UNITED STATES OF AMERICA

COMMODITY FUTURES TRADING COMMISSION

AGRICULTURAL ADVISORY COMMITTEE MEETING

Washington, D.C.

Tuesday, September 22, 2015

PARTICIPANTS:

Moderator:

RANDY FORTENBERY, Chairman, Agricultural Advisory Committee

Introduction and Opening Statements:

TIMOTHY MASSAD, CFTC Chairman

SHARON BOWEN, CFTC Commissioner

J. CHRISTOPHER GIANCARLO, CFTC Commissioner

Ag Market Update:

TIM ANDRIESEN, CME Group

TIM BARRY, ICE Futures U.S.

LAYNE CARLSON, Minneapolis Grain Exchange

FCM - Market Trends:

KEVIN PICCOLI, CFTC, Division of Swap Dealer and Intermediary Oversight (DSIO) Deputy Director

EILEEN FLAHERTY, CFTC, DSIO Director

SAYEE SRINIVASAN, CFTC, Chief Economist

Position Limits:

MARK FAJFAR, CFTC, Office of the General Counsel

JOE HAWRYSZ, CME Group

ERIK HAAS, ICE Futures U.S.

PARTICIPANTS (CONT'D):

Other Participants:

CORY CLAUSSEN, CFTC, Director, Office of Legislative Affairs; AAC, Designated Federal Officer

ED ELFMANN, American Bankers Association

BILL MAY, American Cotton Shippers Association

JOHN ANDERSON, American Farm Bureau Federation

RYAN WESTON, American Sugar Alliance

LANCE KOTSCHWAR, Commodity Markets Council

ROBBIE BOONE, Farm Credit Council

TOM KADLEC, Futures Industry Association

MARK SCANLAN, Independent Community Bankers of America

BRYAN DIERLAM, International Swaps and Derivatives Association, Inc.

PAUL PENNER, National Association of Wheat Growers

JOE KOVANDA, National Cattlemen's Beef Association

LYNN CHRISP, National Corn Growers Association

JOHN OWEN, USA Rice Federation

CHRIS CLARK, North American Millers' Association

PARTICIPANTS (CONT'D):

STEPHEN STRONG, North American Export Grain Association

NEIL DIERKS, National Pork Producers Council

EDWARD GALLAGHER, National Milk Producers Federation

BOB WHITE, National Grange

M. J. ANDERSON, National Grain and Feed Association

ZACK CLARK, National Farmers Union

SCOTT CORDES, National Council of Farmer Cooperatives

RON LEE, National Cotton Council of America

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P R O C E E D I N G S

(11:00 a.m.)

MR. FORTENBERY: Good morning. I'm Randy Fortenbery, the Chairman of the Agricultural Advisory Committee, and it's my pleasure to call this 38th meeting of the Committee to order. Before we go to our first panel I'd like to turn some time over to Chairman Massad and Commissioners Bowen and Giancarlo for a few comments. Mr. Chairman?

MR. MASSAD: Well, thank you, Randy. And thank you all for taking the time to be here today. I really want to just welcome everyone to this meeting of the CFTC Agricultural Advisory Committee. Particularly for those of you who live outside of D.C., I really appreciate you traveling in for this. As you may know our city is already known as one of the worst cities in the nation for gridlock and traffic, and now we are going to welcome Pope Francis so it's very possible that Washington's traffic problems will soon reach biblical proportions, and I wish you all good luck in getting out of town. We'll do our best to end the meeting on time.

I'm very pleased that both Commissioner Bowen and Communication Giancarlo can be here today. We are only three now, but believe me, we're all committed to still carrying out the full Commission workload as best we can.

Before we begin, let me just underscore the importance of the meetings of this Committee and all of our advisory committees. They provide a much-needed opportunity for us to hear directly from those who are participating in these markets and affected by our work, and in addition to these meetings I know all of us have had opportunities to meet with many of you and meet with others in the agricultural industry, agricultural companies and associations. I've given speeches at industry conferences, visited production facilities such as most recently a grain mill in Kansas City. I know Commissioners Bowen and Giancarlo have also, and all of those meetings and interactions provide very valuable insights for us into the issues that you all face. I look forward to doing more of that in the future.

I think we are all keenly aware of the importance that these markets play in the agricultural industry and to your businesses and to many aspects of American life, and I often note that most Americans don't participate in the derivatives markets. They probably seem very esoteric to most Americans, and yet they do profoundly affect our economy and the prices that people pay in their everyday lives for so many goods, obviously including agricultural products but also the cost of heating your home or driving your car. And so, these markets are so critical to many sectors of our economy, including agriculture, [critical] to the ability of companies in those sectors to hedge routine commercial risk.

I want to thank Randy for his service as Committee Chair, for his dedication to that task, for his work in facilitating this meeting and helping to put together the agenda. I want to thank our CFTC staff for all their work in preparing for this meeting, and I want to thank our panelists; those who are making presentations. We're very grateful to you.

Let me just note quickly the topics we're going to cover. I'll just give a couple thoughts of mine on these. Our first session will include presentations related to developments and innovations in the agricultural derivatives markets in particular with respect to certain contracts, and I think that will be very interesting. We'll have presentations from ICE, CME, and the Minneapolis Grain Exchange.

We'll then have a discussion about trends in the futures commission merchant industry and how those trends may affect your ability to participate in the derivatives markets. I think we all know there's been a decline in the number of FCMs. Now, you'll see some data today that I think is very interesting on how that decline has occurred over a number of years going back at least to 2005, and it's likely the result of many factors. At the same time, overall volumes in the industry have increased, and there has been concentration of business among the largest firms, and these are all trends that I am very interested in hearing your thoughts on today.

Let me just say from my point of view it's very important that we have a robust FCM industry. It's very important that all customers including particularly smaller customers can access these markets efficiently and effectively, and so I think we're all interested in hearing your thoughts and suggestions on what's happening in the industry and whether there are issues that this Committee should examine or the staff of the CFTC can examine further.

Finally we'll talk about position limits. In particular, today we're going to talk about two issues in that area. One is the possibility of exchanges granting non-enumerated hedge exemptions. This is an idea that I am certainly open to considering, and we'll hear from the exchanges on how that would work. And this would be -- if we were to go forward with this -- this would be a change to the proposed position limits rules that were issued in 2013.

We will also discuss another proposal to modify those rules, and this one pertains to the aggregation provisions, and I'm pleased to announce that this proposed change will be released for public comment today. All of us on the Commission have supported issuing this for public comment. This proposal aims to make a significant, streamlined change to the process of waiving aggregation requirements.

Under the proposal, instead of requiring a participant to apply for an exemption and wait to receive CFTC approval for an exemption, we would instead rely on a notice filing. So, a participant who owns 50 percent or more of an entity can obtain the exemption by attesting to the Commission that it has no control over the trading of that entity and no access to its information. We have notice filings in other areas as well that work well, and so this notice process would mean it would be the same exemption process whether you own more than 10 percent and less than 50 or even above 50 percent.

The proposed position limit rules that were issued by the Commission two years ago are important and complex, and I know all of you are very interested in these rules. You've expressed concerns about them. All of us currently on the Commission were not here when these rules were proposed, and therefore I think we're all very committed to taking the time to make sure we listen to you, listen to other market participants and consider carefully the implications of these rules. We appreciate very much the input you've given us to date, and we look forward to discussing today's issues.

We understand that it's vitally important that as we finalize these rules we make sure that the rules work, that commercial end-users are able to continue to use these markets efficiently and effectively for risk management and price discovery.

So, I think all of the presentations and the discussion we'll have will give us good information about what's going on in the markets today and will help us better do our job of making sure these markets function with integrity and without fraud or manipulation. And to that end we've been committed to listening to market participants on a whole host of issues and particularly we have taken a number of actions to address end-user concerns since all of us took office. All of us took office now -- what -- about 15 months ago? And our goal has been to make sure we don't create unnecessary burdens on commercial end-users, and so we've finalized a change, for example, to the rule on residual interest. We proposed changes to record keeping. We've made some important adjustments to the rules on trade options and contracts with embedded volume metric optionality. There's a whole host of sort of end-user things that we've done, and we will continue to focus on these concerns.

Let me just note for a minute other

things that are on our agenda for the fall -- and happy during the breaks to discuss these. We are looking at ways to strengthen the security and resilience of our clearinghouses and exchanges with respect to cyber-attacks and technological failures. Obviously that is a subject that is on everyone's minds. We are looking closer at automated trading, and I expect that we will propose some additional rules for consideration there to make sure automated trading does not result in disruptions or unfairness. And we also have on our agenda the proposed rule on margin for uncleared swaps which as you know exempts commercial end-users and that's obviously very important.

So, we have other things on our agenda but let me end it here just in the interests of time, and let me just say again thanks for being here and I look forward to today's session. Let me turn it over to Commissioner Bowen.

MS. BOWEN: Thank you, Mr. Chairman, for holding this meeting today. I commend the

Committee for examining the FCM marketplace, and I look forward to today's discussion about trends in FCMs, and of course position limits again.

Why is today's discussion particularly relevant? As we enter the fall harvest season producers begin to see the fruits of their efforts this year. Financially they see if they met their targets, if their hedges paid off. Farmer's and rancher's access to financing and FCMs is crucial. Effective hedging is key to affordable financing.

Regarding position limits, I look forward to this Commission moving forward on its rule. Earlier this year I was fortunate to visit Kansas City. I spoke with a wide range of farmers, processors and others involved in producing the food that we eat and the plant-based products that we use.

At Garrett and Cara Reikhof's farm in Higginsville, Missouri, Garrett and Cara highlighted significant capital investments necessary to farm, the low profit margins involved, and the unpredictability of income and losses. Without access to cost-effective hedging, financing would be impossible for the Reikhof's to obtain. I was impressed with their commitment to food production and biofuels, and I am committed to making sure that our position limits rule does not make their already difficult job more difficult.

At this point we have probably heard all possible comments on this rule. If we need to do a supplemental proposal to improve the rule, let's just do it. I believe there are ways to move forward on issues such as bona fide hedging to fit within the rules of the existing framework. So, I look forward to working with my colleagues and staff to improve the existing proposal to address such issues, and I hope we can move forward soon. Thank you again for convening today's meeting.

MR. GIANCARLO: Thank you Commissioner Bowen and thank you Chairman Massad for convening today's meeting. I thank you also for your sponsorship of the Agricultural Advisory Committee. It's important that we meet today.

When I was a young corporate lawyer building my practice I made it a policy with each new client to spend time in their offices learning how they made a living, and I've continued doing that in my first year as a commissioner as have my fellow commissioners. I've traveled to Indiana, Kentucky, Illinois, and Minnesota, and I've met with cattle, pork, poultry, corn, soybean, dairy and other ag producers and I've also met with grain elevator operators, cooperatives, and manufactures who serve them.

What I heard most about was the steep drop in commodity prices that is threatening farmers' bottom lines and personal checkbooks. In fact, since the last meeting of this Committee the U.S. Department of Agriculture has issued a report estimating that net farm income will plummet 36 percent by the end of this year against last year reaching its lowest level in 9 years.

Many of the everyday working people I met on Midwest farms and in factories don't know and don't care what Washington does. They just want politicians and bureaucrats to not interfere with their ability to earn a living. I'm very concerned that our current position limit proposals will do just that, so I look forward to a new approach to aggregation of positions under our current position limits proposal, and I support the revised aggregation proposal that the Chairman announced; one that better recognizes the very corporate structures of American farmers, energy producers, manufacturers, and trading institutions that do business around the globe today.

Still there are many other changes that are needed to make the CFTC's approach to position limits less harmful to the risk management activities of businesses facing variable commodity values. We must avoid adopting unworkable rules that prevent our commodity markets from operating effectively at a time of falling commodity prices. That means not displacing the everyday commercial judgment of farmers and business people with a small set of allowable hedging options that have been preselected by a Washington commission with limited experience in commercial risk management.

I also look forward to a discussion of the state of America's futures commission merchants. As I have said, America's FCMs are becoming an endangered species due to government regulations and policies including the fed's decade-long zero-interest-rate program.

FCMs continue to consolidate at an alarming rate, and it is no secret that the remaining FCMs have refused to retain their smaller, less-active clients including many small ag producers. I'd like to know whether the remaining FCMs have stabilized their business models to better serve the clients they have retained, and I'd like to know how smaller farmers and ag producers will be serviced by a reduced FCM industry; an industry that increasingly imposes limits on customer size and capacity. We must not allow Washington regulations to wipe out smaller FCMs and their customers in the same way that Dodd-Frank regulations have wiped out small community banks across America's agriculture landscape.

