113TH CONGRESS
2d Session

HOUSE OF REPRESENTATIVES

REPORT
113–469

# FUTURES CUSTOMER PROTECTION ACT

JUNE 5, 2014.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. LUCAS, from the Committee on Agriculture, submitted the following

## R E P O R T

[To accompany H.R. 4413]

[Including cost estimate of the Congressional Budget Office]

The Committee on Agriculture, to whom was referred the bill (H.R. 4413) to reauthorize the Commodity Futures Trading Commission, to better protect futures customers, to provide end users with market certainty, to make basic reforms to ensure transparency and accountability at the Commission, to help farmers, ranchers, and end users manage risks to help keep consumer costs low, and for other purposes, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

### BRIEF EXPLANATION

### Title I—Customer Protections

The Customer Protection and End-User Relief Act, H.R. 4413, will better protect farmers and ranchers who use the futures markets by cementing several new regulatory customer protections into law. Added protections include mandates to:

- Require electronic confirmation of customer fund account balances held at depository institutions. No longer will the fraud that occurred at Peregrine Financial be allowed to occur due to forged paper documents.
- Require firms that move more than a certain percentage of customer funds from one account to another to follow strict reporting and permission requirements before doing so. No longer will a firm be able to move funds from one account to another, as happened during the MF Global bankruptcy, without regulators knowing about it.

39–006

• Require firms who become undercapitalized to immediately notify regulators so they can assess the firm's viability and act, if needed, to protect customer funds.

• Require firms to file an annual report with regulators from the chief compliance officer containing an assessment of a futures commission merchant's (FCM) internal compliance programs.

• Ensures farmers, ranchers, and other futures customers have an additional day to get their needed margin to an FCM, which mitigates the effect of pre-funding accounts.

• Provide legal clarity for futures customers that the assets of a bankrupt commodity broker would be used to help pay back any misappropriated or illegally transferred customer segregated funds.

• Require firms to calculate and report customer account balances electronically to regulators on a regular basis.

• Require the CFTC to complete a study on high frequency trading.

Title II—Commodity Futures Trading Commission Reforms

Since the enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act (P.L. 111–203) (the Dodd-Frank Act) in July of 2010, the U.S. Commodity Futures Trading Commission (CFTC) has finalized over 60 new rules to enforce the new law and has issued an unprecedented 170 "no-action" letters in that same span of time to delay, revise, or exempt application of these regulations upon various market participants. The rulemaking process has proven confusing given the lack of a comprehensive plan for setting a schedule for compliance. In addition, the prolific use of no-action letters by the Commission to revisit new Dodd-Frank Act regulations have been used in lieu of a more thorough rulemaking process. H.R. 4413 makes basic reforms to the CFTC to help make it more effective and ensures that all Commissioners' voices are heard in the rulemaking process. These reforms include:

• Modifying the Commodity Exchange Act's (CEA's) cost-benefit analysis requirements for proposed rules, to closely track President Obama's Executive Order 13563 for the entire executive branch.

• Making the Commission's division directors answerable to the entire Commission, not just the Chairman's office.

• Creating a new Office of the Chief Economist, answerable to the entire Commission, to provide objective economic data and analysis.

• Enhancing the CFTC staff procedures governing the issuance of "no-action" or interpretive letters to improve Commission oversight of the process and to prevent staff from being able to issue letters at the last moment in an attempt to regulate or deregulate markets outside of the official CFTC rulemaking process without the possibility of Commission review.

• Requiring the Commission and the Office of the Chief Economist to develop comprehensive internal risk control mechanisms to safeguard and govern all market data storage, all market data sharing agreements, and all academic research using market data.

• Creating a judicial review process similar to that of the SEC's for rulemakings to ensure the two regulators charged with overseeing the derivatives markets have similar procedures in place to allow market participants to challenge Commission rules.

• Directing the Government Accountability Office (GAO) to conduct a study on the sufficiency of CFTC resources and examine prior expenditures of funds on market surveillance and market data collection, standardization, and harmonization.

Title III—End-User Relief

Title III of the Customer Protection and End-User Relief Act was developed in response to the CFTC's implementation of the Dodd-Frank Act. Many of the CFTC's new rules have negatively impacted end-users, such as our farmers, ranchers, manufacturers, and utilities, by making it more difficult and costly to manage risks associated with their businesses. Despite America's end-users representing 94 percent of the job creators in the United States, they comprise only 10 percent of the swaps markets. Even though Congress intended to exempt end-users from some of the most costly new regulations associated with using derivatives during consideration of the Dodd-Frank Act, the CFTC has narrowly interpreted the law. As a result, the ability of producers to affordably protect against risks associated with farming and ranching has been threatened. Title III addresses the following concerns:

• True commercial end-users should not be treated as financial entities. The bill amends the CEA to allow many end-users who are legitimate "commercial market participants" to avoid being inadvertently classified as financial entities.

• Certain non-financial end-users should not be disadvantaged in the marketplace if they use contracts that trade infrequently. This issue has cost certain end-users millions of dollars in fuel hedging costs because their identifiable positions in thinly-traded markets are immediately reported to the marketplace.

• The bill provides relief to grain elevators, farmers, agriculture counterparties, and commercial market participants from burdensome and unnecessarily costly recordkeeping rules that currently require the recording of all forms of communication that may possibly lead to a trade. Instead, the bill specifies that keeping searchable written records of the final material economic terms of an agreement will be sufficient.

• The bill provides relief for end-users who use contracts that result in actual physical delivery of a commodity that has a standalone or embedded option to change the amount of a commodity delivered. This impacts utilities that use natural gas to produce electricity, in addition to millions of consumers who use natural gas to heat their homes.

• The bill corrects an illogical and unworkable capital requirement imposed on non-bank swap dealers that would result in those entities holding much more capital than their bank counterparts, likely making the business too expensive, resulting in fewer participants in the marketplace. The CFTC now must consult with the other regulators in formulating workable capital requirement formulas and recognize formulas already approved by other regulators.

• The bill amends the CEA to simply require a vote by the CFTC before the swap dealer de minimis level automatically changes from the current level of $8 billion established by the CFTC in regulations.

- The bill makes a conforming change to CFTC regulations to bring its rules in line with the Jumpstart Our Business Startups Act (JOBS Act) (P.L. 112–106). An oversight in the JOBS Act omitted funds that were also registered as Commodity Pools, and the bill allows those funds to also solicit certain potential new investors.
- The bill allows for end-users to continue to hedge against anticipated business risks by providing a more workable definition of bona fide hedging related to position limits.
- The bill also includes CEA portions of the following measures that passed the House Agriculture Committee and/or the U.S. House of Representatives with overwhelming bipartisan support:
  - H.R. 634, the Business Risk Mitigation and Price Stabilization Act that passed the House on June 6, 2013, by a vote of 441–12.
  - An amended bipartisan version of H.R. 677, the Inter-affiliate Swap Clarification Act, which originally was passed by House Agriculture Committee on March 20, 2013 by voice vote and by the Financial Services Committee on May 7, 2013, by a vote of 50–10.
  - H.R. 742, the Swap Date Repository and Clearinghouse Indemnification Act that passed the House on June 12, 2013, by a vote of 420–2.
  - H.R. 1038, the Public Power Risk Management Act that passed the House on June 12, 2013 by a vote of 423–0.
  - H.R. 1256, the Swap Jurisdiction Certainty Act that passed the House on June 12, 2013, by a vote of 301–124.

## Purpose and Need

### Title I—Customer Protections

When futures commission merchant (FCM) MF Global, Inc., failed in November of 2011 and Peregrine Financial Group, Inc. (PFGBest), followed suit in July of 2012, thousands of farmers, ranchers, and futures customers collectively lost more than a billion dollars in customer funds that were thought to be segregated by law apart from the funds of the FCMs. The bankruptcy of these two firms, caused by gross mismanagement or outright fraud, resulted in tremendous hardship for a large segment of the U.S. agricultural community and created serious public doubts about the safety of using the futures markets to manage risk. After both failures, the Committee held half a dozen hearings and heard from numerous witnesses over the course of the 112th and 113th Congresses to examine why these failures occurred and how public confidence could be restored in the futures markets.

As a result of the Committee's work, Title I of H.R. 4413 is designed to better protect futures customers and restore confidence in the marketplace while also providing regulators with enhanced tools to supervise FCMs. Importantly, sections 102, 103, and 104 of H.R. 4413 would codify regulatory changes already implemented by both the National Futures Association (NFA) and the U.S. Commodity Futures Trading Commission (CFTC), therefore the Committee does not intend for any of these sections to require new rulemakings by the NFA or CFTC in order to implement the requirements of the legislation. Section 105, however, contains statutory changes that are in conflict with existing CFTC regulations, so the Committee would expect expedited action from the CFTC to conform its regulations to the legislation when enacted into law to provide for certainty in the marketplace.

*Sec. 102—Enhanced customer protections for customers*

After MF Global filed for bankruptcy, it was revealed that in the final days before the firm's failure, customer segregated funds (cash deposits, securities, or other property of customers held by the firm to margin or guarantee futures trading) were used to fund the company's liquidity needs related to aggressive and ultimately ill-advised investments in European sovereign debt securities. Section 102 would provide the NFA and CFTC with the statutory authority to help supervise and prevent future mismanagement involving the illegal transfer of customer segregated funds.

Accordingly, Section 102 would broadly codify regulatory changes proposed by the NFA, and approved by the CFTC in July 2012, (NFA Financial Requirements Section 16) requiring FCMs to strengthen their controls over the treatment and monitoring of funds held for customers trading in the U.S. ("segregated") and foreign ("Part 30 secured") futures and options markets. Notable changes contained in the new NFA rules that would meet the statutory requirements of Section 102 include: (1) FCMs must now hold sufficient funds in Part 30 secured accounts to meet their total obligations to customer trading; (2) FCMs must maintain written policies and procedures governing the maintenance of excess (i.e., proprietary or residual) funds in customer segregated and Part 30 secured trading accounts; (3) any withdrawals of more than 25% of the excess segregated or Part 30 secured funds that are not for the benefit of customers must be pre-approved in writing by the FCM's senior management; and (4) FCMs must file notice with the NFA of any withdrawal of 25% or more of the excess segregated or Part 30 secured amount funds that are not for the benefit of customers.

On July 25, 2012, at a hearing entitled "Oversight of the Swaps and Futures Markets: Recent Events and Impending Regulatory Reforms," the following testimony was provided by witnesses with respect to NFA provisions incorporated in Section 102:

> All of these rule changes promote greater transparency for both customers and regulators and should help prevent a recurrence of the type of problems we saw at MF Global. These rule changes, however, are only the beginning. The MF Global and Peregrine customer losses are a painful reminder that we must continuously improve our surveillance, audit and fraud detection techniques to keep pace with changing technology and an ever-more-complicated financial marketplace.—Mr. Daniel Roth, President, NFA

> In direct response to the MFG collapse, the "Corzine Rule" will be implemented on September 1st. The "Corzine Rule" requires the CEO or CFO of the FCM to pre-approve in writing any disbursement of customer segregated funds not made for the benefit of customers and that exceeds 25% of the firm's excess segregated funds. The CME (or other SROs) must be immediately notified of the pre-ap-

> proval.—Mr. Terrance A. Duffy, Executive Chairman & President, CME Group Inc.
>
> We also recommended and supported rules adopted by the Chicago Mercantile Exchange and National Futures Association that subject all FCMs to enhanced recordkeeping and reporting obligations, including . . . requiring the chief financial officer or other appropriate senior officer to authorize in writing and promptly notify the FCM's DSRO whenever an FCM seeks to withdraw more than 25 percent of its excess funds from the customer segregated account in any day. These changes have now been approved by the Commission.—Hon. Walt Lukken, President & Chief Executive Officer, Futures Industry Association (FIA)

On March 14, 2013, at a hearing entitled "Examining Legislative Improvements to Title VII of the Dodd-Frank Act," the Hon. Gary Gensler, Chairman, U.S. Commodity Futures Trading Commission, provided the following testimony with respect to provisions that were ultimately included in Section 102:

> The Commission also worked closely with market participants on new customer protection rules adopted by the self-regulatory organization (SRO), the National Futures Association (NFA). These include requiring FCMs to hold sufficient funds for U.S. foreign futures and options customers trading on foreign contract markets (in Part 30 secured accounts). Starting last year, they must meet their total obligations to customers trading on foreign markets under the net liquidating equity method. In addition, withdrawals of 25 percent or more of excess segregated funds would necessitate pre-approval in writing by senior management and must be reported to the designated SRO and the CFTC.

On May 21, 2013, testifying before the Committee at a hearing entitled "The Future of the CFTC: Market Perspectives," Mr. Daniel Roth, President, NFA, provided the following testimony with respect to the provisions included in Section 102:

> All FCMs maintain excess segregated funds. These are funds deposited by the FCM into customer segregated accounts to act as a buffer in the event of customer defaults. Because these funds belong to the FCM, the FCM is free to withdraw the excess funds, but after MF Global, NFA and the CME adopted rules to ensure notice to regulators and accountability within the firm. Now all FCMs must provide regulators with immediate notification if they draw down their excess segregated funds by 25% in any given day. Such withdrawals must be approved by the CEO, CFO or a financial principal of the firm and the principal must certify that the firm remains in compliance with segregation requirements. This rule became effective on September 1, 2012.

*Sec. 103—Electronic confirmation of customer funds*

On Monday, July 9, 2012, the founder and Chairman of Peregrine Financial Group, Inc., Russell R. Wasendorf Sr., unsuccessfully attempted suicide outside of the firm's Cedar Falls, Iowa, headquarters. He left a note admitting to producing elaborate forgeries of bank documents submitted to regulators. In court filings the next day, the CFTC alleged that PFGBest and Wasendorf "committed fraud by misappropriating customer funds, violated customer fund segregation laws, and made false statements in financial statements filed with the [CFTC]" and that Wasendorf may have falsified certain bank records. According to press reports, Mr. Wasendorf's suicide attempt which led to the discovery of the fraud occurred only days after the NFA first required PFGBest to electronically confirm customer balances directly through a third-party electronic auditing system with PFGBest's banks. Prior to this requirement, self regulatory organizations such as the NFA and CME had relied on paper statements from an FCM's bank.

Section 103 would provide broad statutory authority to codify regulatory changes first proposed in 2012 by a special committee composed of futures industry SROs (including the CME Group, NFA, InterContinental Exchange, the Kansas City Board of Trade, and the Minneapolis Grain Exchange) to require: (1) confirmation of the balances of customer segregated bank accounts for all FCMs using a web-based electronic confirmation process; (2) all FCMs to provide their designated-SRO with direct online access to confirm segregated and secured funds balances at the banks which hold the FCM's customer segregated and secured funds; and (3) any bank that fails to provide electronic online access will not be considered an acceptable depository for holding customer segregated and secured funds.

Notably, in light of the PFGBest fraud, Section 103 would also provide the statutory authority for regulations that require FCMs to file segregation and Part 30 secured amount computations on a daily basis with the NFA. Additionally, FCMs must file with the NFA detailed information regarding the banks holding customer funds and the investments made with customer funds as of the 15th and last business day of each month.

On July 25, 2012, at a hearing entitled "Oversight of the Swaps and Futures Markets: Recent Events and Impending Regulatory Reforms," the following testimony was provided by witnesses with respect to provisions the Committee decided to include in Section 103:

> NFA intends to expand this approach, once it is implemented, to receive daily reports from all depositories for customer segregated accounts, including clearing FCMs. We will develop a program to compare these balances with those reported by the firms in their daily segregation reports. While there may be reconciling items due to pending additions and withdrawals, the system will generate an immediate alert for any material discrepancies. We have also agreed with the CME to perform an immediate confirmation of all customer segregated bank accounts for all of our FCM Members using the e-confirmation process I referred to earlier. The completion of this work within the next week or so should help ensure that another Peregrine is not lurking in the industry.—Mr. Daniel Roth, President, NFA

> First, FIA strongly supports providing regulators with the independent ability to electronically review and confirm customer segregated balances across every FCM at any time. Second, FIA supports the creation of an automated confirmation process for segregated funds that will provide regulators with timely information that customer funds are secure. Technology solutions can help prevent this type of event from occurring again.—Hon. Walt Lukken, President and Chief Executive Officer, FIA

On October 2, 2013, testifying before the Committee at a hearing entitled "The Future of the CFTC: Perspectives on Customer Protections," Mr. Daniel Roth, President, NFA, provided the following testimony:

> For years, NFA and other SROs confirmed FCM reports regarding the customer segregated funds held by the FCM through traditional paper confirmations mailed to the banks holding those funds. These confirmations were done as part of the annual examination process. In early 2012 NFA began confirming bank balances electronically through an e-confirm process. That change led to the discovery of the fraud at PFG, but e-confirms were still done as part of the annual examination. We had to find a better way and we did. We partnered with the CME and developed a process by which NFA and the CME confirm all balances in all customer segregated bank accounts on a daily basis. FCMs file daily reports with NFA and the CME, reflecting the amount of customer funds the FCM is holding. Through a third-party vendor, NFA and CME get daily reports from banks for the over 2,000 customer segregated bank accounts maintained by FCMs. We then perform an automated comparison of the reports from the FCMs and the reports from the banks to identify any suspicious discrepancies. In short, Mr. Chairman, the process by which we monitor FCMs for segregated fund compliance is now far ahead of where it was just one year ago. We have recently expanded this system to also obtain daily confirmations from clearing firms and will expand it again by the end of the year to include clearinghouses as well.

*Section 104—Notice and certifications providing additional customer protections*

On October 22, 2012, the CFTC proposed additional rules to enhance several aspects of supervision in order to better protect customers of FCMs. Just over a year later, these new rules were finalized and adopted by the CFTC. In order to codify the CFTC's authority to increase customer protections, Section 104 would require that FCMs notify both the CFTC and the appropriate self-regulatory organization when they become under-capitalized or under-segregated. By legally requiring that an FCM notify authorities as soon as the firm is faced with an undercapitalization scenario, regulators will have the power to step in and take preventative or corrective action to protect customer segregated funds. This would help prevent the same type of harm to customers that occurred when MF Global illegally transferred hundreds of millions of dollars of customer segregated funds to cover its trading shortfalls.

Similarly, Section 104 requires FCMs to file a report at the end of each fiscal year that details an assessment of an FCM's internal compliance programs so the Commission can evaluate whether the controls are adequate or need to be improved or modified.

On October 2, 2013, testifying before the Committee at a hearing entitled "The Future of the CFTC: Perspectives on Customer Protections," Mr. Dan Roth, President, NFA, provided the following testimony with respect to the CFTC's provisions included in Section 104:

> The Commission also proposed its own changes to customer protection rules in a 107-page Federal Register release last year. Certain parts of the Commission's proposals have provoked strong opposition both from the industry and from end-users of the markets, particularly in the agricultural sector. As described below, NFA shares many of the concerns raised by others, but we fully support many of the Commission's proposals. For example, the Commission's proposed rules would:
>
> • Require SROs to expand their testing of FCM internal controls and develop more sophisticated measures of the risks posed by each FCM;
>
> • Require that FCM certified annual financial reports and reports from the chief compliance officer be filed within 60 days of the firm's fiscal year end;
>
> • Require that an FCM that is undercapitalized provide immediate notice to the Commission and its DSRO . . .

*Section 105—Futures Commission merchant compliance*

On October 22, 2012, the CFTC proposed additional rules to enhance several aspects of customer protections at FCMs. Among the proposals was a requirement to shorten the time period an FCM has to collect additional funds for a margin call from a customer to one business day. Another proposal would require an FCM to hold enough of its own capital (known as "residual interest") to cover the changing positions of all customers at all times of the day. As a result, many FCMs would have to use their own capital to satisfy these margin calls, and customers could also be required to hold more funds at an FCM.

Unfortunately for many farmers and ranchers who use futures to hedge their operating risks, a part of the CFTC "customer protection" rule finalized in October of 2013 could result in significant harm to these core constituencies of the Committee. The new rule will require farmers and ranchers to pre-fund their margin accounts due to onerous new requirements that force FCMs to hold large amounts of cash in order to pay clearinghouses at the start of trading the next business day. The increased costs of pre-funding margin accounts will likely drive many small and medium-sized agricultural producers out of the marketplace. When the small players are forced out of the markets, the small and medium-sized FCMs will be forced to consolidate, giving customers fewer choices.

On May 21, 2013, testifying before the Committee at a hearing entitled "The Future of the CFTC: Market Perspectives," the following testimony was provided by witnesses with respect to problems with the CFTC's proposed rule:

> However, this rulemaking also seeks to fundamentally change the way in which the futures marketplace operates. As we explained in our comment letter, if a proposed "protective" measure is so expensive or its impact on market structure is so severe that customers cannot effectively use futures markets to mitigate risk or discover prices, the reason to implement that measure needs to be re-examined. Among the proposed rules to reevaluate is the rule that would require *at all times* an FCM's residual interest (its own funds) in segregated accounts to exceed the margin deficiencies of its customers. It does not appear that any system currently exists or could be construed in the near future will permit FCMs to accurately calculate customer margin deficiencies, continuously in real-time. Without access to this data, FCMs will be required to maintain substantial residual interest in segregated accounts or require customers to significantly over-collateralize their accounts. We believe this will be a significant and unnecessary drain on liquidity that will make trading significantly more expensive for customers to hedge. We believe this rule and others could have a very significant impact on certain sectors in the marketplace, particularly smaller FCMs that serve the agricultural community.—Mr. Terrance A. Duffy, Executive Chairman and President, CME Group Inc.

> In the end, this new interpretation will result in FCMs requiring customers to put up more money at all times, likely resulting in customers being asked to pre-fund their margin. In addition to requiring customer pre-funding, some have suggested that this rule will likely require an FCM to double a customers' overall margin requirements: in essence requiring customers to fund their potential margin deficiencies. As such, the customer would be required to keep margin funds far in excess of exchange minimum margin requirements. Our mid-sized commercial customers rely upon their lending institutions, such as CoBank, a member of the Farm Credit System, to fund their commercial activities including their hedging activities. A potentially doubling of their funding needs to support their hedging activities would significantly impact the profitability of such customers. In addition to the negative customer impact, the rule will also put significant financial pressure on FCMs. If the sum of an FCM's customer margin deficits is greater than the residual interest an FCM typically maintains in their customer accounts, then the FCM would have to increase the amount of residual interest it maintains in customer segregated accounts. On "limit up" or "limit down" days in the agricultural exchange traded markets, our firm may be required to deposit up to $400 million to satisfy exchange demands for margin. In order to ensure that our residual interest would be in excess of the sum of all of our customers margin defi-

> ciencies in such a situation, we would need to require our customer pre-fund their potential margin deficiencies or in effect require us to pre-fund their potential margin requirements by maintaining our capital in customer segregated accounts. Requiring massive additional injections of our own capital to support the new residual interest requirements will, at some point, become unsustainable for us and others, again leading to the real and substantial risk of increased concentration in an already shrinking market.—Mr. William J. Dunaway, CFO, INTL FCSTONE, Inc.

