MINUTES OF THE THIRY-SIXTH MEETING
THE U.S. COMMODITY FUTURES TRADING COMMISSION
AGRICULTURAL ADVISORY COMMITTEE
JULY 25, 2013

The Agricultural Advisory Committee ("AAC" or "Committee") convened for a public meeting on Thursday, July 25, 2013, at 9:31 a.m., at the U.S. Commodity Futures Trading Commission's ("CFTC" or "Commission") Headquarters Conference Center, located at Three Lafayette Center, 1155 21st St. NW, Washington, DC. The meeting consisted of an overview of the Dodd-Frank Legislation, its implementation, and three panels. Panel I featured a discussion on Customer Protection. Panel II included a discussion concerning Ethanol/RINs. Panel III highlighted a discussion on Voice Recording (1.35).

<u>AAC Members in Attendance</u>

Dr. Randall Fortenbery, AAC Chairman, School of Economics, Washington State University
M.J. Anderson, Regional Sales Manager, Andersons, Inc., National Grain and Feed Association
Jim Bair, Vice President, North American Millers Association
Scott Cordes, President, CHS Hedging Inc., National Council of Farmer Cooperatives
Neil Dierks, Chief Executive Officer, National Pork Producers Council
Curtis Friesen, Vice Chair of Public Policy Action Team, National Corn Growers Association
Edward Gallagher, President, DFA Risk Management, National Milk Producers Federation
Jennifer Han, Associate General Counsel, Managed Funds Association
John Hays, Senior Vice President for Policy Analysis, Farm Credit Council
Brittany Jablonsky, Director of Advocacy Communications, National Farmers Union
Dwight Lanclos, Director, Strategic Data Acquisition and Analysis, USDA-Risk Management Agency
Lance Kotschwar, Senior Compliance Attorney, The Gavilon Group LLC, Commodity Markets Council
Ed Luttrell, President, National Grange
Bill May, President, American Cotton Shippers Association
David Miller, Director of Research and Commodity Service/Iowa Farm Bureau, American Farm Bureau Federation
John Owen, Chairman, USA Rice Producers' Group, USA Rice Federation
Paul Penner, Vice President, National Association of Wheat Growers
Diana Preston, Vice President, American Bankers Association
F. Don Reynolds, Chairman and CEO, Regional Missouri Bank, Independent Community Bankers of America
David Senter, Consultant, American Agricultural Movement, Inc.
Stephen Strong, Feed Grain Product Line Manager, Bunge North America, North American Export Grain Association
Steve Wellman, Chairman, American Soybean Association
Robert Yonkers, Vice President and Chief Economist, International Dairy Foods Association

CFTC Commissioners and Staff in Attendance
Chairman Gary Gensler
Commissioner Scott O'Malia
Commissioner Mark Wetjen
Christa Lachenmayr, Designated Federal Officer
Gary Barnett, Director, Division of Swap Dealer and Intermediary Oversight
Lee Ann Duffy, Assistant General Counsel, Office of General Counsel
Ward Griffin, Associate Chief Counsel, Division of Swap Dealer and Intermediary Oversight
Laurie Gussow, Special Counsel, Division of Market Oversight
Vince McGonagle, Senior Deputy Director, Division of Enforcement
Scott Mixon, Acting Chief Economist
Kevin Piccoli, Deputy Director, Division of Swap Dealer and Intermediary Oversight
Ananda Radhakrishnan, Director, Division of Clearing and Risk
Robert Wasserman, Chief Counsel, Division of Clearing and Risk

Also in Attendance
Ann Bagan, Managing Director, Audits, CME Group
Dr. Phillip Verleger, President, PKVerleger LLC

I. Opening Remarks

Dr. Randall Fortenbery, newly appointed AAC Chairman, called the thirty-sixth AAC meeting to order at 9:31 a.m. After thanking the attendees for coming to the meeting, Dr. Fortenbery made his opening remarks. He then introduced Chairman Gensler.

Chairman Gensler indicated a change in format of having an outside chairperson for this advisory committee, and then noted his role as the sponsoring Commissioner. He then introduced Christa Lachenmayr as the Committee's Designated Federal Officer. Chairman Gensler also recognized and thanked former Commissioner Mike Dunn for his previous work with the AAC. In addition, he thanked committee members for their advice and input as being critical to the CFTC's mission.

Chairman Gensler continued with his opening remarks. Because this meeting comes at a time when Dodd-Frank is being implemented, he stated that advice from committee members is critical, and to hear their feedback would be helpful. Chairman Gensler asked committee members, what was going well, what was not, and what adjustments or flexibility should be made, as it relates to farmers, ranchers, producers, merchants, and other agricultural interests.

Chairman Gensler also indicated the CFTC would be finalizing customer protection rules in the fall, and input from committee members would be helpful at this time. With respect to swaps market reform, he stated that it is about making sure that farmers, ranchers, producers, merchants, and others, who use these complex products called derivatives, work for the agricultural community. Finally, Chairman Gensler noted that, in his view, agricultural swaps are really relevant to hedging and lowering risk in agricultural community.

Commissioner Wetjen then made his opening remarks. He also thanked those committee members for bringing useful attention to some key areas in the remaining rules where the agricultural interests have a perspective that is important to understand. Commissioner Wetjen noted the most important issues are related to residual interest and the customer protection rulemaking that the CFTC hopes to finalize soon. He complimented the Committee for highlighting these issues and making sure the CFTC fully understands them before considering the final draft. Finally, he thanked everyone for their advocacy on these issues, both in terms of customer protection and other rulemakings.

Before getting started, Dr. Fortenbery asked AAC members to introduce themselves.

II. Overview

A. Presentation by Ms. Duffy, CFTC

Ms. Duffy provided an overview of the Dodd-Frank legislation. She noted that Dodd-Frank was enacted to reduce risk, increase transparency, and promote market integrity within the financial system. She also noted that under the Dodd-Frank Act, the CFTC now regulates swap dealers, which requires standardized derivatives to be centrally cleared and traded on regulated exchanges, or swap execution facilities, as well as, oversees a new swaps reporting and record-keeping regime.

B. Presentation by Ms. Gussow, CFTC

Ms. Gussow reported on her involvement with the implementation of the Dodd-Frank legislation. She noted that she had worked on the reporting of swap data to Swap Data Repositories (“SDRs”), and public dissemination of certain price and volume information regarding those transactions. She also discussed the CFTC’s reporting rules in parts 43 and 45, and the historical swap reporting regulations in part 46. She also noted that the CFTC provisionally registered SDRs in the Chicago Mercantile Exchange (“CME”), Depository Trust & Clearing Corporation (“DTCC”), and Intercontinental Exchange (“ICE”) Trade Vault.

She next described the deadlines for reporting, and noted that implementation was based upon the status of the market participant. She then discussed the phased reporting of regulatory (nonpublic) swap transaction data to SDRs. With respect to interest rate and credit default swap classes, Ms. Gussow indicated that Swap Dealers (“SDs”) & Major Swap Participants (“MSPs”) began reporting on December 31, 2012 and February 28, 2013; financial entities began reporting on April 10, 2013; and non-SD, non-MSP, and non-financial entities began reporting on July 1, 2013. She also noted that reporting by the equity, foreign exchange, and other commodity asset classes began on August 19, 2013. She then described the reporting hierarchy set forth in part 45 in the following order: (1) swap dealer; (2) major swap dealer; (3) financial entity; (4) tie-breaker; (5) US person vs non US person; and (6) non US person.

Ms. Gussow then discussed assigning a unique identifier for each counterparty to a swap, which is called the Legal Entity Identifier (“LEI”). She noted that during the phase-in process, the

CFTC is using the CFTC Interim Compliant Identifier ("CICI"). She further noted that each counterparty to a swap must obtain an LEI or in the interim a CICI, and that the registration process is quick and easy. She also discussed the CFTC's no action letters and interpretative guidance providing relief that address several different reporting scenarios. She noted that all of this information is available to the public on the CFTC's website.