Let us agree on one thing. American farmers had absolutely nothing to do with the financial crisis; nothing whatsoever. We must think carefully about imposing an inflexible position limits rule set seven years after the crisis when our farmers today are relying on the derivative markets to manage the falling price of the 2015 harvest.

If our position limits rules have the perverse effect as I fear they will of adding liquidity risk to the everyday practice of risk management then the American farmers I met with will be confirmed in their belief that once again Washington politicians are part of the problem, not part of the solution. Thank you very much.

MR. FORTENBERY: Thank you, Chairman Massad and Commissioners Bowen and Giancarlo. So, at this point we'll turn to our first topic of discussion, an update on U.S. ag markets, and this morning we have three presenters: Mr. Tim

Andriesen from the CME Group, Mr. Tim Barry from ICE Futures USA, and Mr. Layne Carlson from the Minneapolis Grain Exchange.

What I'm going to ask the Committee to do is keep track of your questions and/or comments, but let's wait until all three presenters have spoken, and then we'll have a general discussion. Mr. Andriesen?

MR. ANDRIESEN: Sorry about that. Thank you for giving me the opportunity to be here. So I was asked to talk a little bit about changes in terms of our contracts, and I thought the best way to do that is to put that in context of the process that we use when we look at contracts and we look at changes.

Over the last couple of years we have put in place a very specific approach that we've taken -- that we think has served us well. I'll walk you through that, and then we'll talk about some of the specific changes that are in the offing. I find it really nice in having this conversation that there are quite a few people at this table that have been participants in that process and have been involved in some of the recent changes in our contracts.

One of the things we think is important is to take a proactive approach to looking at our contracts. When you have a contract where the underlying delivery process is tied to physical markets, those physical markets change and evolve over time. Most recently, for example, on the livestock side, one of the things we've seen is heavier and heavier animals, so because we have contracts where there are parameters around the weight of the animal and the delivery process, it's important that we're constantly looking at updating those contracts to reflect those sort of things.

In grains... we see different patterns of movement in the grains. We see different issues constantly presenting themselves: freight costs, et cetera. So, one of the things that we have committed to doing on a regular basis is evaluating all of our major contracts. I would say on about a two-to-three-year cycle we look at all of our contracts and whether we think they're operating extremely well or whether we think there's room for improvement. We put them through a process where we really reach out to the industry to get feedback.

The first thing we do in that process is we'll take our economics team. We'll look at the contract, look at changes in the underlying markets and identify what they think might be some of the potential issues with the contract. That's pretty much an internal process.

What we'll then do is put together a focus group of anywhere from 10 to 20 people. The vast majority of those people are physical users of the contract, but we will include financial participants in that marketplace -- or in that group -- as well. We take the issues that we've identified. We schedule roughly two- hour interviews with those firms independently and talk through the issues and get an assessment as to whether they think it's an issue. What do they think we could potentially do? And are there any other issues that we should be looking at that maybe we haven't identified?

Coming out of that, what we'll then do is pull all those people together. Typically, we'll invite them to Chicago and lay out for them what we've heard from the rest of the focus group, and we'll do it in a way that we'll say, "here's an issue -- here's issue A, we have some people who think this should happen, we have some people who think that should happen. Let's discuss that." And we've really found those discussions to be really powerful in that you get people with different views around these issues that then articulate those to us, and we can hear the pros and cons from that group.

Coming out of that, we'll again circle around and say, "did we hear something that we feel is significant enough to address the contract or to change a contract, and if so, what do we think might be a path forward?"

Once we've done that we go into what we

would call a broader request for comment stage where we will put out in the public using organizations or using other sorts of media "Here's some things that we're considering doing." It may or may not take the form of a questionnaire. It just depends on if the question we're asking is something that lends itself well to a questionnaire-type approach or not. That gives us some feedback as to what we really think we should potentially change. It also gives a much wider group the ability to comment. Essentially our goal is that before anything even is submitted to the CFTC as a potential change, it's well, well vetted in the industry so that everybody has an opportunity to opine on whether it makes sense or not.

If through that process we finally get to something that we believe should be changed with the contract, then we'll finally make a proposal and submit it to the CFTC for approval. So, the whole idea of this process is to ensure that first we get deep, local knowledge, deep industry knowledge involved in what potential changes might be made, and then later to make sure that everybody in the industry and beyond has an opportunity to opine on does that make sense or not.

We think it's served us pretty well, and I think that people that have been involved in the process for the most part would say it's one that's been reasonably effective.

So, I was asked to talk about some of the contracts and what their status is right now. We currently have four major contracts that are in that process. We've recently completed that process on the lean hog contract. We really didn't see at this time any particular changes that we felt we needed to make.

We are going through that process with the corn futures contract. We have just recently closed a feedback period and a survey. We're assessing the data that we've gotten back, then there are three different areas that we're looking at for potential changes. One is in terms of quality discounts to align them more specifically with the delivery market. Another is to look at freight differentials. The freight differentials on the upper Illinois River have changed, and we're looking at potentially updating those. And the final is whether we should look at potentially extending the delivery territory down the Illinois River to St. Louis.

The feeder cattle contract is another that we're looking at. We just recently put out some comments, and we're looking for feedback on that. In particular we're looking at the weight range on feeder cattle. And then the Kansas City wheat contract is another contract that we've just gone through the process with. We have asked for some additional comments from the industry as a whole around it, though the feedback from the industry in general was that they didn't really anticipate any changes or any need for changes.

So, we continue to do this with all of our products. I would say that the cycle is about a two-to-three-year cycle that should cover almost all of our major contracts, and why I say it's a little bit iffy is we don't want to load up with too many at the same time because in many cases we're tapping into some of the same groups to get feedback from, so it's really about making sure that we come to the right conclusions.

What I didn't point out in here is there are times when we will come up with issues where we say, "This is a really complex issue. We think potentially there is something that needs to be done here." But what we really need to do is get a smaller group to dig into it. So for example the delivery of heifers on the cattle contract was one of those things. We identified it as something we thought was important. It wasn't something that we could quickly make a recommendation for, so we actually worked with the NCBA and with other organizations to get a small group together, and over the course of about a year got to where we had what we thought was a reasonable approach to including them in the delivery process. So, those would be my comments.

MR. FORTENBERY: Thank you, Mr. Andriesen. Mr. Barry from ICE Futures USA.

MR. BARRY: Thank you, Tim. I'd like to thank Chairman Massad and Commissioners Bowen and Giancarlo for the opportunity to address the Committee on ICE's new world cotton futures contract. It's probably the most significant development that we've had at ICE on the agricultural side in quite some time, and it's something that we've been working on with our cotton commercial market customers for nearly two years.

We're nearing our November 2nd launch date. We are expecting to file the contract rules with the CFTC later this week, so the timing of today's meeting is for us quite advantageous, quite good.

ICE and its predecessor exchanges -- the New York Board of Trade and the New York Cotton Exchange -- have been offering price discovery and risk management tools to the cotton trade for over a hundred years, and in fact the first futures contract listed on the New York Exchange was the original cotton contract traded on the New York Cotton Exchange. It was listed just a few years after the first grain contract in Chicago, so our history here goes way back, and our current contract, the No. 2.

Contract remains the global benchmark for cotton world-wide, and it's consistently one of our three most active and heavily-used agricultural futures contracts, but as the quote on the screen and the brief presentation somewhat suggests, over the past decade or so our commercial cotton customers have given us a consistent stream of commentary that the U.S.-only terms of the No. 2 contract -- can, in particular market conditions, create an unwanted disconnect between the contract and world market fundamentals, and that this condition, when it occurs, can diminish the utility of the No. 2 contract and its key reasons for being: price discovery and risk management to the trade.

One indicator of these types of trends

is the - that has led to concerns -- is the change in the share of global cotton production and exports, and the chart -- the slide above uses some USDA data -- and it shows that as recently as 2003-2004 season U.S. cotton accounted for 19 percent of global production. That number in the 2013-2014 season had declined all the way down to 11 percent, and even more dramatically if you look at USDA export data that shows up in the 2003-2004 season where the U.S.-origin cotton accounted for 41 percent of global cotton exports, and as recently as '13- '14 that number had shrunk down to 27 percent.

So, clearly as other origins around the world have increased production and also improved their quality and reliability in serving those around the world, the dominant role that the U.S. once played in global exports has decreased, which brings us to the World Cotton contract, which is intended to address those commercial market concerns head-on.

To be clear, what we're doing with the

World Cotton contract is introducing a new, separate, stand-alone price discovery and risk management tool. We're not amending the terms of the current contract. The new contract will trade alongside the No. 2 contract which the exchange will continue to support and continue to offer, and the World Cotton contract terms themselves are built on the successful and tested terms of the No. 2 contract with differences where needed to better serve the increasingly international global cotton trade.

Some of the similarities are that, like the No. 2, the terms of World Cotton contract will include at expirations, physical delivery and exchange certified licensed warehouses, pricing in U.S. cents per pound to two decimal places, five contract months a year -- March, May, July, October and December -- and a trading day running from roughly 9 p.m. at night to 2:20 in the afternoon covering a fair share -- a very large share -- of the commercial global cotton trading day.

And now the differences: The first key difference between the World [Cotton] contract and the No. 2 contract is in the par quality that's deliverable on the contract. For the World contract, the par quality is color 31, or middling, as it's referred to in the cotton trade; leaf 3, staple 36, strength 27 in a particular micronaire range.

For all but micronaire these par terms are significantly -- are higher in quality -- than they are in the existing No. 2 contract. And not only that, the World Cotton contract terms also provide for a higher minimum delivery quality than does the No. 2 contract. The terms on the No. 2 contract -- the quality terms were set quite a long time ago, and they have not been updated, in some cases, for some quality parameters in quite some time.

The difference between the contract terms and the difference between the minimum deliverable qualities here is not small. Based on USDA classing data for the most recent season completed, typically roughly 90 percent of U.S. cotton production last year would have met the grade specifications for the No. 2 contract. Looking at the higher minimum quality specifications for the world, only about 60 percent of the U.S. cotton produced last year would have met the world contract specifications, so significant differences in terms of quality.

A second key difference is deliverable origins. Unlike the No. 2 contract which allows for delivery of U.S.-grown cotton only, the World Cotton contract allows for delivery of cotton from the U.S. and eight other significant commercially relevant origins which are Australia, Brazil, India, and then Benin, Burkina Faso, Cameroon, Ivory Coast, and Mali. Those last five we collectively refer to as the West African growths.

For deliveries under the contract, U.S. is the par origin and each other origin is deliverable at pre-set premium or discount that's fixed annually and can change once a year on a fixed pre-set schedule.

At launch, the schedule provides for a 6 cent per pound or 600-point premium for Australia, and for discounts for each other origin. A 300-point or 3 cent discount for Brazil, a 700-point or 7 cent discount for India, and a 6 cent or 600-point discount for West African growths, and those differentials were set based upon a survey we conducted on key market participants and their history of the relative value of those origins against the U.S. origin for the last several seasons.

As you would expect, these origins were not -- that are allowed to be deliverable -- were not chosen on a whim. They were chosen for a reason. Collectively, again using USDA data, these origins, in the 2013-14 season, accounted for almost 3/4 of total global exports of cotton, so it's clear to see why these origins were selected.

Finally, the third key differentiator between the World Cotton contract and the No. 2 contract is delivery points. Like the origin terms of the No. 2 contract, which is U.S. origin only (the No. 2 contract allows for delivery of cotton in U.S. delivery points only) - the world contract will allow for delivery in the U.S., the same five delivery points that are currently available in the No. 2 contract. It will also allow for delivery in Australia in three locations and then in two locations in Malaysia and two locations in Taiwan.

For delivery purposes, these two Asian countries -- which we are referring to as the destination countries, as opposed to origin countries of Australia and the U.S., these destination locations are par and delivery in any of U.S., and delivery in any Australian delivery point will be at a pre-set discount that roughly equates for the cost of moving that cotton in containers from Australian points or U.S. points to the destination locations. At launch those discounts will be 200 points or 2 cents a pound for Australia and 325 points or 3.25 cents per pound for the U.S.

And again, just as the selection of origins was made based on commercial market considerations, the selection of delivery points was also made based on commercial market considerations. Per USDA data for recent seasons including 2013-14, Asia collectively has accounted for between 60 and 70 percent of global cotton imports over the last several seasons.

So, in conclusion, our launch date is November 2. Our first delivery month will be the May 2016 contract, but I need to stress that just as the concerns about a potential disconnect between the U.S.-focused No. 2 contract and the increasingly international commercial marketplace came to us from our cotton customers, so too did these terms that I've just described for the World Cotton contract.

The initial term sheet came to the exchange from a joint working group of the American Cotton Shippers, which is represented on this Committee, and a group based in Liverpool called the International Cotton Association who collectively came together and recognized the need to develop a viable, functioning, international cotton contract to complement the No. 2 and it brought those terms to ICE as the exchange they felt could best bring it to successful listing quickly.