On July 24, 2013, at a hearing entitled "The Future of the CFTC: End-User Perspectives," the following witnesses also provided testimony with respect to problems with the CFTC's proposed rule:

> Regulations that would accelerate a further consolidation in the FCM industry would have the adverse effect of leaving commodity hedgers with fewer options, while concentrating risk among fewer FCM entities . . . [a]nother provision would require that an FCM's residual interest in the customer-segregated account must at all times be sufficient to exceed the sum of the margin deficits that the FCM's customers have in their accounts. This requirement is counter to the historical interpretation, which requires an FCM to maintain residual interest to cover customer-segregated accounts with negative net liquidating balances (debit equity). This gives an FCM time to collect customer funds prior to the time a payment must be made to the clearing house. In addition to increased costs for hedgers, this proposed rule would be more burdensome to firms like farmer cooperative-owned FCMs, which largely deal only with hedgers. Although the risk profile of the customer base is very low, customers are predominantly on one side of the market and therefore more susceptible to big swings in the market. To require all deficits to be covered immediately would be overly burdensome on these FCMs given the low-risk profile of their customers as hedgers.—Mr. Scott Cordes, President, CHS Hedging, Inc., on behalf of the National Council of Farmer Cooperatives (NCFC)

> Specifically, CMC strongly believes that the proposed requirement that FCMs maintain a residual amount sufficient to cover on a constant basis the aggregate of customer margin deficits could create considerable liquidity issues and increase costs for FCMs, producers, and end-users. Such a decrease in liquidity could be substantial and limit the number and type of transactions FCMs clear, the number of customers they service, and the amount of financing they provide. The proposal would require FCMs to fund accounts holding their customers' collateral with proprietary assets in excess of the aggregated margin deficiencies of all its clients on a continuous basis. The proposal also appears to require executing FCMs to collect collateral for give-ups so that customer positions are fully margined in the event a clearing FCM rejects a trade. If the proposed residual interest provision were to be final-

> ized, FCMs may be forced to take steps such as over-margining clients, requiring clients to pre-fund their margin accounts, imposing punitive interest rate charges on margin deficit balances, and introducing intra-day margin calls. Such steps would dramatically increase the cost of using futures markets and may force many end-users to decrease or discontinue hedging and risk management practices, which is the reason these markets were created.—Mr. Lance Kotschwar, Senior Compliance Attorney, The Gavilon Group, LLC, on behalf of the Commodity Markets Council

On October 2, 2013, testifying before the Committee at a hearing entitled "The Future of the CFTC: Perspectives on Customer Protections," the following additional testimony was provided by witnesses with respect to their concerns about the CFTC's proposed rule:

> We believe that the CFTC's proposal respecting the required residual interest that must be maintained by FCMs in the customer segregated account will adversely impact customers and fundamentally change the way in which futures markets operate. If a proposed "protective" measure is so expensive or its impact on market structure is so severe that customers cannot effectively use futures markets to mitigate risk or discover prices, there is no justification for implementing that measure. The proposal on "residual interest" fails this test . . . [t]he residual interest rule is not necessary to protect customer funds. Its costs and negative consequences outweigh any added protection. This over-collateralization is unwarranted from a risk management standpoint. No regulatory risk model assumes that *all* customers with margin requirements will fail promptly to meet them. The proposed rule will unnecessarily drain liquidity and increase the cost of hedging financial and commercial risk especially for farmers and ranchers using our markets. Smaller and mid-sized firms that serve them will suffer the greatest impact of these increased costs, and may be driven out of business, leaving farmers and ranchers with fewer FCMs to facilitate their risk management goals. This will actually increase systemic risk by concentrating risk among fewer firms. Ironically, the proposal would force customers to place more collateral with their FCM—when they may be trying to actively avoid fellow-customer risk or FCM misconduct. We understand the Commission is considering phasing in the rule, possibly to mitigate the consequences I just described. A phase-in does not cure the problem. Instead, CME supports the FIA alternative—that would permit an FCM to calculate its required residual interest as of 6:00 p.m. on the first business day after the trade date.—Mr. Terrance A. Duffy, Executive Chairman & President, CME Group Inc.

> Other provisions of the Commission's proposals, however, raise serious concerns, particularly with regard to the so-called "residual interest" issue . . . [t]he Commission has now proposed that all FCMs must maintain at all

times a residual interest sufficient to exceed the sum of all margin deficits that the customers in each account class have. Essentially, FCMs would have to assume that every customer will default on every margin call and maintain capital in the segregated account to cover that possibility. Several points need to be made on this proposal. First, it has absolutely nothing to do with the problems encountered at either MF Global or PFG. Neither of those cases had anything to do with customers failing to meet margin calls. Second, this is the first time in the Commission's 39-year history that it has ever taken the position that the Act requires FCMs to assume that all customers will default on all margin calls. Third, the underlying assumption that in this day and age no customers meet margin calls by writing checks is wrong. Agricultural hedgers frequently meet their margin calls with checks. Fourth, the impact of this proposal could be devastating for both agricultural end-users and the relative handful of FCMs that service those customers. Customers will have to post much more margin funds with their FCMs or the FCMs will have to maintain much more capital in their business. Either way, there will be fewer customers using futures markets to hedge and fewer FCMs handling their accounts. This proposal does not just fix something that is not broken, it threatens to do real harm to a longstanding system that has worked well for both customers and the markets.—Mr. Daniel Roth, President, NFA

For many years, grain hedgers and the futures commission merchants (FCMs) with whom they work to manage their risk have relied on a consistent interpretation of the Commodity Exchange Act by the Commodity Futures Trading Commission (CFTC) with regard to posting margin funds to their hedge accounts. Unfortunately, in the name of customer protection, that interpretation recently has been thrown into question by a new proposal from the CFTC that we believe would dramatically increase customer risk. We understand that CFTC Commissioners currently are evaluating a final staff draft of this rule, with the goal of voting on a final rule later this month. The rule seeks to bolster futures customer protections—a laudable goal that the NGFA supports fully. However, two very troublesome provisions would have the perverse effect of significantly increasing financial risk to futures customers—and in the process, dramatically changing the way business has been conducted in futures markets for decades . . . [t]he second provision potentially is even more troublesome and more expensive to futures customers. It would change the timing of FCMs' calculation of residual interest for futures accounts—in other words, it appears the proposal would require all customers to be fully margined at all times. While this may sound like common sense, it is a huge departure from the CFTC's interpretation for decades that FCMs be allowed a certain period of time to "top up" hedge accounts while they wait for customers to make margin calls. This new proposal would lead to one of two outcomes: either the FCM would have to move more of its own funds (i.e., residual interest) into customers' hedge accounts; or FCMs would be forced to require pre-margining and, perhaps, intra-day margining, to ensure that each individual customer is fully margined at any moment. The practical end result would be that futures customers would be required to send much more money to their FCMs in advance in anticipation of futures market moves that might never happen. Some customers likely would exit futures markets in favor of lower-cost risk management alternatives. We believe this potential exodus from futures markets would be most clearly seen among agricultural producers who utilize futures for risk management purposes and among smaller grain-hedging firms. Taken to its logical conclusion, we believe strongly that neither proposal accomplishes the Commission's stated goal of enhancing customer protection. To the contrary, customers would be sending much larger amounts to their FCMs, leading to much greater volume of funds at risk if another MF Global situation occurs. If this rule had been in place when MF Global failed, perhaps twice as much customer money would have been missing and a correspondingly larger amount still would not be returned to customers.—Mr. Michael J. Anderson, Regional Sales Manager, The Andersons Inc., on behalf of the National Grain and Feed Association

Requiring FCMs to increase risk management standards, increasing the requirements for residual interest in segregation, and the reduction in days to collect margin calls before they become capital charges are all aimed at protecting an FCM's customer from losses incurred by other customers of the FCM. Most of these changes have significant costs associated with them . . . [t]he requirement to maintain residual interest in segregated funds greater than all margin calls at all times will not only be very difficult to track, but force us to choose between doubling or possibly tripling our capital, or greatly increasing the funds we require our customers to deposit to ensure they never have a margin call. For smaller customers, or those who can't follow the markets on a minute to minute basis, meeting margin calls on a moment's notice is a difficult thing to do. This is especially true of small hedge customers, who would then be faced with liquidation of hedges. For Frontier Futures as a firm, the option to increase our capital by that much may not be possible, and increasing margins may cause many of our customers to either leave us for other firms or cease trading altogether. The broader consequence of the residual interest rule may be to force a consolidation in the number of small to mid-sized FCMs. Currently, FCMs charge margins based on margin requirements set by the exchanges. The new rules will create a competitive imbalance favoring firms with access to large amounts of capital, such as the bank owned FCMs, as these firms will be able to fund margin calls by their customers with this capital. Firms without this ac-

> cess will be forced to charge much higher margin rates to their customers, and may result in a migration of some customers out of these firms. With fewer customers available to some firms, there is bound to be consolidation. This will mostly affect small to mid-sized FCMs who clear small hedgers as well as guarantee Introducing Brokers.—Mr. Theodore Johnson, President, Frontier Futures, Inc.

In order to address the significant concerns voiced by market participants, regulators, and other stakeholders, the Committee directs the CFTC, in carrying out the requirements of Section 105, to consider an FCM in compliance with any requirements to use its own proprietary funds, in the form of residual interest, to satisfy margin deficits of the FCM's customers if such requirements are met at the end of the first business day following a trade date. This would obviate the need for pre-funded margin accounts.

*Section 106—Certainty for Futures customers and market participants*

Section 190.08(a)(1)(ii)(J) of the CFTC's regulations (17 C.F.R. § 190) defines customer property as including "cash, securities or other property of the debtor's estate, including the debtor's trading or operating accounts and commodities of the debtor held in inventory, but only to the extent that the property enumerated is insufficient to satisfy in full all claims of public customers." The Committee's plain reading of this CFTC regulation is that property of the debtor FCM, even though not held as customer property, becomes customer property to the extent necessary to satisfy net equity claims of "public customers," who are defined in CFTC Regulations Section 190.01 as all customers other than certain control persons, affiliates, and related parties (i.e.: non-public customers). In effect, in order to protect the funds of customers held in segregation, CFTC Regulation 190.08 subordinates the claims of non-public customers and non-customer creditors, other than properly perfected liens on such property of the debtor, to the claims of public customers with respect to the property of the FCM that was not held (and not required to be held) as customer property.

However, in 2000, doubts as to the validity of CFTC Regulation Part 190.08(a)(1)(ii)(J) arose after a federal bankruptcy court (*In re Griffin Trading Co.,* 245 B.R. 291 (Bankr. N.D. Ill. 2000)) rejected an attempt by the trustee to use a bankrupt commodity broker's estate to pay shortfalls in the customer accounts. Among the issues in the case, which was later settled and the court's holding vacated therefore resulting in no binding judicial precedent, was whether the CFTC's broad definition of "customer property" in section 190.08 of the CFTC regulations would determine which assets could be used to repay customers. The court found that the CFTC exceeded its statutory authority in enacting section 190.08 with a definition of customer property more expansive than that used in the U.S. bankruptcy code. Further, the court found that, "any shortfall in the customer property as defined in [the bankruptcy code] must be treated as a general unsecured claim." This vacated court decision has left uncertainty about whether, in the event that customer assets are insufficient to cover all customer claims, customers can have first priority to an FCM's general estate assets until all customer claims are paid in full.

On October 2, 2013, testifying before the Committee at a hearing entitled "The Future of the CFTC: Perspectives on Customer Protections," Mr. Daniel Roth, President, NFA, provided the following testimony with respect to the need for the provisions included in Section 106:

> NFA believes, however, that Congress should consider a statutory change to strengthen customer protections and priorities in the event of a future FCM bankruptcy. Over 30 years ago the CFTC adopted rules regarding FCM bankruptcies. Among other things, those rules provided that if there was a shortfall in customer segregated funds, the term "customer funds" would include all assets of the FCM until customers had been made whole. Several years ago, a district court decision cast doubt on the validity of the CFTC's rule. That decision was subsequently vacated but a cloud of doubt lingers. Congress can and should remove that doubt about the priority customers should received if there is a shortfall in segregated funds and can do so by amending Section 20 of the Act. Section 20 gives the CFTC authority to adopt regulations regarding commodity brokers that are debtors under Chapter 7 of Title 11 of the United States Code. We would suggest an amendment to clarify the CFTC's authority to adopt the rule that it did.

In order to provide clarity for the marketplace and make clear that the CFTC did not exceed its authority to promulgate Rule 190.08 under Section 20(a) of the Commodity Exchange Act, the Committee intends for Section 106 to provide for the broad use of the assets of a commodity broker's estate, other than secured property (such as property held at a clearinghouse, including offset or netting rights of creditors with respect to such type of property), to satisfy shortfalls in customer property beyond what was held in customer segregated accounts at the time of a firm's failure.

*Section 107—Study on high frequency trading*

The Committee recognizes growing public concern and multiple questions arising from the practice in derivative markets commonly known as "automated" or "high frequency" trading. During hearings in the 112th and 113th Congresses, one CFTC Commissioner and two end-user groups testified as to their apprehension about this practice and its implications for derivative markets. Before taking any action, it is prudent for the Committee to learn more about high frequency trading. To that end, the Commission is charged with providing the Committee with a report examining the impact this practice has upon markets under its jurisdiction. It should be noted that the Committee recognizes that on September 9, 2013, the CFTC approved a "concept release" on "Risk Controls and System Safeguards for Automated Trading Environments" that examines marketplace conditions and explores possible regulatory changes with respect to high frequency trading. To speed compilation of the results, the Committee would view that the Commission has completed the requirements of Section 107 if the study results are incorporated as part of further action on its concept release.

Title 2—Commodity Futures Trading Commission Reforms

*Section 202—Extension of operations*

The most recent reauthorization for CFTC budgetary appropriations was approved in 2008 as a part of the Food, Conservation and Energy Act (P.L. 110–246), prior to the financial crisis of 2008 and the enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act (P.L. 111–203) (The Dodd-Frank Act). That statutory authorization expired September 30, 2013. Although the CFTC relied on unauthorized appropriations between 2005 and 2008, successful legislative reauthorizations occurred in 1978, 1983, 1986, 1992, 1995, and 2000. These have ranged from basic legislative reauthorizations, such as the CFTC Reauthorization Act of 1995, to significant changes in the law, such as the Commodity Futures Modernization Act of 2000. Section 202 would reauthorize the Commission to receive budgetary appropriations through 2018.

*Section 203—Consideration by the Commodity Futures Trading Commission of the costs and benefits of its regulations and orders*

Section 15(a) of the Commodity Exchange Act sets forth requirements for the CFTC to consider the costs and benefits of the Commission's actions. In each proposed rule, however, the CFTC identifies the limitations of Section 15(a) in requiring cost-benefit analysis, stating "[b]y its terms, Section 15(a) does not require the Commission to quantify the costs and benefits of an order to determine whether the benefits of the order outweigh its costs; rather, it requires that the Commission 'consider' the costs and benefits of its actions."

Consequently, the CFTC's Office of Inspector General (OIG) issued an investigative report in April of 2011 that examined the cost-benefit analysis performed by the Commission in connection with Dodd-Frank rulemakings. In that report, the OIG stated ". . . it is clear that the Commission staff viewed section 15(a) compliance to constitute a legal issue more than an economic one, and the views of the Office of General Counsel therefore trumped those expressed by the Office of the Chief Economist . . . [w]e do not believe this approach enhanced the economic analysis performed. . . ."

On January 18, 2011, President Obama issued Executive Order No. 13563, which requires non-independent executive branch agencies to conduct cost-benefit analyses to ensure that both the quantitative and qualitative costs and benefits of proposed rulemakings are taken into account. The Executive Order also requires that regulations be accessible, consistent, written in plain language, and easy to understand. Because the CFTC is an independent agency, it was not required to abide by the order for any of its Dodd-Frank Act rulemakings.

As the CFTC continues to advance new rules that govern a large sector of the derivatives marketplace for the first time, this section raises the legal standard for cost-benefit analysis and evaluation. Further, the legislation is intended to operate consistently with Executive Order 13563. However, so as to not disrupt the regulatory process, this legislation is not retroactive in nature and would not impact previously proposed or finalized rules promulgated by the CFTC.

On March, 14, 2013, at a hearing entitled “Examining Legislative Improvements to Title VII of the Dodd-Frank Act,” the following testimony was provided with respect to provisions included in Section 203:

> . . . SIFMA has encouraged regulators to conduct comprehensive cost-benefit analysis for all Dodd-Frank Rules. This is consistent with the Obama Administration’s efforts to promote better cost benefit analysis for Federal agencies through Executive Order 13563, which requires all agencies proposing or adopting regulations to include cost-benefit analyses in an attempt to minimize burdens, maximize net benefits and specify performance objectives. The President also stated that regulations should be subject to meaningful public comment, be harmonized across agencies, ensure objectivity and be subject to periodic review. In 2012, in testimony before the House Committee on Government Reform, SEC Chairman Schapiro stated “I continue to be committed to ensuring that the Commission engages in sound, robust economic analysis in its rulemaking, in furtherance of the Commission’s statutory mission, and will continue to work to enhance both the process and substance of that analysis.” Congressman Conaway has introduced legislation (H.R. 1003) that would require the CFTC’s cost-benefit analysis to be both quantitative and qualitative and specifies in greater detail the costs and benefits that the CFTC must take into account as part of their cost-benefit analyses.—Hon. Kenneth E. Bentsen, Acting President and CEO, the Securities Industry and Financial Markets Association (SIFMA)
>
> Finally, because of our experience with the $25 million sub-threshold, we are intrigued by another bipartisan bill recently introduced in the House. The legislation, H.R. 1003, would require the CFTC to quantify the costs and benefits of future regulations and orders. Sadly, the legislation is prospective, but we believe that had such an analysis been made, it could have prevented the turmoil currently being caused by the $25 million special entity sub-threshold.—Mr. Terrance P. Naulty, General Manager and CEO, Owensboro Municipal Utilities (Owensboro, KY)

On May 21, 2013, at a hearing entitled “The Future of the CFTC: Market Perspectives,” Mr. Stephen O’Connor, Chairman, International Swaps and Derivatives Association, Inc. (ISDA), provided the following testimony with respect to provisions included in Section 203:

> An appropriate cost-benefit analysis was both required and desirable prior to finalization of rules; however in a number of instances the CFTC’s analysis did not comply with the regulatory standard. As the Jun. 2012 report by the CFTC Inspector General stated: “. . . Generally speaking, it appears CFTC employees did not consider quantifying costs when conducting cost-benefit analyses for the definitions rule. As indicated in the rule’s preamble, the

> costs and benefits associated with coverage under the various definitions (in light of the various regulatory burdens that could eventually be associated with coverage) were not addressed . . ." The lack of an appropriate cost-benefit analysis makes it especially important that the application and implementation of the final rules be phased in a flexible manner. Doing so would help ensure that rules achieve the purposes for which they are intended and do not impose burdensome costs on the financial system. It would also help regulators to identify and avoid unintended consequences of their actions. And it would encourage regulators to properly allocate limited resources.

*Section 204—Division Directors*

In order to ensure Division Directors are responsive to the entire Commission, this section requires that the heads of each of the units of the Commission serve at the pleasure of the Commission, perform functions as the Commission may prescribe and report directly to the Commission. Given this language is modeled after identical language currently in the CEA applicable to the General Counsel and Executive Director, the Committee expects this section to be implemented in a similar manner to those two positions.

*Section 205—Office of the Chief Economist*

In order to enhance the legitimacy of economic analysis of rules promulgated by the Commission, this section establishes an Office of the Chief Economist (OCE) with structure and power mirroring that of the Office of the General Counsel. Again, to prevent the Chief Economist from serving solely at the pleasure of the Chairman, this section establishes that the Chief Economist will be appointed by the Commission, report directly to the Commission, and perform functions at the request of the Commission in a manner similar with the General Counsel and Executive Director.

*Section 206—Procedures governing actions taken without a commission vote*

With respect to Title VII of the Dodd-Frank Act alone, the Commission has finalized 43 rules, with 15 additional rules proposed, while CFTC staff has issued over 170 non-binding staff "no-action relief" letters since July 2012 alone. At least 24 of these no-action letters are self-described as permanent. At times, "no-action" letters provide market participants with guidance on how the Enforcement Division staff of the CFTC would act in the event of market emergencies or would interpret recently proposed rules, at least in the short term. However, it appears that over the past year, staff "no-action" letters have become commonplace to revise the implementation of key regulations of Dodd-Frank, and as such do not require a vote of the Commission. Additionally, regardless of a designation as permanent, "no-action" letters are still non-binding in the legal sense that CFTC staff could decide to withdraw the letter at anytime or the Commission could take a different position and overrule the letter.

On July 23, 2013, at a hearing entitled "The Future of the CFTC: Commission Perspectives," CFTC Commissioner Scott O'Malia provided the following testimony with respect to problems with this approach:

> . . . [i]nstead of undertaking Commission action to amend problematic rules, CFTC staff has issued an unprecedented number of no-action letters, some of which are indefinite and have no expiration. So far, CTFC staff has issued over 100 no-action letters granting relief from its new regulations under Dodd-Frank, and I won't be surprised if this number continues to grow. No-action letters are not voted on by the Commission and are not published in the Federal Register. They do not include comment periods and many impose conditions on affected parties. This process is at odds with basic principles of the APA, like public participation and the opportunity to be heard. It also goes against President Obama's Executive Orders Nos. 13563 and 13579, mandating that administrative agencies "create an unprecedented level of openness in Government" and "establish a system of transparency, public participation, and collaboration."

In order to bring policy making back to a more open and transparent manner, Section 206 requires that the Commission be provided 7 days notice before any division or office of the Commission issues a response to a formal, written petition for an exemptive, no-action or interpretive letter. The Committee would view any attempt to needlessly delay providing notice to the Commission until a regulatory deadline or need for no-action relief is imminent (so as to avoid the statutorily required 7 day review period) as a violation of the requirements contained in Section 206.

After receiving notice, any member of the Commission may request a meeting of the Commission to further consider the staff-proposed action, and if the Commission decides to hold the meeting by majority vote, the matter may not be issued until the meeting has concluded. The 7 day notice requirement can be waived by a majority vote of the Commission, but only if the Commission determines that requiring such notice would be impracticable, unnecessary, or contrary to the public interest.

*Section 207—Strategic technology plan*

On July 23, 2013, at a hearing entitled "The Future of the CFTC: Commission Perspectives," Commissioner Scott O'Malia provided the following testimony with respect to the need for provisions the Committee included in Section 207:

> A critically important component to any solution for the Commission's approach to its greatly expanded mission is the use of technology in order to accept, sort, aggregate, and analyze the new sources of market information provided for under the Dodd-Frank Act. I'd like to highlight two major challenges in data and technology: (1) problems faced by market participants in the swap data reporting rules and (2) problems faced by the Commission in understanding the massive data flows as a result of our enhanced oversight of the swaps and futures markets . . . [g]iven the Commission's expanded regulatory responsibilities, it is imperative for the Commission to develop a tech-

> nology plan that can assist the Commission with meeting its regulatory objective. I believe the Commission must develop a five-year strategic plan that is focused on technology, with annual milestones and budgets. To keep up to speed with the challenges of enhanced regulatory oversight, this technology plan would require each CFTC division to develop a technology budget that reflects the regulatory needs and responsibilities of that particular division.

In order to solve the problems enumerated by Commissioner O'Malia, Section 207 requires the Commission to develop and file a strategic technology plan every 5 years with the House and Senate Agriculture Committees. The plan shall include a detailed technology strategy focused on market surveillance and risk detection, market data collection, aggregation, interpretation, normalization, standardization, harmonization, streamlining, and internal management and protection of data collected by the Commission. The report must also include a detailed accounting of how appropriated funds provided for technology will be used, and set annual goals to be accomplished along with the annual budgets necessary to accomplish those goals.

*Section 208—Internal risk controls*

On December 14, 2012, it was widely reported that the CME Group, Inc., wrote a letter to the CFTC expressing concern that confidential and sensitive market data had been shared with non-CFTC employees who then used the data to write academic papers. CME attorneys claimed that the use of the data for the preparation of non-Commission sponsored publications was a violation of federal law meant to protect trade secrets. At least two academic papers written on the subject of high-frequency trading were either co-written or advised by Andrei Kirilenko during his time as the CFTC Chief Economist. Upon leaving the CFTC in late 2012, Kirilenko took a position at MIT. As a result of the CME letter and corresponding internal investigation, the CFTC halted the research program which allowed outside academic researchers and economists almost unlimited access to proprietary trading information across various markets and the CFTC OIG launched an internal investigation.

On July 23, 2013, at a hearing entitled "The Future of the CFTC: Commission Perspectives," Commissioner Scott O'Malia provided the following testimony:

> Currently the Commission's Inspector General is investigating whether or not market data was properly controlled by the Office of the Chief Economist when visiting scholars/contractors were assisting the Office of the Chief Economist in research efforts. While I support collaborative study programs that bring in new and innovative thinking, it is vital that the Commission has policies and procedures in place to protect against the illegal release of market data.

On March 21, 2014, a heavily redacted version of the CFTC's OIG report was released to the public. In this report, the OIG found that:

> The administrative review revealed that there had been poor recordkeeping with regard to the so-called "on-boarding" process for OCE economists. The deficiencies included inadequate documentation of security clearances, issues regarding nondisclosure agreements, and non-submission of employment data to the National Finance Center, as well as incomplete personnel forms, one contract lacking the contractor's signature, and other administrative errors. There were no indications of fraud by OCE economists, or that OCE economists were not actually appointed by the Chief Economist, just a number of administrative errors pertaining to the Agency's so-called on-boarding process. The review also uncovered information security concerns. Specifically, personally owned external hard drives and thumb drives were found in close vicinity to the computers that served the OCE economists. In addition, badges for former CFTC OCE economists were located in the Chief Economist's desk.

With respect to the potentially harmful data breaches that occurred at the CFTC and the need to correct them to ensure integrity of the marketplace, the OIG's report concluded that:

> We agree that the physical and information technology concerns exist; however, they are Agency-wide, and are currently being addressed at least in part in connection with an OIG audit of CFTC's Fiscal Year 2013 implementation of the Federal Information Security Management Act. The absence of controls is significant: lacking a reliable way to determine whether confidential information was improperly taken from the CFTC, we will not jump to the conclusion that misconduct did or did not occur based on contradictory opinions of Agency employees. We can make no finding.