Chairman Gensler then expanded the discussion on the implementation of the Dodd-Frank legislation in terms of three broad areas. First, there are now three data repositories that collect data from market participants so regulators can see the full scale and scope of the marketplace providing transparency in the marketplace. Second, there is public market transparency where price and volume of transactions can actually be seen as they flow through the system, similar to a modern-day ticker tape. Third, there is a centralized market structure or a platform called swap execution facilities ("SEFs"). He noted that if a trading platform offers agricultural swaps there are rules of the road in place to offer various ways to transact business, and this information will be sent to the data repository.

Chairman Gensler also discussed another major piece of Dodd-Frank, which is the lowering of risk through central clearing and oversight of dealers. He noted that central clearing, which was part of the futures industry for about 120 years, has now come to the swap marketplace. He emphasized that non-financial parties, farmers, ranchers, producers, and millers have a choice, and do not have to be involved in central clearing. However, financial entities that make up ninety percent of the derivatives market have to use central clearing to lower the risk of an interconnected financial system.

Chairman Gensler next noted that another part of lowering risk is where dealers and large banks in the United States and abroad started registering with the CFTC last year. He explained that their registration means they are now subject to various business conduct rules on their sales practice; these rules make the markets fair and less subject to abuse. He also noted that throughout the process the CFTC has been listening and working with agricultural cooperatives and others around the table to ensure that they are not caught up in the swap dealer definitions. However, it would be helpful to get advice on this reform. He stated that the CFTC is over ninety percent finished with the regulatory issues, and more than halfway in terms of implementation. He also noted that this meeting comes at a timely moment to hear about what is working, what is not working, and what tweaks or adjustments are appropriate. Finally, Chairman Gensler indicated that according to Mike Dunn, as the CFTC votes for these rules, it should always stand ready to adjust, which is a view he also shares.

C. Questions and Discussion

Following the presentations on the overview of the Dodd-Frank implementation, Dr. Fortenbery asked committee members for questions or comments. Mr. Cordes first commented there is some confusion in the industry that needs to be worked through, and a better understanding of what applies to whom, when, and where. In response, Chairman Gensler stated that Mr. Cordes' comment was helpful, and called on committee members for specifics, particularly as it relates to agricultural interests, and not to hesitate to inform the CFTC.

Commissioner Wetjen then asked a series of follow up questions regarding the cause of the confusion: was it because market participants were trying to comply for the first time, were the rules not clear enough, did CFTC provide sufficient guidance, or a combination of these. Mr. Cordes thought it was a combination, and noted that the biggest challenge is meeting the compliance deadlines because people are not up to speed on what is required. He commented that clearer timelines or further clarification would be helpful.

Mr. Friesin commented that his local grain elevator is very confused about the reporting requirements and does not know if it is a swap dealer or not. He also commented that as farmers become adept at using more risk management tools, elevators are developing products to help farmers market their grain, and there is concern that these products will be considered swaps. Mr. Friesin asked whether there could there be a floor dollar amount where anything below would not have to be reported.

Mr. Gallagher, as a follow up, commented he has seen the same in the dairy industry, and that some of the swaps they contemplate writing are going to be pretty small, nominal amounts that will not be an issue for the security of the economy of the United States. He further stated that the dairy industry is a little different with some special needs. Mr. Gallagher noted that as a dairy cooperative it has a lot of marketing contracts with volumetric optionality, which he described as a dairy "grid," which serves to ensure that whoever wants milk can get milk when they need it. As a result, the cooperative has a lot of volumetric optionality in their contracts. Mr. Gallagher, in his view, does not consider these contracts to be swaps. However, in his opinion, the rules are vague enough to be of concern and more dialogue is needed for a better understanding.

Commissioner Wetjen expressed his appreciation for the question and raising the issue. He noted that volumetric optionality was part of the CFTC's swap definition rule about a year ago, and that a volumetric optionality test was done on an interim basis, which the CFTC had sought additional comment. He then asked Mr. Gallagher whether his group filed a comment letter in response. If not, Commissioner Wetjen urged that a comment letter be filed, so the CFTC can think about addressing the issue. Chairman Gensler added that he shared Commissioner Wetjen's thoughts that even if Mr. Gallagher's group had filed a comment letter, they might want to re-file something, or set up a meeting. Ms. Duffy also added that CFTC staff that worked on the products definition still consults on questions of the products definitions, and invited Mr. Gallagher to contact her or Dave Aron also in CFTC's Office of the General Counsel. Chairman Gensler commented that staff stands ready, time permitting, to deal with the hundreds of questions that come up, which can be addressed through staff interpretations.

Ms. Preston commented that the American Bankers Association ("ABA"), which represents interests on all sides of the equation, is often seen as representing the largest most active players, although it also encompasses the smallest players who do swaps, in some cases once every five years. She noted her appreciation for the dialogue with the CFTC, and found the staff extremely responsive and willing to listen. She described the new trade affirmation platforms which the dealers and the end user banks, and the banks in the middle all had to deal with, as very challenging. She expressed her appreciation for the CFTC's accommodation in terms of enforcement actions while things get sorted out.

Mr. Gallagher asked Committee members why a dairy farmer would need to have an annual re-submission and annual re-payment for an LEI or CICI when he/she is going to the same address for decades. He was also curious if other agricultural or farm-based groups had the same thought or idea, as to why a farmer should have pay an annual LEI fee when that farmer remains in the same place all the time. Mr. Dierks, from the producers' perspective, commented that he knows some of their members, who have started using swaps in agriculture, encounter the same kind of thing, and they are pretty identifiable, and have been there forever. He asked is there a way to sign up for the LEI or CICI that does not need to be renewed, or a longer time for renewal. Chairman Gensler then emphasized there needs to be a definite renewal requirement to refresh data integrity, whether once a year, and in some circumstances more often or less often, to ensure the right party is identified.

Ms. Han, with respect to LEIs and CICIs, commented that her group, the Managed Funds Association ("MFA"), wants to make sure everything is working correctly, and that all of the information kept at the swap data repositories is maintained in a confidential manner. She noted that members of the MFA have been aware of instances when trade data has been released to the counterparty and are quite concerned. She emphasized that the MFA would like the CFTC to ensure that SDRs maintain data confidentiality.

Ms. Preston pointed out that the ABA has a clearing mandate that has been implemented through many parts of the marketplace; however, she expressed serious concerns about a proposed exemption from clearing for cooperatives, for Farm Credit. She noted that Farm Credit, in particular, has a swaps portfolio of $26 billion, and there appears to be a contradiction with the CFTC's mandate for centralized clearing.

Upon conclusion of the this portion of the Committee meeting, Dr. Fortenbery mentioned that the slides being presented today will all be available after the meeting. He then informed the Committee members that the AAC would be taking a 15-minute recess, and that the next subject would be customer protection.

III. Panel I: Customer Protection

A. Presentation by Ms. Bagan, CME Group

Dr. Fortenbery introduced the panelists discussing customer protection, and then turned to Ms. Bagan for her presentation. Ms. Bagan reported that, over the past couple of years, a number of the industry groups were brought together to look at ways to enhance customer protections. She noted that the Futures Industry Association ("FIA") had put a group together called the Financial Management Group, who prepared frequently asked questions that explained how customer segregation works, and that the FIA also had put a group together to look at potential enhancements. She then noted that the National Futures Association ("NFA") had put a group together for self-regulatory organizations ("SROs") to suggest enhancements to customer protection, and that CME had examined ways to suggest enhancements to customer protection.