The effort has taken us longer than we thought, and we've been working for nearly two years with continued input from our commercial customers to refine that term sheet into a viable futures contract and also to make sure that all the services needed to support a physical-delivery contract in those locations with those origins will be there including grading, warehousing, and provision of electronic warehouse receipts.

One unexpected challenge that we faced and that we hit in the process was learning that some of the planned World Cotton contract terms that we were given -- and that we feel are appropriate -- conflicted with the nearly 100-year-old provisions of the Cotton Futures Act. That meant that to list this contract in the U.S.

with those terms that the trade wanted us to keep, we literally needed an act of Congress and we got it. It took nine months, and it only succeeded because of the help and support we received from our cotton customers including ACSA as well as the National Cotton Council who's also on this Committee.

The exchange is very grateful for the support we've received in developing the terms of the World Cotton contract and in getting to the point where we're just about a little more than a month away from launch. We're continuing to work hard to ensure a successful launch and we look forward to that first trading day, and that's the end of my presentation. Thank you.

MR. FORTENBERY: Thank you, Mr. Barry. Mr. Carlson from the Minneapolis Grain Exchange.

MR. CARLSON: Good morning to the distinguished members of this Committee and all those in attendance. Thank you very much for the opportunity to speak before you. My name is Layne Carlson. I'm proud to say I represent the

Minneapolis Grain Exchange. Our institution has been around since 1881, so about 135 years, so we must be doing something right. I believe we've earned the respect of generations of farmer-producers, grain elevators, exporters and millers, as well as speculators.

We started as a regional cash grain market and have grown now into a global service provider by means of the electronic marketplace. Our principal contract is a North American Hard Red Spring Wheat contract and each of you around this table should have material before you describing a little bit about our contract.

Trading volume has been growing dramatically. For our last fiscal year, just ended August 31, we set a new record in terms of volume exceeding well over 2 million contracts. This is a 13.4 percent increase over last year's record, a 69 percent increase over two years ago, and an 87 percent volume increase from just three years ago.

What makes these volume numbers

impressive is that they have occurred in the face of a strong headwind. There's been a dramatic decrease in FCMs, an ever-growing and complex regulatory burden, and a rise in required capital to be set aside for margining and security purposes. Volume growth is going to be harder to come by as a result, and liquidity is an essential element for market participants to get in and out of the marketplace at a price that they desire; therefore all regulatory authorities, whether MGEX or CFTC, must seriously weigh the costs of rulemaking compared to the benefits they're supposed to provide.

The main purpose of the commodity futures industry in general is -- , in our high-risk Spring Wheat contract, in particular -- to provide a means for risk mitigation and price discovery. If we cannot provide this service to our market participants we fail them; consequently MGEX has a vested interest ensuring the contract is able to be used for risk mitigation and price transparency. Therefore MGEX is constantly reviewing our contract to determine whether it's meeting the needs of its users. In fact, we have our market participants on a Hard Red Spring Wheat contract Committee. They have both been vital in ensuring our contract's performance. As a result, MGEX has made changes to the contract to enhance its value.

For example, effective with the September 2012 contract month, a delivery elevator no longer has to provide a certificate of U.S. origin unless requested. This was in direct response to the fact that Canadian spring wheat was entering more and more into the U.S. supply and delivery chain. In fact, Canadian customers are using our contract to hedge.

Additionally, effective with the May 2013 contract month, all warehouse receipts issued for delivery against the Hard Red Spring Wheat contract had to be marked with a vomitoxin limit. This was a direct result of customers wanting to ensure any delivered wheat that entered into the food supply could be used here and abroad.

Additionally what we've done is we've added another contract, a Calendar-Spread Options contract this year. Calendar-Spread Options are options on a price differential between two different futures delivery months. This allows contract traders to efficiently spread between delivery months at a single transaction. Furthermore, to improve transparency we've added daily grain movement reports and put them on our website. This provides more transparency into the marketplace, and that has been well received.

Another essential element that has contributed to the success of the contract has been reliable, measurable futures-and cash price convergence. That reliability has been cited again and again by market users as a reason they can trust our contract. Of course, there have been unusual factors that can interfere in some of that normal price convergence, and we witnessed some of that in 2014 and early 2015 with the rail car shortage, but however MGEX looks to guard the importance of convergence by monitoring all the various factors involved including transportation and storage costs.

And of course monitoring our Hard Red Spring Wheat contract is something we take very seriously, particularly trades surveillance in the regulatory aspect, as well as customer satisfaction in terms of contract performance and risk mitigation and price discovery.

When we conduct market surveillance, we monitor for improper activity that might be manipulative or disruptive such as trading ahead, and we keep watch on the contract specs as mentioned earlier; however a real concern of MGEX and our market participants is proposed regulatory changes. I don't think that we can over-emphasize the importance of the topic of speculative position limits, particularly the negative impact the 2013 Notice of Proposed Rulemaking will likely have on our market participants and our MGEX contract.

The amount of Hard Red Spring Wheat grown in North America is well over a billion bushels. With such a large commodity, I guess our preference would be that position limits really are not necessary. Rather, the contract markets that list products for trade, such as ours for Hard Red Spring Wheat, should be allowed the ability to set position limits; however, we realize that no limits or setting limits ourselves may be too much to ask considering that the CFTC has listed Hard Red Spring Wheat as a core referenced contract. Therefore we must stress the importance of parity of speculative position limits among the three domestic wheat contracts; specifically Hard Red Winter and Soft Red Winter in Chicago, and our Hard Red Spring Wheat contract. All three contracts are listed as core referenced contracts of the 28 listed by the CFTC in the Notice of Proposed Rulemaking in 2013.

The CFTC has historically recognized the importance of position limit parity among the three wheat contracts, and while history is on our side, there really are fundamental and practical reasons for maintaining wheat contract position limit parity. All three contracts have market participants that trade all three contracts. Those market participants are both commercial hedgers and speculators, and both put on active spread trades between the different wheat contracts to hedge risk or to take advantage of perceived price differentials. And speculators are essential to contract pricing and spread trading. At times perhaps three- fourths of all daily trading involved in Hard Red Spring Wheat is involved in either market spread trading, and furthermore over half of all Hard Red Spring Wheat is exported, and most of that is sometimes, or in some manner, hedged in the futures marketplace.

As already stated, the annual production of North American hard red spring wheat is over one billion bushels, making that wheat class the largest wheat class in North America. This is why I mention annual production, and the concern we have with the initial proposed rulemaking in 2013 which starts out with our contract having a position limit of only 3,300 contracts, Hard Red

Winter would start at 6,500, and Soft Red Winter would start at 16,200 contracts. And that formula is derived from the CFTC's proposed rule for non-spot month position limits using a formula of 10 percent of the first 25,000 of the contract's open interest and 2.5 percent of open interests thereafter. However, this approach allows the third largest wheat contract to have almost five times higher limits than the largest wheat class, and this really makes no sense. Consequently, we would suggest that we look at production and volume as opposed to open interest.

Because a large volume of intermarket spreading, the proposed limits may very well harm all three contracts as traders may limit activity to the wheat contract with the lowest limits; therefore, a one-size-fits-all formulaic approach is not a good approach to setting position limits, and that's why MGEX is continuing to make the case that non-spot position limits among the wheat products must be treated equally if the CFTC is going to have position limits. To do otherwise is only going to cause confusion, if not likely cause price distortion among the three wheat contracts. Should a definition of bona fide hedging be narrowed, as proposed, that would only increase the importance of the need for parity among the wheat contracts.

And that brings up another important topic to all market participants who use our contract. Narrowing or restricting a definition of a bona fide hedge from its current use is not the best route to solve perceived or real abuse. Rather, it's only going to cause consternation and frustration among a group of hedgers who legitimately use the futures market for which it's intended to be used. I will quickly add that anticipatory hedging is a bona fide hedging form.

In closing I just want to thank this Committee for the opportunity to speak, and thank the Commission for the support of this advisory committee.

MR. FORTENBERY: Thank you, Mr. Carlson. At this point we'll open it up to the

Committee for questions and/or discussion. I'll just remind you to please hit the button and turn your microphone on when you speak, and then turn it off when you're done. Any questions or comments?

I have a question for Mr. Barry. Do you have a sense for whether or not the volume of trade, at least initially, in the World Cotton contract is likely to come from current trade in the domestic No. 2 contract, or is there sort of a latent demand for this activity that hasn't been accomplished anywhere else in the market in the past?

MR. BARRY: In your question do you mean first that we would see traders who are active in the No. 2 also being active in the world contract, or moving their activity from one to the other?

MR. FORTENBERY: Moving their activity from the domestic to the world.

MR. BARRY: That's a question we grappled with from the beginning as to what extent the new contract might cannibalize the existing contract. The net feedback that we've gotten from current market participants is that there is latent demand from producers in other areas for whom the U.S. focused price is not necessarily as good a barometer or as good as -- the current contract, the U.S.-only terms, doesn't give them a sufficiently relevant price to use, so we think there's latent demand. We think there also will be significant pickup from current users of the contract, but we think there would also be some arbitrage opportunities between the world price and the U.S. price, so we're here to see. We think there's a bit of all three.

MR. CLAUSSEN: Could you guys speak more directly into the microphones. It's really hard to hear up here. Thanks.

MR. FORTENBERY: We have a few Committee members that are connected by telephone as well. Do we have any questions from the folks that are remotely connected?

MR. WANDS: Yes, my name is Hayden Wands. I'm with Bimbo Bakeries USA. Just to let everybody know, we're the largest baking company in the U.S. We currently have about 62 bakeries in the U.S. and we're owned by Grupo Bimbo, which is located in Mexico City, and they are the largest baker in the world having bakeries in North America, South America, Europe and China, and so I appreciate everybody's initial comments on this, and again thank you to the CFTC for continuing these discussions because as you can be well aware, the agricultural exchanges, or futures, to us as an entity are vital, and we want to see the fluidity of those markets continue -- or the liquidity of those market continue.

I have a question for Mr. Carlson of the Minneapolis Grain Exchange. Mr. Carlson, you mentioned a note that you don't want to change the definition of the current bona fide hedger. Is that correct?

MR. CARLSON: That's correct. We believe certainly that the current application and use of the definition of bona fide hedging specifically under 1.3 (z) is adequate for the marketplace, and unless there's evidence to the contrary showing that it needs to be narrowed, I think we should support the current use of the definition and its application.

MR. WANDS: And so I'm not quite -- I'm not aware of that rule. Where do the index funds fall on that? Are they considered now a bona fide hedger or not?

MR. CARLSON: I'll have to let some others speak more specifically to that, but I think the application of bona fide hedging is contract-wide, not specific or limited by the type of contract; whether it's physical or index.

MR. WANDS: Okay. My only concern is we do quite a bit of hedging in the Minneapolis Grain Exchange, obviously because we buy a fair amount of U.S. spring wheat and Canadian spring wheat. What we want to avoid obviously is 2008 with what happened in Minneapolis, and so do you think the definitions that you have now as a bona fide hedger, are you comfortable that that won't -- we put in kind of a guardrails where that won't occur again?

MR. CARLSON: The incidents in 2008 were across all commodity markets, where there was a fundamental increase in prices not only limited to our contract. Again, I think what we find, is that the commercial industry...in particular, we should be listening to them in terms of how they use the specific different contracts for hedging, and continue to use or allow them to use those futures contracts for hedging purposes. I would say that in 2008 hedging was not the instigator for the increase in pricing at that time.

MR. WANDS: Oh, no, and I don't want to occupy everyone's time. I absolutely agree that hedging was not the incidence. It was just the price action. Minneapolis was, at least, of the different indexes that we use, was the most volatile, and so that's -- I just wanted to get your opinion on if you think that the definition of bona fide hedgers will circumvent that from occurring again. That was my only point.

MR. FORTENBERY: Other questions either

from those remotely connected or sitting in the room?

MR. KOVANDA: Mr. Carlson, just a quick question. You mentioned at the beginning the growth in your volume, and then you mentioned the challenges that are being faced. Why do you think the two have coincided?

MR. CARLSON: It's interesting in that I think what we've been able to do is show them value of our contract, meaning that we have more international participants involved in our contract, and that has contributed significantly to the growth of that contract. Plus as I mentioned earlier, we have made contract changes so that people can use the value of the contract, specifically removing U.S. origin requirement, if that was a requirement, and then adding vomitoxin limits as two specific examples. So, despite the headwind we still have people seeing the value of the contract. It's just that it's becoming more and more difficult I think to see that type of growth if this type of trend continues.