To guard against these sorts of leaks, this section requires the Commission, led by the Chief Economist, to develop internal risk control mechanisms to safeguard the storage and privacy of market data by the Commission. Special attention should be given to market data sharing agreements and academic research performed at the Commission using market data. The Commission shall report to the authorizing congressional committees on progress made in implementing the internal risk controls 60 days after enactment, and again 120 days after enactment of the Act.

*Section 209—Subpoena duration and renewal*

On July 23, 2013, at a hearing entitled "The Future of the CFTC: Commission Perspectives," Commissioner Scott O'Malia provided the following testimony with respect to his concerns on the operation of the Commission's subpoena power:

> CFTC regulations ensure that the Commission is made accountable for all enforcement matters by requiring a Commission order to initiate investigations by the Division of Enforcement. Just recently, I dissented on an enforcement matter that involved a radical procedural shift in the authorization of investigations for potential violations of

> the CEA. What I found troubling is that the Division of Enforcement sought to circumvent the powers of the Commission by proposing to bring investigations on a summary basis through the use of an "absent objection" process. I was surprised to be advised by the Commission's Office of General Counsel that the Commission cannot block a staff-initiated absent objection circulation because this process is not a Commission "vote." To ensure fairness in terms of true separation of functions, Congress gave power to the members of the Commission to reconsider CFTC staff recommendations by independently assessing facts and legal justifications for initiating various actions. In other words, Congress intended that any decision to bring an investigation by the CFTC is reflective of a shared opinion of the majority of the Commissioners, rather than a unilateral assessment by the Division of Enforcement's staff. The new absent objection process described by the Office of General Counsel is a clear abrogation of the Commission's powers and a violation of Commission rules relating to investigations.

In order to ensure continuing investigations by the Commission's Division of Enforcement are warranted and properly reviewed by the Commission, Section 209 would ensure that the Commission complies with controlling Supreme Court precedent on the issuance and duration of subpoenas. As such, a subpoena authorized to be issued by the Commission shall state in good faith the purpose of the investigation, shall require only information reasonably relevant to the purpose of the investigation and shall be for a finite period. Renewal of a subpoena may only occur by Commission vote.

*Section 210—Implementation plan for commission rulemakings*

In order to increase market certainty through the rulemaking process, Section 210 would require that all proposed rules include a plan for when and how long a comment period will be open, and when compliance with the final rule will be required. As Commissioner O'Malia stated when he testified before the Committee on July 23, 2013, "it is virtually impossible to achieve good policy outcomes without establishing a sound process for reaching those outcomes. Unfortunately, the Commission has failed to do so in our implementation of the Dodd-Frank Act." The Committee does not intend for these requirements to become duplicative of requirements already demanded under the Administrative Procedure Act (APA).

*Section 211—Applicability of notice and comment requirements of the Administrative Procedure Act to guidance voted on by the Commission*

As the Committee learned from numerous witnesses through testimony and saw firsthand through press reports and letters from foreign financial regulators, the Commission voted on guidance to interpret key provisions of the cross-border provisions of the Dodd-Frank Act instead of conducting rulemaking under the APA, which requires notice and comment. The Commission now has a set of guidelines to govern the cross-border application of the Dodd-Frank Act, setting up probable legal conflicts between the CFTC's guidance and the SEC's proposed cross border rule that followed all requirements of the law and allowed for extensive public comment. Concerns about "guidance" that has the practical effect of an official rulemaking was described in testimony before the Committee on March 14, 2013, by the Hon. Kenneth E. Bentsen, Acting President and CEO, SIFMA, when he stated that:

> [E]qually significant, the CFTC has issued its proposed cross-border release as "guidance" rather than as formal rulemaking process subject to the Administrative Procedure Act. By doing so, the CFTC avoids the need to conduct a cost-benefit analysis, which is critical for ensuring that the CFTC appropriately weighs any costs imposed on market participants as a result of implementing an overly broad and complex U.S. person definition against perceived benefits.

On July 23, 2013, at a hearing entitled "The Future of the CFTC: Commission Perspectives," Commissioner Scott O'Malia voiced additional concerns in testimony about the approach taken by the Commission:

> I believe that putting the label of "guidance" on this document did not change its content or consequences. The courts have held that when agency action has the practical effect of binding parties within its scope, it has the force and effect of law, regardless of the name it is given. Legally binding regulations that impose new obligations on affected parties—"legislative rules"—must conform to the APA. As a threshold matter, the cross-border swaps guidance rests on thin statutory authority, because Congress limited the extraterritorial application of U.S. swap regulations, and therefore the CFTC's jurisdiction, to foreign activities that have a "direct and significant" impact on the U.S. economy. Despite the statutory limitation, the cross-border swaps guidance sets out standards that it applies to virtually all cross-border activities in the swaps markets, in a broad manner similar to the application of the swap dealer definition to market participants. For practical reasons, market participants cannot afford to ignore detailed regulations imposed upon their activities that may result in enforcement or other penalizing action. Accordingly, I believe that the cross-border swaps guidance has a practical binding effect on market participants and it should have been promulgated as a legislative rule under the APA. Similarly, I cannot support any future interpretive guidance that would be more properly issued as a notice-and-comment rulemaking.

In an attempt to address concerns highlighted above, Section 211 applies the notice and comment provisions of the APA to any future guidance voted on and issued by the Commission. Importantly, to ensure responsiveness to the regulated marketplace, the Committee intends that Section 211 only apply to guidance voted on by the CFTC Commissioners (and therefore officially issued by the CFTC) but not to any guidance provided by the Commission staff in response to inquiries from the public.

*Section 212—Judicial review of Commission rules*

In order to address concerns from stakeholders to fairly and efficiently challenge CFTC final rules in court, Section 212 aligns the CFTC judicial review process with that of the U.S. Securities and Exchange Commission (SEC) set forth in section 25(b) of the Securities Exchange Act of 1934. As such, the Committee intends for Section 212 to allow review of a CFTC final rule may be obtained directly with the United States Court of Appeals for the District of Columbia Circuit or the U.S. Court of Appeals for the circuit where the adversely affected party resides or situates its principal place of business.

On July 24, 2013, at a hearing entitled "The Future of the CFTC: End-User Perspectives," Mr. Andrew Soto, Senior Managing Counsel, Regulatory Affairs, American Gas Association (AGA), provided the following testimony with respect to the need for provisions included in Section 212:

> First, AGA recommends that Congress amend the Commodity Exchange Act (CEA) to provide clear and defined procedures for challenging CFTC rules and orders in court. Although the CEA currently contains provisions allowing for judicial review by a U.S. Court of Appeals of certain agency actions, the provisions are very limited and provide no defined avenue for challenging CFTC rules and orders generally. A broad judicial review provision allowing for the direct challenge of CFTC rules and orders would have both a rehabilitative effect on the current process and a prophylactic effect on future agency action. Specific judicial review provisions would allow interested parties to challenge particular agency actions that are unreasonable and hold the CFTC accountable for its decisions. In addition, judicial review would have an important prophylactic effect by requiring the agency to think through its decisions before they are made to ensure that they are sustainable in court, thus enabling the agency to be a more conscientious and prudent regulator. In the absence of specific judicial review provisions, the general review provisions of the Administrative Procedure Act (APA) would apply, requiring parties seeking to challenge CFTC rules to file a claim before a U.S. District Court, move for summary judgment (as a hearing would likely be unnecessary), obtain a ruling and then, if necessary, seek further judicial review before a U.S. Court of Appeals. In the recent litigation over the CFTC's position limits rule, which followed the review provisions of the APA, the CFTC's General Counsel acknowledged the efficiency and desirability of direct review by the U.S. Court of Appeals of agency rules, and stated that the agency would have no objection to such direct review assuming Congress were to authorize it. Accordingly, provisions allowing for direct review by a U.S. Court of Appeals of rules and orders of the CFTC would enable both the industry and the agency to benefit from the administrative economy, procedural efficiency and certainty of having a dedicated forum in which agency decisions are reviewed.

*Section 213—GAO study on adequacy of CFTC resources*

In each of the five full and subcommittee hearings held this Congress related to the CFTC, some witnesses have spoken out for additional resources for the Commission. Whether it is from the Commission itself, end-user groups, or regulated market participants, varying levels of concern have been voiced that the CFTC lacks sufficient funds to do the job that Congress has asked. To obtain an impartial view on whether more resources are necessary, the Committee charges the Government Accountability Office (GAO) to conduct a study to look into this question.

The Committee would expect the GAO, as part of its study, to also closely examine and report on whether the CFTC has efficiently used its resources related to hiring and firing practices within the Commission, especially related to positions that are duplicative, outdated in their purpose, or underutilized. The efficient expenditure of funds related to computer programs, technology upgrades, consultants, and other noteworthy usages of Commission funds should also be closely examined.

## Title 3—End-User Relief

### SUBTITLE A—END-USER EXEMPTION FROM MARGIN REQUIREMENTS

*Section 311—End-user margin requirements*

Section 311 amends Section 4s(e) of the Commodity Exchange Act (CEA) as added by Section 731 of the Dodd-Frank Act to provide an explicit exemption from margin requirements for swap transactions involving end-users that qualify for the clearing exception under 2(h)(7)(A).

"End-users" are thousands of companies across the United States who utilize derivatives to hedge risks associated with their day-to-day operations, such as fluctuations in the prices of raw materials. Because these businesses do not pose systemic risk, Congress intended that the Dodd-Frank Act provide certain exemptions for end-users to ensure they were not unduly burdened by new margin and capital requirements associated with their derivatives trades that would hamper their ability to expand and create jobs.

Indeed, Title VII of the Dodd-Frank Act includes an exemption for non-financial end-users from centrally clearing their derivatives trades. This exemption permits end-users to continue trading directly with a counterparty, (also known as trading "bilaterally," or over-the-counter (OTC)) which means their swaps are negotiated privately between two parties and they are not executed and cleared using an exchange or clearinghouse. Generally, it is common for non-financial end-users, such as manufacturers, to avoid posting cash margin for their OTC derivative trades. End-users generally will not post margin because they are able to negotiate such terms with their counterparties due to the strength of their own balance sheet or by posting non-cash collateral, such as physical property. End-users typically seek to preserve their cash and liquid assets for reinvestment in their businesses. In recognition of this common practice, the Dodd-Frank Act included an exemption from margin requirements for end-users for OTC trades.

Section 731 of the Dodd-Frank Act (and Section 764 with respect to security-based swaps) requires margin requirements be applied to swap dealers and major swap participants for swaps that are not centrally cleared. For swap dealers and major swap participants that are banks, the prudential banking regulators (such as the Federal Reserve or Federal Deposit Insurance Corporation) are required to set the margin requirements. For swap dealers and major swap participants that are not banks, the CFTC is required to set the margin requirements. Both the CFTC and the banking regulators have issued their own rule proposals establishing margin requirements pursuant to Section 731.

Following the enactment of the Dodd-Frank Act in July of 2010, uncertainty arose regarding whether this provision permitted the regulators to impose margin requirements on swap dealers when they trade with end-users, which could then result in either a direct or indirect margin requirement on end-users. Subsequently, Senators Blanche Lincoln and Chris Dodd sent a letter to then-Chairmen Barney Frank and Collin Peterson on June 30, 2010, to set forth and clarify congressional intent, stating:

> The legislation does not authorize the regulators to impose margin on end-users, those exempt entities that use swaps to hedge or mitigate commercial risk. If regulators raise the costs of end-user transactions, they may create more risk. It is imperative that the regulators do not unnecessarily divert working capital from our economy into margin accounts, in a way that would discourage hedging by end-users or impair economic growth.

In addition, statements in the legislative history of section 731 (and Section 764) suggests that Congress did not intend, in enacting this section, to impose margin requirements on nonfinancial end-users engaged in hedging activities, even in cases where they entered into swaps with swap entities.

In the CFTC's proposed rule on margin, it does not require margin for un-cleared swaps when non-bank swap dealers transact with non-financial end-users. However, the prudential banking regulators proposed rules would require margin be posted by non-financial end-users above certain established thresholds when they trade with swap dealers that are banks. Many of end-users' transactions occur with swap dealers that are banks, so the banking regulators' proposed rule is most relevant, and therefore of most concern, to end-users.

By the prudential banking regulators' own terms, their proposal to require margin stems directly from what they view to be a legal obligation under Title VII. The plain language of section 731 provides that the Agencies adopt rules for covered swap entities imposing margin requirements on all non-cleared swaps. Despite clear congressional intent, those sections do not, by their terms, exclude a swap with a counterparty that is a commercial end-user. By providing an explicit exemption under Title VII through enactment of this provision, the prudential regulators will no longer have a perceived legal obligation, and the congressional intent they acknowledge in their proposed rule will be implemented.

The Committee notes that in September of 2013, the International Organization of Securities Commissions (IOSCO) and the Bank of International Settlements published their final recommendations for margin requirements for uncleared derivatives.

Representatives from a number of U.S. regulators, including the CFTC and the Board of Governors of the Federal Reserve participated in the development of those margin requirements, which are intended to set baseline international standards for margin requirements. It is the intent of the Committee that any margin requirements promulgated under the authority provided in Section 4s of the Commodity Exchange Act should be generally consistent with the international margin standards established by IOSCO.

On March 14, 2013, at a hearing entitled "Examining Legislative Improvements to Title VII of the Dodd-Frank Act," the following testimony was provided to the Committee with respect to provisions included in Section 311:

> In approving the Dodd-Frank Act, Congress made clear that end-users were not to be subject to margin requirements. Nonetheless, regulations proposed by the Prudential Banking Regulators could require end-users to post margin. This stems directly from what they view to be a legal obligation under Title VII. While the regulations proposed by the CFTC are preferable, they do not provide end-users with the certainty that legislation offers. According to a Coalition for Derivatives End-Users survey, a 3% initial margin requirement could reduce capital spending by as much as $5.1 to $6.7 billion among S&P 500 companies alone and cost 100,000 to 130,000 jobs. To shed some light on Honeywell's potential exposure to margin requirements, we had approximately $2 billion of hedging contracts outstanding at year-end that would be defined as a swap under Dodd-Frank. Applying 3% initial margin and 10% variation margin implies a potential margin requirement of $260 million. Cash deposited in a margin account cannot be productively deployed in our businesses and therefore detracts from Honeywell's financial performance and ability to promote economic growth and protect American jobs.—Mr. James E. Colby, Assistant Treasurer, Honeywell International Inc.

On May 21, 2013, at a hearing entitled "The Future of the CFTC: Market Perspectives," Mr. Stephen O'Connor, Chairman, ISDA, provided the following testimony with respect to provisions included in Section 311:

> Perhaps most importantly, we do not believe that initial margin will contribute to the shared goal of reducing systemic risk and increasing systemic resilience. When robust variation margin practices are employed, the additional step of imposing initial margin imposes an extremely high cost on both market participants and on systemic resilience with very little countervailing benefit. The Lehman and AIG situations highlight the importance of variation margin. AIG did not follow sound variation margin practices, which resulted in dangerous levels of credit risk building up, ultimately leading to its bailout. Lehman, on the other hand, posted daily variation margin, and while its failure caused shocks in many markets, the variation margin prevented outsized losses in the OTC derivatives markets. While industry and regulators agree on a robust

> variation margin regime including all appropriate products and counterparties, the further step of moving to mandatory IM [initial margin] does not stand up to any rigorous cost-benefit analysis.

Based on the extensive background that accompanies the statutory change provided explicitly in Section 311, the Committee intends that initial and variation margin requirements cannot be imposed on uncleared swaps entered into by cooperative entities if they similarly qualify for the CFTC's cooperative exemption with respect to cleared swaps. Cooperative entities did not cause the financial crisis and should not be required to incur substantial new costs associated with posting initial and variation margin to counterparties. In the end, these costs will be borne by their members in the form of higher prices and more limited access to credit, especially in underserved markets, such as in rural America. Therefore, the Committee's clear intent when drafting Section 311 was to prohibit the CFTC and prudential regulators, including the Farm Credit Administration, from imposing margin requirements on cooperative entities.

### SUBTITLE B—INTER-AFFILIATE SWAPS

*Sec. 321—Treatment of affiliate transactions*

"Inter-affiliate" swaps are contracts executed between entities under common corporate ownership. Section 321 would amend the Commodity Exchange Act to provide an exemption for inter-affiliate swaps from the clearing and execution requirements of the Dodd-Frank Act so long as the swap transaction hedges or mitigates the commercial risk of an entity that is not a financial entity. The section also requires that an "appropriate credit support measure or other mechanism" be utilized between the entity seeking to hedge against commercial risk if it transacts with a swap dealer or major swap participant, but this credit support measure requirement is effective prospectively from the date H.R. 4413 is enacted into law.

Importantly, with respect to Section 321's use of the phrase "credit support measure or other mechanism," the Committee unequivocally does not intend for the CFTC to interpret this statutory language as a mandate to require initial or variation margin for swap transactions. The Committee intends for the CFTC to recognize that credit support measures and other mechanisms have been in use between counterparties and affiliates engaged in swap transactions for many years in different formats, and therefore, there is no need to engage in a rulemaking to define such broad terminology.

Section 321 originated from the need to provide relief for a parent company that has multiple affiliates within a single corporate group. Individually, these affiliates may seek to offset their business risks through swaps. However, rather than having each affiliate separately go to the market to engage in a swap with a dealer counterparty, many companies will employ a business model in which only a single or limited number of entities, such as a treasury hedging center, face swap dealers. These designated external facing entities will then allocate the transaction and its risk mitigating benefits to the affiliate seeking to mitigate its underlying risk.

Companies that use this business model argue that it reduces the overall credit risk a corporate group poses to the market because they can net their positions across affiliates, reducing the number of external facing transactions overall. In addition, it permits a company to enhance its efficiency by centralizing its risk management expertise in a single or limited number of affiliates.

Should these inter-affiliate transactions be treated as all other swaps, they could be subject to clearing, execution and margin requirements. Companies that use inter-affiliate swaps are concerned that this could substantially increase their costs, without any real reduction in risk in light of the fact that these swaps are purely for internal use. For example, these swaps could be "double-margined"—when the centralized entity faces an external swap dealer, and then again when the same transaction is allocated internally to the affiliate that sought to hedge the risk.

The uncertainty that exists regarding the treatment of inter-affiliate swaps spans multiple rulemakings that have been proposed or that will be proposed pursuant to the Dodd-Frank Act. Section 321 provides certainty and clarity as to what inter-affiliate transactions are and how they are not to be regulated as swaps when the parties to the transaction are under common control.

On March, 14, 2013, at a hearing entitled "Examining Legislative Improvements to Title VII of the Dodd-Frank Act," the following testimony was provided with respect to efforts to address the problem with inter-affiliate swaps:

> [I]nter-affiliate swaps provide important benefits to corporate groups by enabling centralized management of market, liquidity, capital and other risks inherent in their businesses and allowing these groups to realize hedging efficiencies. Since the swaps are between affiliates, rather than with external counterparties, they pose no systemic risk and therefore there are no significant gains to be achieved by requiring them to be cleared or subjecting them to margin posting requirements. In addition, these swaps are not market transactions and, as a result, requiring market participants to report them or trade them on an exchange or swap execution facility provides no transparency benefits to the market—if anything, it would introduce useless noise that would make Dodd-Frank's transparency rules less helpful.—Hon. Kenneth E. Bentsen, Acting President and CEO, SIFMA

> This legislation would ensure that inter-affiliate derivatives trades, which take place between affiliated entities within a corporate group, do not face the same demanding regulatory requirements as market-facing swaps. The legislation would also ensure that end-users are not penalized for using central hedging centers to manage their commercial risk. There are two serious problems facing end-users that need addressing. First, under the CFTC's proposed inter-affiliate swap rule, financial end-users would have to clear purely internal trades between affiliates unless they posted variation margin between the affiliates or met spe-

> cific requirements for an exception [i]f these end-users have to post variation margin, there is little point to exempting inter-affiliate trades from clearing requirements, as the costs could be similar. And let's not forget the larger point—internal end-user trades do not create systemic risk and, hence, should not be regulated the same as those trades that do. Second, many end-users—approximately one-quarter of those we surveyed—execute swaps through an affiliate. This of course makes sense, as many companies find it more efficient to manage their risk centrally, to have one affiliate trading in the open market, instead of dozens or hundreds of affiliates making trades in an uncoordinated fashion. Using this type of hedging unit centralizes expertise, allows companies to reduce the number of trades with the street and improves pricing. These advantages led me to centralize the treasury function at Westinghouse while I was there. However, the regulators' interpretation of the Dodd-Frank Act confronts non-financial end-users with a choice: either dismantle their central hedging centers and find a new way to manage risk, or clear all of their trades. Stated another way, this problem threatens to deny the end-user clearing exception to those end-users who have chosen to hedge their risk in an efficient, highly-effective and risk-reducing way. It is difficult to believe that this is the result Congress hoped to achieve.—Ms. Marie N. Hollein, C.T.P., President and CEO, Financial Executives International, on behalf of the Coalition for Derivatives End-Users

## SUBTITLE C—INDEMNIFICATION REQUIREMENTS RELATED TO SWAP DATA REPOSITORIES

### *Section 331—Indemnification requirements*

Section 331 strikes the indemnification requirements found in Sections 725 and 728 of the Dodd-Frank Act related to swap data gathered by swap data repositories (SDRs) and derivatives clearing organizations (DCOs). The section does maintain, however, that before an SDR, DCO, or the CFTC shares information with domestic or international regulators, they have to receive a written agreement stating that the regulator will abide by certain confidentiality agreements.

Swap data repositories serve as electronic warehouses for data and information regarding swap transactions. Historically, SDRs have regularly shared information with foreign regulators as a means to cooperate, exchange views and share information related to OTC derivatives CCPs and trade repositories. Prior to Dodd-Frank, international guidelines required regulators to maintain the confidentiality of information obtained from SDRs, which facilitated global information sharing that is critical to international regulators' ability to monitor for systemic risk.

Under Sections 725 and 728 of the Dodd-Frank Act, when a foreign regulator requests information from a U.S registered SDR or DCO, the SDR or DCO is required to receive a written agreement from the foreign regulator stating that it will abide by certain confidentiality requirements and will "indemnify" the Commissions for any expenses arising from litigation relating to the request for information. In short, the concept of "indemnification"—requiring a party to contractually agree to pay for another party's possible litigation expenses—is only well established in U.S. tort law, and does not exist in practice or in legal concept in foreign jurisdictions.

These indemnification provisions—which were not included in the financial reform bill passed by the House of Representatives in December 2009—threaten to make data sharing arrangements with foreign regulators unworkable. Foreign regulators will most likely refuse to indemnify U.S. regulators for litigation expenses in exchange for access to data. As a result, foreign regulators may establish their own data repositories and clearing organizations to ensure they have access to data they need to perform their supervisory duties. This would lead to the creation of multiple databases, needlessly duplicative data collection efforts, and the possibility of inconsistent or incomplete data being collected and maintained across multiple jurisdictions.

In testimony before the House Committee on Financial Services in March of 2012, the then-Director of International Affairs for the SEC, Mr. Ethiopis Tafara, endorsed a legislative solution to the problem, stating that:

> The SEC recommends that Congress consider removing the indemnification requirement added by the Dodd-Frank Act . . . the indemnification requirement interferes with access to essential information, including information about the cross-border OTC derivatives markets. In removing the indemnification requirement, Congress would assist the SEC, as well as other U.S. regulators, in securing the access it needs to data held in global trade repositories. Removing the indemnification requirement would address a significant issue of contention with our foreign counterparts . . .

At the same hearing, the then-General Counsel for the CFTC, Mr. Dan Berkovitz, acknowledged that they too have received growing concerns from foreign regulators, but that they intend to issue interpretive guidance, stating that "access to swap data reported to a trade repository that is registered with the CFTC will not be subject to the indemnification provisions of the Commodity Exchange Act if such trade repository is regulated pursuant to foreign law and the applicable requested data is reported to the trade repository pursuant to foreign law."

To provide clarity to the marketplace and remove any legal barriers to swap data being easily shared with various domestic and foreign regulatory agencies, this section would remove the indemnification requirements found in Sections 725 and 728 of the Dodd-Frank Act related to swap data gathered by SDRs and DCOs.