Ms. Bagan next explained that the FIA and NFA, through the work of their groups, developed similar ideas, which have now been implemented. The goal was to have greater transparency, increased detection, and increased deterrence from situations where customer funds could be potentially lost. She noted that all futures commission merchants ("FCMs") must now report all customer segregation computations to their designated self-regulatory organization ("DSROs") on a daily basis, which is either the CME or NFA. Ms. Bagan discussed that to date the CME has received approximately 15,000 reports, which are reviewed every single day. In addition, the CME is now receiving semi-monthly detailed reports of where FCMs are now investing their customer funds. The CME also has a rule that if an FCM is going to decrease its excess segregated funds, and if that excess decreases by 25 percent on any given day, the FCM must notify its DSIO, which must be approved by a senior executive at the firm. She noted that if a firm does not report that 25 percent decrease on the day it happens, the CME's management team will call the firm, and discuss a potential disciplinary action if the CME is not notified.

Ms. Bagan also reported that a year ago, the CME started using Confirmation.com, which allows the CME to get direct confirmations from banks of balances being held, which could be used in regulatory examinations. She then reported that both the NFA and CME have engaged an outside vendor called AlphaMetrix 360, which aggregates balances at banks, including all cash and securities held on behalf of customers. This information is used as a measure against what firms are reporting to make sure that they are in line and that the funds are there. She further noted that the CME is currently in phase II, which will also obtain balances from carrying brokers and clearing organizations, and hopefully will be up and running this year.

Ms. Bagan also discussed a study developed by the FIA, the NFA, the Institute for Financial Markets ("IFM"), and the CME, which focused on whether insurance could be used as a potential tool. Currently, the information in the study is being reviewed and analyzed. When completed, the groups will search for insurance quotes to determine the costs. She also described the farmer fund, which was put together to pay customers back, perhaps on a more timely basis than through a bankruptcy. The CME used it for Peregrine Financial Group ("PFG"), and paid out approximately $2 million to customers.

Finally, Ms. Bagan noted that the CME conducts regulatory examinations on its firms, every nine to fifteen months, on a surprise basis. She noted that the CME is also going in intra-month just to look at customer balances to make sure that what they are doing during the month is also in compliance with all regulations. She further noted that the CME goes in intra-month again, on a surprise basis, to verify the balances, and uses the AlphaMetrix balances to make sure the funds are where they are supposed to be.

B. Presentation by Mr. Barnett, CFTC

Following Ms. Bagan's presentation, Dr. Fortenbery turned to Mr. Barnett for his presentation. Mr. Barnett noted that the CFTC's mission is to help ensure the integrity of futures and swaps markets, and to protect customers and their funds. He described how the CFTC has reached out broadly on ways to enhance customer protections. In addition, he explained that the CFTC has conducted three roundtables, and consulted with the SROs, many industry participants, the buy side customers, as well as held discussions with fellow regulators, and the accounting and auditing industry. The CFTC has also considered over 125 comment letters regarding the Notice of Proposed Rulemaking Enhancing Protections Afforded Customers and Customer Funds Held by Futures Commission Merchants and Derivatives Clearing Organizations, 77 Fed. Reg. 67866 (Nov. 14, 2012).

Mr. Barnett then discussed that, before the proposed rule set, the CFTC had completed amendments to Rule 125 to prevent the use of customer funds for in-house lending through repurchase agreements. He noted that the CFTC required clearinghouses to collect margin on a gross basis so that FCMs would not be offsetting one customer's collateral against another, and sending only the net amount to the clearinghouse. He also noted that the CFTC adopted the legal segregation with operational commingling ("LSOC") rule for swaps to help ensure customer money was being protected, individually, all the way to the clearinghouse. He further reported that the CFTC adopted customer protection enhancements for designated contract markets ("DCMs"), codifying staff guidance on minimum requirements for SROs.

Mr. Barnett next described the requirements of the customer protection rule set. First, he discussed fixing Part 30, which requires that sufficient funds be held in the Part 30 accounts to meet the FCM's total obligations to customers under the net liquidating equity method, and no longer holding just what is needed for margin offshore with the rest being subject to risk. He also discussed maintaining written policies and procedures governing the excess funds, and making the additional reports available, including daily computations of segregation and secured accounts.

Mr. Barnett noted that daily information for bank and custodial accounts is very important, and the CFTC supports the aggregator method. He also noted that CFTC staff continues to recommend the need for a mechanism to allow the CFTC to have direct electronic access to bank information and custodial account information. He further noted that increasing disclosure to customers regarding the risks associated with futures trading, and requiring FCMs to provide current and potential customers with specific information, including information about the institution is needed. He emphasized that greater enhanced controls at FCMs in connection with how customer accounts are handled is important, which is included in the proposed rule set.

Mr. Barnett also described the CFTC's requirements regarding standards for SRO examination and certified financial statement audits, including raising the minimum standards for independent public accountants. He noted that the CFTC has proposed additional filings that would give an effective early warning system to allow the CFTC to get ahead of problems. He also noted that the CFTC instituted a liquidity requirement for FCMs, to better detect if FCMs become distressed putting customer funds at risk. All of these points are about ensuring customer confidence that the funds they post as margin or collateral are fully segregated and protected.

Finally, Mr. Barnett discussed generally that the following still needs to be done: (1) require more effective risk management; (2) require the delivery of more forward-looking information to allow the CFTC to get ahead of issues; (3) assure better examinations by outside certified public accountants ("CPAs"), SROs, and the CFTC; (4) provide more information and disclosure for customers; and (5) implement some changes concerning capital and liquidity.

C. Presentation by Mr. Kevin Piccoli, CFTC

Following Mr. Barnett's presentation, Mr. Piccoli discussed the oversight process, which he described as the three legs of a stool. He described the first leg as the CPA, who performs an annual audit of the intermediary, and that the purpose of the CPA is twofold. First, the purpose is to provide the CFTC with a level of comfort that the financials the CFTC receives on a daily and monthly basis have an element of reliance. Second, through the CPA's material inadequacy letter, the purpose is to also provide CFTC with a level of comfort and reliance when CFTC receives the monthly numbers. Mr. Piccoli explained that if a CPA fails to identify an error, CFTC staff will ask the CPA why the error was not identified, which is an important aspect of the CFTC's oversight function.

Next, Mr. Piccoli described the second leg, the DSROs themselves. The two primary DSROs are the CME and the NFA, who perform a risk-based internal controls review every nine to fifteen months at the firms, and get into the details on the firms themselves. He noted that in the event of a crisis, the CFTC will coordinate with the CME and NFA on any particular issue.

Then, Mr. Piccoli discussed the third leg of the stool, which is also twofold. One is oversight of DSROs, making sure the CME and the NFA are performing their oversight tasks appropriately. Second, the CFTC performs for-cause examination to determine if a firm is having control problems that require the CFTC to specifically look in to it. The CFTC's scope of examination is limited due to the lack of staffing to conduct a full exam. Accordingly, the CFTC relies on the CME and the NFA to perform this function.

Finally, Mr. Piccoli discussed the CFTC's daily and monthly monitoring of a firm's financials that are received into the system. He explained that the CFTC performs the following: (1) a regression analysis; (2) a trend analysis; and (3) a comparative analysis to determine any standout issues.

Following the presentations on customer protection, Mr. Barnett asked for comments. Chairman Gensler commented that this meeting is crucial for preparing a final document to be presented to the Commissioners. He noted that input from Committee members comes at a critical time.

Commissioner O'Malia asked if the comments made during the meeting would be included in the comment file for the rule. In response, Chairman Gensler stated that they should be, and the whole transcript of this section could be placed in the administrative record.

Commissioner Wetjen also discussed the importance of examining FCMs. He emphasized that committee members are uniquely positioned to help the CFTC. He noted that after MF Global and PFG, one of the best ways for conducting comprehensive examinations of FCMs is having sufficient CFTC personnel and resources. He further noted that the CFTC is underfunded, and has more responsibilities than it did three years ago. Commissioner Wetjen further commented that in addition to performing examinations, the CFTC needs to engage and be more responsive to Committee members, rather than having them bring their issues to the CFTC, which is more reason for additional resources, additional staff and personnel here to provide answers to questions, and undertake these examinations, both of which are very important.