MR. GALLAGHER: Tim Barry, thank you for presentation on the new cotton contract. I'm a dairy guy and way out of my league on cotton here, but I really appreciate how the cotton industry looked at the changing global marketplace and created a global contract that trades with the existing U.S. contract. Right?

So, we had a -- Tim Andriesen -- remember we had attempted to do something like that at the CME with nonfat dry milk, and Tim, I think we were a little bit premature, but I am interested. We have a challenge within the global dairy industry about world powder derivatives and not having a go-to place, but I am interested in your -- one of the challenges gets back to delivery discounts, and so you've worked with the industry to identify what they should be. Do you have a plan to review those over a period of time to see if they change? And, if they do change, will you enact changes to those at that point?

MR. BARRY: Yes, for both the origin and the location discounts that I referenced. The rules dictate specifically when each, for each origins, for example. Each year by July 1 the exchange has to announce a new schedule that will take effect not that same December but December a year forward, so any changes in the new schedule will be announced on July 1; in 2016 will take effect for December 2017 delivery.

So, yes, we have a built-in schedule by which we need to review them on best available evidence at that time, announce them to the world, and at sort of a staggered effective date for each, so that built into the contract is an annual review for quality -- sorry, for location and origin discounts.

MR. GALLAGHER: Tim Andriesen, so when you're thinking about -- when you look at the need to change contracts it is generally the industry coming to you to look for changes, or is it more the CME reviewing things and suggesting changes to the industry? How does that dynamic work?

MR. ANDRIESEN: I think it's a bit of both. We're outside of just simply having a review process. We're generally engaged with the industry on a pretty frequent basis, so by the time you get to a review process you've generally had comments and feedback from people that help you form what are the things that we potentially want to look at.

There are cases when it's our thought process -- in terms of identifying those things that are driven by the industry -- and there are times when those things are driven internally where we, as the research and product development team, look at the macro drivers, the market and they see as things that potentially are challenging for the contract in the future.

MR. GALLAGHER: So you have an interactive approach with the industry in general that you've got contacts, you know the people, they know you, you're constantly working with them. I'm assuming it's the same for ICE and the Minneapolis Grain Exchange? It's no different, and so one of the things that I'm a proponent of is if there are questions as to whether something is a bona fide hedge that the exchanges decide on whether something's a bona fide hedge, and if so if there were some sort of a rule that there was -- with everybody in the room here that we think that I agree with Wayne that the existing bona fide hedge rule should continue, but from time to time there's going to be new things that are going to pop up, and so new ways of using derivative markets to hedge a transaction including using swaps instead of futures. So for instance, in dairy, there's only one dairy clearing -- CME's the only one that clears dairy or handles dairy, and so we may have some innovative way to utilize a hedge transaction for our farmers or for the businesses that we own that may be done by swaps, and so we're going to want to know in advance or if that swap transaction is going to be a bona fide hedge, and so we'd like the exchanges to be involved and I'm curious, if they were -- if in their infinite wisdom the CFTC agreed and decided to let the exchanges identify whether something is a bona fide hedge that is outside whatever the parameters are that may exist at the time it's implemented, how quickly could the CME make a determination as to whether something would be a legitimate bona fide hedge if it was sort of this new thing that hadn't been tried before?

MR. ANDRIESEN: Very respectfully I'd suggest Joe Hawrysz is on this afternoon and he's in market reg. He would be one of the key decision-makers if we were to look at doing something like that, so I would suggest that he would be the person to ask that question to.

MR. DIERKS: If I could follow up with what Ed just said, I would fundamentally agree that I think the exchange is in a positon to offer more real-time observation. I'm not going to -- we'll wait until this afternoon, but I'd also say, since you mentioned hogs, in the process you went through in the hog contract I would let the commissioners know that I think the pork industry's been satisfied with the outreach the CME does, the input it solicits. Sometimes it almost over-solicits, but they make sure that all the parties have an opportunity in that process. I would also say that I think it's not just a single spot in time like, oh, gee, the contracts -- there's no change to the contracts now, okay, but there's still discussions going on within the industry with the exchanges on what the future looks like.

One of those is the exchange just started publishing a new pork index that may be the precursor long-term for other kind of risk management tools that we need in the industry.

And the final comment I'd just - I'd like to compliment ICE. One of the concerns that I guess I've had personally is that as we look in the future and the globalization of agriculture, one of our strategic resources is our domestic U.S. exchanges -- the exchanges occurring or taking care of business for pricing globally because I'll tell you, in the U.S. pork industry there are strategic advantages long-term for our exports if we continue to -- even though there's no physical pit anymore in Chicago, if we continue to base it here in the United States it should be global in reach, but it needs to reach the global market, but in 2008 when we saw $8 corn, $9 corn, we had people backfilling corn in the United States from South America we would have been at a tremendous disadvantage for the pork industry perspective because suddenly we started pricing corn off of São Paulo or somewhere else, and I think it's critically important we keep these exchanges in a leadership positions.

MR. MASSAD: Thanks, Randy. I wanted to ask Tim Barry a couple questions. First, is there any significant competition anywhere on sort of an alternative cotton contract from anywhere in the world? Number one.

And number two, you noted -- I'm just kind of curious on the composition. You note on page eight the new contract deliverable origins were up 73 percent of world cotton exports and you give the breakdown. U.S. is 27 percent, though I think I heard you say that the amount of U.S. production that would be eligible -- that would meet the criteria is about 60 percent. I'm just curious when you look at it in terms of production that meets the criteria, who are the other big [producing countries] -- is it pretty much proportional to what you have here on page eight or is there any variance?

MR. BARRY: Sure, on the first question there is no direct competitor currently. There is a very actively-traded cotton contract on the Zhengzhou exchange in China. It was one of their -- I think it may have been their first successful agricultural products. They also now trade sugar which trades even more volume there than their cotton contract does. That contract prices delivery in China; Chinese only, so it's -- as a benchmark it's potentially a competitor, but it's not a direct competitor.

In terms of exports, the U.S. -- even haircutting for quality which we've done and when obviously that will be in our deliverable supply estimates when we make our filing later this week - the U.S. would be the largest contributor to the deliverable supply for the contract. Australia is typically number two, India number three, and then the contributors get smaller, so it's not equal, by any means, but the U.S. is still the biggest single contributor to that number.

MR. FORTENBERY: Any other of the remote contacted Committee members have a question? Yes, Mr. Kadlec.

MR. KADLEC: Tim Andriesen, [I have a question regarding] CME's very successful dairy products. Have you explored expanding into Europe knowing that their consumption is, I think, on an individual basis, more than us in the United States? Do you have any initiatives or thoughts of expanding your contract there?

MR. ANDRIESEN: So, obviously that market's gone through some deregulation this year. I'd say just generically we're always looking at markets that are in transition as possible opportunities.

MR. FORTENBERY: Mr. Carlson, I have one quick question. You mentioned that from your perspective the need for parity, I guess that is the way to phrase it, in terms of position limits across all the wheat contracts, you talked a little bit about spreads, and I interpreted that maybe falsely to mean time spreads, calendar spreads. But I'm wondering is there much spread activity between spring wheat and the winter wheat contracts, and would differential position limits -- is it significant enough that they might have an impact on that volume of trade?

MR. CARLSON: I think that when we look at the activity in our marketplace and among the three wheat contracts, our market participants seem to be active in all three wheat contracts, and our real concern is that under the 2013 Notice of Proposed Rulemaking the initial limits proposed are so disruptive or potentially disruptive to the marketplace, I think I briefly mentioned that with the amount of spread activity, I think it harms all participants because -- those that are actively spreading among wheat contracts in order to avoid potential violations -- they might limit their activity during that date to the contract with the lowest position limits, and I think that does a very disservice to providing liquidity to all three contracts for those that are speculators.

MR. CORDES: Just a follow-up question. Layne, when you talked about parity on the position limits, all three, you talked about a better way maybe looking at production. In those numbers are you considering U.S. and Canadian or just one or both, or how's that factoring in your thought process?

MR. CARLSON: That's a good question. When we look at our contract it's really -- we look at it as a North American hard red spring wheat contract meaning both domestic, U.S., and Canadian origin. A lot of Canadian spring wheat is crossing the border and being delivered into our supply chain, and we see a lot about Canadian participation in our marketplace because they see the value and the correlation of using our contract with our marketplace.

And when I say -- when you asked about volume, I think that when you look at North American spring wheat you see a billion bushels or more being grown, and that's far and away the largest wheat class in all of North America. Henceforth that would -- I think we look at the need of having position limits established more on a -- perhaps if there's going to be position limits -- if we looked at it that way we would look at potential deliverable supply and not just limit it to potential open interest.

MR. FORTENBERY: Any more questions or comments? Okay, thank you very much, Mr. Andriesen, Mr. Barry, Mr. Carlson. We're going to break for about 15 minutes, so we'll reconvene at noon to take up our second panel, and I will see you then. Thank you.

(Break)

MR. FORTENBERY: Okay, I'd like to call the meeting back to order, please, so if you're still lingering around if you could maybe take your seats. For the second panel I'd like to introduce Mr. Piccoli who's with the CFTC's Division of Swap Dealer and Intermediary Oversight, and he's going to talk about FCM market trends. Mr. Piccoli.

MR. PICCOLI: Thank you very much.

MR. FORTENBERY: One quick interruption. Please lean into your microphone when you speak. We're having a little bit of a difficulty hearing from one end of the room to the other, so as you ask questions or you present, please lean well into the microphone. Thank you.

MR. PICCOLI: Thank you very much. As the chairman said in his introductory comments we're going to be talking here a little bit about some of the statistics on FCMs over the last few years and taking a look at what's going on and taking just a little bit of a deep dive behind the trends in FCMs.

So, I think the initial analysis shows from 2005 we were at 180 FCMs and then that dropped down to 76 at the end of 2014, but I think when you do that deep dive I think here you really have to parse out the main groups that are involved within the FCM community. So in 2005 you had three large groups. You had, on the top in light green, 84 FCMs that had no customer assets, so in essence introducing brokers that were there but with an FCM registration so they were FCMs. Also, we had 11 FCMs with firms that had more than 1 FCM registrant, so for example, you had Morgan Stanley and Co. and Morgan Stanley Dean Whitter, so they were -- had not -- did not merge MS Dean Whitter and MS and Co. into one FCM. You had Wells Fargo that has 3 FCMs out there and other examples of that - firms that had a multiple number of FCMs out there.

And then you had 85 FCMs that held customer assets, and we'll go into a little bit more detail behind the trend and what's going on behind each one of these data points, but at a high level I think when you look at 2009, for example, and this was chosen as right after the financial crisis we dropped down to 133 FCMs.

We still had 62 FCMs that did not hold

any customer money, and you had a decrease in the number of FCMs that had -- a number of firms that had multiple FCMs from 11 down to 6. We also had some other things going on there.

There were two bankruptcies that happened during this period; Sentinel and Lehman Brothers. We have four firms that were acquired by others, and a lot of this was pre-crisis, and it was firms that were doing natural industry consolidation trying to get more firm assets, more customer assets, so we saw that naturally happening in the 2005 to 2008 period.

And then you still had a small number of FCMs that did go out of business. You had a number of FCMs that changed their registration status from a formal FCM -- fully registered FCM -- to an introducing broker, a CPO or a CTA. And again, I'll go into a little bit more detail on that in a minute.

Then if you look at 2014 -- so what happened here? We had a sizable drop in the number of FCMs that did not carry customers, and part of the reason for this is you had, I think, the NFA making a little bit of push, talking to these FCMs, and saying, "okay, why are you registered an FCM? You really don't need to be." In some cases it was the FCMs insisted --I'm sorry, --the NFA's insistence that, no, that FCM was really a commodity pool operator, and so therefore you need to register as a CPO. So, I think you had a little bit of a push from the NFA focusing in on this group of firms, and we see the drop there.

Some of the firms simply were rationalizing. You know, then just saying, look, the barrier to entry, the cost of being an FCM is a little bit higher. We had new customer protection regulations coming in that required every FCM to have a chief compliance officer, to have risk management procedures, to have documented business continuity practices, and testing these things, so a number of things that came in with our customer protections regulations during that timeframe. So those I think were some of the rationale behind all of that. So let's go to the next slide. This just focuses in on that lower tier going from in 2005 down to 14 -- sorry, 60 -- in 2014, and you see total drop during that period about 29 percent. [It's] still an important number that we can't lose sight of, but the drop from 2009 to 2014 -- a net decrease of five. Keep in mind net because I think there are a lot of ups and downs through there.

