



NATIONAL CATTLEMEN'S BEEF ASSOCIATION

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February 21, 2000

COMMENT

Jean A. Webb
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

**Received CFTC
Records Section**

FEB 22 PM 3 44

RE: Proposed Revision of the Commission's Procedure for the Review of Contract Market Rules

Ms. Webb:

Initiated in 1898, the National Cattlemen's Beef Association is the trade association of America's cattle farmers and ranchers, and the marketing organization for the largest segment of the nation's food and fiber industry. NCBA is producer-directed but consumer-focused, with offices in Denver, Chicago and Washington D.C. The National Cattlemen's Beef Association (NCBA) appreciates the opportunity to comment on this proposed rule.

The NCBA will address specific concerns our members have with this proposed rule. Secondly, we will respond to the "Request for Comment" section of the proposed rule as requested by CFTC. From the outset, NCBA policy clearly supports the CFTC as the sole regulator of the commodity trading industry. Additionally, NCBA will oppose any legislation or regulatory action that would not allow reasonable opportunity for input from the cattle industry on futures contract changes. Based on this policy, NCBA is **opposed** to this proposed rule because opportunity for input by beef producers is not assured. Comments made by NCBA in response to specific CFTC "Requests for Comment" in the proposed rule should not be construed as meaning the NCBA supports this rule in whole or in part.

NCBA Concerns with the Proposed Rule

The National Cattlemen's Beef Association (NCBA) is concerned with the broad authority this proposed rule would grant to the exchanges. The Commission voiced concerns over how this rule would apply to contracts with open interest. The NCBA is surprised that CFTC concerns with this rule would be limited to questions regarding open interest. The NCBA, while supportive of less regulation and not more, would prefer that deregulation be done in a manner that encourages direct competition. NCBA is concerned that this proposed rule will create a system in which one party is able to exercise leverage over other parties without CFTC oversight, without the benefit of competitive market discipline, and without opportunity for input from the cattle industry on contract changes.

Broad Authority

Of great concern to NCBA and to our members who actively trade, hedge and deliver live cattle is the potential for removal of the CFTC from the rule modification and approval process. This issue was addressed by several of the agricultural organizations at the December 8th meeting of the Agriculture Advisory Committee (AAC). Members of the AAC that are closely affiliated with the exchanges assured the agriculture producer groups that the exchanges would behave in a responsible manner with this authority. However, it is not the past or current behavior on the part of the exchanges that we are concerned about, it is the authority that this rule would grant and the behavior modification that this rule could engender.

When the marketplace has required futures contract rule changes, the various industry segments and the exchanges have worked together to craft rules and important rule changes beneficial to all parties. The most recent changes in the corn contract delivery points are a prime example of this interaction. Further, NCBA will support immediate rule changes if egregious harm or competitive inequities exist. The CFTC also has the authority to investigate rules that harm participants and to stay the implementation of rules that cause harm. For these reasons, the need for exchanges to have the unhindered authority to make rule changes with one days notice, as proposed in this rule, does not seem warranted or necessary at this time. Under current procedures, the CFTC is the arbiter for rule changes. Under 1.41(z), exchanges would become the authority as far as contract rule changes are concerned and there is no guarantee, implicit or otherwise, that beef producer concerns would be included in the exchange decision making process.

A current situation will demonstrate NCBA's concern with this proposed rule. It is well known by the Chicago Mercantile Exchange, Congress and the CFTC that the beef industry and NCBA have been seeking for many years several rule changes to the Live Cattle contract. We have been in a virtual impasse with the CME. These rule changes include allowing heifer delivery and removing the inequity that exists between cattle delivered live (on the hoof) and cattle delivered as carcasses (on the rail). Simultaneously, members of the CME would like to increase the speculative limits that are currently in place on the front month of the live cattle contract. A change the beef industry opposes. At the time of submission of these comments, the CFTC is also accepting public comments on the CME's request to increase the front month speculative limits on the Live Cattle contract. To date, the NCBA has been unable to persuade the CME to address our proposed delivery rule changes while it is evident they are moving ever closer to increasing the speculative limits.