D. Questions and Discussion

Following the comments made by the Chairman and Commissioners, Dr. Fortenbery asked Committee members for questions and discussion. Mr. Gallagher asked whether a case study could be done using MF Global and PFG as examples to show how the changes that have been made with Dodd-Frank would have created a red flag, or an alert to identify the issues sooner. He also asked what the CFTC would have done to alert those with accounts at those two entities.

In response, Mr. Barnett stated that neither PFG nor MF Global could be used until there is sufficient history, and everything has been made public. However, he commented that according to CFTC rules, customer funds cannot be commingled nor used improperly. He noted that one thing the CFTC learned was that failing to have sufficient internal review or risk management can be an issue, and operating company risk can put customer funds at risk. He also noted that the industry is looking at alternative segregation systems, and the CFTC supports that consideration, whether it is insurance, or an alternative segregation system. He further noted that the orientation is toward greater risk management to help mitigate the human problem, such as misfeasance or malfeasance. Finally, he mentioned that the Financial Industry Regulatory Authority and the Securities and Exchange Commission went to a more risk-based orientation six to seven years ago, and in trying to stay current with other best practices, the CFTC has tried to address those things in this rule set.

Chairman Gensler also addressed Mr. Gallagher's question. He emphasized that CFTC's ability to directly see what is in a given bank account and custodial account and to have an online affirmative confirmation of those accounts, directly addresses the issues Mr. Barnett raised. He noted that the NFA, CME, and others are using AlphaMetrix, which allows direct electronic views daily into the cash and custodial accounts. Chairman Gensler then mentioned that he was not participating in the specific matters surrounding MF Global; however, he was participating generally in the public policy issues, ensuring that an FCM keeps its books and records in a stronger way, and that nobody can pull out more than 25 percent of what is called the excess, without a chief executive officer's signature or senior officer signature.

Mr. Gallagher asked what action is taken by the CFTC if it discovers an issue with an FCM, and will the CFTC alert the account-holders of the FCM about the issue? In response, Chairman Gensler stated that if an FCM is inappropriately using customer money at any point that is a violation. He also explained that Mr. Piccoli and Mr. Barnett, and sometimes the full Commission, are alerted about the inappropriate use of customer funds and there is a very intense discussion with the FCM.

Mr. Piccoli also commented that whenever the CFTC becomes aware of any issues it reviews the matter and asks whether could this happen to registrants. He noted that, in such circumstances, the CFTC considers whether or not a change should be made in the internal examination, or whether letters should be sent to FCMs identifying the issue and advising them of it.

Ms. Bagan added that, speaking from the perspective of an SRO, there is an assortment of emergency actions that can be taken. For example, she noted that if an FCM was not holding customer funds that they said they had, the CME would immediately begin transferring customers and finding out where the money went.

Commissioner O'Malia then asked that the question regarding when a customer is notified if something has gone wrong with an account be addressed. In addition, he asked how the CFTC will interface with a customer under the proposed customer protection rules. In response, Mr. Barnett noted that there is a tension between having forward-looking information as a regulatory tool, and then accelerating the problem by making it public. He further noted that the CFTC often struggles with this issue, and that there have been situations when the CFTC could not provide information, and has turned to the CME for assistance.

Commissioner O'Malia asked Mr. Piccoli to discuss some of the changes concerning FCMs that were made a year ago to help customers understand where they are putting their money, and who they are investing with. In response, Mr. Piccoli noted that FCM financial information, such as segregation amounts and net capital, and where funds are invested, is available through the NFA's website for all investors to view. Therefore, anyone wanting to conduct due diligence on their FCM can look at it and get a lot of useful financial data, which is updated on a monthly basis.

Ms. Han noted that the MFA supports all the information that the CFTC proposes to require FCMs to disclose. However, there should be more information disclosed to customers, such as: (1) schedules for the segregation amount; (2) the secured amount in cleared swaps; (3) cleared swaps; (4) customer segregation amount; (5) summary balance sheet; and (6) some of the monthly income statements. She further noted that this information would be very helpful to customers, who can then make their own assessments.

Mr. Friesen commented that being a small producer, who has used the Chicago Board of Trade and then the CME for the last thirty years, he has never had a problem. He noted that if margin requirements are made any tighter, he will probably stop using the CME. He also noted that he would have to put more of his money at risk to a MF Global type entity as he would have more margin money there, and therefore be at a higher risk. He then commented that insurance would be beneficial, but the cost would be passed on to him as well. Mr. Friesen also noted that he used to keep quite a bit of money with his FCM, to avoid having to send money back and forth, but now he conducts a regular sweep of his funds because the trust is gone. He further noted that the disclosure of information about his FCM is not useful to him. In response to Mr. Friesen, Mr. Barnett emphasized the margin deficit residual interest issues are a very important question, and the CFTC is looking at it very carefully.

Mr. Anderson next commented that the National Grain and Feed Association ("NGFA") represents over 1,000 member companies encompassing all aspects of the agribusiness in the United States. He appreciated the CFTC's efforts into some of the insurance funds, and is anxiously waiting to see the results on cost. However, he noted issues with two things that could greatly increase customer risks. First, the timing of when an FCM takes a capital charge. The NGFA has urged the CFTC to stay at the three-day window. Second, the concept of residual interest where an FCM can "top up" the account until it receives the margin call. If that is changed, there is a strong likelihood that FCMs will require pre-funding of the margin accounts. As result, more money is potentially at risk in case someone circumvents the regulations, again creating a similar situation to an MF Global.

Chairman Gensler discussed the comments made by Mr. Anderson and Mr. Friesen. He noted that one of the challenges is within the law itself, which has been in place for some time and is the "thou shall not use one customer's money to secure or guarantee another customer's position or deficit" rule. He also discussed the three-day window for a margin call due to a deficit, and asked Committee members to consider what FCMs are doing during those three days. He also noted that the proposed rule addresses what happens if the FCM is not putting up its own money to secure the deficit, which is the challenge before the CFTC.

Mr. Gallagher commented that the National Milk Producers Federation ("NMPF") would support the idea that a customer's funds not be used for another customer's deficit as well. However, he noted his concern is more with the dollars needed to margin an account, and whether it is going to increase dramatically putting more money at risk in case of a default.

Mr. Miller commented that his concern involves an FCM using his excess funds for internal investments that are not subject to margining rules. He further commented that he is concerned about an MF Global type situation, not the inter-transfer among customer segregated accounts. He stressed the need to understand this movement to one-day versus industry practice, particularly with small customer accounts. Mr. Miller also stated that there may be issues with the law that need to be addressed by the CFTC. However, he does not want to see the creation of problems that will make it riskier at the farm level in the name of customer protection.

Mr. Cordes added that in his view the discussion is how Committee members interpret the new rules or the laws. He noted that the conversation is not so much about deficits, but about potential margin calls. He also noted that the way the rules are written today, the customer is going to be asked to double-fund the margin call. Specifically, the customer is going to have the initial margin call and going to have money in the account to fund the one-day's move. He asked the CFTC staff or one of Commissioners to comment on how the CFTC is looking at handling the revised interpretations or rules.

Ms. Bagan added that she agreed with Mr. Cordes that the concern is not about a negative account balance as firms have to put their own money in to cover those issues today. Instead, she noted that the concern is margin calls.

In response to Mr. Cordes' comments, Mr. Radhakrishnan and Mr. Wasserman cited several examples of why an FCM must not use customer funds to margin, secure, or guarantee the obligations of another customer. Mr. Radhakrishnan further noted that the CFTC does not want a situation where the FCM puts its own capital into a segregated account. Mr. Wasserman explained if an FCM goes bankrupt and a customer's funds are not there because it is being used to margin another customer's positions, the first customer would be upset. On the other hand, there are practical issues where the CFTC does not want to put customers in a position where there needs to be double margining.