And just one other point I'd make because we are into 2015. In 2015, currently, there is a little bit of a decrease that we see currently. We saw a couple of firms - Vision, that I think the NFA had a little bit of a push on that one to help get them to transfer their customer assets. Institutional Liquidity has gone out. We had Newedge that went over to Société Générale when Société Générale bought 100 percent of the firm, so we'll still see that, and we know that there are a couple of other firms that are rationalizing the number of multiple FCMs that they have, so I suspect we'll see a little bit of a decrease by the end of 2015. We've seen a little bit of it now, and we'll see a little bit more as these firms are rationalized and particularly the banks that have to deal with the Basel standards and some of their banking regulations. They are looking to consolidate the multiple FCMs that they have.

So, now let's jump into the actual ups and downs. So here you can see there's a lot of volatility on both sides of the ledger here. We've got a number of firms that have been added during this period from 2006 to 2014, and then additionally a number of withdrawals, and we'll go through -- you can see the ledger on the top that indicates which.

When we look -- let's start with the added firms, firms that came into being as an FCM during this period. You'll see early 2006 a number of firms coming in and then taking an opportunity after 2009, after the financial crisis to come in.

Some of these firms are small and still

remain small. I think [there are] some [that] are, in fact, more significant FCMs now, such as Macquarie, [who] is new to the FCM world. TD Ameritrade has come in. Phillips Futures, Straits, ED&F Man, E-Trade, and the most recent being Wedbush that has just come in with the acquisition of Crossland and taking over or buying Knight Capital Group, the old Penson Futures FCM coming in, so a fair amount of activity on the add side, so it just wasn't all a net decrease or total decrease. There were some on the upside too.

When we drill down a little bit into the withdrawals and what was going on there, starting with the red on the bottom you'll see there were the four bankruptcies that came through: Sentinel, Lehman, MF Global, and Peregrine that came through with a fair amount -- about $10 billion of customer assets associated with those bankruptcies -- and those customers were obviously absorbed into other FCMs.

We also had a number of firms that you

see in the, I guess, the grayish brown -- the brown on the screen, gray on my screen here -- that had become IBs, CPOs or CTAs, and as I said before some of this was the NFA going in and pushing the firms and saying "let's take a look at what's your business model, where should you be registered," so you see that coming through there.

And you'll see a lot more of the activity in the 2009 to 2011 period where you had that rationalization. Part of that is the profit margin. Interest rate spreads remain very low. A lot of these firms were dependent on the spread, and it just wasn't there, and they couldn't possibly sustain it for a long period of time at low interest rates.

You had new customer protection regulations coming in, which some of these firms had had $10 to $15 million in customer assets. The additional requirement -- for them... it was, they said, "okay, we have to take out a chief compliance offer" so that -- I think, was another factor that possibly came into consideration.

Overall, though, there is only $440 million of customer assets associated with these firms, but there are a number of small firms that are in here: Frontier, Pioneer, MBF Cleary, Far Financial, Shay Green, Gelber, which I guess earlier in the period, probably 2008 is when those guys became IBEs or CPO, CPAs.

The next group, which is the light gray on this slide, represents the firms that went out of business, and some of these were at the NFA's insistence, but a fair number were there. Three of them make up the majority of the customer assets, and that was Trilon, Temco, and Bank of New York Mellon -- which is interesting as they sort of came in as a new player and then went out a few years later -- but those three firms made up a vast majority of the customer assets that were there; a total of $1.1 billion of customer assets in firms that went out of business, but the story I think is there still were a large number of small firms that at an average of $10 million of customer assets that did go out of business, and obviously those customers have transferred to other firms.

And then the final group that you see there in the green are... there are 10 firms that were acquired by others. I think early in the period we saw firms like Fortis, A.G. Edwards, and Iowa Grain moving. I think a couple of them went to Mr. Kadlec's firm, ADM. Another went to Wells Fargo. A.G. Edwards went over to Wells Fargo. Then you had others -- Penson went over to Knight Capital Group -- and then a consolidation of some small and mid-size firms coming into play.

So I think the factors that are there, [such as] profit margin. There we see the profit margin for the industry at a low in 2008. It's increased since then, but it's still at a relatively known low number averaging in total around 5 percent, but that's a number that really needs to be analyzed to make sure we fully understand what's behind that, but just the raw number is there.

And the ag firms, the firms that have a

predominant amount of their customer business as agriculture-based -- and this is based on the number of customers, not necessarily the revenue. We don't have that detailed level of information to how much revenue is from ag firms. We just simply -- the number of ag customers that the firms tell us they have -- whatever, 40 - 50 percent of their business -- is from ag customers. That's still a fair number of firms, but it is the smaller firms that are there, I think. The other factor that we ought to mention is the new customer protection rules coming in, I think, had some impact on the firms that are withdrawing.

So here just a different view of the industry during this timeframe, so the bars represent the dollars of customer assets and the left-hand axis is the frame to go by there, so you see us going from that $130 billion in customer assets to a total of $250 billion in customer assets right now.

And now, important to note -- there is the green in there-- the cleared swaps. Then up at the very top, the very small bar that is tough to see, is the FOREX assets. Both of those sort of came in with the new regulations. So, but even backing out the cleared swaps number, it's still an increase of 53 percent in customer assets that were with these firms from 2005 to 2014. Yet you see the line represents the number of FCMs that were there. So dropping from, I would say, 133 down to about 60 coming in the end of 2014. So, just an interesting pictorial. I think they're raising some questions and thoughts on that.

Taking another look and taking a look at the largest FCMs, looking at seg and secured assets only -- so we carved out the cleared swaps because from a comparative perspective you need to be apples and apples,so 2005 did not have cleared swaps so we took that out -- but you can see the top 10 firms, [the] top 10 firms in 2005, in particular. So in 2014 you have MF Global. That obviously fell out. We had two Newedge firms that consolidated into one; two JP Morgan firms. Now, JP Morgan Securities is still there and predominant. There's another JP Morgan Clearing that's still there but it's significantly dropped off. It's now down to number 25 in the rankings.

So, we [can] look at 2014 and some of the things that come out. You see Barclays replaced Lehman Brothers, so I think that's just sort of a push on that. But you have Deutsche [Bank] and Credit Suisse coming in. Deutsche [Bank] and Credit Suisse are always in the top 15. During this timeframe I think they just have consistently added market share, but the thing also to note is [that] in 2005, 67 percent of the customer assets were with the top 10. In 2014, the top 10 holds 75 percent of customer assets. Again, just the seg, secured, and a little bit of FOREX that's out there, so their market share has increased from 67 percent to 75 percent. In most of these firms, you've got to look at where these firms are at now, in being mainly banks. They do have pressure from Basel, the new leverage ratios coming in and some hover rates on return on equity that are going to be challenging to these firms going forward, so we have to think about the customer portability of these firms, and their ability to take on other [customers] and continue to grow market share... or is that going to stabilize? Don't know.

Customer portability over the last couple of years; we had Vision, Global Futures, and FOREX, Jefferies, and Penson all sort of moved over nicely to a number of different firms, but I think going forward looking at the concentration, it just raises some questions on that standpoint.

Here I will first say that this is definitely not a graph that a finance guy would do. It's much too exciting. It is -- the donut here just presents a different view of the top firms, and 196 represents -- including cleared swaps -- so just a slightly different view, but you see how all of the other firms are sort of going into a smaller and smaller band in there, so I thought this was interesting and an interesting point for discussion.

The final thing I just want to mention

is on the CFTC website and here's a picture of the website and the link to it. We do have all of the FCM financial data -- obviously non-confidential data isn't there. You see in the bottom box -- every month you see the data in.pdf as well as Excel formats so you can play around with that.

Here is what that looks like when you actually pull it up, and I think it presents some interesting information to the industry and to customers, potential customers. Key data points being -- from my perspective -- excess capital, target residual. Here are some of the things -- and we know a lot of the firms look at this frequently to see where they are verses others in the industry. So, it's an interesting thing.

I wish we could have made this bigger so you could see the whole thing, but hopefully you'll go to the website and take a look and see where we stand. And you can also see the firms that are FCMs with no customer assets, still bigger ones with zeros going across the line. So, I think that's the end of the comments I had and the analysis that I had, and Mr. Chairman, go right ahead please.

MR. FORTENBERY: Thank you very much. Before I throw it open for comments or questions, let me just recognize Ms. Eileen Flaherty and also Dr. Srinivasan who will be helping answer questions and engaging in discussion.

And just a quick reminder, if you're in the room, please mute your phone. If you're a Committee member who's connected remotely, if you're having a local discussion could you please mute your phone while that goes on as well.

At this point I'm open for questions or discussion. Yes, sir, Mr. Chairman.

MR. MASSAD: Let me just add because I don't know that all of you have met Eileen. Eileen is the new director of DSIO, so we're just delighted that she joined us just a couple weeks ago, and Sayee is our chief economist, so delighted to have both of them here.

And Kevin, I just had one question because I may have -- I don't think I heard what you said. On the last -- on the donut chart, the 196 total assets, that's without including swaps, is that right?

MR. PICCOLI: That is including -- it's the total assets of the top 10 including swaps.

MR. MASSAD: Just the top ten?

MR. PICCOLI: Just the top ten. The $250 billion in total; $196 billion is the top 10 alone. Sorry, I should have clarified that.

MR. GIANCARLO: Mr. Piccoli, thank you for that. Your knowledge of not only the statistics but just the change in nature of the market and who's going where is really authoritative, and it's great to have you on the beat -- keep an eye on things.

The thing I'm concerned about is not just the changing trend of the top 10 firms -- which are, there's a certain stability in the nature of those firms even if their names are changing -- but what I'm concerned about is recent reports, as I'm sure you know, when SocGen acquired the storied Bache firm from Jefferies recently it was widely reported that they let go a sizable number of the smaller customers and that, and that report also reflects a number of other mergers that I've been reading about recently.

So, my question is where do those small customers go when they get the notice from the new acquirer that, sorry, but we just can't accommodate a small account like yours anymore? Where do they take their business, and do they have a place to take their business?

MR. PICCOLI: Sure, thank you, Mr. Commissioner. So, a couple of points. One, when Jefferies did let us know that they were going to be exiting the Bache business, we, obviously, from an examination standpoint, were very actively involved with them, met with them on a daily basis upfront, and then weekly thereafter focusing in on those small customers and making sure that they just didn't leave people out high and dry. So, those customers, I think, with the -- and I've got to give credit to Jefferies because they certainly did the right thing as I think almost all FCMs would and that is making sure those customers did find a home.

A number of them went to some of the firms that specialize in that type of product. The ag firms, ag customers, I think lot of those went to some of the ag firms that we would traditionally see take on those firms. We had, in some cases, the metals desk at Jefferies - the ones trading the metals futures - that whole team moved to another firm, so those customers associated with that moved with that team to that other firm.

So the -- I think -- and I want to be careful not to give out any confidential data, but I think that the customers themselves, I think, pretty much found a home where, [number] one, they were comfortable, I assume, right? And [number] two, where the firm said, "yes, these are the types of customers that we would like." But you're absolutely correct that when SocGen took the customers from Jefferies there were quite a few that SocGen did not take for a variety of reasons, the least of which is because they didn't want the firm, the customer. It just didn't fit into their business model, so [the portability of these customers] is certainly one of the things that is important to look at, so you're absolutely right there.

MR. GIANCARLO: And I just have one follow-up question. I understand from speaking to some of the larger trading houses that it's good policy to have access to more than one FCM as far as just a diversity of access and putting their positions, and I'm told that today that's very hard to do; that most trading houses, if they have one FCM they can work with, they're fortunate. It's very hard to have more. Is that your experience? Can you comment on that?

MR. PICCOLI: From what we have seen I think we find that certainly the largely institutional customers and the professional traders -- the large professional traders, not the old floor traders -- do have more than one FCM. They have their primary FCM and then a hot back-up, if you will, that they do actually trade with, so we tend to see that, and that's one of the reasons that we saw not all of the customers went from Jefferies to SocGen because these institutional customers already had an account at SocGen -- Société Générale, excuse me, and so they didn't want to go there, so they went over to another firm; JP, JP Morgan Securities, Goldman, whoever. So, on the large customers or the large institutions I think we tend to see them more than one FCM, most likely just two, but there are a couple that are with three.

MR. LEE: In our discussion with the Committee I'd be interested to know whether that experience is mirrored in the experience of the Committee members.

MR. KADLEC: Thank you, Kevin, not only for this presentation but a rational thought to regulation. Commissioner, the lesson learned post-MF Global was the fact that most of our constituents in this room have two clearinghouses, so I can confirm to you that most of our best customers on the commercial side have two relationships.

The large trading houses present what I believe is to me a different problem. They're the most educated if you're talking about propriety shops, and my view is they don't want to pay a fair rate. That's -- whenever we evaluate business, and we have been fortunate to receive a fair amount of business in the last six years because of disruptions in the marketplace that Kevin covered.