Our proposed changes would increase deliverable supply, increase likelihood of convergence, improve price discovery, reduce volatility, and improve producer confidence in the marketplace. Increasing front month speculative limits would increase basis volatility and give undue leverage to the long speculator during the delivery process. The CME's proposed change would further reinforce producer distrust of the markets. If 1.41(z) were final, increased speculative limits would already be a done deal and the CFTC would not have had the opportunity to review the concerns of a majority of participants of the market before the changes took place.

If this rule, as published by the CFTC becomes final, the CME's Live Cattle Committee becomes the ultimate arbiter in this discussion. Decisions of the Live Cattle committee will be driven by the financial interests of individual live cattle committee members and commission-paying speculators—not by improved price discovery for live cattle, the interests of producers of the underlying physical commodity, or increased producer confidence in the market.

Judicial Review

As published, Section 1.41(z) states, "Exemption from the rule review procedure requirements of Section 5a(a)(12) of the Act and related regulations." One of the statutory clauses in Section 5a(a)(12) concerning rule review and approval is "The determination by the Commission whether any such rules are of major economic significance shall be final and not subject to judicial review." The NCBA believes there is absence of clarity in the proposed rule about how broadly the CFTC will interpret the phrase "rule review procedure requirements" of 1.41(z). Will 1.41(z) supercede all of 5a(a)(12) or will it simply supercede sections that can be strictly interpreted as part of "rule review"? If interpreted strictly, what remains of the statutory exemption from judicial review that is created when the CFTC makes a "determination", as defined in Section 5a(a)(12)? For rule changes made under Section 1.41(z), no approval or determination would ever be made by the CFTC. What would be the status of the exemption from judicial review under this scenario?

If this rule is adopted, the NCBA believes that exemptions from judicial review should be removed for all rule changes made under Section 1.41(z). Additionally, any contract rule change without official "approval" by CFTC must not be exempt from judicial review.

"Substantive Opposing Views"

As written, the proposed rule would allow rule changes to take affect one day after submission to the CFTC. This submission should include a brief explanation and any substantive opposing views. What does the Commission mean by "substantive opposing views"? If the exchange decides to change a rule, than any opposing views must not be substantive. If there were substantive opposing views would that not change the decision to change the rule? Under 1.41(z), who decides what is substantive? Under the current procedure, the CFTC decides what is substantive and what is not. This proposed rule would allow the exchanges and their rule committees to be the judge and jury on what issues constitute substance.

Would the CFTC consider the beef industry's concerns with the aforementioned speculative limits issue "substantive"?

Legal Certainty

The NCBA fully supports legal certainty for parties that engage in futures activity. Legal certainty is of even greater concern when futures contract markets consider rule changes under 1.41(z). Notwithstanding the rule enforcement obligations of Section 5a(a)(8) of the Act, the

NCBA would like additional clarity on how the CFTC would enforce contract rules that are at some point deemed illegal. For example, if a contract market makes a rule change under 1.41(z), and buyers and sellers trade based on the terms of this rule change, and subsequently the rule change is deemed by CFTC under 1.41(z)(2)(ii) to need revision--what is the legal standing and recourse of the parties given that the contract shall not be void or voidable under 1.41(z)(2)?

Distinction from Regulation 5.3

The CFTC has now published regulation 5.3 in its final form. As the Commission well knows, this regulation will allow exchanges to list commodity futures or option contracts for trading without Commission approval of the contract or its terms and conditions, including any subsequent amendments thereto. Like the CFTC, the NCBA believes 5.3 will enable the exchanges to develop new contracts as the market changes and opportunities for new contracts evolve. The exchanges will list new contracts and the marketplace will decide if it wants to trade in these items. However, proposed rule 1.41(z) would apply directly to currently traded contracts such as the Live Cattle contract that has a long history of use and confidence on market makers. It does not appear that 1.41(z) would create the same level of competition that could result from 5.3. Regulation 5.3 clearly opens the door for increased competition between domestic and foreign exchanges. It is not clear that 1.41(z) will increase competition between exchanges for existing commodity futures contracts.