Commissioner O'Malia then asked a series of questions regarding the daily margin true-up rule and the pro rata distribution in bankruptcy, and whether the rulemaking makes any changes to the pro rata distribution. In response Mr. Wasserman explained that idea of the rulemaking was to reduce the likelihood of problems occurring in segregated accounts; however, the rule was not intended to change the pro rata distribution in bankruptcy.

Chairman Gensler cited another example involving an FCM bankruptcy with a shortfall in segregation. He asked if a pro rata distribution will be made in bankruptcy. In response, Mr. Radhakrishnan explained that if the loss is big enough, there is a short fall in segregation as a whole, and there is a bankruptcy filing, then the pro rata distribution rules will go into effect.

Mr. Miller expressed concern that a bankruptcy issue is being resolved with a CFTC ruling regarding pro rata distributions. He emphasized that the focus is margins, not deficits. In response, Chairman Gensler assured Mr. Miller that the CFTC is trying to be very careful. He then noted among other things that there are risks even when using someone else's margin.

Commissioner O'Malia asked Mr. Wasserman and Mr. Radhakrishnan to discuss the CFTC's interpretation of the rule "thou shall not use one customer's money to secure or guarantee another customer's position or deficit" and what was the CFTC's standard before. In response, Mr. Radhakrishnan stated that the CFTC assumed that people knew what the law was and were in compliance. However, because of the two unfortunate events with MF Global and PFG, he noted that the CFTC realized that people had a different view of the law.

Ms. Bagan disagreed and commented that the CME with its regulatory examinations have made sure that FCMs are following the law, and are holding the funds that need to be held. In response, Mr. Radhakrishnan commented that as the Chairman had already stated, the statute is very clear, one customer's money, funds, or property cannot be used to margin, secure, or guarantee the obligations of another.

Mr. Friesen commented that his biggest concern is that if he has excess margin and his FCM goes bankrupt, then why is he unable to get all of his money back if customer accounts are segregated. Mr. Cordes opined on the practicality of a situation where during the trading day there are wire transfers in and wire transfers out, although the transfers are not always submitted in the order requested.

Finally, Commissioner O'Malia commented that Ms. Bagan was celebrating her birthday and 25 years of service with the CME. With that, Dr. Fortenbery introduced the next panel.

IV. Panel II: Ethanol/Renewable Identification Numbers

A. Presentation by Mr. Verleger, PK Verleger

Dr. Fortenbery introduced the panelists discussing Ethanol and renewable identification numbers ("RINs"), and turned to Mr. Verleger for his presentation.

Mr. Verleger first noted that he had submitted a paper to the Committee, entitled *Renewable Identification Numbers* (2013). He then provided a summary of the paper for Committee members. He stated that ethanol has been used as a fuel additive for many years in the oil business, and that it has a high octane level that makes it popular with refiners, especially when the price is low because it cuts the cost of producing gasoline. He also noted that today, refiners, if they could, would blend more ethanol into gasoline, and that the result would be a lower-octane gasoline with lower manufacturing costs. Mr. Verleger then stated that the existing infrastructure within the petroleum industry limits the amount of ethanol in gasoline to ten percent, and this is due to a regulation concerning fire hazards and the rules established by UL laboratories. He also stated that Congress dictated a specific volume of ethanol that had to be blended into motor fuels when it passed the Energy Act of 2004, and more recently the Energy Independence and Security Act of 2007.

Mr. Verleger next reported that this year, 20 billion gallons of renewable fuels must be blended in gasoline and other motor fuels, and that 16.5 billion of those are ethanol. He also stated that last year, the Energy Information Administration ("EIA") had projected that gasoline and diesel use would be 183 billion gallons, calling for a blend of eleven percent. Mr. Verleger then noted that the Environmental Protection Agency ("EPA") has introduced tradable credits called RINs, which are eighteen-digit numbers that the EPA tracks and can be traded like pollution credits. He also noted that EPA has encountered difficulties enforcing the laws involving biodiesel RINs. Specifically, buyers of fraudulently created RINs were required to replace them; however, EPA has since instituted a certification program to address the issue.

Mr. Verleger then discussed six types of RINs, focusing his discussion on the D6 RIN, which is the ethanol RIN that is traded on the CME. He noted that until this year, the prices of RINs were negligible because companies were well below the ten percent blend rate, and were using more ethanol than required, so there was no cost to RINs. However, gasoline demand has failed to keep up with the projected levels that were used by Congress when they passed the Act, and currently there is a twenty percent shortfall in gasoline consumption with and absolute fixed requirement for blending gasoline. Accordingly, the price of RINs has risen dramatically. He noted that at the beginning of the year, the price of RINs was at zero, but last week they were trading at $1.40. He also mentioned that Valero, one of the largest refiners is going to spend between $600 and $800 million this year for RINs. Accordingly, refiners have been asking Congress to change the law to reduce their obligation.

Mr. Verleger next discussed E85, which is an ethanol fuel blend of 85% ethanol and 15% gasoline, and noted that E85 has been available in the Midwest for years, but that the price has not been attractive. He also reported that as prices of RINs have increased, the price of E85 has been falling. Mr. Verleger then discussed a pricing experiment in Minnesota where sales of E85 have tripled, and also noted that there are other parts of the country where the energy equivalent price of E85 has dropped to a point where it is profitable. He next noted that, in his view, if the programs continue, and the EPA does not show flexibility (on the mandate), then the market will clear. He also noted that trade in the CME contract will help the market to clear. However, there are some significant obstacles. For example, the oil industry has been calling for the repeal of the Renewable Fuels Act, although the consensus of Congress is that will not happen. He also noted that the EPA rules have not been issued in a timely fashion which has caused uncertainty in the market, and that Congress frequently imposes regulations that are too complicated to be implemented in a timely fashion. In closing, Mr. Verleger commented that the RIN program is basically sound, and it is going to take some adjustment provided that some flexibility is allowed.

B. Presentation by Dr. Mixon, CFTC

Dr. Mixon delivered his presentation next. He noted that economic research at the CFTC clearly benefits from hearing the input of market participants, which helps the CFTC to focus on developing appropriate and thoughtful regulations. He also noted that part of the CFTC's motivation is to think about the RIN market and understand some of the details, both from the top-down perspective in terms of the fundamental forces of supply and demand. He commented that this is an interesting market, even though the CFTC has not focused on it as much as other agricultural markets because it has only existed for a few years. He further noted that what caught everyone's attention was the fact that the price of RINs spiked up from a nickel to a dollar within a couple months toward the end of 2012, and has continued to show volatility.

Dr. Mixon focused his discussion on three different RINs: (1) the D6 RIN, which is a corn-based ethanol; (2) the D4 biodiesel, which is a soybean-based product; and (3) the D5, which is a more advanced biofuel. He mentioned that prices did seem to be moving in line with the Renewable Fuel Standard ("RFS") program regulations. 40 C.F.R. 80 subpart M (2013). However, he also noted that the CFTC did not readily observe these prices being out of line with each other when they were evaluated. He further noted that because the regulations obligated parties to deliver these RINs to the EPA, the parties could substitute D4 or D5 RINs, for D6 RINs. However, substitution only works one way, and the D6 RINs have to be less than or equal to the D4 or D5 RINs. Given the status quo, with the imposed requirements on blending: (1) for marketing; (2) for shares of the different types of products; and (3) for the amounts that have to be blended, Dr. Mixon observed that the amounts required to be blended exceed the amounts that the market could make available with the current technology.

Chairman Gensler then asked Dr. Mixon some questions about the slides discussed in his power point presentation. In response, Dr. Mixon explained that although one of the slides represented a number of assumptions, it essentially represents what the industry says about the maximum amount of gasoline that can be blended given the amount expected to be sold in a given year. Concerning another slide, he explained that even if RINs are not used, a refiner can still buy credits to deliver to the EPA. He noted that the supply of RINs, which has been built up over the past few years, will be completely depleted in 2014, and will become more valuable.