You go through a process of due diligence, and the one thing that 2008 and 2009 really reinforced to anybody is real stern and proper due diligence that covers regulatory affirmation of the customers that you're acquiring, proper pricing and capital allocation. Are they a needy customer? What are their service requirements? And that's something that we did get into a great deal, and all FCMs should dig in a great deal, and the ability to say no at times to customers is perhaps the best decision I can make because it is a strategic relationship, and I cannot emphasize that enough.

In the chair that I sit in my day job is that I view customers as a strategic partner in our business. I would like, in terms of regulatory outlook, to look at the Commission and exchanges as a strategic partner, in a different way, but I really feel that all of our vendors are -- we have agendas with them and -- it's about gaining operational efficiencies -- and I think that the biggest message if you look at the cost structure of FCMs as they jump around a bit.

The cost structure of regulatory oversight has doubled in the last five years for us. It's a direct reflection of Dodd-Frank, Basel and the MF Global and Peregrine. I'm not judging, but to answer all the questions, to properly engage the customer protection rules -- that's what it takes to run an FCM these days. The effect is that we have to raise prices on many of our customers in this room, and we are in the process of passing those costs on and trying to do it in a rational and proper and well-defined way, and I just -- I appreciate these type of forums to further explore areas that with the Commission and with exchanges that we can work together to do many of the things that you talk about in your position limits.

I think in terms of efficient processes. This morning -- I'm sorry, I can't recall your name -- but your question was and I was concerned about whether you were going to ask the CME group to tell us in real time who's a hedger and who's not? I think we should embrace the exchanges and the Commission to define our hedges, but I think it's the responsibility of a customer to be able to prove that they fit into one of the buckets. It's critically important that the real-time decisions are trading decisions and not whether or not they fit into one of the hedge-exemption buckets. If that's where we're going, that's going to be a challenging day, so I got a lot more to say, Kevin, as you know, but I turn it over to my fellow Committee members for now. Thank you.

MR. MAY: Thank you. On behalf of U.S. cotton merchandisers, just a few comments on this subject. End users such as our members rely on FCMs to facilitate their hedging business on futures exchanges. We're growing increasingly concerned about the health of this sector and believe that with many swaps now being pushed through clearinghouses, further Dodd-Frank mandates, we arguably need more FCMs, not less; however that is what we are seeing. FCMs are pulling out of the business. We encourage the CFTC to use its expertise and resources to investigate this growing problem and see what you can do to help this current trend. Thank you.

MR. CORDES: Thank you, Chairman. Question for you Kevin -- and I appreciate the analysis on this -- I've looked at some of this stuff myself, and in my day job as president of CHS Hedging we always look at this and I'd echo the comments around rules and regulations. We've doubled our costs around headcount, compliance, and we're probably headed to triples, so we always asking ourselves, "how do we continue to have the size and scale to compete?" We represent one of these small bars [in the chart], but yet as being owned by farmers and ranchers and local cooperatives our mission is to serve agriculture.

So my question...you referenced the piece around the top 10 and the seg assets here, the agricultural-type piece, I think you mentioned around 40 to 50. Do you have more definition where that's at because I know in my day-to-day activities and who I compete with, there's a lot of FCMs that wouldn't be in the top 10 that are in the ag space, and I think for this panel here it's probably real important [to see] where that's represented and who has that size and scale to work with them.

MR. PICCOLI: I think some of that, the information that we have there on who, such as firms like yours, have a percentage of the customer base that is ag-related verses minerals verses financial futures, et cetera -- I think there are a number -- from our estimate about 12 firms - that are predominantly, or significantly I should say, more ag-customer oriented, but again I caution because that's a bit -- it's just one number, but you need to truly analyze it because I don't know how much of that represents revenue verses just number of customers, so it's a difficult number to get our hands on. But I think it is an excellent point, and I think it's one that I think would be helpful in getting at the earlier comment of really diving in and trying to understand what that means and where these firms are and portability of customers. If one of these firms went out, where would they go? Very important questions.

MR. MASSAD: Yes, just to note on that I think we have, as Kevin said, some data, some estimates. Unfortunately some of that's also not public information that we can make available, but I suspect all of you guys know who the main players are anyway.

I'd like to ask Eileen whether she has any sort of general thoughts, and again for those of you who don't know, Eileen now has had about four weeks as a regulator after about 25 years in the industry including at Newedge and other places, so I think your perspective on all this would be very helpful. And then Sayee, also, if you have any thoughts.

MS. FLAHERTY: Sure, thank you. I obviously can't comment on the SG takeover of Newedge because I came from Newedge, and my background really is in this industry for the past 25-plus years, and I've worked for multiple FCMs. I've worked for proprietary trading firms, and just focusing from the FCM space with my new regulatory hat, I do bring the practical perspective.

It's a very expensive business to be in, and the profit margins are very, very low. I wouldn't blame it entirely on regulation, although there are a lot of rules that have come out that firms have had to comply with, some of them as a result of some defaults, failures, [such as] Peregrine, so obviously customer protection is very important. It's very important to the ag market; it's important to all markets, so some of those [regulations] are just necessary to keep the customer funds safe, and other [regulations] -- Congress decided they would put this extra layer of Dodd-Frank on, and so, yes, it does squeeze the FCMs because I got to see on a daily basis profit numbers, et cetera, cost, but just the infrastructure cost -- putting aside regulation, the infrastructure costs are incredibly expensive to run an FCM business.

Between your back-office accounting systems, between your risk management systems, and Tom, has a view to that. He sees it every day, but just the fundamental cost aside from regulation just to be in the business, and you're basically a guarantor to the clearinghouses. You're the insurance entity to the clearinghouses, so if you have a customer that is not -- is experiencing financial bad health -- you are the guarantor to the clearinghouse. And put on top of that the low-interest-rate environment it's a very difficult business to be in and to make any money, and I used the example to Tim a couple weeks ago, you know, would you want in your 401(k) something that took a couple billion dollars in capital to run, had relatively very little profit margin, and you kind of had unlimited liability, so it's a really -- it's a tough thing that -- would you want that in your 401(k)? I might have my view, but it's -- it is difficult to attract more FCMs to the space given just the cost that it takes to run the business.

MS. BOWEN: Can I ask a question also from a customer protection? Having been at SIPC at the time of MF Global and Peregrine and having seen customers not have access to their money, and frankly not having those funds be segregated came at an immense cost. Talk a little about that part of it as well?

MS. FLAHERTY: Sure, lots of us lived through all the bankruptcies in this industry for 25 years, and they're -- MF Global was one -- but you're right.

The difficulty in a bankruptcy -- you know, and again, having sat at different sides of the table in these situations, the difficulty is finding homes, finding big shoulders for those customers.

I think the CME worked as diligently as it could along with the Commission to try and find homes for those customers, but again some of the firms have their own risk- management policies where they don't just take bulk transfers of customers anymore, whereas 10 years ago maybe they would have, but now they have requirements and they have to look at every customer, and so, you know, the idea of portability is a great concept, but in the event of a bankruptcy it becomes very difficult to port and to get, again, big shoulders to take large groups of customers without that individual risk analysis of, you know, is this customer going to default to me the very next day after having taken them on as a transfer.

But with respect to -- I don't know that there's a better way to do it, and yes, maybe customers don't have access to their funds for a period of time when they're being transferred, but the reality is you've got to get them off the books of the defaulting clearing firm onto someplace. Then they can, you know -- which many firms did or clients did at that point -- then once they were ported then they ported themselves out, you know, to other firms that they had selected when there was more time for them to be able to do it. I don't know that there's a better way to do that.

MR. FORTENBERY: Let me ask quickly -- I'm sorry, sir, if there's anybody remotely connected that has a question? Go ahead.

MR. KADLEC: The customer seg rules are actually quite well done which I'm surprised to say now that I've lived through it versus when they were first written, but if I look back and compare them, we had time. They were clear and concise, and they were critically important to the marketplace, so that -- it's just so important to model additional rules and regulations similar to that process, and I -- Chairman Massad - clarity, the importance of clarity from the Commission is critically important, and I just -- I cannot emphasize enough.

Eileen, I agree with everything you said and just emphasize the one thing that I've already talked about is portability. We love getting business for free. Don't make any mistake about it. Not having a capital investment and having accounts come to us is really a neat thing; however, you have to do the due diligence now. If there's one thing that we've learned in the last 10 years with the crisis, that is we have...we have to really dig down and do proper due diligence, and we try to do that along with our competitors.

MR. SRINIVASAN: So, as an economist, when I think about this business and I have three or four factors or things that came to my mind. One, is the point that Eileen was making about -- a bunch of points -- about this being is an industry which is going through transition for various reasons.

The point that Commissioner Giancarlo made earlier about rates having been really low -- this was an industry wherein the fees that you were charging the customer were being subsidized by the float you were getting, and I don't see the rates -- I'm not a macroeconomist, but I don't see rates -- really going back up any time soon. So the float, which has a way of subsidizing transaction costs, is not a viable option in the near future. So the question I have -- and then also the third point that is clearly a shrinkage in the number of players in this market -- so the question I have for the ag community is when you look at the FCM landscape and this is -- you need to go to these firms to access the futures markets -- what do you anticipate in terms of some of the services you expect to get from the FCM going forward? What is going to be the cost -- what are your FCMs telling you? Has the transition been made from that side? Are you expecting more fees or costs -- to increase going forward? What is it that you're seeing -- what are you hearing from the FCMs?

MR. M. J. ANDERSON: We haven't been seeing it, but we're being told it's coming. We've had visits to our office by a couple people of various charges, and I'm sure we're not unique in the industry from that perspective.

MR. KOTSCHWAR: I'd echo that. There's nothing we see that's going to be lowering costs, and I would be remiss if we didn't remind folks in here it's really outside our control, but Basel and leverage ratios and our segregated funds being classified for purposes, that is -- we're concerned about that too. That's going to add costs, and it's going to put continued pressure on the number of FCMs. We don't know exactly how, but it's not going to be good for us. Another unintended consequence of -- although the ag space was not really being a part of the financial crisis but yet our costs are increasing because of that -- so we're concerned about it.

MR. SRINIVASAN: So the other point that

was made, that maybe some firms are not willing to actually pay the higher costs. So the costs just changed; the cost structure in the industry has changed fundamentally. So, which means -- as an economist thinking about how the cost structure has changed-- fees are going to go up, and are there going to be opportunities that other FCMs see here?

I like to think in terms of entry barriers, right, so if a marketplace is a healthy marketplace, then you're going to see exit and entry, so the information that was presented earlier by Kevin says that there's been some exit; there's been some entry. In going through a transformation -- at some point you reach a steady state. Once again talking like an economist here -- and it's important to see whether there will be entry barriers -- and from the Commission's perspective, what is it that we can do in the margin to sort of be supportive innovation -- new business models, new pricing models, new ways to sort of service the ag community?

So maybe not here, but later... I'd be interested in having a conversation with the community so that we can get [information from you]. You're on the front line. You're having conversations with the FCMs, albeit a few steps removed, so anything that you can share with us about how your business is changing, how FCMs are [changing]. New firms are going to enter this space - [we're] sort of eager to hear if you have any thoughts.

MR. MASSAD: Yes, just to underscore that, if there are maybe particular aspects to these issues then it would be helpful for us to hold a further session of this Committee on, or helpful for our staff to examine, those suggestions are welcome.

I also want to follow up on this point that Sayee touched on, and I don't know if, Tom, it was your comment or someone else's, and maybe I'm reading too much between the lines, but I'm curious about the pricing as between, say, someone who is participating in these markets and holding positions over a longer term versus traders who maybe are basically flat at the end of the day. Obviously, we see a lot of volume increasingly in highly electronic markets from traders who are flat, or at least aren't holding significant positions, and I don't know -- I'd be curious as to what the pricing differentials are and how that affects the thinking in this business.

MR. KADLEC: Well, without giving away too many state secrets, it really is capital allocation, and that -- and an assessment of risk in terms of counterparty risk, regulatory risk, and gauging the service that you need to provide to a customer.

So, the math on the capital allocation is very straightforward. Eight percent of margin on an overnight basis is what we use. We probably add 10 percent because no one can run their book at 8 percent, and then you bring in a number of subjective factors, and you try to price your product accordingly. And I think Kevin's return is -- sounds reasonable. I assume that's on an after-tax basis, but it varies based on the four or five things that I mentioned.

MR. SRINIVASAN: Just sort of building on the point the Chairman was making, we have observed that in a lot of these markets, the market structure has changed. It's no longer a flow-based trading. It's all electronic. So the question is: the volumes have gone up -- so when you're looking at the cost of accessing the futures markets for hedging and other business reasons, we are also sort of interested, to the extent you can share -- what's happening to the total cost, I guess, with the change in market structure? Have spreads changed because, you know, the fee that you pay the FCMs is just one aspect of the total transaction cost, right? And on that basis, I think, we're interested in anything you can share with us on what's happening to the total costs with the change in market structure. Have spreads changed in the marketplace - are you able to move volumes, and also, sort of, the services that you're expecting from the FCM?