Responses to CFTC's "Request for Comments"

Exclusivity of Regulation 14.1(z) Process

The NCBA believes that, should this proposed rule be adopted, the CFTC should maintain the current practice of reviewing proposed rule changes, consistent with Regulation 1.41(b) and 1.41(c). A submission to the CFTC for review under these regulations provides feedback from the Commission to the exchange and provides a window of opportunity for interested parties to review the request made by the exchange. In the proposed rule, the Commission states that "the existence of these various rule review procedures may create confusion for market participants..." Notwithstanding the fact that confusion may indeed occur, the NCBA perceives that review by CFTC of an exchange proposed contract rule change will be of more value to producers than confusion will be a detriment.

The exchanges would have the option for CFTC review under 1.41(b) and 1.41(c) or they could adopt contract rule changes under 1.41(z) without prior approval. Depending upon the situation and potential impact of any contract rule change on market participants, the exchange could best decide which method of changing contract rules would be in the best interest of the exchange, exchange members and all concerned market participants.

The option to review contract rule changes under 1.41(b) and 1.41(c) should apply to all proposed contract rule changes including rule changes that would apply under proposed Regulation 1.41(z) and 5.3

Suspension of Effectiveness of a Rule

If the proposed rule is adopted, the Commission should maintain the authority to stay or suspend the operation of an exchange rule if the contract rule is causing harm to market participants once the Commission has begun a review proceeding under Section 5a(a)(10), 5a(a)(12), 8a(7) or 8a(9) of the Act.

Contracts with Open Interest

No rule changes should be allowed for contracts with open interest under this or any other proposed regulation the Commission might promulgate. Changes in contract rules should be allowed only for contract months of existing commodity futures and option contracts that have not yet begun trading. Rule changes should not take affect until the opening day of trading of that contract month and on contract months thereafter.

If an existing contract rule is causing harm to market participants, then the commission has the authority under Section 5a(a)(10), 5a(a)(12), 8a(7) or 8a(9) of the Act to suspend or stay operation of an exchange rule.

Emergency Rules

If this rule is adopted as published, it would appear that proposed rule 1.41(z) would indeed obviate the need for emergency rule changes under Section 5(a)(12)(b). The NCBA can make no distinction between an emergency rule change and any rule change that might be made under proposed regulation 1.41(z).

New Electronic Trading Systems

Regulation of electronic trading systems should be flexible to take into account the ability to collect real-time data and the uniqueness of electronic mediums. The NCBA supports a regulatory structure on electronic trading systems that is no more restrictive than that for pit or open outcry trades. Regulation of electronic systems should be less restrictive because real time information could be gathered more easily using an electronic audit trail characteristic of electronic systems.

Increased regulatory flexibility is crucial to encourage new competition and new entry into the industry and for the survival of creative and visionary entrepreneurs. It is critical that the CFTC have authorization to be innovative and flexible from a regulatory standpoint. NCBA will work with industry, the CFTC and Congress to determine how much flexibility the Commission needs to address the changing technological environment. Given this regulatory agility, the CFTC can encourage, and not impede, those who think outside of the traditional box.

Thank you again for the opportunity to comments on this proposed rule. Please do not hesitate to contact us if the CFTC has further questions regarding our comments or our position on this proposed rule.

Sincerely,

A handwritten signature in cursive script that reads "Lemmy Wilson". The signature is written in black ink and is positioned to the right of the word "Sincerely,".

Lemmy Wilson
Chairman
NCBA Live Cattle Marketing Committee