Dr. Mixon also reported on the research conducted by his office, including discussion with market participants some brokers of RINs. He noted that these products have only existed for a few years, and prior to 2010 it was really a “spreadsheet-based” market. He also noted that the EPA established the Moderated Transaction System (“MTS”), which is not a traditional market. Specifically, the transactions occur outside of the system, but are then booked into the MTS. He further noted that while market participants can see what transactions they have done, participants do not see the entire market place. He then commented that out of 2.6 billion RINs that were available at the end to 2012, on a slow day, there may have been 5 or 10 million RINs traded. On an active day, with a lot of volatility, one might see 100 million RINs being traded. Dr. Mixon also noted that one of the difficulties observed from 2010 and 2011 were some fraudulent trades that were entered for D5 RINs. In response to this, Chairman Gensler commented that these were alleged frauds, and not frauds prosecuted by the CFTC’s Division of Enforcement (DOE). Dr. Mixon agreed and clarified that fraud cases have concerned violations of the Environmental Protection Act.

Dr. Mixon next noted that market participants have reported that some financial institutions have entered the markets, but have encountered difficulties establishing relationships because these financial institutions are not refiners, not established in those markets, and do not know the same people. In closing, Dr. Mixon described the RINs market as a young evolving market to which futures contracts were introduced only recently and that the number of contracts is quite small. He also noted that his office is watching the RINs market, very mindfully, because it is connected to a number of other products and commodities, such as corn, soybeans, gasoline, and ethanol.

C. Questions and Discussion

Following the presentations, Dr. Fortenbery asked Committee members to comment on the RINs markets. Mr. Verleger expressed his concern about Congressional actions concerning RINs and commented that when the RIN market was created by Congress, it prohibited RINs accumulated two years ago from being valid. As an example, he noted that a RIN generated in 2011 from selling gasoline with ten percent ethanol, which had no value in 2011, could be used to meet a 2012 obligation. However, that 2011 RIN could not be used to meet a 2013 obligation. As another example, he noted that RINs accumulated in 2012 could be used for 2013; however, because these RINs expire at the end of the year, they cannot be used for 2014. Mr. Verleger also expressed his concern that the regulations regarding RINs only allow a person to carry 20 percent of 2012 RINs forward to 2013, and if that person is deficit in 2014, then that person can only use RINs in 2015 up to a certain point. He then added that trading is even more complicated if the gasoline blend wall is not reached as the EPA administrator has the right to change or relax the standard.

Following this, Chairman Gensler asked the Committee members for their views about how the markets for corn and soy are being affected, and what issues they see for the CFTC. Mr. Friesen commented that the National Corn Growers Association ("NCGA") has been following RIN prices closely in Nebraska, which he believes is the second largest ethanol producer in the country. He noted that petroleum marketers in the area are making a $1.20 per gallon profit on E85 because of the current RIN price, and profits are not being passed on to customers. In addition, the customers are unaware of this because they do not understand the RIN market. Mr. Friesen then commented that the petroleum industry is blocking the use of E15, which would lower the price of RINs, and that the RIN market is going to be extremely volatile, especially if suddenly the public starts using more E85 and the demand for those RINs drops.

Commissioner O'Malia next discussed a wire story reporting that RINs had dropped fifty cents over the last week, and asked the Committee members for their comments on what might have contributed to this volatility. Mr. Verleger commented that volatility may be attributable to uncertainty in regulation and the lack of data. For example, the EIA provides no information on the volumes of E10, E15, or E85 sold. He further noted that the market clearing mechanisms are there, but are not as transparent.

Chairman Gensler then asked the Committee members for their thoughts on what is happening on the ground for farmers. Mr. Miller commented that farmers are aware of the RIN market. He then noted that the value of RINs has an indirect rather than direct connection to the value of corn. The value ultimately deals with the incentives that a person might have for particular types of ethanol, not only the production but the blending and opportunities that come with the incentives. He also noted that the substitution effect also brings in the soybean oil market in connection with biodiesel.

Chairman Gensler next asked Committee members whether farmer who is planting corn or soybeans benefits if the RIN prices are high or low. Mr. Miller commented that the higher the RIN price, the more incentive there is to produce ethanol. In response, Chairman Gensler asked the Committee members whether the price relates back to the farmer. Mr. Friesen commented that RIN prices do not significantly impact ethanol production. This is because the RIN transfers with the gallon of ethanol, and the entity that uses the ethanol for blending can use that RIN in connection with their marketing ability.

Mr. Wellman commented that the price of RINs is is not correlated well with the farmer's price for corn. However, if the farmer has investments in an ethanol facility, then the farmer might be more in tune with RIN values. Mr. Wellman then asked Dr. Mixon whether he could further discuss the comparison and the valuations between the D5 and D4. He also asked if there is any correlation between the D4s, 5s, and 6s when the D6 value changes. Mr. Mixon first emphasized that the CFTC is not a price-setting agency. He then noted that based on his understanding of the regulations, and because of the deliverability of the D4 or D5 to satisfy the D6 obligation, the D4s and 5s seem to have at least as much value as the D6. He further noted that prior to the gains made in the value of D6 RINs, the D4 and D5 RINs were more valuable because of different EPA policies. However, as the D6 policy constraint became more binding, the values among the different RINs appeared to be more closely related. Dr. Mixon then qualified his response by stating that his observations were based on the chart presented at the meeting.

Dr. Fortenbery next informed the Committee members that the AAC would be breaking for lunch and that the meeting would continue at one o'clock.

V. Panel III: Voice Recording (1.35)

The afternoon portion of the AAC meeting continued with introductions of the panelists for Panel III: Voice Recording (1.35).

A. Presentation by Mr. Griffin, CFTC

Mr. Griffin began his presentation with a discussion of the background and purpose of the final rule amendments to Regulations 1.31 and 1.35, which require FCMs, retail foreign exchange dealers, certain introducing brokers, and certain members of designated contract markets or swap execution facilities to record and retain records of oral communications. He noted the purpose of the final rule amendments was to promote market integrity and protect customers, and that the CFTC believes that the collection of and access to searchable records, both oral and written, are indispensable tools the CFTC needs to ensure market integrity and to protect customers. Mr. Griffin next noted that technological advances have contributed to tremendous growth and that, as a result, CFTC has had to adapt and new rules are part of that adaptation. He then commented that CFTC has sought to apply the existing record-keeping requirements of Regulation 1.35(a) to swap dealers and major swap participants.

Mr. Griffin next discussed the comments received by the CFTC in response to the proposed amendments to Regulation 1.35, which included: (1) the costs involved, as well as the necessity and feasibility of the oral record-keeping requirement; (2) the application to members of DCMs and swap execution facilities ("SEF") and non-intermediaries who are not registered with the CFTC to keep records of their cash commodity transactions; (3) the requirement that each record be maintained in separately identifiable electronic file, known as tagging; and (4) other additional issues raised by commenters, such as a significant compliance time table, alternative treatment for smaller firms, and a shorter record retention period.

Mr. Griffin noted that the final rule significantly advances the CFTC's efforts to detect and deter abusive, disruptive, fraudulent, and manipulative acts and practices that seriously harm market integrity and customers. He also noted the changes made by the CFTC in the final rule to address the comments received from the public, which included: (1) limiting the oral record-keeping to oral communications that lead to a transaction in a commodity interest and related cash or forward transactions; (2) excluding small introducing brokers, oral communications of a floor broker who is a member of a designated contract market DCM or a SEF that do not lead to the purchase or sale for any person other than the floor broker, and certain members of the DCM or SEF including floor traders, commodity pool operators, and members that are not registered or required to be registered with the CFTC, as well as, permitting covered persons to contract with other CFTC registrants to retained the required records provided that the records are retained by the contractor registrant are the same records; (3) removing the requirement that each transaction be maintained as a separate electronic file; and (4) reducing the retention period for the oral records from five years to one year.