On March, 14, 2013, at a hearing entitled "Examining Legislative Improvements to Title VII of the Dodd-Frank Act," Mr. Larry Thompson, Managing Director and General Counsel, the Depository Trust and Clearing Corporation, provided the following testimony with respect to provisions of H.R. 742, which were included in Section 331:

> The Swap Data Repository and Clearinghouse Indemnification Correction Act of 2013 would make U.S. law con-

sistent with existing international standards by removing the indemnification provisions from sections 728 and 763 of Dodd-Frank. DTCC strongly supports this legislation, which we believe represents the only viable solution to the unintended consequences of indemnification. H.R. 742 is necessary because the statutory language in Dodd-Frank leaves little room for regulators to act without U.S. Congressional intervention. This point was reinforced in the CFTC/SEC January 2012 Joint Report on International Swap Regulation, which noted that the Commissions "are working to develop solutions that provide access to foreign regulators in a manner consistent with the DFA and to ensure access to foreign-based information." It indicates legislation is needed, saying that "Congress may determine that a legislative amendment to the indemnification provision is appropriate." H.R. 742 would send a clear message to the international community that the United States is strongly committed to global data sharing and determined to avoid fragmenting the current global data set for over-the-counter (OTC) derivatives. By amending and passing this legislation to ensure that technical corrections to indemnification are addressed, Congress will help create the proper environment for the development of a global trade repository system to support systemic risk management and oversight.

SUBTITLE D—RELIEF FOR MUNICIPAL UTILITIES

*Sections 341, 342, 343—Transactions with the utility special entities; utility special entity defined; utility operations-related swap*

Sections 341, 342, and 343 of H.R. 4413 would preserve the ability of government-owned utilities, classified in the bill as "utility special entities," to have uninterrupted and cost-effective access to the customized, non-financial commodity swaps that utility special entities have used for years. In effect, the counterparties of utility special entities would now be subject to the much higher $8 billion de minimis swap dealer registration threshold. Importantly, the legislation does not include an exemption for interest rate, credit, equities, currency asset classes, or agriculture commodities, other than commodities used for electric energy or natural gas production or generation. Instead, H.R. 4413 creates a new category of swap known as the "utility operations-related swap" and provides relief to counterparties of utility special entities only when those specific types of swaps are used. To ensure transparency, the bill still requires all special entity swap transactions to be reported to the CFTC.

On May 23, 2012, the CFTC published a rule further defining who is considered a "swap dealer" under the Dodd-Frank Act, which directly impacted many swap counterparties of government-owned non-profit utilities. The rule became effective on July 23, 2012, with registration as a swap dealer not being required until on or after October 12, 2012. The CFTC's swap dealer rule includes an exception for entities from having to register as a swap dealer if their outstanding annual gross notional swap positions do not exceed either of the two following thresholds:

1. $3 billion (subject to an initial three year phase-in level of $8 billion), referred to as the "general de minimis threshold"; and
2. $25 million with regard to swaps where an entity's counterparty is a "special entity" as defined in Section 731 of the Dodd-Frank Act, referred to as the "special entity de minimis threshold."

On October 12, 2012, after several public power groups petitioned the CFTC to relieve their counterparties from compliance with the much lower registration threshold, CFTC staff issued a non-binding "no-action relief" letter instead, which increased the "special entity sub-threshold" to $800 million from $25 million.

As mentioned above, a "special entity" is broadly defined in Section 731 of the Dodd-Frank Act to include any government-owned enterprise, such as public school boards, state governments, and any publicly-owned producer or supplier of electricity or natural gas. Casting such a broad net in defining "special entity" was a policy decision made by the drafters of the Dodd-Frank Act which sought to protect taxpayers from the use of complex financial swaps by their municipality. For example, the use of fixed-for-floating interest rate swaps tied to municipal bonds issued by Jefferson County, Alabama, contributed to the county's multi-billion dollar debt that rapidly expanded during the 2008 financial crisis, later resulting in what was at the time the largest municipal bankruptcy filing in U.S. history.

Prior to enactment of the Dodd-Frank Act, however, many publicly-owned utilities relied on their non-financial counterparties, such as natural gas producers, independent power generators, and investor-owned utility companies to enter into swaps in order to hedge against operational risks. Many of these utilities have heard from numerous counterparties who are evaluating their future business plans in light of the final CFTC rules. These counterparties are strictly limiting their business, or completely cutting all ties with utility special entities given the special entity sub-threshold and uncertainty surrounding the new regulatory regime for the swaps marketplace.

Unless counterparties can determine with certainty that their swap activities with special entities will not result in them being classified as a "swap dealer" under the Dodd-Frank Act, it appears that numerous counterparties may avoid doing business with them altogether. This ultimately limits competition and forces special entities to do business with financial institutions or large swap dealers, which concentrates risk and may raise costs for many utility special entities eventually leading to increased costs for ratepayers. The Committee recognizes that on March 21, 2014, the Commission staff provided a "no-action letter" to utility special entities so they are not subjected to the $25 million de minimis threshold. However, permanent statutory relief that would be provided in Sections 341, 342, and 343 is still needed due to the questionable legal certainty contained in this—and all—CFTC no-action letters, which state that "[a]s with all no-action letters, the Division retains the authority, in its discretion, to further condition, modify, suspend, terminate or otherwise restrict the terms of the no-action relief provided herein."

On May 22, 2014, the CFTC released a proposed rulemaking to permanently correct the missteps that would be corrected by Sections 341, 342, and 343. While a regulatory change is welcomed by the Committee, statutory certainty can provide millions of consumers across the country with greater certainty that their utility rates will not increase due to the Dodd-Frank Act.

On March, 14, 2013, at a hearing entitled "Examining Legislative Improvements to Title VII of the Dodd-Frank Act," Mr. Terrance P. Naulty, General Manager and CEO, Owensboro Municipal Utilities, provided the following testimony with respect to the provisions included in Sections 341, 342, and 343:

> Government-owned utilities depend on nonfinancial commodity transactions, trade options, and "swaps," as well as the futures markets, to hedge commercial risks that arise from their utility facilities, operations, and public service obligations. Together, nonfinancial commodity markets play a central role in the ability of government-owned utilities to secure electric energy, fuel for generation, and natural gas supplies for delivery to consumers at reasonable and stable prices . . . [t]he CFTC has said that it retained the $25 million threshold in light of the special protections that the Dodd-Frank Act affords to special entities. However, the statute does not require—even mention—special protections for special entities in regard to the swap dealer definition. As noted above, the law imposes requirements on swap dealers and major swap participants advising or entering into swaps with special entities. Nowhere does the law mention deeming a participant to be a swap dealer solely based on its volume of swaps with government-owned entities. Government-owned utilities understand the operations-related swap transactions they use to manage their commercial risks and do not need the special protections provided by the $25 million sub-threshold. In fact, and ironically, these "protections" are likely to limit the ability of these utilities to hedge operational and price risks rather than to protect these utilities and their customers from risk. On July 12, 2012, APPA, the Large Public Power Council (LPPC), the American Public Gas Association (APGA), the Transmission Access Policy Study Group (TAPS), and the Bonneville Power Administration (BPA), filed with the CFTC a "Petition for Rulemaking to Amend CFTC Regulation 1.3(ggg)(4)." . . . [t]he legislation [H.R. 1038] largely mirrors the intent and effect of the NFP EEU petition to the CFTC, providing narrowly targeted relief for operations-related swaps for government-owned utilities. Specifically, the legislation would provide that the CFTC, in making a determination to exempt a swap dealer under the de minimis exception, shall treat a utility operations-related swap with a utility special entity the same as a utility operations-related swaps with any entity that is not a special entity. . . . [t]he legislation carefully defines which entities would qualify as a "utility special entity." It also specifically defines the types of

swaps that could and could not be considered a "utility operations-related swap." For example, the legislation specifically prohibits interest, credit, equity, and currency swaps from being considered as a utility operations-related swap. Likewise, except in relation to their use as a fuel, commodity swaps in metal, agricultural, crude oil, or gasoline would not qualify either. Finally, the legislation also confirms that utility operations-related swaps are fully subject to swap reporting requirements. When implemented, this legislation should provide the certainty to nonfinancial entities that they can enter into swap transactions with government-owned utilities without fear of being deemed a swap dealer. It truly levels the playing field. And, it does nothing to otherwise alter the CFTC's implementation of the Dodd-Frank Act.

### SUBTITLE E—END-USER REGULATORY RELIEF

*Section 351—End-users not treated as financial entities*

Section 351 is intended to remove non-financial end-users that were unintentionally captured in the definition of "financial entity" in Section 2(h)(7)(C) of the Commodity Exchange Act due to a cross-reference to Section 4(k) of the Bank Holding Company Act of 1956. By defining "commercial market participants" using long-standing CFTC terminology found in the Joint CFTC–SEC Rule Defining Swap (CFTC Reference: 77 FR 48207) and current CFTC Regulations governing Trade Options (CFTC Regulations Part 32.3(a)(1)(ii)), the Committee seeks to provide narrow relief to these entities who are not traditional financial institutions that may incidentally be swept in to the Dodd-Frank regime simply because they engage in futures contracts, forward contracts, or commodity options which call for physical delivery of a commodity.

On July 24, 2013, at a hearing entitled "The Future of the CFTC: End-User Perspectives," Mr. Richard F. McMahon, Jr., Vice President, Edison Electric Institute (EEI), provided the following testimony with respect to the need for the provisions included in Section 351:

> The Dodd-Frank Act defines the term "financial entity", in part, as an entity that is "predominantly engaged in activities that are in the business of banking, or in activities that are financial in nature, as defined in section 4(k) of the Bank Holding Company Act of 1956." Incorporating banking concepts into a definition that also applies to commercial commodity market participants has had unintended consequences. Unlike our members, banks and bank holding companies generally cannot take or make delivery of physical commodities. However, banks and bank holding companies can invest and trade in certain commodity derivatives. As a result, the definition of "financial in nature" includes investing and trading in futures and swaps as well as other physical transactions that are settled by instantaneous transfer of title of the physical commodity. An entity that falls under the definition of a "financial entity" is generally not entitled to the end-user exemption—an exemption that Congress included to benefit

commercial commodity market participants—and can therefore be subject to many of the requirements placed upon swap dealers and major swap participants. In addition, the CFTC has used financial entity as a material term in numerous rules, no-action relief, and guidance, including, most recently, its cross-border guidance. The Dodd-Frank Act allows affiliates or subsidiaries of an end-user to rely on the end-user exception when entering into the swap on behalf of the end-user. However, swaps entered into by end-user hedging affiliates who fall under the definition of "financial entity" cannot take advantage of the end-user exemption, despite the fact that the transactions are entered into on behalf of the end-user. Many energy companies structure their businesses so that a single legal entity within the corporate family acts as a central hedging, trading and marketing entity—allowing companies to centralize functions such as credit and risk management. However, when the banking law definitions are applied in this context, these types of central entities may be viewed as engaging in activity that is "financial in nature," even with respect to physical transactions. Hence, some energy companies may be precluded from electing the end-user clearing exception for swaps used to hedge their commercial risks and be subject to additional regulations applicable to financial entities. Importantly, two similar energy companies may be treated differently if, for example, one entity uses a central affiliate to conduct these activities and another conducts the same activity in an entity that also owns physical assets or that has subsidiaries that own physical assets. Accordingly, Congress should amend the definition of "financial entity" to ensure that commercial end-users are not inadvertently regulated as "financial entities."

*Section 352—Reporting of illiquid swaps so as not to disadvantage certain non-financial end-users*

Real-time public reporting of swap transactions as required by the CFTC may ultimately lead to more efficient prices for commercial end-users. However, based on the fact that liquidity diminishes for longer-dated contracts further out in time, there is a point where the benefits derived from public reporting do not outweigh the detriment to those who are trading in illiquid markets. While transparency is helpful in establishing a price between buyers and sellers, if market participants become easier to identify in certain sparsely traded swaps, other market participants will be able to take advantage of their positions and increase their cost of doing business for future trades. These sparsely traded swaps are used by a handful of companies with excellent credit ratings to provide long-term protection against price fluctuations for commodities such as oil and jet fuel.

While the goal of increasing market transparency was well intended, the CFTC's final rule on reporting requirements does not differentiate between the appropriate times needed for reporting between different types of swaps contracts. Instead, this rule has led to a change in market behavior that affects long-established business models which traditionally allowed companies to protect against commodity price increases. Effective risk management helped these companies keep prices low for consumers. Southwest Airlines offers a prime example of how this new CFTC regulation has impacted its business and its customers. Because their exact market positions became known by competitors due to near instantaneous reporting of market positions, Southwest Airlines has been forced to pay more in order to protect against the rising cost of fuel.

There is precedent in CFTC policy in recognizing the sensitivity around transaction counterparty identities in public data reporting. The Commission has for years issued publicly a weekly "Commitment of Traders Report" (COT). In describing the issuance of this report, the Commission states: "The [COT] reports provide a breakdown of each Tuesday's open interest for markets in which 20 or more traders hold positions equal to or above the reporting levels established by the CFTC." In other words, when the number of market participants in a reportable contract drops below a certain level, the Commission has recognized there can be damage to counterparty anonymity when there are a limited number of participants in a given market, and therefore does not issue a report for that contract. Because the Committee believes that the number of participants and transactions in a given market diminishes for longer-dated contracts, the Commission shall create a standard for reporting all swap asset classes based off of when liquidity in a contract lowers to the level of being able to easily identify market participants.

As such, Section 352 would correct the unintended consequences of the new CFTC reporting regime while still maintaining the goal of increasing market transparency. This section preserves the real-time reporting of these sparsely traded swaps directly to the CFTC to ensure that government regulators have the information they need to police the markets. By simply making a technical change to the timeframe in which end-users are required to release their trading information to the general public, Section 352 achieves market transparency in a manner that does not harm long-standing business models and that helps keep costs low for millions of Americans.

On July 24, 2013, at a hearing entitled "The Future of the CFTC: End-User Perspectives," Mr. Chris Monroe, Treasurer, Southwest Airlines, Co., provided the following testimony with respect to the need for provisions included in Section 352:

> One key to our unparalleled success has been our ability to hedge fuel through legitimate end-user derivatives purchased in the futures markets. Hedging at Southwest is enterprise risk management—essential in our view given our $6 billion annual fuel bill. To hedge, we commonly enter into transactions many months or years in advance of needing the physical product. Trading in these illiquid markets allows us to manage our fuel costs, which in turn helps us to keep fares low and maintain large jet (Boeing 737) flights in the communities we serve. I am here today to highlight a few issues that have begun to impact these important markets that companies such as Southwest relay on to manage risk. One area where we are seeing a negative commercial impact is the Commodity Futures

> Trading Commission's ("CFTC's") Real-Time Public Reporting of Swap Transaction Data Rule ("Real-Time Reporting Rule") . . . [i]mportantly, trades between a legitimate commercial end-user and a dealer must be reported within the dealer's shorter time limit. Given that the vast majority of bilateral trades entered into by commercial end-users are transacted with a dealer, this means nearly all commercial end-user trades are reported on the accelerated time limit. The dealer time delays may be sufficient for liquid markets, but the timeframes are not sufficient for illiquid markets, which, as I said before, is where Southwest commonly trades. Only a few market participants trade that far out the curve, which makes the contracts highly illiquid, even in contracts that may be liquid in the front months such as crude oil. Additionally, Southwest has a particularly identifiable trading strategy, a hedging "DNA" if you will, which makes us quite visible in a market with few participants. This is particularly harmful. When a dealer has to report illiquid trades to the market quickly, the dealer is less likely to be able to lay off the risk of that trade in the prescribed time. If the dealer is still holding a large amount of the risk when the trade is shown to the public, the dealer can be front-run and, as a result, take a loss on the trade. That increased risk to the dealer will either curtail trades or materially increase the costs of the trade to the end-users.) If an end-user like Southwest can no longer access the markets to hedge fuel it would be contrary to the purposes of the legislation and in our view hostile to Congressional intent.

*Section 353—Relief for grain elevator operators, farmers, agricultural counterparties, and commercial market participants*

As a service to their customers, farmer-owned cooperative FCMs have a network of branch operations embedded in locations such as grain elevators, whose primary business is handling the cash grain volume of their farmer customers. As a branch office of a cooperatively-owned FCM, these commercial grain elevators have chosen to provide brokerage services as a means of providing access to risk management tools for their farmer customers who want to hedge their production volume through futures and/or options.

In response to the Dodd-Frank Act, the CFTC greatly expanded record keeping requirements by making it necessary for brokers to retain all forms of written and oral communication that might "lead to the execution of a transaction in a commodity interest". Given the infrequent and low volume of futures/options transactions handled by "branches" associated with those FCMs, complying with the recording requirements under this vague regulation would not be economically feasible. The necessary investment to put in place and maintain a system to record every form of communication that might "lead to the execution of a transaction" would exceed not only any profits, but in many cases the total revenues of those FCM branches. Local branches could no longer provide brokerage services resulting in reduced risk management options, and their use, by farmers and ranchers.

Section 353 does not eliminate a grain elevator's record keeping responsibilities, but merely relieves them from purchasing and maintaining costly technology to record and save all incoming communication that may lead to a transaction in a commodity interest. Grain elevators and other end-users will still be required to maintain a written record of such transactions that include all of the transactions' material economic terms. Without Section 353, the vague, sweeping language of the CFTC's current regulation will result in significant time and financial costs to commercial grain elevators attempting to comply with the rule. Rather than facilitating the collection of useful transaction records, the rule is likely to result in grain elevators' no longer providing useful brokerage services to their customers. As a result, countless farmers and ranchers will lose access to valuable risk management tools that allow them to hedge their production volume.

On July 24, 2013, at a hearing entitled "The Future of the CFTC: End-User Perspectives," the following witnesses provided testimony with respect to provisions included in Section 353:

> A significant and concerning expansion of current data requirements beyond the scope of Dodd-Frank is related to record-keeping requirements in Part 1 of Commission regulations. In accordance with Dodd-Frank, the CFTC expanded the futures record-keeping requirements that existed for certain markets participants to swaps. However, they also significantly expanded the written requirements, as well as created a new requirement to record oral conversations. Compliance costs have already been incredibly substantial now that compliance with the written requirements is mandatory and will only increase once compliance with the oral recording requirement comes into effect later this year. Again, the market is searching for a reason for and measurable benefit of all of this new information that must be maintained and archived in a particular way. In addition, the rule is vague as to which communications must be retained, so in an abundance of caution, market participants are effectively saving every e-mail, news article, or any other piece of information that might "lead to the execution of a transaction" and soon will have to begin recording every phone call that might "lead to the execution of a transaction." This vague "lead to . . ." language appears nowhere in any prior iteration of Rule 1.35 or in any prior CFTC Advisory relating to the rule, and operates to expand substantially the scope and burdens of the rule. Also, the application of the requirements to members of an exchange seems to have no regulatory rationale and only serves as a disincentive to be an exchange member. Finally, the cost figures contained in the cost-benefit analysis in the final rule are not justified. Compliance costs are exponentially higher than they estimate, and in some cases the technology is not even available to market participants. Requests for clarification have not yet been answered, and CMC will be submitting a written request soon in a continued effort to clarify and hopefully narrow the scope of what must be retained and, therefore, reduce what we view as unnecessary compliance costs.—Mr.

Lance Kotschwar, Senior Compliance Attorney, The Gavilon Group, LLC, on behalf of the Commodity Markets Council

Given the infrequent and low volume of futures/options transactions handled by "branches" associated with those FCMs, complying with the oral recording requirements (recording of all phone calls) under this regulation would not be economically feasible. The necessary investment to put in place and maintain a system to comply with the regulations would exceed not only any profits, but in many cases the total revenues of those FCM branches—to the point that those local branches could no longer provide brokerage services. The effect would be reduced risk management options, and their use, by farmers and ranchers.—Mr. Scott Cordes, President, CHS Hedging, Inc., on behalf of the NCFC

*Section 354—Relief for end-users who use physical contracts with volumetric optionality*

Forward contracts that result in the physical delivery of commodities are expressly exempted from the definition of a "swap" under the Commodity Exchange Act. Section 354 would clarify the application of this exemption in order to prevent unnecessary and costly regulations on companies that enter into transactions to ensure the efficient physical delivery of commodities necessary to conduct their core business operations. Without clarification, the CFTC could impose costly regulations on risk management transactions, which increases companies' operating costs and ultimately results in increased costs to consumers across the nation.

Risk management contracts that allow for an adjustment of the quantity of a commodity delivered do not pose a threat to the stability of financial markets and should not be regulated the same as financial derivatives. These contracts do provide companies with an efficient and cost effective means of acquiring the commodities they need to conduct their daily business, such as providing affordable sources of energy to millions of American households. The misguided regulation of these harmless transactions will actually have the effect of increasing companies' costs of doing business, will consolidate risk in the marketplace because some businesses will be forced out of the market, and will ultimately raise costs for everyday American consumers. Such costly and unnecessary regulation defies the intent of Congress and needlessly subjects a large segment of the energy marketplace to burdensome regulation under the Dodd-Frank Act.

The Dodd-Frank Act, passed to reform the U.S. financial system, should not result in increased utility rates for consumers of natural gas, electricity, and other forms of energy used to heat homes, run factories, and power the American economy. Without relief, many utilities and energy companies will not be able to effectively manage risk—which will only increase their costs and possibly lead to higher energy rates for millions of Americans—an unacceptable result during a period of tremendous economic uncertainty.

As such, Section 354 would exempt forward contracts between end-users that allow for deferred delivery or shipment of a non-financial commodity, so long as the contract results in an actual physical settlement obligation, is between commercial market participants, and the option to receive more or less of a commodity cannot be sold separately for financial gain. The Committee notes that optionality includes both allowing a counterparty to reduce the amount of commodity delivered and allowing a counterparty to increase the amount of commodity delivered.

On July 24, 2013, at a hearing entitled "The Future of the CFTC: End-User Perspectives," the following witnesses provided testimony with respect to provisions included in Section 354:

> Because gas consumption to residential and commercial customers is largely weather driven (consumption increases as the weather gets colder) and predicting the weather is not an exact science, gas supply contracts with delivery flexibility help AGA members make sure gas supplies are, or can be made, available when the customers actually need the gas without having to pay excessively higher prices at the actual time of need and/or other fees associated with pipeline imbalance penalties. There remain disagreements and confusion within the natural gas industry as to which types of gas supply transactions, if any, will be subject to CFTC regulation. These transactions are normal commercial merchandising transactions that parties use to buy and sell natural gas for ultimate delivery to end-use customers. They would not normally be considered speculative, financial transactions as the parties contemplate physical delivery of the commodity. Nevertheless, transactions that contain some option or choice for one or the other counterparty, raise questions for some as to whether they would be considered commodity options regulated as swaps, meet a three part test and a seven-part test to be excluded as options embedded in forward contracts, be viewed as trade options subject to a lessened reporting burden, or be considered facility use agreements that meet a three-part test and then a five-part test and not subject to regulation at all.—Andrew K. Soto, Senior Managing Counsel, Regulatory Affairs, AGA

> Recently, however, in light of the CFTC's seven-part interpretation in the rule, some NCFC members have raised concerns over the appropriate treatment of forward contracts commonly used in physical supply arrangements that contain volumetric optionality. If the CFTC were to take a narrow view of the seven-part interpretation, it may view as options many other routine physical supply contracts in which the predominant feature is delivery. Such an interpretation would require those common commercial forward contracts to come under the regulations intended for swaps such as reporting and position limits. The uncertainty of the CFTC interpretation of these types of contracts, all previously covered under the forward contracting exclusion, will require NCFC members to expend significant labor and costs to review hundreds of sales transactions to determine if they continue to meet the forward contract exclusion. Again, this is an unnecessary resource and cost burden on end-users that should be avoid-

ed. We hope CFTC will interpret this exclusion consistently with its historical understanding and prior guidance.—Mr. Scott Cordes, President, CHS Hedging, Inc., on behalf of the NCFC

*Section 355—Commission vote required before automatic change of swap Dealer de minimis level*

Section 355 would simply require the CFTC Commissioners to vote before changing the current $8 billion swap dealer *de minimis* exemption from registering as a swap dealer. Without Section 355, a CFTC rule will automatically set the *de minimis* exemption at $3 billion, potentially requiring dozens of end-users to register with the Commission in the coming years as "swap dealers" and imposing costly new regulations on public utilities, energy companies, and other end-users that played no part in the financial crisis.

As the regulations currently stand, if a company does more than $8 billion worth of swap business per year (known as the *de minimis* level of swap dealing), it must register with the CFTC as a "swap dealer." The CFTC's regulations will arbitrarily lower the registration threshold to $3 billion starting five years from October of 2012 (and possibly sooner) with no Commission vote, despite rules requiring a Commission "study" to determine if the swap dealer registration threshold is appropriately set at $8 billion.

An arbitrary 60% decline in the swap dealer registration threshold from $8 billion to $3 billion creates significant uncertainty for non-financial companies that engage in relatively small levels of swap dealing to manage business risk for themselves and their customers. Lowering the swap dealer registration threshold below its current level of $8 billion could drive many non-financial companies out of the business of offering their customers risk management products, which will limit risk management options for end-users, and ultimately consolidate marketplace risk in only a few large swap dealers. This consolidation runs counter to the goals of the Dodd-Frank Act to reduce systemic risk in the marketplace.