When there was trading on the floor, it was all manual. You had one set of services that you were expected from the FCM. Now things have gone electronic. That's more sort of desk management tools. There's a lot more automation and potentially more efficiency gains to be got from that also, so any insights that you can share with us would be helpful.

MR. DIERLAM: Let me just pose this question just out of curiosity more than anything. Obviously the charts that you've presented here focus on, say, the top 10 FCMs and the consolidation and the concentration in the top 10 FCMs. Over the past decade or so -- and is there a way to -- perhaps for the benefit of the group here, talk about what you've seen or observed among the FCMs that would be the top 10 FCMs that provide retail services to ag-specific customers, or the top 10 FCMs for the folks around the table, and would they be inordinately impacted by maybe the types of things that Lance indicated -- by the supplemental leverage ratio, the regulatory requirements? Would they be impacted more? What's happening more to them? Would they be impacted more, say, than the larger institutions in any way? Would you expect to see any more concentration or consolidation there than you would the other top 10? Would there be a difference?

MR. PICCOLI: Yes, that's an excellent question because I think you're absolutely right. If you look at the top 10, [they are] predominantly banks or directly owned by a bank, so a lot of them had the risk management. They had the compliance, processes, procedures. They had a lot of the elements that we saw -- and a more diverse revenue model as well -- so a very different audience.

I think if you look at the mid-size, or even the large, firms that are more traditional FCMs, they would not be as impacted by Basel, by the leverage ratio, by return equity hurdles that are now being pushed down and even customer-based return equity as Tom was mentioning before, where firms are taking a close look at what's the return on that customer.

And in some cases the return is going to be more dependent on a customer that trades much more often than an agricultural customer... that would be maybe a straight hedge, so they're going to put the hedge on and they'll roll it when it comes or when they need to, or just take it off when they need to, but not an actively trading firm [or] customer.

So, I think you are going to get a very different perspective on that. I think that's one -- it's a great point, and I think that we could drill down on and try and take a look at these [firms] or the firms in that category and what's driving the revenue model, the expense model.

As a number of people pointed out, that does impact everyone. We put out a regulation and it goes to everyone. It's a question of how does that regulation get applied to small firms as well as large firms. A lot of the large firms already have a lot of this [compliance infrastructure] in place, so it wasn't necessarily an added cost, but a cost nonetheless, so it's an excellent point that I think would be worth drilling down on.

MR. M. J. ANDERSON: Following up on that, it's anecdotal, but a few customers we know...FCMs, I think... Tom and Scott, you guys are doing good at 2-X. We've heard three, four, five X in terms of increased headcount as it relates to regulation, so I think that follows up on your point.

And also Commissioner Giancarlo, we operate with 2 FCMs -- we just -- our view is we can't afford to walk in and not be able to service our customers.

MR. KOVANDA: Just a question as I think about this consolidation, we've talked about the due -- it's been talked about -- the due diligence on the part of the FCMs, in light of the increased requirements in regulations, but has anyone observed increased due diligence by those who have been referred to as customers in evaluating which FCM to do business with in light of the -- well, I'll just use MF Global as an example where many that transacted business in the futures market didn't believe something like that could happen. Is there -- is part of the consolidation really a function of customers doing due diligence and moving towards firms that are more stable as it relates to seg funds or other financial measurement?

MR. PICCOLI: If I may just add onto that because it's a great point. If the customer-protection rules, particularly disclosure rules and a lot of the information that is now out there, if that helped that point because I think that's great.

MR. GALLAGHER: Yes, funny you should bring up MF Global. I lived through that and I never want to live through something like that again, and I do appreciate everything that the CFTC and the CME did to make that as bearable as it possibly could. At the end of the day we got all our money back, but it wasn't immediate.

To your point, we look at -- we have a

different standard of looking at -- who we are going to deal with as an FCM, and my mission is to find FCMs who are too big to fail. And if a new FCM comes along that I don't think is capitalized very well, they are -- I don't give them the time of day at this point in time so there probably is going to be more consolidation over time because of concerns of FCM failure and looking to see who's better capitalized. There are going to be [more consolidations]. At the end of the day it's just the way it is. They're going to be the winners at the end of the day. As long as they're willing to serve agriculture, they're going to win.

MR. KADLEC: Just to emphasize Kevin's point, our data, our financial data, our customer's seg and or capital and our statement of financial condition is publicly disclosed on our website and the CFTC's website on a daily basis, which is the mandate so your customers, our customers, are able to judge us on a daily basis and that's a positive thing.

I meet regularly -- I probably allocate 10 to 15 percent of my time with customers; that's similar to the Commissioners -- went out to visit our customers and our constituents. That's part of the duty of any FCM leader. I meet with boards and walk through our financial statements regularly and customers appreciate it and value that and should do that.

MR. FORTENBERY: Let me check in quick with the remote members again and see if there's a question.

MR. CORDES: Thank you. Just to add on to that, and again I would say some of the same comments, but post-MF I've had a lot of conversations with potential customers and customers who came over just like Tom mentioned. Prior to the MF bankruptcy, typically people, customers, would say, okay, who's the broker I'm dealing with? I like Joe and that kind of information. Never had the discussion about who's holding my money and my positions. MF changed that. We had a lot of discussions that went around that; customers that came over wanted to have more due diligence about who you are, what you are.

To add on to a few of the other comments you asked about the pricing model. The one thing I would add is in the expectations -- and this comes from the farmers. It comes from local cooperatives. They expect more volume in their business will get them a lower rate, so that's a big consideration that comes in as well.

The other point around what is the customer looking for in the future, and this gets into the cost of doing business. It's not only regulation. You mentioned, Eileen, around back-office technology. Our customers are really expecting us, coming from the farmer and the new generation that's got that smartphone; they want access 24 hours a day. Can I trade through that? Can I look up my positions? Do I know where I'm at? Well, that puts another increased burden on the FCM, especially as we get into cybersecurity to make sure you don't lose something there and to keep those systems up and running at all times, size and scale again to do that, so those are some of the expectations that are coming out of the customer as we move forward.

MR. FORTENBERY: Any more questions or comments? Yep?

MR. STRONG: So, Kevin, did maybe I understand or infer from your comments that the ag industry FCMs may have been hit worse over the last five years, or so, or do you just not know that?

MR. PICCOLI: No, I didn't mean to infer that at all. I think that's one of the things that we could look at and take the -- do an analysis of to figure out if that is the case and take into consideration all the other comments that came through here to figure that. I'm sorry. I apologize. I did not mean to infer that they were hit harder.

I think they were probably hit as well as everyone else. You know, it's a question of the type of firm, the size of the firm. If they have a lot of capital maybe they can withstand a low-interest rate environment for a lot longer than the firm that has a million dollars of excess capital and maybe can't ride out the low-interest-rate spreads and couldn't change their revenue model or the technology that customers are looking for. Just the cost of that was too much and they felt they couldn't pass that on to customers, so I'm not sure. I think it's one of the things that would be interesting to look into.

MR. STRONG: Okay, and as a follow up I think we heard that all customers ended up finding a home at another FCM, but can you give us any more color commentary because it seems to me that we've heard a lot around this room about increasing costs and evaluating service requirements that those customers' needs. I can't believe all of those happily landed with another firm providing great service at a great price.

MR. PICCOLI: Well, from what we've seen, and again just thinking of the more recent ones such as Vision, Global Futures, and FOREX, Jefferies that was talked about -- I think they're, the customers, are all ported to a variety of different firms out there. You're not going to find one [firm] -- in the very large situations like Jefferies or Vision where you're talking $500 million plus in customer assets.

I know not all are going to end up at one firm, and I think that's where the portability question comes in. How do we make sure that we can port all customers over and that we can make sure it can get sustained. Whether the customers stay there -- I think one of the things that you see when customers are transferred over, we try to insist that the customer can transfer without any fees subsequent to that. That's something that we ask of the firms, but it's up to the firm to do, but we do try to make sure that the customers have an opportunity to move to another firm once they're with an existing FCM and whether it's something that's done quickly overnight because of the urgency. Sometimes it takes a little bit of time for the customers to understand and get used to it -- for the firms to do their due diligence and know their customer and make sure it's a customer that they want. Sometimes it's the firm that will actually say to a customer, sorry, you know, thanks but we'd like you to find another firm over time.

MR. MASSAD: Yes, I want to just make sure I understand because maybe Kevin and Eileen or Sayee also can respond. I take it we can look at issues like this at the moment of transfer where you've got a failing firm or some other problem. We don't track what's going on in terms of customers and whether a firm is keeping customers or whether they're doing things to kind of maybe push a customer out the door. We don't have that kind of data. I mean we look at -- I take it what we look at is a moment where there has to be a transfer, we look at what they're going to port those positions as opposed to liquidating positions. Is that correct, Eileen?

MR. PICCOLI: Yes, absolutely, Mr.

Chairman. It's the -- making sure that we can transfer all customers immediately if need be, or in some cases over time, such as Jefferies. We make sure that that firm is there and will continue to have the support for those customers until they're transferred over so that they can protect the customer assets during that period. But then once the customers are transferred to another firm then it's -- you know, the customer does what they have to do. If they like the firm, great. If they don't, that's their decision.

MR. SRINIVASAN: We don't necessarily collect that information. Firms are not required to send us information on a regular basis, so default would be making calls on an ad hoc basis.

MR. FORTENBERY: Okay, at this point I'd like to thank the panel. Oh, I'm sorry. One more question.

MR. STRONG: Mr. Chairman, maybe, I was -- I was just wondering if Kevin had some other color commentary since he was cracking off names of firms that left the business or merged that many of us know intimately, and I can also chime in with the other question about multiple clearing firms. While we're a commercial self-clearing, we also have a significant backup.

MR. FORTENBERY: Okay, at this point we're going to adjourn for lunch. We will reconvene at 2:00. I believe the Committee members that are lunching together, we need to go upstairs. We'll be escorted, so somebody will meet you out front, out in the lobby, and escort you up to lunch. See you at 2:00. Thank you.

(Lunch break)

MR. FORTENBERY: Okay, welcome back. I'm going to call the meeting back to order. Just a couple reminders. All the slides and presentations that we are experiencing today will be available on the website after the meetings are over, and we're also being webcast so just to let you know there's a broader audience paying attention as well.

What we're going to do is start with our third panel this afternoon which is basically on position limits, and first we're going to hear from Mark Fajfar, who is with the Office of General Counsel at the CFTC, and then Joe Hawrysz from the CME Group and Erik Haas from ICE Futures will also speak to us. So, with that, Mr. Fajfar.

MR. FAJFAR: Thank you. Good afternoon. I'm happy to be here to describe the Commission's recent approval of a supplement to its proposed amendments to the aggregation standards for the position limits regime. In short, the Commission has proposed to modify how aggregation rules will address situations when aggregation is required on the basis of ownership of greater than 50 percent of another entity. Under the new modified proposal, owners of more than 50 percent would have access to the same relief that's available to owners of 50 percent or less of another entity.

Now before I go any further I should say the Commission has approved for publication in the Federal Register a supplemental notice of Proposed Rulemaking that explains the proposed modifications in full detail.

Now, I'm going to try and highlight the key details, but what I say here is just a summary of that notice, and if there's a conflict or if I've left anything out, the notice approved by the Commission takes precedence, so I'm going to briefly describe the existing proposal from November 2013 and then describe how the Commission has just proposed to supplement it.

First, what do we mean by aggregation for purposes of position limits? The Commodity Exchange Act requires aggregation of all positions which a person owns or controls and all positions of persons acting pursuant to an express or implied agreement or understanding. To implement the statutory requirement, the Commission's current regulations require that a person aggregate all positions in which the person has a 10 percent or greater ownership interest, that is. When a person determines what his position is for purposes of determining whether it's over or under the limit, it has to include the position of other entities in which it has a 10 percent or greater ownership interest. Either way, this rule applies in the same way for all federal position limits, and the Commission intends that it would continue to apply for all federal position limits that may be adopted in the future.

There are exemptions from the aggregation requirement in the current regulations for, among other things, eligible entities with independent account controllers. When the position limit regime in Part 151 was adopted, exemptions were added for info sharing that would cause a violation of federal law or regulations and for an underwriter's ownership of an unsold allotment of securities, so those are situations where a person would not be required to aggregate.

In November 2013 the Commission proposed four additional exemptions from aggregation, one related to information sharing and the second was a new exemption for broker/dealers. The third and fourth exemptions were for persons who hold an ownership interest in another entity.