Mr. Griffin next reported that the CFTC significantly extended the amount of time affected entities would be afforded to come into compliance with the final rule for recording oral communications. He also noted that all affected CFTC registrants must be in compliance with the oral record-keeping requirement of Regulation 1.35 by December 21, 2013, which marks the one year anniversary of the publication of the final rule in the Federal Register. Mr. Griffin then explained that the Division of Swap Dealer and Intermediary Oversight ("DSIO") has the authority to grant alternative compliance schedules to affected registrants provided certain requirements are met. In closing, he stressed that time is of the essence, and that affected firms should already be well underway in working towards full compliance.

B. Presentation by Mr. McGonagle, CFTC

Mr. McGonagle delivered his presentation next. He first briefly discussed his initial involvement with the issue of record-keeping, which began several years ago through an agency task force that included representatives of the Division of Market Oversight ("DMO"), the former Division of Clearing and Intermediary Oversight ("DCIO") and the Office of General Counsel ("OGC"). He then commented on the purpose of the audio taping rule from an enforcement perspective, and generally described several enforcement actions brought by the CFTC in the past year based on audio taped conversations, including: (1) disclosures of material non-public information; (2) segregation; (3) failure to supervise; (4) speculative limits; (5) wash sales; (6) non-bona fide prices; (7) fraud; (8) false reporting; and (9) manipulation.

Mr. McGonagle then noted that in reviewing the comments to the proposed rule, the CFTC became aware of the concerns of individuals, as small players, would be affected in the market versus the larger market interests. He emphasized that the scope of the rule was narrowed to focus on entities that deal only with customers to strike a balance that preserves information most likely to be of concern to an enforcement investigation.

Mr. McGonagle commented that in his view, with respect to taping transactions, more is better. He also commented that the record-keeper should be able to readily access and identify records pertaining to a transaction or counterparty by running a search of the raw data. He explained that compliance with search ability can happen through the use of commercially available products capable of conducting speech analytics on recordings. He noted that both land lines and mobile telephones should be recorded, and covered persons must ensure that covered communications do not occur on personal phones that lack the recording capability.

Finally, Mr. McGonagle noted that the CFTC did not adopt any explicit safe harbors. However, he stressed that the CFTC will consider good faith compliance with the policies and procedures reasonably designed to comply with the oral communications component.

C. Presentation by Mr. Cordes, National Council of Farmer Cooperatives

Mr. Cordes then delivered his presentation. He discussed the issues and challenges faced by the CHS Hedging branch offices (approximately 64), in complying the oral taping rule. He explained that most of these branch offices have a relationship with the local cooperative or entity, and there is an individual that is licensed and registered there. In addition, most of these branch offices see a revenue stream ranging from $5,000 to $250,000 a year, with an average of $20,000, and handling a total number of trades from 100 to 4,000 a year, dealing in grains and livestock. Mr. Cordes then explained that once a trade takes place, the branch office will either call or use an electronic order entry system to place the trade. He also explained that as an FCM in the home office, CHS Hedging will manage the order, handle the margin calls, and the money moving back and forth. He then noted that this system provides farmers or ranchers at the local level with a trusted contact to deal with, easy access, and provides them with another risk management choice.

Mr. Cordes next commented that the way the rule is written, these branch offices would have to comply with oral taping requirements. He noted that because they are part of the FCM, as a branch office and as an FCM, the CHS Hedging branch offices are required to tape, which is currently being done in the home office, and two other major offices in Kansas City and Indianapolis. Mr. Cordes then raised concerns about complying with the rule. Specifically, (1) if CHS Hedging goes forward with compliance, will the branch offices drop off because they can't comply; and (2) what will happen to the risk management choices offered at the local level to the farmer?

D. Questions and Discussion

Following Mr. Cordes' presentation, Chairman Gensler asked Mr. Cordes for further clarification on the makeup of most of the branch offices. Mr. Cordes responded that most branches consist of one or two-person offices servicing the agriculture community which only carry out futures transactions. For further clarification, Mr. Dierks asked Mr. Cordes whether an individual in one of those single person branch offices might spend only fifteen or twenty minutes a day dealing with futures. In response, Mr. Cordes stated that Mr. Dierks was correct, some single person branch offices might spend fifteen minutes a day, and other offices might not look at trades for a day or two.

Mr. Anderson then asked CFTC staff to clarify the distinction between what is required for a member of an exchange versus someone who is not a member of an exchange. In addition, Mr. Cordes asked CFTC staff to discuss whether cash transactions require taping. Mr. Griffin explained that there were a number of concerns about how the proposed rule had been phrased to include cash commodity transactions if a person was a non-registrant member of a contract market. As a result, the CFTC changed the language of final rule so that cash commodity transactions were not included.

As a follow-up, Mr. Anderson asked whether this rule only applies when a person is not a member of an exchange, and what happens if one is doing cash transactions and is a member of an exchange. In response, Mr. Griffin explained there are two components. First, if a person is just engaging in cash commodity transactions, and is a member, but not an FCM, that person is not another registrant above a certain threshold or within certain parameters. The second component is the nature of who the registrant is, and this pertains specifically to the oral record-keeping requirement alone, and does not pertain to written records or things of that nature.

Mr. Griffin also explained that the oral record-keeping requirement is not applicable to: (1) oral communications that leads solely to the execution of a cash or forward transaction; (2) transactions by floor brokers who are transacting for themselves; (3) small IBs that have an aggregate revenue of not more than $5million total over the preceding 3-year period; and (4) floor traders, members of DCMs or SEFs that are not registered or required to be registered by the Commission.

Chairman Gensler commented that the CFTC needs to take a closer look at Mr. Cordes' branch office issue. He also noted, however, that when the rule was being drafted, Commissioners worked together with staff to narrow it and include various exceptions and carve-outs to principally include members of exchanges, FCMs that are members, and introducing brokers ("IBs") over a certain size.

Mr. Strong then asked Mr. Cordes whether the carving out of cash transactions from the recording requirement resolves the issues concerning the sixty-some branch offices. In response, Mr. Cordes stated that it does with respect to activities surrounding cash transactions, but it does not with respect to activities involving exchange-traded products because it is a futures transaction. And, the way the rule is written today, it would still bring the branch offices under review.

Mr. Kotschwar commented that the Commodity Markets Council ("CMC") has been very interested in this issue. He explained that while a lot of grain is bought and sold with a phone call, more transactions are taking place with a text or an instant message. He also explained that because texts and instant messages are included in the now expanded definition of an electronic record, CMC has decided to stop using such features on cell phones. He noted that this is a huge problem for the CMC membership, and that a lot of CMC members are very concerned. As a follow-up, Chairman Gensler asked Mr. Kotschwar if his company is a registered FCM. Mr. Kotschwar stated that his company is a non-clearing member of a DCM.

Mr. Miller commented that the points being made with respect to voice recording are salient because an increasing amount of transactions, particularly into things like branch offices, are coming from farmers in the form of texts, instant messages, and other types of things. He encouraged the CFTC to take a look at the type of requirements and administrative burdens being imposed by expanding the recording requirement beyond voice recordings. Mr. Miller noted that he probably does half of his cash grain transactions by text messaging. He then noted that the recording requirement raises other issues, including the length of time the recordings need to be stored, and that the reach and burden of the regulation needs to be considered.

Mr. Friesen next posed hypothetical scenarios involving Rule 1.35. For example, he asked if his broker is traveling, whether he will be required to call his broker's home office or somewhere to place his order. In response Mr. Griffin explained that it would depend on how the broker or the FCM set up their structure. He discussed one solution that firms have employed, as a bit of a stopgap measure, is the use of bridge conference lines with the home office. He noted the actual call itself is being routed through the home office, and the bridge conference line is then being recorded, making sure the call is fully compliant. Chairman Gensler added that the largest FCMs, who are broker-dealers and part of the same swap dealer families, are addressing this issue by using a bridge conference line.