CFTC regulations should not arbitrarily change the swap dealer registration *de minimis* level without a formal rulemaking process. The regulations themselves require a formal study by the Commission to determine if the current $8 billion level is appropriate. However, the study is completely irrelevant because the *de minimis* level is moved to $3 billion in five years regardless of the study's findings. Because provisions embedded deep within CFTC regulations failed to mandate that the Commission must vote to determine what policy is best for future market conditions, our markets could be forced to adhere to outdated policies for years to come. Further, as demonstrated in the context of utility special entities, a *de minimis* exception threshold that is too low can significantly disrupt markets, hinder competition, and leave non-financial businesses with limited ways to manage their economic and operational risks. Section 355 would result in a Commission review of whether lowering the *de minimis* exception threshold would drive participants out of the swap market, limit competition and potentially harm end-users. In particular, pursuant to Section 355, the Committee expects that the Commission would periodically review the *de minimis* exception threshold to consider whether, in light of changes in prices and market structure, the *de minimis* exception threshold should also be increased to greater than $8 billion to ensure non-financial end-users are able to obtain risk management solutions from a broad range of counterparties.

On July 24, 2013, at a hearing entitled "The Future of the CFTC: End-User Perspectives," the following witnesses provided testimony with respect to the need for the provisions included in Section 355:

> Current regulations have arbitrarily established a *de minimis* level, the breach of which requires registration as a swap dealer, at $8 billion with a drop to $3 billion following an unpredictable CFTC decision making process. The only certainty in the process is that a lack of action will result in the *de minimis* level declining in 5 years. This $3 billion level is also arbitrary and would significantly affect the number of firms defined and regulated as swap dealers. Changes should not be made through such a long and ill-defined process, which includes several unpredictable and difficult to follow steps for market participants. We need a more predictable process.—Mr. Lance Kotschwar, Senior Compliance Attorney, The Gavilon Group, LLC, on behalf of the Commodity Markets Council

> A new category of market participants, swap dealers, was created by the Dodd-Frank Act. These swap dealers must register with the CFTC and are subject to extensive record-keeping, reporting, business conduct standards, clearing, and—in the future—regulatory capital and margin requirements. However, the Act directed the CFTC to exempt from designation as a swap dealer entities that engage in a *de minimis* quantity of swap dealing. The CFTC issued a proposed rule on the *de minimis* threshold for comment in early 2011. After review of hundreds of comments, a series of Congressional hearings and after dozens of meetings with market participants, the CFTC set this *de minimis* threshold at $8 billion. However, it will then be reduced automatically to $3 billion in 2018 absent CFTC action. We oppose such a dramatic reduction in the *de minimis* threshold without deliberate CFTC action. Inaction is always easier than action, and inaction should not be the default justification for such a major regulatory action. In addition, we believe the CFTC should not have the authority to change the *de minimis* level without a formal rulemaking process that allows stakeholders to provide input on what the appropriate threshold should be. Absent these procedural changes, we are concerned a deep reduction in the *de minimis* level could result in commercial end-users being misclassified as swap dealers, hindering end-users' ability to hedge market risk while imposing unnecessary costs that eventually will be borne by consumers.—Mr. Richard F. McMahon, Jr., Vice President, EEI

*Section 356—Capital requirements for bon-bank swap dealers*

Under currently-proposed CFTC regulations for capital and margin, non-bank swap dealers would be forced by the CFTC to adhere to an inflexible capital requirement standard (based partially on the capital requirements based on the soon-to-be outdated Basel II Accords first proposed in 2004, which have since been eclipsed by the Basel III Accords proposed in 2011). According to testimony received from Mr. William J. Dunaway, CFO, INTL FCSTONE, Inc., before the Committee on May 21, 2013, under the CFTC's proposal, a firm could be assessed a capital charge beyond their net position in a contract, especially in relation to commodity swaps. Furthermore, the CFTC's capital requirements stand in stark contrast to the SEC's capital requirements for security-based swap dealing due to the SEC's allowance for dealers to utilize pre-approved internal capital models. As a result, the Committee learned that, under a worst case scenario, "the same derivatives portfolio that would require a bank-affiliated Swap Dealer to hold $10 Million in regulatory capital using standard internal models would require us to set aside up to $1 Billion in capital". At the same hearing on May 21, 2013, entitled "The Future of the CFTC: Market Perspectives," Mr. Dunaway provided more insight on how to correct such a potentially harmful result for the marketplace:

> The Commodity Exchange Act requires the CFTC, the prudential regulators, and the SEC to establish and maintain "comparable" minimum capital requirements for all Swap Dealers. However, the proposed Capital Rules clearly are not "comparable." Pursuant to its mandate under the CEA, we believe that the CFTC should revise its proposed capital rules to ensure that the capital and margin requirements applicable to non-bank Swap Dealers are comparable to those applicable to bank-affiliated Swap Dealers. This can be accomplished by altering the rules to permit the following: [i]nternal Models—The CFTC could permit all Swap Dealers, including Commodity Swap Dealers, to request approval of, and rely upon, internal models to measure market risk. To the extent that the CFTC currently lacks the resources to review and approve such internal models, it should permit Swap Dealers to certify to the CFTC or the NFA that their models produce reasonable measures of risk, subject to verification by the CFTC when its resources enable it to do so.—Mr. William J. Dunaway, CFO, INTL FCSTONE, Inc.

Because this potential disparity in capital charges for non-bank versus bank affiliated swap dealers could harm more than one market participant, Section 356 would require that the CFTC amend its proposed rule so as to closely consult with the SEC and prudential financial regulators and to allow the use of comparable capital requirements that will be utilized by swap dealers regulated by the SEC and prudential regulators.

*Section 357—Harmonization with the Jumpstart Our Business Startups Act*

In letters to the CFTC, stakeholders representing a wide variety of market participants, such as SIFMA, the Managed Funds Association (MFA), and the Financial Services Roundtable requested that the Commission harmonize its "private offering" requirements in CFTC Rules 4.7 and 4.13(a)(3) with the broadened scope of solicitation permitted by the SEC after it proposed amendments to Rule

506 of Regulation D and Rule 144A under the Securities Act of 1933. The SEC's proposed changes to the solicitation rules for securities offerings came about after the Jumpstart Our Business Startups Act (JOBS Act) (P.L. 112–106) was signed into law in April of 2012 which allows for solicitation of accredited investors for private securities offerings in order to raise needed capital for companies to expand and create jobs.

While the JOBS Act mandates consistent treatment of Regulation D, Rule 506 offerings across the federal securities laws, unintentionally omitted harmonizing changes to the CFTC's regulations, which creates an inconsistency between the SEC's rules and the CFTC's rules governing solicitation. Accordingly, because the relief is needed quickly as to not impede use of the JOBS Act by the marketplace, Section 357 would directly amend CFTC regulations (which would obviate the need for a Commission rulemaking) to provide an exemption for any registered commodity pool operator to engage in the general solicitation for the sale of commodity pools parallel to the exemption provided for general solicitation of securities under the JOBS Act.

*Section 358—Bona fide hedge defined to protect end-user risk management*

In 2010, the Dodd-Frank Act instructed the CFTC on how to define what constitutes a bona fide hedging transaction (i.e.: non-speculative trading) or position so those trades would not count towards any positions limits. The statutory definition states that the reduction of risk inherent to a commercial enterprise is a component in determining what qualifies as a bona fide hedging transaction. However, in a change from prior practice, the CFTC's approach in both the originally proposed 2011 position limits rule (which was overturned by a federal district court for the District of Columbia in September 2012) and the position limits rule proposed in November of 2013 was to limit the availability of the bona fide hedge exemption to a limited set of transactions, unless the CFTC gave specific approval to a particular form of transaction.

In the most-recently proposed position limits rule, instead of providing a clear bona fide exemption from position limits to allow end-users of physical commodities to properly hedge their commercial risk was not included, many risk-reducing practices commonly used in the futures markets today were excluded from the list of bona fide hedging transactions prescribed in CFTC Rule 151.5(a)(2). This concern was confirmed by Mr. Jeffrey Sprecher, CEO of Intercontinental Exchange, Inc., in testimony before the Committee on May 21, 2013, when he stated that "[t]he narrow definition of bona fide hedge will likely hurt commercial end-users that these markets are intended to serve, and thus support the bona fide hedge exemption relied upon historically would bring greater certainty to end-users in executing their risk management operations."

The CFTC's limitation of bona fide hedges to only a handful of transaction types places significant limitations on many end-users' ability to hedge risk efficiently. As such, the Committee formulated Section 358 to provide for a workable hedge exemption process. The bona fide hedge provisions in Section 4a(c) of the Commodity Exchange Act are intended to provide market participants with certain relief from position limits therefore give end-users with the flexibility necessary to hedge their legitimate anticipated business risks.

One of the main purposes of Section 358 is to make clear that the statutory requirements with respect to what constitutes a bona fide hedge transaction must be reflected in the CFTC's further definition of that term. Specifically, changing "may" to "shall" in Section 4a(c)(1) reflects the intent of the Committee that the CFTC is not authorized to promulgate a further definition of "bona fide hedge transaction" that is narrower or more restrictive than what is described in the CEA. In addition, Section 358 intended to clarify that the CFTC's further definition of "bona fide hedge transaction" must include hedges of legitimate anticipated business needs.

Section 358 is also intended to provide more flexibility to market participants as hedging practices evolve. It is Congress' intent that the CFTC provide bona fide hedge status to all legitimate risk management practices now and in the future. A narrow definition of what constitutes bona fide hedging that is limited to an enumerated list of transactions will place significant limitations on many end-users' ability to hedge risk properly and efficiently. In further defining what constitutes a bona fide hedging transaction, the CFTC should provide flexibility such that changes and advances in hedging practices so they can easily be incorporated into the bona fide hedging regime in an efficient and timely manner, without further Commission rulemakings that would add uncertainty to the marketplace.

On July 24, 2013, at a hearing entitled "The Future of the CFTC: End-User Perspectives," the following witnesses provided testimony with respect to the need for provisions included in Section 358:

> Congress provided a definition of a bona fide hedge within Dodd-Frank that the CFTC has unnecessarily narrowed, including related to anticipatory hedging, and has created at least five different definitions in various rules of what constitutes a bona fide hedge. This is nonsensical and creates unnecessary confusion, while disrupting legitimate risk mitigation practices. We are committed to working with Congress to set clearer direction on bona fide hedges so that transactions that limit economic risks are viewed as bona fide hedges by the CFTC.—Mr. Lance Kotschwar, Senior Compliance Attorney, The Gavilon Group, LLC, on behalf of the Commodity Markets Council

> On September 28, 2012, the U.S. District Court for the District of Columbia vacated final CFTC rules regarding position limits. These vacated rules defined the term bona fide hedging. As written in the CFTC's rule that was vacated, the definition was unnecessarily narrow and would have discouraged a significant amount of important and beneficial risk management activity. Specifically, the rule narrowed the existing definition considerably by providing that a transaction or position that would otherwise qualify as a bona fide hedge also must fall within one of eight categories of enumerated hedging transactions, a definitional change neither supported in nor required by the Dodd-Frank Act. This restrictive definition of bona fide hedging

> transactions could disrupt the commodity markets, make hedging more difficult and costly, and may increase systemic risk by encouraging end-users to leave a relatively large portion of their portfolios un-hedged.—Mr. Richard F. McMahon, Jr., Vice President, EEI

*Section 359—Cross-border regulation of derivatives transactions.*

As the global financial system has evolved, U.S. institutions have expanded their derivatives operations overseas to provide services to both U.S. and non-U.S. customers. At the same time, foreign institutions have established subsidiaries and branches in the U.S. to offer derivatives directly to U.S. customers. The growth of this cross-border activity makes questions regarding the application of the Dodd-Frank Act to activities that occur outside the U.S. (known as "extraterritorial") complex and critical.

Section 722(d) of Title VII sets forth that provisions of the Dodd-Frank Act shall not apply to activities outside the United States unless those activities: (1) have a direct and significant connection with activities in, or effect on, commerce of the United States, or (2) contravene such rules or regulations as the CFTC prescribes are necessary to prevent evasion of the Dodd-Frank Act. This is consistent with historical practice by both the CFTC and the prudential regulators in their treatment of foreign entities with operations in the U.S., or of U.S. entities with regard to their operations in foreign jurisdictions. Generally, the regulatory agencies have deferred to foreign regulatory authorities for the supervision of entities located abroad if the agencies found that those entities were subject to a regulatory regime comparable to that imposed by the U.S.

However, in April of 2012, the prudential regulators proposed a rule for the application of margin requirements as required by Title VII for Major Swap Participants and Swap Dealers. Under the prudential regulators' proposal, margin requirements would apply to all transactions of U.S. financial institutions—whether they involve their U.S. or non-U.S. customers. For example, a foreign subsidiary of a U.S. bank in Europe would be subject to the Dodd-Frank Act's margin rules even when dealing with European customers.

On June 29, 2012, the CFTC issued proposed "interpretive guidance" for the cross-border application of Title VII of the Dodd-Frank Act. The release of this guidance, approved by all five commissioners, was done so without the concurrent release of similar guidance from the SEC for security-based swaps and, as it was not in the form of a proposed rule, did not include a cost-benefit analysis. When the guidance was released, then-CFTC Commissioner Jill Sommers stated that "[CFTC] staff had been guided by what could only be called the 'Intergalactic Commerce Clause' of the United States Constitution, in that every single swap a U.S. person enters into, no matter what the swap or where it was transacted, was stated to have a direct and significant connection with activities in, or effect on, commerce of the United States. This statutory and constitutional analysis of the extraterritorial application of U.S. law was, in my view, nothing short of extra-statutory and extra-constitutional."

On December 13, 2012, the Committee on Agriculture Subcommittee on General Farm Commodities and Risk Management held a hearing where Commissioners Sommers and Chilton testified alongside top regulators from Japan and the European Commission. Combined, the three regulatory jurisdictions testifying at the hearing represented an overwhelming majority of the global derivatives marketplace. Based on testimony the subcommittee received, there appeared to be a serious lack of coordination between both foreign and domestic regulators.

For example, Mr. Masamichi Kono with the Financial Services Agency of Japan (who at the time was Chairman of IOSCO) testified during the hearing that "much needs to be done" by the CFTC and that "it is important that the details of the applicable laws and regulations are made clear as much as possible before their implementation in order to minimize regulatory uncertainty." Further, with respect to minimizing risk in the marketplace—a goal central to the creation of the Dodd-Frank Act—Mr. Kono testified that:

> [S]uch risks need not be addressed by extraterritorial application of the U.S. laws and regulations; rather, the U.S. authorities could rely on foreign regulators upon establishing of course that the foreign regulators have the required authority and competence to exercise appropriate regulation and oversight over those entities and activities. This is what we consider as the most efficient and effective approach, in line with the principles of international comity between sovereign jurisdictions.

At the same hearing, Mr. Patrick Pearson with the European Commission also testified before the Committee about regulatory conflicts between the United States and 27 member nations of the European Union. With respect to the risk posed to global markets if international regulators do not properly coordinate the regulation of the markets, he stated that:

> [T]rades will not be able to be cleared. If they can't be cleared, they won't take place. This means that firms and users will not hedge their risks, or firms will hedge their risks but they will only take place within one jurisdiction, which means that risk will be concentrated in one jurisdiction on the planet. That could be the United States. If your firms can't hedge their risks outside of the United States, they'll have to hedge them here. The consequences of that is obviously a fragmented market and a significant concentration of financial risk in the U.S. system, and this is exactly what we tried to prevent with our global regulatory reform.

In the 113th Congress, on March 14, 2013, at a Committee hearing entitled "Examining Legislative Improvements to Title VII of the Dodd-Frank Act," the Hon. Kenneth E. Bentsen, Acting President and CEO, SIFMA, provided the following testimony that informed the drafting of Section 359:

> Though Title VII was signed into law 2½ years ago, we still do not know which swaps activities will be subject to U.S. regulation and which will be subject to foreign regulation. Section 722 of the Dodd-Frank Act limits the CFTC's jurisdiction over swap transactions outside of the United States to those that "have a direct and significant connec-

> tion with activities in, or effect on, commerce of the U.S." or are meant to evade Dodd-Frank. Section 772 limits the SEC's jurisdiction over security based swap transactions outside of the United States to those meant to evade Dodd-Frank. However, the CFTC and SEC have not yet finalized (or, in the SEC's case, proposed) rules clarifying their interpretation of these statutory provisions. The result has been significant uncertainty in the international marketplace and, due to the aggressive position being taken by the CFTC as described below, a reluctance of foreign market participants to trade with U.S. financial institutions until that uncertainty is resolved. While the CFTC has proposed guidance on the cross-border impact of their swaps rules, that guidance inappropriately recasts the restriction that Congress placed on CFTC jurisdiction over swap transactions outside the United States into a grant of authority to regulate cross-border trades. The CFTC primarily does so with a very broad definition of "U.S. Person," which it applies to persons with even a minimal jurisdictional nexus to the United States. In addition, the CFTC has released several differing interim and proposed definitions of "U.S. Person" for varying purposes, resulting in a great deal of ambiguity and confusion for market participants. SIFMA supports a final definition of U.S. Person that focuses on real, rather than nominal, connections to the United States and that is simple, objective and determinable so a person can determine its status and the status of its counterparties.

On April 18, 2013, the finance ministers of the European Commission, France, Germany, United Kingdom, Japan, Switzerland, Russia, South Africa and Brazil wrote to Treasury Secretary Jacob Lew stating that "[w]e are already starting to see evidence of fragmentation in this vitally important financial market as a result of lack of regulatory coordination" and "[w]e are concerned that, without clear direction from global policymakers and regulators, derivatives markets will recede into localised and less efficient structures, impairing the ability of business across the globe to manage risk."

On May 21, 2013, testifying before the Committee at a hearing entitled "The Future of the CFTC: Market Perspectives," the following testimony was provided by witnesses with respect to provisions included in Section 359:

> If regulators fail to harmonize, the effects of uncertainty and the prospect for regulatory arbitrage will be damaging. Because markets are global and capital flows across borders, no single country or regulatory regime oversees the derivatives market. In order to make long-term business decisions, market participants require certainty that their transactions will not be judged on conflicting standards. The derivatives markets are international: the majority of companies that operate globally use derivatives to manage price risks, and they conduct these transactions with both U.S. and non-U.S. counterparties. The likely outcome will be that regulators deem other countries' financial regulatory systems as "nonequivalent", which would

lead to those countries erecting barriers to its financial markets. It is crucial to understand that if countries erect these barriers, WE markets and market participants will be damaged. Currently, the U.S. derivatives markets are home to vital global benchmark contracts in agriculture, energy, financial asset classes. These have become benchmark contracts because Asian and European market participants have direct access to U.S. markets. Importantly, the long-standing global nature of the derivatives markets and the resulting international competition has lead to advances in transparency, risk management, and historically, regulatory cooperation. Over the past year, ICE has been delivering this message to domestic and international regulators, yet regulations continue to diverge, particularly in the U.S. and Europe. We ask the Committee, in its oversight role, to impress upon the Commodity Futures Trading Commission the importance of working with European and Asian counterparts to harmonize regulation and avoid creating unintended, unpredictable impacts on financial markets and their users. The time for agreement is closing.—Mr. Jeffrey C. Sprecher, Founder, Chairman, and CEO of IntercontinentalExchange, Inc.

ISDA and our members believe that a globally harmonized approach to cross-border regulation is of paramount importance. What they face now is considerable uncertainty. Uncertainty is never a good thing in financial markets, as there are typically only two things to do in face of that uncertainty. One response is to pull back and wait until such time as greater certainty is provided. On a firm level, that means missed opportunity. On a market level, that translates to less efficient, less liquid and more volatile markets, material harm to financing and investing activities and a drag on the economy in general. To achieve the goal of a globally harmonized framework, the CFTC and SEC should work together to achieve consensus with global regulators. H.R. 1256 would help the U.S. regulators to provide a unified front when addressing the extraterritorial application of U.S. rules and when dealing with non-U.S. regulators. Harmonization of regulatory approaches, particularly on issues with systemic risk implications, and a concerted program of mutual recognition of regulatory regimes by global regulators are essential parts of the solution to ET.—Mr. Stephen O'Conner, Chairman, ISDA

As of the writing of this Report, global regulators have yet to harmonize their approach to global derivatives regulation. In order to address the serious concerns voiced by both international and domestic regulators, Section 359 would require the CFTC to propose and finalize a rule, not "guidance" to which the APA does not apply, on cross-border swaps regulation. The bill would also require that the CFTC grant the top 9 global jurisdictions for swaps transactions by volume substituted compliance to regulate institutions operating within their borders unless the CFTC makes a determination that a jurisdiction's rules are not equivalent to the regulations of the United States.

## SECTION-BY-SECTION

Sec. 1 is the short title of the bill.
Sec. 2 is the table of contents.

### Title I—Customer Protections

Sec. 101 is the short title of title I.

Sec. 102 amends section 17 of the Commodity Exchange Act (CEA) to require that each member of a registered futures association (NFA) maintain written policies concerning the residual interest in segregated accounts, cleared swaps collateral accounts, and secured amount funds in foreign futures and options customer accounts. The member must also establish rules to govern the withdrawal, transfer or disbursement by a futures commission merchant (FCM) of the same funds.

Sec. 103 amends section 17 of the CEA to require an FCM to use an electronic system to report financial and operational information to the NFA in accordance with such terms and conditions that the NFA establishes. A registered FCM must require any depository institution that holds segregated accounts and the customer secured amount funds to report balances to the NFA. If the depository institution will not report the fund balances, the registered member cannot use the depository institution to hold customer segregated funds or secured amount funds.

Sec. 104 amends section 17 of the CEA to require an FCM to immediately report to the CFTC and the NFA when the funds in a customer's account, segregated account or secured amount account are less than required by regulation. It also requires the chief compliance officer of the FCM to file with the Commission a yearly assessment of the FCM's internal compliance programs.

Sec. 105 amends section 4d of the CEA to allow an FCM one business day after a trade to comply with the amounts of money, securities and property required to be held in a customer account by section 4d(a)(2) of the CEA.

Sec. 106 amends section 20(a) of the CEA to allow the use of the cash, securities or other property of a bankrupt commodity broker to satisfy any deficient public customer account.

Sec. 107 requires the CFTC to report to the authorizing committees on high-frequency trading on markets under its jurisdiction. The report shall examine the technology, personnel and other resources the Commission may require to monitor high-frequency trading; the role the trading plays in providing market liquidity; whether the technology creates discrepancies in the marketplace; and whether the Commission's existing authority protects the market and fosters transparency.

### Title II

Sec. 201 is the short title of title II.

Sec. 202 amends section 12(d) of the CEA to reauthorize the CFTC through FY 2018.

Sec. 203 amends section 15(a) of the CEA to harmonize the cost benefit requirements of the CFTC with those of executive order

13563. The section also requires that the cost benefit analysis be performed by the Chief Economist and published within the proposed rule along with the rule's statutory justification.

Sec. 204 amends section 2(a) of the CEA to require that each division of the CFTC have a Director that is hired by the Commission, and performs functions as the Commission may prescribe.

Sec. 205 amends section 2(a) of the CEA to establish the Office of the Chief Economist. The structure and powers of the Office of the Chief Economist mirrors the structure and powers of the General Counsel.

Sec. 206 amends section 2(a)(12) of the CEA to require 7 days notice to the Commission before any division or office of the Commission issues an interpretive rule of general applicability, a statement of general policy, response to a petition for guidance, or an exemptive, a no-action, or an interpretive letter. After receiving notice, any member of the Commission may request a meeting of the Commission to further consider the staff-proposed action, and if the Commission decides to hold the meeting by majority vote, the matter may not be issued until the meeting has concluded. The 7 day notice requirement can be waived by a majority vote of the Commission if the Commission determines that requiring such notice would be impracticable, unnecessary, or contrary to the public interest.

Sec. 207 amends section 2(a) of the CEA to require the Commission to file with the authorizing committees a strategic technology plan every 5 years. The plan shall include a detailed technology strategy focused on market surveillance and risk detection, and must include a detailed accounting of how the funds provided for technology will be used.

Sec. 208 amends section 2(a)(12) of the CEA to require the Commission staff, led by the Chief Economist, to develop internal risk control mechanisms to safeguard the storage and privacy of market data by the Commission. Special attention should be given to market data sharing agreements and academic research performed at the Commission using market data. The Commission shall report to the authorizing committees on progress made in implementing the internal risk controls 60 days after enactment, and again 120 days after enactment of the Act.

