesses that include grain elevators, feed manufacturers, oilseed processors, flour mills, biofuels producers and related businesses. We estimate that the 1,050 NGFA-member firms nationwide operate more than 7,000 facilities and purchase, store, process and export well in excess of 70% of U.S. annual grains and oilseeds production. Many of our member firms are country elevators that work very closely with their farmer-customers to merchandise their crops and manage their risk.

The MF Global Holdings bankruptcy has been a shock to our industry and to our firm. We have believed for decades that risk to segregated customer funds held by members of the clearinghouse was virtually zero. Now, we know that was not the case.

Immediately following the October 31 bankruptcy filing, MF Global customers struggled with lack of access to futures positions, no access to funds in their accounts, having accounts transferred to new futures commission merchants (FCMs), and understanding how and why various adjustments to account balances took place. In those early days, there was a dearth of information to help customers manage their financial exposure and resume normal risk management activities.

Today, former MF Global customers continue to deal with the aftermath of the situation. Customers now have access to hedge accounts, but only about sixty percent of initial margin funds needed for the transferred positions have been transferred to the new accounts. We welcomed the SIPA trustee's proposal last week for an additional distribution of funds and property that would bring the value of customer distributions to about two-thirds of original account values for all customers. However, many firms still will have significant amounts of margin funds and excess cash tied up with the trustee – or missing. Even at a relatively small firm like Central Missouri Agri-Service, we are trying to manage a $600,000 deficit in the value of our account. We are fortunate to have close relationships with our lenders, who have responded with strong support of their ag sector customers.

We were pleased to see that the trustee recently announced a claims process for former commodities customers of MF Global. However, that process looks to be complicated and cumbersome. Even the seemingly simple task of informing the trustee of the amount a commodities customer is claiming is not straightforward. Should a customer use his account equity on October 31 when the bankruptcy was filed to establish a claim? Or should that customer use the account equity at the close of business four days later when the bulk account transfer took place? The difference can be hundreds of thousands of dollars. We need clarification from the trustee and the exchanges on proper reporting of such claims.

Ultimately, the number one goal of the NGFA is to advocate the return of funds and property to customers as quickly as possible. By law, these customer funds were to be segregated and not used for other purposes. Title documents like warehouse receipts are property of specific customers and should be returned without requiring a surcharge for customers to buy back their own property. At the end of this process, customers must be made whole – any other outcome will result in a damaging loss of confidence in our risk management system. We urge this committee, regulators and exchanges, and the trustee to make return of customer funds and property the highest priority.

Make no mistake – the U.S. risk management system for agribusiness and producers has been one of the industry's strengths and competitive advantages over the last century. The ability to hedge risk on an exchange has allowed thousands of businesses like mine to offer producers a wide range of cash forward contracts that help optimize income from markets. Many individual producers also hedge their risk through use of futures and options on a regulated exchange. To this point, we have done so with confidence. We knew we could lose money on a trade, but we also thought we knew that our funds were safe with a member of the clearinghouse.

Looking ahead, it will be very important to re-establish confidence in futures markets and the safety of segregated customer funds and property. As part of that process, we need to know just what happened at MF Global and whether changes need to be made so that producers and agribusiness – as well as their lenders who support the entire risk management process – are confident that their funds are being protected and always will be available.

We suggest that serious questions need to be answered by regulators and the self-regulatory organizations they oversee. What customer protections currently are in place to safeguard segregated customer funds? Were audit procedures properly implemented in a timely way? How often were accounts audited, and who was responsible for enforcing compliance? Questions like these need to be examined to determine exactly what happened and how customer funds apparently were misappropriated.

Very importantly, changes may be needed to begin restoring confidence in future use of exchange-traded risk management tools. Weaknesses in customer protections brought to light by MF Global's failure have left customers unsure of whether segregated funds will continue to be fully available. It may be that some entity other than FCMs should be responsible for holding and safeguarding segregated customer funds. Rather than a clearing firm, should the clearinghouse or the exchange itself or some independent third party perform that role? Should SIPC insurance be expanded to provide coverage for commodities as well as securities? Or is there some private-sector solution that would better provide insurance against any future losses? Are changes needed in the ways segregated customer funds are allowed to be invested? Should exchanges bear some responsibility for customer funds lost in the case of bankruptcy and/or malfeasance by a clearing member?

We make no judgments or recommendations on these questions today – and to be clear, we are not proposing that legislation or additional regulatory authority are needed – but the issues need to be examined carefully and quickly.

Ultimately, our goals are twofold: to pursue all possible actions that will ensure that assets of MF Global customers will be returned quickly, and to make sure this situation never happens again. The U.S. agricultural sector relies heavily on regulated exchanges for risk management. The ability of both commercial and producer hedgers to use futures markets to manage price risk depends on lenders agreeing to meet margin calls, which demands full confidence by all lenders in the safety of those funds. We must be confident the system works, that it properly safeguards customer funds, and that customers can have full confidence in continuing to utilize exchange-traded tools.

Again, the NGFA appreciates the opportunity to share its views today. That concludes my prepared remarks, Mr. Chairman. I would be happy to respond to any questions.

John Fletcher
Professional Bio

John Fletcher is a founder and is General Manager of Central Missouri AGRIService LLC. (CMAS) CMAS is a part of a larger multi faceted agricultural business in the Midwest consisting of Grain Elevators, Feed Mills, Retail Agronomy, Fertilizer Terminals, and Transportation operations. Prior to becoming General Manager of CMAS, Mr. Fletcher managed the trading and transportation segments of one of the member companies of CMAS.

Fletcher has served on the Board of Directors and Executive Committee of the National Grain and Feed Association, the leading industry organization representing the grain and feed industry in Washington DC. He has served as Chairman of NGFA's Country Elevator Committee and currently serves as Chairman of NGFA's PAC Committee

Fletcher has also served as a member of the board of Directors of the Missouri Agri-business association, has served as a city councilman and Mayor Pro-tem of the City of Marshall, Missouri, and currently serves as the Board Chairman of Saline County E911. He is treasurer of Arrow Rock Lyceum Theatre, an organization that produces professional theatre for thirty thousand patrons a year in a town of 125 people.

Fletcher has provided congressional testimony on the operation and implementation by USDA of US farm policy. Mr. Fletcher received his BS in Economics with honours at Missouri Valley College in 1978. Fletcher and his wife Patricia have 4 grown children and 10 grandchildren.