Mr. Cordes asked the CFTC staff to look at the cell phone recording issue, because it comes down to what is a practical size and scale, and what is at risk to the industry. With respect to his situation, he stated that the three main offices deal with farmers and commercial entities in the trade; however, the majority of his business is transacted in the office over the phone. He then noted that because of extended trading, occasionally one of his employees could get a call from a customer on the way home or on the way to work, which might happen once a week or once a month. He asked CFTC staff how these calls should be handled, and whether Rule 1.35 is so strict that every single phone call needs to be recorded. In response, Mr. McGonagle commented that the CFTC did discuss this issue in coming out with the rule and there was concern if CFTC did not cover the use of mobile phones, business would migrate to mobile phones to avoid the recording requirement. He noted that if a person is going to use a mobile phone as part of the business, then that person must use the available technology to record the conversations or seek an alternative compliance schedule with the CFTC as soon as possible.

Mr. Wellman commented that, as a producer, if he is not making his own trades on the CME, he is calling one of those small branch offices and speaking to an employee on his or her personal cell phone. He then questioned the necessity of recording the call.

Mr. Friesen, speaking from the perspective of a hedger, commented that he is not a speculator, and does not trade in large volumes. He asked whether the rule provides him protection as a consumer. In response, Chairman Gensler commented that this is the reason for the rule; it's about market integrity and enforcement. He also noted that the CFTC needs to address Mr. Cordes' issue of the one-or two person offices, but that the rule is meant to cover members of an exchange, FCMs, or IBs over a certain size. He further emphasized that the purpose of the rule is not to stop someone from making the occasional cell phone call at night. To follow up on Mr. Friesen's point, Mr. Anderson commented that when the call is made in the middle of the night for that transaction, there will be a follow up in writing, requiring a signature that is another touch point after that phone call.

Mr. Kotschwar next commented that many CMC members have exchange memberships, and that they are non-clearing members who do all of their business through an FCM. He explained that these members are on the exchange for economic reasons and to take advantage of membership benefits. He then noted that CMC's concern is not the oral recording, but the written records that are associated with the recordings. Mr. Kotschwar then noted that his company has hundreds of locations across the country and engages in multiple transactions on any given day. Because of the recording rule, his company must keep all the electronic communications leading up to a sale and he is not sure if that is a very good policy. Mr. Kotschwar also noted that his company keeps the records with farmers that are commercially necessary, and commented that retaining text messages is a burden. Adding to Mr. Kotschwar's, Mr. Anderson commented that Mr. Kotschwar's competition may not be required to keep recordings because the competition may not be a member of an exchange.

In response, Mr. Griffin commented that the pre-existing Rule 1.35 already required retention of written records by members of DCMs as noted in a 2009 DMO advisory. Mr. Kotschwar then commented that it's likely that no one in the CMC membership was aware of the advisory. Mr. McGonagle then commented that the obligation to retain records is driven by the contents of the communication, and that the focus should not be on the method of communication. He further noted that DCMs, FCMs, and RFEDs have been required to maintain records of cash transactions for twenty-five to thirty years. He also stressed that the requirement is not a new obligation.

Mr. Anderson commented that NGFA members were caught a little off guard by the recording requirement, but have quickly caught up. However, he pointed out there is a dichotomy between what members of an exchange may be required to do even if clearing is done through an FCM versus the competition which may not be a member and therefore not required to keep records. In response, Mr. Griffin noted that with respect to communications between a member of a contract market and the FCM through which the business is conducted, there can be an agreement with the FCM that the FCM will retain those records for the required period. Mr. Anderson then clarified his previous comment noting that he was referring to farmers. He noted that the recording requirement applies when, for example, a farmer contacts someone who is a member of an exchange asking about the price of corn. However, if that same farmer contacted a nonmember, there is no obligation to record and retain that text.

Mr. Gallagher commented that his company is not required to follow the recordkeeping requirement, but voiced his concerns about it. Specifically, he noted that he understood the importance of keeping records at a large firm like Goldman Sachs which makes multiple billion dollar transactions. However, he did not understand why the rule also applies to farmers calling about corn. Chairman Gensler commented that the farmer would not need to make an oral recording, and that CFTC needs to address the branch issue.

Mr. Penner commented that his cooperative representative refuses to accept texts as orders anymore as a result of the recordkeeping requirement, and that even phone calls are discouraged to avoid any problems. He then noted that this actually discourages farmers from making timely marketing decisions.

Ms. Preston next asked CFTC for further explanation of bridge technology. She asked how the technology works, how it is setup, and how it applies to incoming and outgoing calls. Mr. Griffin explained that bridge technology involves conferencing in the parties on a phone call through a home office. Ms. Preston then asked, with respect to bridging, whether it could be done through a third party, or whether it had to be done through the party that has the recording obligation. Mr. Griffin replied that the recording obligation belongs to the registrant, but that the registrant can contract with a third party vendor to assist with recording and retaining oral communications.

Mr. Friesen commenting from a producer perspective noted his concerns about the costs of bridge technology being passed down to him. In response, Mr. McGonagle explained that a cost-benefit analysis was conducted and CFTC viewed the costs as typical costs. Mr. Gallagher then asked CFTC if it could provide specifics about the companies that provided cost estimates for the technology. Mr. McGonagle replied that the rule identifies the companies that provided estimates.

Mr. Miller commented that the recording rule is changing the dynamics of who can accept text and email communications versus who cannot accept them, and the decisions being made influence a competitive structure. He noted that there is a market access issue that ultimately falls to the farmer. For example, he explained that the texting capabilities on his phone often work better than voice. He then explained that the record-keeping rule may result in unintended consequences, and encouraged the CFTC to look at the branch office issues, as well as other related issues.

Mr. Anderson then asked whether there is a benefits analysis also included in the rule. In response, Mr. Griffin stated that the benefits were not quantified in terms of dollar amount, particularly since it is difficult to put a dollar figure on market integrity. However, he also noted that there is a great deal of discussion of costs, and to the extent specific numbers and figures were given they were included and considered.

Mr. Penner asked Mr. Cordes if he utilized this technology would he not be covering the required percentage of call and orders to satisfy the amount of the volume of trades. In response, Mr. Cordes commented in the affirmative and noted that the way the rule is written one is required to record everything. He then noted that, with respect to cost-benefit, costs for implementing the bridging technology could quickly add up based on the number of employees.

Mr. Friesen commented that with the advancement of technology, the recordkeeping requirement will soon be moot as phones will likely have applications that can make trades that are electronically tracked. Chairman Gensler agreed and also commented that most large offices are already using voice recording possibly protect the FCM against a customer’s “amnesia” trade. He further commented among other things that CFTC is trying to capture the audit trail and that CFTC may need to address the one-person branch office issue. Mr. Friesen then noted that his local elevator has estimated a recording cost of $20,000 per location, but he did not know what technology the elevator was looking at.

Mr. Dierks next commented on the responsibilities that the CFTC has been given the last few years. He asked about what exceptions will be made for agricultural industry, and noted the importance of exempting the industry. He also noted among other things the importance of integrity in the markets because the agricultural industry is still suffering from the two events that damaged trust of the marketplace. Mr. Dierks then thanked the CFTC for holding the AAC meeting, and also commented that the Committee can serve as an advocate to the customers and suggested the agency hold a panel on consumer protection the next time the AAC meets.

Following these comments, Chairman Gensler and Commissioner O'Malia thanked Dr. Fortenbery for chairing the meeting, and the AAC members for their participation. Dr. Fortenbery also thanked Chairman Gensler for sponsoring the Committee, and adjourned the meeting at 2:19 p.m. on July 25, 2013.

I hereby certify that the foregoing minutes are accurate:

June 11, 2014

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Dr. Randall Fortenbery Date

AAC Chairman