Sec. 209 amends section 6(c)(5) of the CEA to require that subpoenas issued by the Commission comply with the common law standards set forth by the United States Supreme Court. A subpoena authorized to be issued by the Commission shall state in good faith the purpose of the investigation, shall require only information reasonably relevant to the purpose of the investigation and shall be for a finite period. A subpoena may be renewed only by Commission vote.

Sec. 210 amends section 2(a)(12) of the CEA to require that all proposed rules include a plan for when and for how long a comment period will be open, and when compliance with the final rule will be required.

Sec. 211 amends section 2(a)(12) to apply the notice and comment provisions of the Administrative Procedure Act to guidance that is issued and voted on by the Commission.

Sec. 212 amends the CEA by adding a new section (section 24) committing the original jurisdiction of the review of a CFTC issued final rule to the United States Court of Appeals for the District of Columbia Circuit or the U.S. Court of Appeals for the circuit where the party resides. This is similar to the judicial review process for rules and orders of the Securities and Exchange Commission set forth in section 25(b) of the Securities Exchange Act of 1934.

Sec. 213 requires the GAO to conduct a study of the Commission's resources and assess whether the resources are sufficient to enable the Commission to effectively carry out its duties. The study shall also examine the prior expenditures of the Commission on hardware, software and analytical processes designed to protect customers in the areas of market surveillance and data collection.

## Title III

Sec. 301 is the short title for title III.

### SUBTITLE A—END-USER EXEMPTION FROM MARGIN REQUIREMENTS

Sec. 311 amends section 4s(e) of the CEA to clarify that initial and variation margin requirements shall not apply to a swap in which one of the counterparties to the swap is not a financial entity and qualifies for the end-user clearing exception in Section 2(h)(7)(A).

Sec. 312 excludes the amendments made by this subtitle from the requirements of the Paperwork Reduction Act and from notice and comment requirements of the Administrative Procedure Act.

### SUBTITLE B—INTER-AFFILIATE SWAPS

Sec. 321(a) amends 2(h)(7)(D)(i) of the CEA to clarify that transactions between affiliates need not be cleared provided that a credit support measure is utilized with a swap entered into with a swap dealer or major swap participant.

Subsection (b) clarifies that the credit support measure requirement contained in (a) shall only be effective in a prospective manner starting on the date of enactment of the act.

### SUBTITLE C—INDEMNIFICATION REQUIREMENTS RELATED TO SWAP DATA REPOSITORIES

Sec. 331 amends section 5b(k)(5) of the CEA by striking the confidentiality and indemnification agreement paragraph of the derivatives clearing organization reporting requirements and inserting a new confidentiality agreement paragraph, eliminating the need to indemnify the Commission for any expense arising from litigation related to information provided under section 8. An identical amendment is made to section 21(d) of the CEA eliminating the indemnification requirement for swap data repositories.

### SUBTITLE D—RELIEF FOR MUNICIPAL UTILITIES

Sec. 341 amends section 1a(49) of the CEA by creating within the definition of swap dealer, a new category of transactions in utility operations-related swaps, which shall be reported according to the reporting requirements of uncleared swaps and exempted from inclusion in an entity's general de minimis calculation established in (D).

Sec. 342 amends section 4s(h)(2) of the CEA to add the definition of a "utility special entity": an entity established by a state, or political subdivision thereof, which owns or operates an electric or natural gas facility; supplies natural gas or electric energy to another utility special entity; has public service obligation under federal, state or local law or regulation to deliver electric energy or natural gas service to customers; or is a Federal power marketing agency.

Sec. 343 amends section 1a(47) of the CEA to add to the definition of swap a list of "commonly known" transactions to further describe a utility operations-related swap. It further amends section 1a to define a "utility operations related swap" as a swap that is entered into to hedge or mitigate risk, is not based on an interest rate, credit, equity, or currency asset class nor a metal, agriculture commodity, or crude oil or gasoline commodity for any grade except as used as fuel for electric energy generation, and is associated with the generation, production or sale of natural gas or electric energy.

### SUBTITLE E—END-USER REGULATORY RELIEF

Sec. 351(a) amends section 2(h)(7)(C)(iii) of the CEA to exclude from the definition of a financial entity those entities not supervised by a prudential regulator and that are commercial market participants, but considered financial entities because they predominantly engage in physical delivery contracts or enter into swaps, futures and other derivatives on behalf of, or to hedge the commercial risk of, non-financial affiliates.

Subsection (b) amends section 1a of the CEA to define a commercial market participant as a producer, processor, merchant, or commercial user of an exempt or agricultural commodity, or the products or byproducts of such commodity.

Sec. 352 amends section 2(a)(13) of the CEA to require the Commission to promulgate a rule that would delay the public reporting of a non-cleared swap traded in an illiquid market and entered into by a non-financial entity to no sooner than 30 days after the transaction has been executed. An illiquid market is defined as any market in which the volume and frequency of trading in swaps is at such a level as to allow identification of individual market participants.

Sec. 353 amends the CEA by adding a new section, 4u, which clarifies the record keeping requirements of non-registered members of a designated contract market (DCM) or swap execution facility (SEF). All recordkeeping requirements, and rules promulgated pursuant to the CEA, shall be satisfied if such entities maintain written records of each transaction in a contract for future delivery, option on a future, swap, swaption, trade option, or related cash or forward transaction. Such records must be searchable by transaction and include the final agreement between the parties as well as the material economic terms of the transaction.

Sec. 354 amends section 1a(47)(B)(ii) of the CEA to clarify that the exclusion from the definition of the term swap includes contracts that are intended to be physically settled that include any stand-alone or embedded option which, if exercised, results in a physical delivery obligation.

Sec. 355 amends section 1a(49)(D) of the CEA to require the Commission to take an affirmative action by rule or regulation to reduce the $8 billion de minimis exception from the swap dealer definition.

Sec. 356 amends section 4s(e) of the CEA to require the Commission to permit swap dealers and major swap participants that are not banks to use financial models that calculate minimum capital requirements and minimum initial and variation margin requirements that have been approved for use by banks by prudential regulators or the SEC.

Sec. 357 requires the CFTC to change the regulation regarding the advertisement of participation in commodity pools. The changes will allow any registered commodity pool that also qualifies for an exemption from the registration requirements of the Securities Act to be sold pursuant to the changes made to section 4 of the Securities Act under the Jumpstart our Business Startups Act (P.L. 112–106).

Sec. 358 amends section 4a(c) of the CEA to require the Commission to recognize anticipatory hedging transactions as part of the exemption from trading limits.

Sec. 359(a) requires the CFTC to issue rules setting forth the application of the U.S. swaps requirements relating to swaps transacted between U.S. and non-U.S. persons. The rules shall address the nature of connections to the U.S. which would require a non-U.S. person to register as a swap dealer or major swap participant; which of the U.S. swap requirements shall apply to the activities of non-U.S. persons, U.S. persons, and their branches, agencies, subsidiaries and affiliates outside the U.S.; and the circumstances under which a non-U.S. person shall be exempt from U.S. swap requirements.

Subsection (b) prohibits the issuance of guidance, memorandum of understanding or any such other agreement in place of the Commission's requirement to issue a rule in accordance with the APA.

Subsection (c) requires the Commission to exempt from U.S. swaps requirements non-U.S. persons that are in compliance with the swaps regulatory requirements of a country or administrative region that has 1 of the world's 9 largest swap markets by notional amount in the preceding calendar year, or other foreign jurisdictions as determined by the Commission, unless the Commission determines that the regulatory requirements are not broadly equivalent to the United States swap requirements.

Exemptions for the 5 largest swap markets by notional amount shall go into effect on the date the final rule is issued. The remaining market exemptions will occur one year after the date the final rule is issued.

Once the final rules are issued, the Commission shall assess the regulatory requirements of the countries or administrative regions described in this subsection to determine if the regulatory requirements of a foreign jurisdiction are not broadly equivalent to U.S. swaps requirements.

Subsection (d) requires the Commission to report to Congress any determination that a foreign jurisdiction is not broadly equivalent to the U.S. swaps requirements within 30 days of that determination.

Subsection (e) defines the terms "U.S. person" and "United States swaps requirements."

Subsection (f) is a conforming amendment.

SUBTITLE F—EFFECTIVE DATE

Sec. 371 sets the effective date for this title as July 21, 2010.

## COMMITTEE CONSIDERATION

### I. HEARINGS

The Committee on Agriculture held five hearings during the 113th Congress in anticipation of legislation to extend and reform the operations of the Commodity Futures Trading Commission.

On March 14, 2013, the Full Committee on Agriculture held a hearing entitled, "Examining Legislative Improvements to Title VII of the Dodd-Frank Act" where the following witnesses testified on several measures that where included in H.R. 4413:

- The Honorable Gary Gensler, Chairman, U.S. Commodity Futures Trading Commission, Washington, D.C.
- The Honorable Kenneth E. Bentsen, Jr., Acting President and CEO, Securities Industry and Financial Markets Association (SIFMA), Washington, D.C.
- Mr. Jim Colby, Assistant Treasurer, Honeywell International Inc., Morristown, New Jersey; on behalf of the Coalition for Derivatives End-Users
- Mr. Terrance Naulty, General Manager & CEO, Owensboro Municipal Utilities, Owensboro, Kentucky; on behalf of the American Public Power Association
- Mr. Larry Thompson, General Counsel, Depository Trust and Clearing Corporation (DTCC), New York, New York
- Ms. Marie Hollein, President and CEO, Financial Executives International (FEI) and Financial Executives Research Foundation, Washington, D.C.; on behalf of the Coalition for Derivatives End-Users
- Mr. Wallace C. Turbeville, Senior Fellow, Demos, New York, New York; on behalf of Americans for Financial Reform

On May 21, 2013, the Full Committee on Agriculture held a hearing entitled, "The Future of the CFTC: Market Perspectives" where the following witnesses testified on matters included in H.R. 4413:

- Mr. Terrence A. Duffy, Executive Chairman and President, CME Group, Inc., Chicago, Illinois
- Mr. Jeffrey C. Sprecher, Chairman and CEO, IntercontinentalExchange, Inc., Atlanta, Georgia
- Mr. Daniel J. Roth, President and CEO, National Futures Association, Chicago, Illinois
- The Honorable Walter L. Lukken, President and CEO, Futures Industry Association, Washington, D.C.
- Mr. Stephen O'Connor, Chairman, International Swaps and Derivatives Association, Inc., New York, New York
- Mr. William Dunaway, Chief Financial Officer, INTL FCStone, Inc., Kansas City, Missouri

On July 23, 2013, the Full Committee on Agriculture held a hearing entitled, "The Future of the CFTC: Commission Perspectives" where the following witnesses testified on matters included in H.R. 4413:

- The Honorable Scott D. O'Malia, Commissioner, U.S. Commodity Futures Trading Commission, Washington, D.C.

• The Honorable Mark P. Wetjen, Commissioner, U.S. Commodity Futures Trading Commission, Washington, D.C.

On July 24, 2013, the Full Committee on Agriculture held a hearing entitled, "The Future of the CFTC: End-User Perspectives" where the following witnesses testified on matters included in H.R. 4413:

• Mr. Scott Cordes, President, CHS Hedging, Inc., St. Paul, Minnesota, on behalf of the National Council of Farmer Cooperatives
• Mr. Lance Kotschwar, Senior Compliance Attorney, The Gavilon Group, LLC, Omaha, Nebraska, on behalf of the Commodity Markets Council
• Mr. Richard F. McMahon, Jr., Vice President, Edison Electric Institute, Washington, D.C.
• Mr. Chris Monroe, Treasurer, Southwest Airlines, Dallas, Texas
• Mr. Andrew K. Soto, Senior Managing Counsel, Regulatory Affairs, American Gas Association, Washington, DC
• Mr. Gene A. Guilford, National & Regional Policy Counsel, Connecticut Energy Marketers Association, Cromwell, Connecticut, on behalf of the Commodity Markets Oversight Coalition

On October 2, 2013, the Full Committee on Agriculture held a hearing entitled, "The Future of the CFTC: Perspectives on Customer Protections" where the following witnesses testified on matters included in H.R. 4413:

• Mr. Terrence A. Duffy, Executive Chairman and President, CME Group, Inc., Chicago, Illinois
• Mr. Daniel J. Roth, President and CEO, National Futures Association, Chicago, Illinois
• Dr. Christopher L. Culp, Senior Advisor, Compass Lexecon, Chicago, Illinois
• Mr. Michael J. Anderson, Regional Sales Manager, The Andersons Inc., Union City, Tennessee, on behalf of the National Grain and Feed Association
• Mr. James L. Koutoulas, Esq., President and Co-Founder, Commodity Customer Coalition, Inc., Chicago, Illinois
• Mr. Theodore L. Johnson, President, Frontier Futures, Inc., Cedar Rapids, Iowa

## II. FULL COMMITTEE

The Committee on Agriculture met, pursuant to notice, with a quorum present, on April 9, 2014, to consider H.R. 4413. Chairman Lucas called the meeting to order to consider the Customer Protection and End User Relief Act. Chairman Lucas gave a statement as did Mr. Peterson, Mr. Conaway, and Mr. David Scott.

Without objection the Customer Protection and End User Relief Act was brought before the Committee, the first reading of the text was waived, and it was open for amendment at any point.

Mr. Conaway offered an amendment to sunset all new CFTC rules or regulations promulgated after the enactment of this act, unless the CFTC reissues the rule or regulation, in a manner consistent with the Administrative Procedure Act and by a majority vote of the Commission, and determines it to have force or effect. Mr. Conaway then withdrew his amendment.

Mr. Goodlatte offered an amendment to require the CFTC to report on actions taken to ensure a stable aluminum market. Mr. Goodlatte then withdrew his amendment.

Mr. Peterson offered a motion that the Committee favorably report the Customer Protection and End User Relief Act to the House with the recommendation that it do pass. By voice vote, the motion was adopted.

At the conclusion of the meeting, Chairman Lucas advised Members that pursuant to the rules of the House of Representatives Members had 2 calendar days to file any supplemental or minority views with the Committee.

Without objection, staff was given permission to make any necessary clerical, technical or conforming changes to reflect the intent of the Committee. Chairman Lucas thanked all the Members and adjourned the meeting.

## COMMITTEE VOTES

In compliance with clause 3(b) of rule XIII of the House of Representatives, H.R. 4413 was reported by voice vote with a majority quorum present. There was no request for a recorded vote.

## COMMITTEE OVERSIGHT FINDINGS

Pursuant to clause 3(c)(1) of rule XIII of the Rules of the House of Representatives, the Committee on Agriculture's oversight findings and recommendations are reflected in the body of this report.

## BUDGET ACT COMPLIANCE (SECTIONS 308, 402, AND 423)

The provisions of clause 3(c)(2) of rule XIII of the Rules of the House of Representatives and section 308(a)(1) of the Congressional Budget Act of 1974 (relating to estimates of new budget authority, new spending authority, new credit authority, or increased or decreased revenues or tax expenditures) are not considered applicable. The estimate and comparison required to be prepared by the Director of the Congressional Budget Office under clause 3(c)(3) of rule XIII of the Rules of the House of Representatives and sections 402 and 423 of the Congressional Budget Act of 1974 submitted to the Committee prior to the filing of this report are as follows:

U.S. CONGRESS,
CONGRESSIONAL BUDGET OFFICE,
*Washington, DC, May 19, 2014.*

Hon. FRANK D. LUCAS,
*Chairman, Committee on Agriculture,*
*House of Representatives, Washington, DC.*

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 4413, the Customer Protection and End User Relief Act.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Susan Willie.

Sincerely,

DOUGLAS W. ELMENDORF.

Enclosure.

*H.R. 4413—Customer Protection and End User Relief Act*

Summary: H.R. 4413 would authorize appropriations for the Commodity Futures Trading Commission (CFTC) through 2018 and make changes in some of the agency's operating procedures. The bill also would amend the Commodity Exchange Act to provide greater protections for customer funds held by entities that broker transactions in commodity futures and to relax requirements on certain participants in swap transactions in a number of different circumstances. (A swap is a contract that calls for an exchange of cash between two participants, based on an underlying rate or index or on the performance of an asset.)

CBO estimates that implementing H.R. 4413 would cost $207 million in 2015 and $948 million over the 2015–2019 period, assuming appropriation of the necessary amounts. CBO expects that enacting H.R. 4413 would affect direct spending and revenues; therefore, pay-as-you-go procedures apply. However, CBO estimates that those effects would not be significant.

H.R. 4413 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA).

Estimated cost to the Federal Government: The estimated budgetary effect of H.R. 4413 is shown in the following table. The costs of this legislation fall within budget function 370 (commerce and housing credit).

| | By fiscal year, in millions of dollars— | | | | | |
|---|---|---|---|---|---|---|
| | 2015 | 2016 | 2017 | 2018 | 2019 | 2015–2019 |
| CHANGES IN SPENDING SUBJECT TO APPROPRIATION | | | | | | |
| CFTC Reauthorization: | | | | | | |
| Estimated Authorization Level | 221 | 228 | 236 | 245 | 0 | 930 |
| Estimated Outlays | 197 | 223 | 231 | 239 | 22 | 912 |
| Other Provisions: | | | | | | |
| Estimated Authorization Level | 12 | 6 | 6 | 6 | 7 | 37 |
| Estimated Outlays | 10 | 7 | 6 | 6 | 7 | 36 |
| Total Changes: | | | | | | |
| Estimated Authorization Level | 233 | 234 | 242 | 251 | 7 | 967 |
| Estimated Outlays | 207 | 230 | 237 | 245 | 29 | 948 |

Notes: CBO estimates that enacting H.R. 4413 would not have a significant effect on revenues or direct spending over the 2014–2024 period.
CFTC = Commodity Futures Trading Commission.

Basis of Estimate: For this estimate, CBO assumes that the bill will be enacted near the end of fiscal year 2014, the necessary amounts will be appropriated near the beginning of each fiscal year, and outlays will follow spending patterns for similar activities at the CFTC.

*Spending subject to appropriation*

CFTC Reauthorization. H.R. 4413 would authorize appropriations for CFTC operations through 2018; for 2014, the CFTC received an appropriation of $215 million. Based on the agency's current budget and adjusting for anticipated inflation, CBO estimates that extending the authorization of appropriations for the current functions of the CFTC through 2018 would cost $912 million over the 2015–2019 period, assuming those inflation-adjusted amounts are appropriated each year.

Other Provisions. H.R. 4413 would require the agency to change certain procedures in its rulemaking process and to improve safeguards of market data in the agency's control. The bill also would direct the CFTC to prepare a report for the Congress examining the effect of high-frequency trading (the use of technology and computer algorithms to rapidly trade contracts) on the markets it oversees.

In addition, the bill would require entities that broker transactions in commodity futures, known as futures commission merchants, and the national association that regulates them to implement practices that provide additional protections for funds held for their clients. Finally, under the bill, certain swap transactions or participants in those transactions would be exempt from new regulations developed to meet the requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act. For example, the bill would, under certain circumstances, exempt nonfinancial entities that enter into a swap transaction from meeting certain margin requirements.

Based on information from the CFTC, CBO estimates that the agency would require 25 additional personnel annually to handle the increased workload under these provisions, an increase of about 4 percent over the agency's 2013 staffing level. We estimate that salaries, benefits, and overhead for those additional staff, as well as new administrative expenses, would cost $36 million over the 2015–2019 period, assuming appropriation of the necessary amounts.

*Direct spending and revenues*

H.R. 4413 would increase costs for the financial regulators (the Federal Reserve System, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency) to amend certain regulations, which would affect direct spending and revenues. The bill also would affect federally owned utilities by changing the way CFTC regulates certain electric and natural gas utility contracts. Taken together, CBO estimates that these costs would not be significant over the 2014–2024 period.

Pay-As-You-Go considerations: CBO expects that enacting H.R. 4413 would affect direct spending and revenues; therefore, pay-as-you-go procedures apply. However, CBO estimates that those effects would not be significant.

Intergovernmental and Private-sector impact: H.R. 4413 contains no intergovernmental or private-sector mandates as defined in UMRA and would impose no costs on state, local, or tribal governments.

Previous CBO estimates: On April 1, 2013, CBO transmitted a cost estimate for H.R. 1003, a bill to improve consideration by the Commodity Futures Trading Commission of the costs and benefits of its regulations and orders, as ordered reported by the House Committee on Agriculture on March 20, 2013. Provisions in title II of H.R. 4413 are similar to H.R. 1003, and the CBO cost estimates are the same.

CBO prepared two cost estimates for H.R. 634, the Business Risk Mitigation and Price Stabilization Act of 2013. On April 11, 2013, we transmitted a cost estimate for a version of the bill ordered reported by the House Committee on Agriculture on March 20, 2013. On May 29, 2013, we transmitted a cost estimate for a version of the bill ordered reported by the House Committee on Financial

Services on May 7, 2013. Both versions of the bill are similar to provisions in title III of H.R. 4413, and the CBO cost estimates for those similar provisions are the same.

CBO prepared two cost estimates for H.R. 677, the Inter-Affiliate Swap Clarification Act. On April 11, 2013, we transmitted an estimate for a version of the bill ordered reported by the House Committee on Agriculture on March 20, 2013. On May 30, 2013, we transmitted a cost estimate for a version of the bill ordered reported by the House Committee on Financial Services on May 7, 2013. Both versions of H.R. 677 would place new requirements on the CFTC and the Securities and Exchange Commission. Provisions in title III of H.R. 4413 are similar to the provisions of H.R. 677 that applied to the CFTC; the CBO cost estimates for the similar provisions are the same.

CBO prepared two cost estimates for H.R. 742, the Swap Data Repository and Clearinghouse Indemnification Correction Act of 2013. On April 11, 2013, we transmitted a cost estimate for a version of the bill ordered reported by the House Committee on Agriculture on March 20, 2013. On May 17, 2013, we transmitted a cost estimate for a version of the bill ordered reported by the House Committee on Financial Services on May 7, 2013. Both versions of the bill are similar to provisions in title III of H.R. 4413, and the CBO cost estimates for the similar provisions are the same.

CBO prepared two cost estimates for H.R. 1256, the Swap Jurisdiction Certainty Act. On May 3, 2013, we transmitted a cost estimate for a version of the bill ordered reported by the House Committee on Agriculture on March 20, 2013. On May 30, 2013, we transmitted a cost estimate for a version of the bill ordered reported by the House Committee on Financial Services on May 7, 2013. Both versions of the bill are similar to provisions in title III of H.R. 4413, and the CBO cost estimates for the similar provisions are the same.

On April 1, 2012, CBO transmitted a cost estimate for H.R. 1038, the Public Power Risk Management Act of 2013, as ordered reported by the House Committee on Agriculture on March 20, 2013. Provisions in title III of H.R. 4413 are similar to H.R. 1038, and the CBO cost estimates are the same.

Estimate prepared by: Federal Costs: Susan Willie; Impact on State, Local, and Tribal Governments: J'nell L. Blanco; Impact on the Private Sector: Paige Piper/Bach.

Estimate approved by: Theresa Gullo, Deputy Assistant Director for Budget Analysis.

## Performance Goals and Objectives

With respect to the requirement of clause 3(c)(4) of rule XIII of the Rules of the House of Representatives, the performance goals and objections of this legislation are to reauthorize the Commodity Futures Trading Commission, to better protect futures customers, to provide end users with market certainty, to make basic reforms to ensure transparency and accountability at the Commission, to help farmers, ranchers, and end users manage risks to help keep consumer costs low, and for other purposes.

## Committee Cost Estimate

Pursuant to clause 3(d)(2) of rule XIII of the Rules of the House of Representatives, the Committee report incorporates the cost estimate prepared by the Director of the Congressional Budget Office pursuant to sections 402 and 423 of the Congressional Budget Act of 1974.

## Advisory Committee Statement

No advisory committee within the meaning of section 5(b) of the Federal Advisory Committee Act was created by this legislation.

## Applicability to the Legislative Branch

The Committee finds that the legislation does not relate to the terms and conditions of employment or access to public services or accommodations within the meaning of section 102(b)(3) of the Congressional Accountability Act (Public Law 104–1).

## Federal Mandates Statement

The Committee adopted as its own the estimate of Federal mandates prepared by the Director of the Congressional Budget Office pursuant to section 423 of the Unfunded Mandates Reform Act (Public Law 104–4).

## Earmark Statement Required by Clause 9 of Rule XXI of the Rules of House of Representatives

H.R. 4413 does not contain any congressional earmarks, limited tax benefits, or limited tariff benefits as defined in clause 9(e), 9(f), or 9(g) of rule XXI of the Rules of the House of Representatives.

## Duplication of Federal Programs

This bill does not establish or reauthorize a program of the Federal Government known to be duplicative of another Federal program, a program that was included in any report from the Government Accountability Office to Congress pursuant to section 21 of Public Law 111–139, or a program related to a program identified in the most recent Catalog of Federal Domestic Assistance.

## Disclosure of Directed Rule Makings

The Committee estimates that H.R. 4413 specifically directs CFTC to conduct one rule making proceedings within the meaning of 5 U.S.C. 551.

## Changes in Existing Law Made by the Bill, as Reported

In compliance with clause 3(e) of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italic, existing law in which no change is proposed is shown in roman):

# COMMODITY EXCHANGE ACT

* * * * * * *

**SEC. 1a. DEFINITIONS.**

As used in this Act:

(1) * * *

* * * * * * *

*(7) COMMERCIAL MARKET PARTICIPANT.—The term "commercial market participant" means any producer, processor, merchant, or commercial user of an exempt or agricultural commodity, or the products or byproducts of such a commodity.*

[(8)] *(9)* COMMISSION.—The term "Commission" means the Commodity Futures Trading Commission established under section 2(a)(2).

[(9)] *(10)* COMMODITY.—The term "commodity" means wheat, cotton, rice, corn, oats, barley, rye, flaxseed, grain sorghums, mill feeds, butter, eggs, Solanum tuberosum (Irish potatoes), wool, wool tops, fats and oils (including lard, tallow, cottonseed oil, peanut oil, soybean oil, and all other fats and oils), cottonseed meal, cottonseed, peanuts, soybeans, soybean meal, livestock, livestock products, and frozen concentrated orange juice, and all other goods and articles, except onions (as provided by the first section of Public Law 85–839 (7 U.S.C. 13–1)) and motion picture box office receipts (or any index, measure, value, or data related to such receipts), and all services, rights, and interests (except motion picture box office receipts, or any index, measure, value or data related to such receipts) in which contracts for future delivery are presently or in the future dealt in.

[(10)] *(11)* COMMODITY POOL.—

(A) * * *

* * * * * * *

[(11)] *(12)* COMMODITY POOL OPERATOR.—

(A) * * *

* * * * * * *

[(12)] *(13)* COMMODITY TRADING ADVISOR.—

(A) * * *

* * * * * * *

[(13)] *(14)* CONTRACT OF SALE.—The term "contract of sale" includes sales, agreements of sale, and agreements to sell.

[(14)] *(15)* COOPERATIVE ASSOCIATION OF PRODUCERS.—The term "cooperative association of producers" means any cooperative association, corporate, or otherwise, not less than 75 percent in good faith owned or controlled, directly or indirectly, by producers of agricultural products and otherwise complying with the Act of February 18, 1922 (42 Stat. 388, chapter 57; 7 U.S.C. 291 and 292), including any organization acting for a group of such associations and owned or controlled by such associations, except that business done for or with the United States, or any agency thereof, shall not be considered either member or nonmember business in determining the compliance of any such association with this Act.

[(15)] *(16)* DERIVATIVES CLEARING ORGANIZATION.—

(A) * * *

* * * * * * *

⟦(16)⟧ *(17)* ELECTRONIC TRADING FACILITY.—The term "electronic trading facility" means a trading facility that—

(A) * * *

* * * * * * *

⟦(17)⟧ *(18)* ELIGIBLE COMMERCIAL ENTITY.—The term "eligible commercial entity" means, with respect to an agreement, contract or transaction in a commodity—

(A) an eligible contract participant described in clause (i), (ii), (v), (vii), (viii), or (ix) of paragraph ⟦(18)(A)⟧ *(19)(A)* that, in connection with its business—

(i) * * *

* * * * * * *

⟦(18)⟧ *(19)* ELIGIBLE CONTRACT PARTICIPANT.—The term "eligible contract participant" means—

(A) * * *

(i) * * *

* * * * * * *

(vii)(I) a governmental entity (including the United States, a State, or a foreign government) or political subdivision of a governmental entity;

(II) a multinational or supranational government entity; or

(III) an instrumentality, agency, or department of an entity described in subclause (I) or (II);

except that such term does not include an entity, instrumentality, agency, or department referred to in subclause (I) or (III) of this clause unless (aa) the entity, instrumentality, agency, or department is a person described in clause (i), (ii), or (iii) of paragraph ⟦(17)(A)⟧ *(18)(A)*; (bb) the entity, instrumentality, agency, or department owns and invests on a discretionary basis $50,000,000 or more in investments; or (cc) the agreement, contract, or transaction is offered by, and entered into with, an entity that is listed in any of subclauses (I) through (VI) of section 2(c)(2)(B)(ii);

* * * * * * *

⟦(19)⟧ *(20)* EXCLUDED COMMODITY.—The term "excluded commodity" means—

(i) * * *

* * * * * * *

⟦(20)⟧ *(21)* EXEMPT COMMODITY.—The term "exempt commodity" means a commodity that is not an excluded commodity or an agricultural commodity.

⟦(21)⟧ *(22)* FINANCIAL INSTITUTION.—The term "financial institution" means—

(A) * * *

* * * * * * *

⟦(22)⟧ *(23)* FLOOR BROKER.—

(A) * * *

* * * * * * *

❲(23)❳ *(24)* FLOOR TRADER.—
(A) * * *

* * * * * * *

❲(24)❳ *(25)* FOREIGN EXCHANGE FORWARD.—The term "foreign exchange forward" means a transaction that solely involves the exchange of 2 different currencies on a specific future date at a fixed rate agreed upon on the inception of the contract covering the exchange.

❲(25)❳ *(26)* FOREIGN EXCHANGE SWAP.—The term "foreign exchange swap" means a transaction that solely involves—
(A) * * *

* * * * * * *

❲(26)❳ *(27)* FOREIGN FUTURES AUTHORITY.—The term "foreign futures authority" means any foreign government, or any department, agency, governmental body, or regulatory organization empowered by a foreign government to administer or enforce a law, rule, or regulation as it relates to a futures or options matter, or any department or agency of a political subdivision of a foreign government empowered to administer or enforce a law, rule, or regulation as it relates to a futures or options matter.

❲(27)❳ *(28)* FUTURE DELIVERY.—The term "future delivery" does not include any sale of any cash commodity for deferred shipment or delivery.

❲(28)❳ *(29)* FUTURES COMMISSION MERCHANT.—
(A) * * *

* * * * * * *

❲(29)❳ *(30)* HYBRID INSTRUMENT.—The term "hybrid instrument" means a security having one or more payments indexed to the value, level, or rate of, or providing for the delivery of, one or more commodities.

❲(30)❳ *(31)* INTERSTATE COMMERCE.—The term "interstate commerce" means commerce—
(A) * * *

* * * * * * *

❲(31)❳ *(32)* INTRODUCING BROKER.—
(A) * * *

* * * * * * *

❲(32)❳ *(33)* MAJOR SECURITY-BASED SWAP PARTICIPANT.—The term "major security-based swap participant" has the meaning given the term in section 3(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)).

❲(33)❳ *(34)* MAJOR SWAP PARTICIPANT.—
(A) * * *

* * * * * * *

❲(34)❳ *(35)* MEMBER OF A REGISTERED ENTITY; MEMBER OF A DERIVATIVES TRANSACTION EXECUTION FACILITY.—The term "member" means, with respect to a registered entity or derivatives transaction execution facility, an individual, association, partnership, corporation, or trust—

(A) * * *

* * * * * * *

A participant in an alternative trading system that is designated as a contract market pursuant to section 5f is deemed a member of the contract market for purposes of transactions in security futures products through the contract market.

[(35)] *(36)* NARROW-BASED SECURITY INDEX.—

(A) * * *

* * * * * * *

[(36)] *(37)* OPTION.—The term "option" means an agreement, contract, or transaction that is of the character of, or is commonly known to the trade as, an "option", "privilege", "indemnity", "bid", "offer", "put", "call", "advance guaranty", or "decline guaranty".

[(37)] *(38)* ORGANIZED EXCHANGE.—The term "organized exchange" means a trading facility that—

(A) * * *

* * * * * * *

[(38)] *(39)* PERSON.—The term "person" imports the plural or singular, and includes individuals, associations, partnerships, corporations, and trusts.

[(39)] *(40)* PRUDENTIAL REGULATOR.—The term "prudential regulator" means—

(A) * * *

* * * * * * *

[(40)] *(41)* REGISTERED ENTITY.—The term "registered entity" means—

(A) * * *

* * * * * * *

[(41)] *(42)* SECURITY.—The term "security" means a security as defined in section 2(a)(1) of the Securities Act of 1933 (15 U.S.C. 77b(a)(1)) or section 3(a)(10) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(10)).

[(42)] *(43)* SECURITY-BASED SWAP.—The term "security-based swap" has the meaning given the term in section 3(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)).

[(43)] *(44)* SECURITY-BASED SWAP DEALER.—The term "security-based swap dealer" has the meaning given the term in section 3(a) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)).

[(44)] *(45)* SECURITY FUTURE.—The term "security future" means a contract of sale for future delivery of a single security or of a narrow-based security index, including any interest therein or based on the value thereof, except an exempted security under section 3(a)(12) of the Securities Exchange Act of 1934 as in effect on the date of the enactment of the Futures Trading Act of 1982 (other than any municipal security as defined in section 3(a)(29) of the Securities Exchange Act of 1934 as in effect on the date of the enactment of the Futures Trading Act of 1982). The term "security future" does not include any agreement, contract, or transaction excluded from this Act under section 2(c), 2(d), 2(f), or 2(g) of this Act (as in effect on the date of the enactment of the Commodity Futures Modernization Act of 2000) or title IV of the Commodity Futures Modernization Act of 2000.

[(45)] *(46)* SECURITY FUTURES PRODUCT.—The term "security futures product" means a security future or any put, call, straddle, option, or privilege on any security future.

[(46)] *(47)* SIGNIFICANT PRICE DISCOVERY CONTRACT.—The term "significant price discovery contract" means an agreement, contract, or transaction subject to section 2(h)(5).

[(47)] *(48)* SWAP.—

(A) IN GENERAL.—Except as provided in subparagraph (B), the term "swap" means any agreement, contract, or transaction—

(i) * * *

* * * * * * *

(iii) that provides on an executory basis for the exchange, on a fixed or contingent basis, of 1 or more payments based on the value or level of 1 or more interest or other rates, currencies, commodities, securities, instruments of indebtedness, indices, quantitative measures, or other financial or economic interests or property of any kind, or any interest therein or based on the value thereof, and that transfers, as between the parties to the transaction, in whole or in part, the financial risk associated with a future change in any such value or level without also conveying a current or future direct or indirect ownership interest in an asset (including any enterprise or investment pool) or liability that incorporates the financial risk so transferred, including any agreement, contract, or transaction commonly known as—

(I) * * *

* * * * * * *

(XXI) an emissions swap; [and]

(XXII) a commodity swap; *and*

*(XXIII) a utility operations-related swap;*

* * * * * * *

(B) EXCLUSIONS.—The term "swap" does not include—

(i) * * *

[(ii) any sale of a nonfinancial commodity or security for deferred shipment or delivery, so long as the transaction is intended to be physically settled;]

*(ii) any purchase or sale of a nonfinancial commodity or security for deferred shipment or delivery, so long as the transaction is intended to be physically settled, including any stand-alone or embedded option for which—*

*(I) exercise results in a physical delivery obligation;*

*(II) cannot be severed or marketed separately from the overall transaction for the purpose of financial settlement; and*

*(III) both parties are commercial market participants.*

* * * * * * *

[(48)] *(49)* SWAP DATA REPOSITORY.—The term "swap data repository" means any person that collects and maintains information or records with respect to transactions or positions in, or the terms and conditions of, swaps entered into by third parties for the purpose of providing a centralized recordkeeping facility for swaps.

[(49)] *(50)* SWAP DEALER.—

(A) * * *

* * * * * * *

[(D) DE MINIMIS EXCEPTION.—The Commission ]

*(D) DE MINIMIS EXCEPTION.—*

*(i) IN GENERAL.—The Commission* shall exempt from designation as a swap dealer an entity that engages in a de minimis quantity of swap dealing in connection with transactions with or on behalf of its customers. The Commission shall promulgate regulations to establish factors with respect to the making of this determination to exempt.

*(ii) The de minimis quantity of swap dealing as described in clause (i) that is currently set at a quantity of $8,000,000,000 shall only be amended or reduced through a new affirmative action of the Commission undertaken by rule or regulation.*

*(E) CERTAIN TRANSACTIONS WITH A UTILITY SPECIAL ENTITY.—*

*(i) Transactions in utility operations-related swaps shall be reported pursuant to section 4r.*

*(ii) In making a determination to exempt pursuant to subparagraph (D), the Commission shall treat a utility operations-related swap entered into with a utility special entity, as defined in section 4s(h)(2)(D), as if it were entered into with an entity that is not a special entity, as defined in section 4s(h)(2)(C).*

[(50)] *(51)* SWAP EXECUTION FACILITY.—The term "swap execution facility" means a trading system or platform in which multiple participants have the ability to execute or trade swaps by accepting bids and offers made by multiple participants in the facility or system, through any means of interstate commerce, including any trading facility, that—

(A) * * *

* * * * * * *

[(51)] *(52)* TRADING FACILITY.—

(A) * * *

* * * * * * *

*(52) UTILITY OPERATIONS-RELATED SWAP.—The term "utility operations-related swap" means a swap that—*

*(A) is entered into to hedge or mitigate a commercial risk;*

*(B) is not a contract, agreement, or transaction based on, derived on, or referencing—*

*(i) an interest rate, credit, equity, or currency asset class; or*

*(ii) a metal, agricultural commodity, or crude oil or gasoline commodity of any grade, except as used as fuel for electric energy generation; and*

*(C) is associated with—*

*(i) the generation, production, purchase, or sale of natural gas or electric energy, the supply of natural gas or electric energy to a utility, or the delivery of natural gas or electric energy service to utility customers;*

*(ii) all fuel supply for the facilities or operations of a utility;*

*(iii) compliance with an electric system reliability obligation;*

*(iv) compliance with an energy, energy efficiency, conservation, or renewable energy or environmental statute, regulation, or government order applicable to a utility; or*

*(v) any other electric energy or natural gas swap to which a utility is a party.*

* * * * * * *

**SEC. 2. JURISDICTION OF COMMISSION; LIABILITY OF PRINCIPAL FOR ACT OF AGENT; COMMODITY FUTURES TRADING COMMISSION; TRANSACTION IN INTERSTATE COMMERCE.**

(a) JURISDICTION OF COMMISSION; COMMODITY FUTURES TRADING COMMISSION.—

(1) * * *

* * * * * * *

(6)(A) Except as otherwise provided in this paragraph and in paragraphs ⟦(4) and (5)⟧ *(4), (5), and (17)* of this subsection, the executive and administrative functions of the Commission, including functions of the Commission with respect to the appointment and supervision of personnel employed under the Commission, the distribution of business among such personnel and among administrative units of the Commission, and the use and expenditure of funds, according to budget categories, plans, programs, and priorities established and approved by the Commission, shall be exercised solely by the Chairman.

* * * * * * *

(C) The appointment by the Chairman of the heads of major administrative units under the Commission shall be subject to the approval of the Commission*, and the heads of the units shall serve at the pleasure of the Commission, report directly to the Commission, and perform such functions and duties as the Commission may prescribe*.

* * * * * * *

⟦(12) The⟧

*(12) RULES AND REGULATIONS.—*

*(A) IN GENERAL.—Subject to the other provisions of this paragraph, the* Commission is authorized to promulgate such rules and regulations as it deems necessary to govern the operating procedures and conduct of the business of the Commission.

*(B) NOTICE TO COMMISSION.—*

*(i) GENERAL RULE.—A division or office of the Commission may not issue an interpretive rule of general applicability, a statement of general policy, a response to a formal, written request or petition from any member of the public for guidance, or an exemptive, a no-action, or an interpretive letter, unless, at least 7 calendar days before the issuance, the division or office has provided the Commission with a copy of the matter to be issued.*

*(ii) OPPORTUNITY FOR MEETING REQUIRED.—After receiving a copy of the matter provided in accordance with clause (i), any member of the Commission may request that the Commission hold a meeting to review the matter, and the Chairman shall immediately put any such request for a meeting before the Commission, and if the Commission decides to hold the meeting by a majority vote, the matter may not be issued until the Commission has concluded the meeting.*

*(iii) LIMITATIONS ON APPLICABILITY.—By a majority vote, the Commission may waive the 7-day prior notice requirement of clause (i) when the Commission finds that requiring such a notice would be impracticable, unnecessary, or contrary to the public interest.*

*(C) INTERNAL RISK CONTROLS.—The Commission staff and the Chief Economist shall develop comprehensive internal risk control mechanisms to safeguard and govern the storage of all market data by the Commission, all market data sharing agreements of the Commission, and all academic research performed at the Commission using market data.*

*(E) REQUIREMENT TO PUBLISH IMPLEMENTATION PLAN FOR COMMISSION RULES.—The Commission shall direct its staff to develop and publish in any proposed rule a plan for—*

*(i) when and for how long the proposed rule will be subject to public comment; and*

*(ii) by when compliance with the final rule will be required.*

* * * * * * *

*(F) APPLICABILITY OF NOTICE AND COMMENT RULES TO GUIDANCE VOTED ON BY THE COMMISSION.—The notice and comment requirements of chapter 5 of title 5, United States Code, shall also apply with respect to any guidance issued by the Commission after being voted on by the Commission.*

(13) PUBLIC AVAILABILITY OF SWAP TRANSACTION DATA.—

(A) * * *

* * * * * * *

(C) GENERAL RULE.—[The Commission] *Except as provided in subparagraph (D), the Commission* is authorized and required to provide by rule for the public availability of swap transaction and pricing data as follows:

(i) * * *

* * * * * * *

*(D) REQUIREMENTS FOR SWAP TRANSACTIONS IN ILLIQUID MARKETS.—Notwithstanding subparagraph (C):*

*(i) The Commission shall provide by rule for the public reporting of swap transactions, including price and volume data, in illiquid markets that are not cleared and entered into by a non-financial entity that is hedging or mitigating commercial risk in accordance with subsection (h)(7)(A).*

*(ii) The Commission shall ensure that the swap transaction information referred to in clause (i) of this subparagraph is available to the public no sooner than 30 days after the swap transaction has been executed or at such later date as the Commission determines appropriate to protect the identity of participants and positions in illiquid markets and to prevent the elimination or reduction of market liquidity.*

*(iii) In this subparagraph, the term "illiquid markets" means any market in which the volume and frequency of trading in swaps is at such a level as to allow identification of individual market participants.*

[(D)] *(E)* REGISTERED ENTITIES AND PUBLIC REPORTING.—The Commission may require registered entities to publicly disseminate the swap transaction and pricing data required to be reported under this paragraph.

[(E)] *(F)* RULEMAKING REQUIRED.—With respect to the rule providing for the public availability of transaction and pricing data for swaps described in clauses (i) and (ii) of subparagraph (C), the rule promulgated by the Commission shall contain provisions—

(i) * * *

* * * * * * *

[(F)] *(G)* TIMELINESS OF REPORTING.—Parties to a swap (including agents of the parties to a swap) shall be responsible for reporting swap transaction information to the appropriate registered entity in a timely manner as may be prescribed by the Commission.

[(G)] *(H)* REPORTING OF SWAPS TO REGISTERED SWAP DATA REPOSITORIES.—Each swap (whether cleared or uncleared) shall be reported to a registered swap data repository.

* * * * * * *

*(17) OFFICE OF THE CHIEF ECONOMIST.—*

*(A) ESTABLISHMENT.—There is established in the Commission the Office of the Chief Economist.*

*(B) HEAD.—The Office of the Chief Economist shall be headed by the Chief Economist, who shall be appointed by the Commission and serve at the pleasure of the Commission.*

*(C) FUNCTIONS.—The Chief Economist shall report directly to the Commission and perform such functions and duties as the Commission may prescribe.*

*(D) PROFESSIONAL STAFF.—The Commission shall appoint such other economists as may be necessary to assist the Chief Economist in performing such economic analysis, regulatory cost-benefit analysis, or research the Commission may direct.*

*(18) STRATEGIC TECHNOLOGY PLAN.—*

*(A) IN GENERAL.—Every 5 years, the Commission shall develop and submit to the Committee on Agriculture of the House of Representatives and the Committee on Agriculture, Nutrition, and Forestry of the Senate a detailed plan focused on the acquisition and use of technology by the Commission.*

*(B) CONTENTS.—The plan shall—*

*(i) include for each related division or office a detailed technology strategy focused exclusively on market surveillance and risk detection, market data collection, aggregation, interpretation, standardization, harmonization, streamlining, and internal management and protection of data collected by the Commission, including a detailed accounting of how the funds provided for technology will be used and the priorities that will apply in the use of the funds; and*

*(ii) set forth annual goals to be accomplished and annual budgets needed to accomplish the goals.*

* * * * * * *

(h) CLEARING REQUIREMENT.—

(1) * * *

* * * * * * *

(7) EXCEPTIONS.—

(A) * * *

* * * * * * *

(C) FINANCIAL ENTITY DEFINITION.—

(i) * * *

* * * * * * *

[(iii) LIMITATION.—Such definition shall not include an entity whose primary business is providing financing, and uses derivatives for the purpose of hedging underlying commercial risks related to interest rate and foreign currency exposures, 90 percent or more of which arise from financing that facilitates the purchase or lease of products, 90 percent or more of which are manufactured by the parent company or another subsidiary of the parent company.]

*(iii) LIMITATION.—Such definition shall not include an entity—*

*(I) whose primary business is providing financing, and who uses derivatives for the purpose of hedging underlying commercial risks related to interest rate and foreign currency exposures, 90 percent or more of which arise from financing that facilitates the purchase or lease of products, 90 percent or more of which are manufactured by the parent company or another subsidiary of the parent company; or*

*(II) who is not supervised by a prudential regulator, and is not described in any of subclauses (I) through (VII) of clause (i), and—*

*(aa) is a commercial market participant and is considered a financial entity under clause (i)(VIII) because the entity predominantly engages in physical delivery contracts; or*

*(bb) enters into swaps, contracts for future delivery, and other derivatives on behalf of, or to hedge or mitigate the commercial risk of, whether directly or in the aggregate, affiliates that are not so supervised or described.*

(D) TREATMENT OF AFFILIATES.—

⟦(i) IN GENERAL.—An affiliate of a person that qualifies for an exception under subparagraph (A) (including affiliate entities predominantly engaged in providing financing for the purchase of the merchandise or manufactured goods of the person) may qualify for the exception only if the affiliate, acting on behalf of the person and as an agent, uses the swap to hedge or mitigate the commercial risk of the person or other affiliate of the person that is not a financial entity.⟧

*(i) IN GENERAL.—An affiliate of a person that qualifies for an exception under subparagraph (A) (including affiliate entities predominantly engaged in providing financing for the purchase of the merchandise or manufactured goods of the person) may qualify for the exception only if the affiliate enters into the swap to hedge or mitigate the commercial risk of the person or other affiliate of the person that is not a financial entity, provided that if the transfer of commercial risk is addressed by entering into a swap with a swap dealer or major swap participant, a credit support measure or other mechanism is utilized.*

* * * * * * *

SEC. 4. (a) * * *

* * * * * * *

(c)(1) In order to promote responsible economic or financial innovation and fair competition, the Commission by rule, regulation, or order, after notice and opportunity for hearing, may (on its own initiative or on application of any person, including any board of trade designated or registered as a contract market or derivatives transaction execution facility for transactions for future delivery in any commodity under section 5 of this Act) exempt any agreement, contract, or transaction (or class thereof) that is otherwise subject to subsection (a) (including any person or class of persons offering, entering into, rendering advice or rendering other services with respect to, the agreement, contract, or transaction), either unconditionally or on stated terms or conditions or for stated periods and either retroactively or prospectively, or both, from any of the requirements of subsection (a), or from any other provision of this Act (except subparagraphs (C)(ii) and (D) of section 2(a)(1), except that—

(A) unless the Commission is expressly authorized by any provision described in this subparagraph to grant exemptions, *or except as necessary to effectuate section 361 of the Customer Protection and End User Relief Act,* with respect to amendments made by subtitle A of the Wall Street Transparency and Accountability Act of 2010—

(i) with respect to—

(I) paragraphs (2), (3), (4), (5), and [(7), paragraph (18)(A)(vii)(III), paragraphs (23), (24), (31), (32), (38), (39), (41), (42), (46), (47), (48), and (49)] *(8), paragraph (19)(A)(vii)(III), paragraphs (24), (25), (32), (33), (39), (40), (42), (43), (47), (48), (49), and (50)* of section 1a, and sections 2(a)(13), 2(c)(1)(D), 4a(a), 4a(b), 4d(c), 4d(d), 4r, 4s, 5b(a), 5b(b), 5(d), 5(g), 5(h), 5b(c), 5b(i), 8e, and 21; and

* * * * * * *

SEC. 4a. (a) * * *

* * * * * * *

(c)(1) No rule, regulation, or order issued under subsection (a) of this section shall apply to transactions or positions which are shown to be bona fide hedging transactions or positions, as such terms shall be defined by the Commission by rule, regulation, or order consistent with the purposes of this Act. Such terms [may] *shall* be defined to permit producers, purchasers, sellers, middlemen, and users of a commodity or a product derived therefrom to hedge their legitimate anticipated business needs for that period of time into the [future for which] *future, to be determined by the Commission, for which either an appropriate swap is available or* an appropriate futures contract is open and available on an exchange. To determine the adequacy of this Act and the powers of the Commission acting thereunder to prevent unwarranted price pressures by large hedgers, the Commission shall monitor and analyze the trading activities of the largest hedgers, as determined by the Commission, operating in the cattle, hog, or pork belly markets and shall report its findings and recommendations to the Senate Committee on Agriculture, Nutrition, and Forestry and the House Committee on Agriculture in its annual reports for at least two years following the date of enactment of the Futures Trading Act of 1982.

(2) For the purposes of implementation of [subsection (a)(2) for contracts of sale for future delivery or options on the contracts or commodities, the Commission shall define what constitutes a bona fide hedging transaction or position as] *paragraphs (2) and (5) of subsection (a) for swaps, contracts of sale for future delivery, or options on the contracts or commodities, a bona fide hedging transaction or position is* a transaction or position that—

(A)(i) * * *

(ii) is economically appropriate to the reduction [of risks] *or management of current or anticipated risks* in the conduct and management of a commercial enterprise; and

* * * * * * *

*(3) The Commission may further define, by rule or regulation, what constitutes a bona fide hedging transaction, provided that the rule or regulation is consistent with the requirements of subparagraphs (A) and (B) of paragraph (2).*

* * * * * * *

SEC. 4d. (a) *(1)* It shall be unlawful for any person to be a futures commission merchant unless—

【(1)】 *(A)* such person shall have registered, under this Act, with the Commission as such futures commission merchant and such registration shall not have expired nor been suspended nor revoked; and

【(2)】 *(B)* such person shall, whether a member or nonmember of a contract market or derivatives transaction execution facility, treat and deal with all money, securities, and property received by such person to margin, guarantee, or secure the trades or contracts of any customer of such person, or accruing to such customer as the result of such trades or contracts, as belonging to such customer. Such money, securities, and property shall be separately accounted for and shall not be commingled with the funds of such commission merchant or be used to margin or guarantee the trades or contracts, or to secure or extend the credit, of any customer or person other than the one for whom the same are held: *Provided, however,* That such money, securities, and property of the customers of such futures commission merchant may, for convenience, be commingled and deposited in the same account or accounts with any bank or trust company or with the clearing house organization of such contract market or derivatives transaction execution facility, and that such share thereof as in the normal course of business shall be necessary to margin, guarantee, secure, transfer, adjust, or settle the contracts or trades of such customers, or resulting market positions, with the clearing-house organization of such contract market or derivatives transaction execution facility or with any member of such contract market or derivatives transaction execution facility, may be withdrawn and applied to such purposes, including the payment of commissions, brokerage, interest, taxes, storage, and other charges, lawfully accruing in connection with such contracts and trades: *Provided further,* That in accordance with such terms and conditions as the Commission may prescribe by rule, regulation, or order, such money, securities, and property of the customers of such futures commission merchant may be commingled and deposited as provided in this section with any other money, securities, and property received by such futures commission merchant and required by the Commission to be separately accounted for and treated and dealt with as belonging to the customers of such futures commission merchant: *Provided further,* That such money may be invested in obligations of the United States, in general obligations of any State or of any political subdivision thereof, and in obligations fully guaranteed as to principal and interest by the United States, such investments to be made in accordance with such rules and regulations and subject to such conditions as the Commission may prescribe.

*(2) Any rules or regulations requiring a futures commission merchant to maintain a residual interest in accounts held for the benefit of customers in amounts at least sufficient to exceed*

*the sum of all uncollected margin deficits of such customers shall provide that a futures commission merchant shall meet its residual interest requirement as of the end of each business day calculated as of the close of business on the previous business day.*

* * * * * * *

(h) [Notwithstanding subsection (a)(2)] *Notwithstanding subsection (a)(1)(B)* or the rules and regulations thereunder, and pursuant to an exemption granted by the Commission under section 4(c) of this Act or pursuant to a rule or regulation, a futures commission merchant that is registered pursuant to section 4f(a)(1) of this Act and also registered as a broker or dealer pursuant to section 15(b)(1) of the Securities Exchange Act of 1934 may, pursuant to a portfolio margining program approved by the Securities and Exchange Commission pursuant to section 19(b) of the Securities Exchange Act of 1934, hold in a portfolio margining account carried as a securities account subject to section 15(c)(3) of the Securities Exchange Act of 1934 and the rules and regulations thereunder, a contract for the purchase or sale of a commodity for future delivery or an option on such a contract, and any money, securities or other property received from a customer to margin, guarantee or secure such a contract, or accruing to a customer as the result of such a contract. The Commission shall consult with the Securities and Exchange Commission to adopt rules to ensure that such transactions and accounts are subject to comparable requirements to the extent practical for similar products.

* * * * * * *

**SEC. 4q. SPECIAL PROCEDURES TO ENCOURAGE AND FACILITATE BONA FIDE HEDGING BY AGRICULTURAL PRODUCERS.**

(a) AUTHORITY.—The Commission shall consider issuing rules or orders which—

(1) prescribe procedures under which each contract market is to provide for orderly delivery, including temporary storage costs, of any agricultural commodity enumerated in section [1a(9)] *1a(10)* which is the subject of a contract for purchase or sale for future delivery;

* * * * * * *

**SEC. 4s. REGISTRATION AND REGULATION OF SWAP DEALERS AND MAJOR SWAP PARTICIPANTS.**

(a) * * *

* * * * * * *

(e) CAPITAL AND MARGIN REQUIREMENTS.—

(1) * * *

(2) RULES.—

(A) * * *

(B) SWAP DEALERS AND MAJOR SWAP PARTICIPANTS THAT ARE NOT BANKS.—The Commission*, in consultation with the prudential regulators and the Securities and Exchange Commission,* shall adopt rules for swap dealers and major swap participants, with respect to their activities as a swap dealer or major swap participant, for which there is not a prudential regulator imposing—

(i) * * *

* * * * * * *

(3) STANDARDS FOR CAPITAL AND MARGIN.—

(A) * * *

* * * * * * *

(D) COMPARABILITY OF CAPITAL AND MARGIN REQUIREMENTS.—

(i) * * *

(ii) COMPARABILITY.—The entities described in clause (i) [shall, to the maximum extent practicable,] *shall* establish and maintain comparable minimum capital requirements and minimum initial and variation margin requirements, including the use of non cash collateral, for—

(I) * * *

* * * * * * *

*(iii) FINANCIAL MODELS.—To the extent that swap dealers and major swap participants that are banks are permitted to use financial models approved by the prudential regulators or the Securities and Exchange Commission to calculate minimum capital requirements and minimum initial and variation margin requirements, including the use of non-cash collateral, the Commission shall, in consultation with the prudential regulators and the Securities and Exchange Commission, permit the use of comparable financial models by swap dealers and major swap participants that are not banks.*

*(4) APPLICABILITY WITH RESPECT TO COUNTERPARTIES.—The requirements of paragraphs (2)(A)(ii) and (2)(B)(ii), including the initial and variation margin requirements imposed by rules adopted pursuant to paragraphs (2)(A)(ii) and (2)(B)(ii), shall not apply to a swap in which a counterparty qualifies for an exception under section 2(h)(7)(A), or an exemption issued under section 4(c)(1) from the requirements of section 2(h)(1)(A) for cooperative entities as defined in such exemption, or satisfies the criteria in section 2(h)(7)(D).*

(f) REPORTING AND RECORDKEEPING.—

(1) IN GENERAL.—Each registered swap dealer and major swap participant—

(A) * * *

* * * * * * *

(D) shall keep any such books and records relating to swaps defined in section [1a(47)(A)(v)] *1a(48)(A)(v)* open to inspection and examination by the Securities and Exchange Commission.

* * * * * * *

(h) BUSINESS CONDUCT STANDARDS.—

(1) * * *

(2) RESPONSIBILITIES WITH RESPECT TO SPECIAL ENTITIES.—

(A) * * *

* * * * * * *

*(D) UTILITY SPECIAL ENTITY.—For purposes of this Act, the term "utility special entity" means a special entity, or any instrumentality, department, or corporation of or established by a State or political subdivision of a State, that—*

*(i) owns or operates an electric or natural gas facility or an electric or natural gas operation;*

*(ii) supplies natural gas and or electric energy to another utility special entity;*

*(iii) has public service obligations under Federal, State, or local law or regulation to deliver electric energy or natural gas service to customers; or*

*(iv) is a Federal power marketing agency, as defined in section 3 of the Federal Power Act.*

* * * * * * *

(5) SPECIAL REQUIREMENTS FOR SWAP DEALERS AS COUNTERPARTIES TO SPECIAL ENTITIES.—

(A) Any swap dealer or major swap participant that offers to enter or enters into a swap with a Special Entity shall—

(i) comply with any duty established by the Commission for a swap dealer or major swap participant, with respect to a counterparty that is an eligible contract participant within the meaning of subclause (I) or (II) of clause (vii) of section ⟦1a(18)⟧ *1a(19)* of this Act, that requires the swap dealer or major swap participant to have a reasonable basis to believe that the counterparty that is a Special Entity has an independent representative that—

(I) * * *

* * * * * * *

**SEC. 4t. LARGE SWAP TRADER REPORTING.**

(a) * * *

(b) REQUIREMENTS.—

(1) IN GENERAL.—Books and records described in subsection (a)(2)(B) shall—

(A) * * *

* * * * * * *

(C) be open at all times to inspection and examination by the Securities and Exchange Commission, to the extent such books and records relate to transactions in swaps (as that term is defined in section ⟦1a(47)(A)(v)⟧ *1a(48)(A)(v)*), and consistent with the confidentiality and disclosure requirements of section 8.

* * * * * * *

***SEC. 4u. RECORDKEEPING REQUIREMENTS APPLICABLE TO NON-REGISTERED MEMBERS OF CERTAIN REGISTERED ENTITIES.***

*Except as provided in section 4(a)(3), a member of a designated contract market or a swap execution facility that is not registered with the Commission and not required to be registered with the Commission in any capacity shall satisfy the recordkeeping requirements of this Act and any recordkeeping rule, order, or regulation under this Act by maintaining a written record of each transaction* *in a contract for future delivery, option on a future, swap, swaption, trade option, or related cash or forward transaction. The written record shall be sufficient if it includes the final agreement between the parties and the material economic terms of the transaction and is identifiable and searchable by transaction.*

**SEC. 5. DESIGNATION OF BOARDS OF TRADE AS CONTRACT MARKETS.**

(a) * * *

* * * * * * *

(d) CORE PRINCIPLES FOR CONTRACT MARKETS.—

(1) * * *

* * * * * * *

(23) SECURITIES AND EXCHANGE COMMISSION.—The board of trade shall keep any such records relating to swaps defined in section [1a(47)(A)(v)] *1a(48)(A)(v)* open to inspection and examination by the Securities and Exchange Commission.

(e) CURRENT AGRICULTURAL COMMODITIES.—

(1) Subject to paragraph (2) of this subsection, a contract for purchase or sale for future delivery of an agricultural commodity enumerated in section [1a(9)] *1a(10)* that is available for trade on a contract market, as of the date of the enactment of this subsection, may be traded only on a contract market designated under this section.

* * * * * * *

**SEC. 5b. DERIVATIVES CLEARING ORGANIZATIONS.**

(a) * * *

* * * * * * *

(k) REPORTING REQUIREMENTS.—

(1) * * *

* * * * * * *

(3) REPORTS ON SECURITY-BASED SWAP AGREEMENTS TO BE SHARED WITH THE SECURITIES AND EXCHANGE COMMISSION.—

(A) IN GENERAL.—A derivatives clearing organization that clears security-based swap agreements (as defined in section [1a(47)(A)(v)] *1a(48)(A)(v)*) shall, upon request, open to inspection and examination to the Securities and Exchange Commission all books and records relating to such security-based swap agreements, consistent with the confidentiality and disclosure requirements of section 8.

* * * * * * *

[(5) CONFIDENTIALITY AND INDEMNIFICATION AGREEMENT.—Before the Commission may share information with any entity described in paragraph (4)—

[(A) the Commission shall receive a written agreement from each entity stating that the entity shall abide by the confidentiality requirements described in section 8 relating to the information on swap transactions that is provided; and

[(B) each entity shall agree to indemnify the Commission for any expenses arising from litigation relating to the information provided under section 8.]

*(5) CONFIDENTIALITY AGREEMENT.—Before the Commission may share information with any entity described in paragraph (4), the Commission shall receive a written agreement from each entity stating that the entity shall abide by the confidentiality requirements described in section 8 relating to the information on swap transactions that is provided.*

* * * * * * *

**SEC. 5c. COMMON PROVISIONS APPLICABLE TO REGISTERED ENTITIES.**

(a) * * *

* * * * * * *

(c) NEW CONTRACTS, NEW RULES, AND RULE AMENDMENTS.—

(1) * * *

* * * * * * *

(4) PRIOR APPROVAL.—

(A) * * *

(B) PRIOR APPROVAL REQUIRED.—Notwithstanding any other provision of this section, a designated contract market shall submit to the Commission for prior approval each rule amendment that materially changes the terms and conditions, as determined by the Commission, in any contract of sale for future delivery of a commodity specifically enumerated in section ⟦1a(10)⟧ *1a(11)* (or any option thereon) traded through its facilities if the rule amendment applies to contracts and delivery months which have already been listed for trading and have open interest.

* * * * * * *

**SEC. 5h. SWAP EXECUTION FACILITIES.**

(a) * * *

* * * * * * *

(f) CORE PRINCIPLES FOR SWAP EXECUTION FACILITIES.—

(1) * * *

* * * * * * *

(10) RECORDKEEPING AND REPORTING.—

(A) IN GENERAL.—A swap execution facility shall—

(i) * * *

* * * * * * *

(iii) shall keep any such records relating to swaps defined in section ⟦1a(47)(A)(v)⟧ *1a(48)(A)(v)* open to inspection and examination by the Securities and Exchange Commission."

* * * * * * *

SEC. 6. (a) * * *

* * * * * * *

(c) PROHIBITION REGARDING MANIPULATION AND FALSE INFORMATION.—

(1) * * *

* * * * * * *

⟦(5) SUBPOENA.—For⟧

*(5) SUBPOENA.—*

*(A) IN GENERAL.—For* the purpose of securing effective enforcement of the provisions of this Act, for the purpose of any investigation or proceeding under this Act, and for the purpose of any action taken under section 12(f), any member of the Commission or any Administrative Law Judge or other officer designated by the Commission (except as provided in paragraph (7)) may administer oaths and affirmations, subpoena witnesses, compel their attendance, take evidence, and require the production of any books, papers, correspondence, memoranda, or other records that the Commission deems relevant or material to the inquiry.

*(B) CONTENT OF SUBPOENA ORDER.—An order of the Commission authorizing the issuance of a subpoena—*

*(i) shall state in good faith the purpose of the investigation;*

*(ii) shall require only the provision of information reasonably relevant to that purpose; and*

*(iii) shall not be for an indefinite duration.*

*(C) RENEWAL.—An order issued under this paragraph may be renewed only by Commission action.*

* * * * * * *

SEC. 12. (a) * * *

* * * * * * *

(d) There are authorized to be appropriated such sums as are necessary to carry out this Act for each of the fiscal years 2008 through ⟦2013⟧ *2018*.

* * * * * * *

**SEC. 15. CONSIDERATION OF COSTS AND BENEFITS AND ANTITRUST LAWS.**

(a) COSTS AND BENEFITS.—

⟦(1) IN GENERAL.—Before promulgating a regulation under this Act or issuing an order (except as provided in paragraph (3)), the Commission shall consider the costs and benefits of the action of the Commission.

⟦(2) CONSIDERATIONS.—The costs and benefits of the proposed Commission action shall be evaluated in light of—

⟦(A) considerations of protection of market participants and the public;

⟦(B) considerations of the efficiency, competitiveness, and financial integrity of futures markets;

⟦(C) considerations of price discovery;

⟦(D) considerations of sound risk management practices; and

⟦(E) other public interest considerations.⟧

*(1) IN GENERAL.—Before promulgating a regulation under this Act or issuing an order (except as provided in paragraph (3)), the Commission, through the Office of the Chief Economist, shall assess and publish in the regulation or order the costs and benefits, both qualitative and quantitative, of the proposed regulation or order, and the proposed regulation or order shall state its statutory justification.*

*(2) CONSIDERATIONS.—In making a reasoned determination of the costs and the benefits, the Commission shall evaluate—*

*(A) considerations of protection of market participants and the public;*

*(B) considerations of the efficiency, competitiveness, and financial integrity of futures and swaps markets;*

*(C) considerations of the impact on market liquidity in the futures and swaps markets;*

*(D) considerations of price discovery;*

*(E) considerations of sound risk management practices;*

*(F) available alternatives to direct regulation;*

*(G) the degree and nature of the risks posed by various activities within the scope of its jurisdiction;*

*(H) the costs of complying with the proposed regulation or order by all regulated entities, including a methodology for quantifying the costs (recognizing that some costs are difficult to quantify);*

*(I) whether the proposed regulation or order is inconsistent, incompatible, or duplicative of other Federal regulations or orders;*

*(J) whether, in choosing among alternative regulatory approaches, those approaches maximize net benefits (including potential economic and other benefits, distributive impacts, and equity); and*

*(K) other public interest considerations.*

* * * * * * *

SEC. 17. (a) * * *

* * * * * * *

*(s) A registered futures association shall—*

*(1) require each member of the association that is a futures commission merchant to maintain written policies and procedures regarding the maintenance of—*

*(A) the residual interest of the member, as described in section 1.23 of title 17, Code of Federal Regulations, in any customer segregated funds account of the member, as identified in section 1.20 of such title, and in any foreign futures and foreign options customer secured amount funds account of the member, as identified in section 30.7 of such title; and*

*(B) the residual interest of the member, as described in section 22.2(e)(4) of such title, in any cleared swaps customer collateral account of the member, as identified in section 22.2 of such title; and*

*(2) establish rules to govern the withdrawal, transfer or disbursement by any member of the association, that is a futures commission merchant, of the member's residual interest in customer segregated funds as provided in such section 1.20, in foreign futures and foreign options customer secured amount funds, identified as provided in such section 30.7, and from a cleared swaps customer collateral, identified as provided in such section 22.2.*

*(t) A registered futures association shall require any member of the association that is a futures commission merchant to—*

*(1) use an electronic system or systems to report financial and operational information to the association, including information related to customer segregated funds, foreign futures and foreign options customer secured amount funds accounts, and cleared swaps customer collateral, in accordance with such terms, conditions, documentation standards, and regular time intervals as are established by the association;*

*(2) instruct each depository, including any bank, trust company, derivatives clearing organization, or futures commission merchant, holding customer segregated funds under section 1.20 of title 17, Code of Federal Regulations, foreign futures and foreign options customer secured amount funds under section 30.7 of such title, or cleared swap customer funds under section 22.2 of such title, to report balances in the futures commission merchant's section 1.20 customer segregated funds, section 30.7 foreign futures and foreign options customer secured amount funds, and section 22.2 cleared swap customer funds, to the registered futures association or another party designated by the registered futures association, in the form, manner, and interval prescribed by the registered futures association; and*

*(3) hold section 1.20 customer segregated funds, section 30.7 foreign futures and foreign options customer secured amount funds and section 22.2 cleared swaps customer funds in a depository that reports the balances in these accounts of the futures commission merchant held at the depository to the registered futures association or another party designated by the registered futures association in the form, manner, and interval prescribed by the registered futures association.*

*(u) A futures commission merchant that has adjusted net capital in an amount less than the amount required by regulations established by the Commission or a self-regulatory organization of which the futures commission merchant is a member shall immediately notify the Commission and the self-regulatory organization of this occurrence.*

*(v) A futures commission merchant that does not hold a sufficient amount of funds in segregated accounts for futures customers under section 1.20 of title 17, Code of Federal Regulations, in foreign futures and foreign options secured amount accounts for foreign futures and foreign options secured amount customers under section 30.7 of such title, or in segregated accounts for cleared swap customers under section 22.2 of such title, as required by regulations established by the Commission or a self-regulatory organization of which the futures commission merchant is a member, shall immediately notify the Commission and the self-regulatory organization of this occurrence.*

*(w) Within such time period established by the Commission after the end of each fiscal year, a futures commission merchant shall file with the Commission a report from the chief compliance officer of the futures commission merchant containing an assessment of the internal compliance programs of the futures commission merchant.*

* * * * * * *

SEC. 20. (a) Notwithstanding title 11 of the United States Code, the Commission may provide, with respect to a commodity broker that is a debtor under chapter 7 of title 11 of the United States Code, by rule or regulation—

(1) * * *

* * * * * * *

(4) any persons to which customer property and commodity contracts may be transferred under section 766 of title 11 of the United States Code; [and]

(5) how the net equity of a customer is to be determined[.]*; and*

*(6) that cash, securities, or other property of the estate of a commodity broker, including the trading or operating accounts of the commodities broker and commodities held in inventory by the commodity broker, shall be included in customer property, but only to the extent that the property that is otherwise customer property is insufficient to satisfy the net equity claims of public customers (as such term may be defined by the Commission by rule or regulation) of the commodity broker.*

* * * * * * *

**SEC. 21. SWAP DATA REPOSITORIES.**

(a) * * *

* * * * * * *

[(d) CONFIDENTIALITY AND INDEMNIFICATION AGREEMENT.—Before the swap data repository may share information with any entity described in subsection (c)(7)—

[(1) the swap data repository shall receive a written agreement from each entity stating that the entity shall abide by the confidentiality requirements described in section 8 relating to the information on swap transactions that is provided; and

[(2) each entity shall agree to indemnify the swap data repository and the Commission for any expenses arising from litigation relating to the information provided under section 8.]

*(d) CONFIDENTIALITY AGREEMENT.—Before the swap data repository may share information with any entity described in subsection (c)(7), the swap data repository shall receive a written agreement from each entity stating that the entity shall abide by the confidentiality requirements described in section 8 relating to the information on swap transactions that is provided.*

* * * * * * *

(f) CORE PRINCIPLES APPLICABLE TO SWAP DATA REPOSITORIES.—

(1) * * *

* * * * * * *

(4) ADDITIONAL DUTIES DEVELOPED BY COMMISSION.—

(A) * * *

* * * * * * *

(C) ADDITIONAL DUTIES FOR COMMISSION DESIGNEES.—The Commission shall establish additional duties for any registrant described in section [1a(48)] *1a(49)* in order to minimize conflicts of interest, protect data, ensure compliance, and guarantee the safety and security of the swap data repository.

* * * * * * *

***SEC. 24. JUDICIAL REVIEW OF COMMISSION RULES.***

*(a) A person aggrieved by a final rule of the Commission under this Act may obtain review of the rule in the United States Court of Appeals for the District of Columbia Circuit or the United States Court of Appeals for the circuit where the party resides, by filing in the court, within 60 days after publication in the Federal Register of the entry of the rule, a written petition requesting that the rule be modified or set aside in whole or in part.*

*(b) A copy of the petition shall be transmitted forthwith by the clerk of the court to an officer designated by the Commission for that purpose. Thereupon the Commission shall file in the court the record on which the rule complained of is entered, as provided in section 2112 of title 28, United States Code, and the Federal Rules of Appellate Procedure.*

*(c) On the filing of the petition, the court has jurisdiction, which becomes exclusive on the filing of the record, to affirm or modify and enforce or to set aside the rule in whole or in part.*

*(d) The findings of the Commission as to the facts identified by the Commission as the basis, in whole or in part, of the rule, if supported by substantial evidence, are conclusive. The court shall affirm and enforce the rule unless the Commission's action in promulgating the rule is found to be arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law; contrary to constitutional right, power, privilege, or immunity; in excess of statutory jurisdiction, authority, or limitations, or short of statutory right; or without observance of procedure required by law.*

*(e) If either party applies to the court for leave to adduce additional evidence and shows to the satisfaction of the court that the additional evidence is material and that there was reasonable ground for failure to adduce it before the Commission, the court may remand the case to the Commission for further proceedings, in whatever manner and on whatever conditions the court considers appropriate. If the case is remanded to the Commission, it shall file in the court a supplemental record containing any new evidence, any further or modified findings, and any new order.*

○