So back in November 2013, the third

exemption that was proposed was for owners of no more than 50 percent of an entity. To use that exemption the owner would file a notice demonstrating compliance with certain conditions that go to a lack of control of the owned entity and the implementation of firewalls.

The fourth exemption proposed in November 2013 was for owners or more than 50 percent of an entity, and to use this exemption the owner would apply to the Commission for relief on a case-by-case basis and have to show that trading is independently controlled and other conditions are met such as the owned entity not being financially consolidated.

So, we received public comment on the November 2013 proposal, and one thing we've heard is that the last exemption for owners of more than 50 percent is too narrow and difficult to qualify for, so that is why, among other reasons, the Commission had determined to revise the proposal so that owners of a greater than 50 percent interest would follow the same procedure that would apply for owners of an interest between 10 and 50 percent, that is, those more-than-50-percent owners would be able to disaggregate the owned entities positions upon filing a notice with the Commission stating that the specified standards about control and firewalls had been met.

In other words and to wrap up, under the proposal as revised, all owners of 10 percent or more of an entity, that is, owners of up and including 100 percent of another entity could obtain an exemption from aggregation following the same procedure. They would file a notice with the Commission that meets specified requirements which mainly relate to a lack of control of trading and implementation of firewalls to prevent access to information.

All other aspects of the November 2013 proposal remain the same and the Commission continues to consider that proposal and the comments submitted during the earlier comment periods. The new proposal is available on the

Commission's website today and comments on the supplemental Notice of Proposed Rulemaking may be submitted in the usual manner -- electronically through the Commission's comments online process. So, thank you for your attention.

MR. FORTENBERY: Mr. Hawrysz.

MR. HAWRYSZ: Thank you, Commissioners and thank you, Committee, for allowing me to speak here on behalf of the CME Group. I kind of feel like Erik and I are an opening act before the big event tonight at 4:00 when the Pope makes town, so I'll try to stay on schedule and not disappoint.

I know there's one thing that we all agree on in this room and that's that getting this rulemaking -- this rulemaking being position limits, and just as importantly if not more importantly, the exemption portion of that -- getting it right. So I think we all have the same objective, but what we're here -- myself and Erik, today -- to speak about is how the exchanges may be able to assist the Commission in the processing and analysis and approval of non-enumerated exemptions.

So, Erik will be presenting that in just a little bit, but I thought before we go there and get to that point it's probably important for us to take a step backwards. We talk a lot about the exchanges having experience and expertise, and I can tell you, having worked in market surveillance for 30 years, I absolutely agree with that, but I thought it would be helpful to give this Committee and the Commissioners some context as to where that expertise comes from. What do those words mean? What does experience mean? So I'm going to take a step backwards to kind of talk about it from an exchange perspective. Who are these people who are processing exemptions?

First, when we talk about the CME Group and agricultural products, we have, as you may imagine, quite a variety of agriculturals. We have the CBOT agricultural products, which have had and continue to have federal limits. So we've operated under a federal limit regime in the CBOT ags, but we also have plenty of other agricultural products, some of which will be included in the 28 core [referenced futures products] in this rulemaking; others that will not, at least initially. Those, as you can see, all have exchange-set limits, right, of a variety of types, primarily spot- and single-month.

How we process exemptions for both CBOT, those with federal limits, and CME, those without federal limits, well, I'll go through that in a bit, but, in short, the analysis that we go through is the same. The process is slightly different given the requirements under the federal rules surrounding CBOT agricultural products.

So who are these people that we talk about having experience and expertise? The exemption process is administered through the regulatory body of CME Group and that's the market regulation department. More specifically it's administered through the market surveillance area within market regulation, and that is an area that I oversee both in New York and Chicago. So who are these people?

Let's talk first a little bit about what their day-in and day-out responsibilities are. Market surveillance's primary responsibility is to deter and detect manipulation, right? The integrity of the markets is of the utmost importance, and I think that's the second thing we can all agree on today; that we all want a market free from manipulation.

But how do we get there? It's a mighty task, right? What do we do to ensure that we're able to detect potential manipulations? Well, we have a group of 56 people in market surveillance across the asset classes, that being in Chicago and New York, right? So analysts come on - the professional folks who have college degrees -- they'll come on and they'll be, after training, assigned a core product to monitor. Quite frankly, when someone gets a core product to monitor, what an analyst does, get this -- he's responsible or she's responsible for living and breathing that contract. In order to be able to detect manipulation, you have to know what manipulation is, right? In order to detect what a price anomaly is, you have to be able to understand price relationships.

So, the first thing they do is they develop a very sound understanding of the physical markets because, as we all know, whether it's hedging or futures trading it's all about relationships. Phases, right? What are those relationships? What is a signal that something may be an anomaly in that price? What is a signal that someone may be using market power in order to influence that price beyond the economics? So they develop a very sound understanding of those physical markets. But that's really only one piece of it.

Once you understand the soundness and the understanding of how those markets price, you have to understand who is in your markets. You have to understand and know and have knowledge about the participants themselves. You have to understand what is the normal -- who are your major participants? Who are your major open-interest holders? What is their normal trading activity? What are the trends? We obviously have very sophisticated tools to allow us to monitor trading activity, position holding. When do we normally see individuals, participants, roll their position? All this is part of market surveillance. So again, you're trying to detect anomalies. There may not be a price anomaly at the time, but you're trying to detect and head off [manipulation]. If we see a particular participant who may be conducting themselves out of the norm which, by the way, out of the norm isn't necessarily bad because the markets themselves are sometimes out of the norm, right? The markets move, but it's really us identifying it and then understanding it, right, that gives us the ability to, again, deter and detect.

And again, we've talked about it before - [position] accountability. It's really the same principle. In order to administer accountability, you need that same expertise. You need to be able to identify concentrations and trading patterns.

So, it's these individuals that I just talked about. These individuals who have the responsibility to ensure there's no manipulation, to be able to detect manipulation.

These very same people are the people who are processing exemptions. If you think about it, people are coming in saying I want to be bigger, right? I need a large position to hedge my business, so obviously we don't take that very lightly, so when an exemption comes in -- and I'll talk through briefly the process in a moment -- but when an exemption comes in, right, there are two things that help us really expedite the processing.

One is, I mentioned, really having knowledge of the physical markets, right? So when an exemption is coming in, we're already ahead of the game in understanding what those physical markets are so we can identify the strategy and how it fits into those physical markets, and for the most part it's likely we know the participant. They may not have needed an exemption before, but in the course of our day-to-day surveillance, we've been watching -- our analysts have been watching -- those markets and understand, you know, have they been in the markets? Have they been large? How do they generally liquidate? Are they orderly, and so forth? So again, I think that expertise really helps us -- not only accurately, and in a very sound manner -- process these. But also, it helps us do it in an expeditious manner.

And I'll talk about experience in a moment as well. But before we get into that -- Erik, again, will be presenting the idea that we collaboratively came together, us and ICE, and some market users, industry users. It's important to understand what we believe are the cornerstone points, right, so before we start talking about how a non-enumerated process will work, which I think is highly critical for us to get that down right, we've got to take a look at the enumerated hedge rules right now.

I've been doing this for 30 years and to my knowledge that list of enumerated hedges hasn't changed, all right, and as Tim talked about -- Andriesen -- earlier today, we all know the cash markets have changed. The risks associated, out there in the physical markets, have changed.

The advent of swaps, right, has changed over the last decades, right, so I think it's important at the onset for us to look at things such as anticipatory merchandising, right, and move that into the enumerated section, right, to not replace what we're going to talk about in non-enumerated land, but to get those things we know are sound -- meeting the definition of hedging -- into the enumerated section, and then we'll move forward.

And then, of course, [we'll] periodically review that enumerated list, and I think it's a good idea for us to do it more than every couple of decades or so, just kind of take a look at that and evaluate if we're approving with the right conditions and agreeing on a certain type of non-enumerated [hedge]. It's become very routine as far as the type of hedge exemptions we're getting in; let's consider whether those should be or shouldn't be placed in the enumerated section.

Secondly, when we get to the proposal, in order for us to do that, there certainly would have to be some rulemaking, I believe, so we are looking for the passage of rules that give the exchange the ability to approve these exemptions from a federal perspective. And also I think it's very important that -- if given that authority to approve our exchange exemptions and it can be applied to the federal structure -- that there's some certainty that participants get, right? When we're approving those exemptions -- while we absolutely believe the Commission has an oversight role here, right, and they can't divorce themselves from the process -- what we don't want to see happen is a day-in and day-out micro managing of the decisions we're making, right, because if that's the case, right, then I think we haven't really accomplished a lot if I and my team are evaluating a particular non-enumerated, and we feel very comfortable that it fits within that and upon sending it to the Commission a day later it's being overturned. That's not going to give anyone any comfort level.

I think there are processes in place, right. Currently there are rule enforcement reviews that are conducted on exchanges where those processes can be reviewed -- to the extent there's something that the Commission feels is egregious, which I don't believe would be the case, but to the extent that there is -- certainly there has to be a process within the Commission. But we just ask that to be kind of outlined at the onset as to what that process would be.

So we go to our current exchange exemption process, I can tell you on the agricultural side in Chicago. It's basically a three-pronged approach, so I talked about how, initially, exemptions will come in, right, and they'll be processed, reviewed, and analyzed by a market analyst. It's the analysts, generally speaking, that are on the front end of this and will have probably two-to-three years' experience, right. Once they conduct their analysis or review they will come up with a recommendation.

A recommendation has two prongs to it; one being, does the exposure meet what that applicant is asking for, and secondly, what level would they suggest that that applicant get, and the two aren't synonymous, right.

If you think about it there are some very big participants out there with very big cash books. What we do is we evaluate not only the exposure and the strategy, which obviously is very critical to make sure it fits within bona fide hedging, but we also have to look at our markets. How much can the market handle? When I say handle, we look at the liquidity profile right there in the spot month period. We'll look at the make-up of the market, the profile of the market overall, and we very well may grant a number that's lower than the exposure would justify. And we're doing that, again, to ensure that our markets -- which at the end of the day trumps everything -- that there's integrity in those markets, but also affording the ability to hedge.

What we'll then do is we'll review that number, assuming we granted a number lower than the exposure. We'll be reviewing that periodically, and as the contract grows, as open interest grows around that exemption showing the contract is being used, since the liquidity grows, and as we get comfortable that the participant who was granted [the exemption] is liquidating in a very orderly fashion within the liquidity profile of that particular product, we very may well go back, right, and increase what we had given them before. Again, provided that the exposure still supports it.

So the application will come in. The analyst will do the review, then give that recommendation to a lead analyst. A lead analyst is someone who overseas that asset class, so in agricultural we're talking about either CBOT ags or CME ags. That lead analyst has usually five to seven years' experience, and they've already been in that analyst role conducting those reviews. So they'll review it. She may agree. She may send it back for more work, or she may disagree.

If she agrees, right, that will then go to the regional heads in Chicago; that's a senior director, so someone with over 10 years' experience who will then make the final determination and send out either an approval letter, a denial letter, or a modification; a modification, again, would be capping it at something below the exposure itself.

The one thing I want to leave this Committee with and the Commission with is something I said earlier on. While this application process is an annual process, once we approve an application it's not a one-and-done, see you in a year, right. We approve these applications, and then we conduct surveillance, right. When someone gets an approval of an exemption, to me it's a contract, right.

They have responsibilities; the

responsibility might be to be hedging. There are responsibilities to act in an orderly and a commercial fashion and to be liquidating and initiating those positions orderly. To the degree we see that the obligation is not being fulfilled, right, we have the ability on the spot to order -- similar to accountability -- order a reduction in that position. We have the ability to say stop growing that position.

And we may do that even if they are being orderly if we see the market around them in a situation such that we don't think the market can handle it, so we have very powerful tools once we grant an exemption as to monitoring the effect of this or that, monitoring the markets, identifying potential anomalies in the pricing, and if need be, either revoke an application or temporarily halt it while we monitor those market situations.

So, with that I'll turn it over to Erik to talk about the idea that we have collaboratively worked on.

MR. HAAS: Thanks, Joe. So this process for non-enumerated exemptions really stems from the EEMAC, the last meeting of the Energy and Environmental Markets Advisory Committee in July. Tom LaSala of CME, Ron Oppenheimer of the working group, and I presented this idea and I'll note that this is one proposal. We've heard others. This is one idea that both ICE and CME can get behind. We think it's workable in all areas and that's why it's the one we're presenting now.

By and large this process would allow the exchanges to continue leveraging their extensive surveillance procedures and practices and apply that to non-enumerated exemptions. We'll start with saying that the application and exchange review process -- what it comes to in this idea -- it wouldn't change from the current process very much.

You're going to fill out an application. You're going to come to the exchange, tell us what your strategy is, what your exposure underlying that strategy is, and you're still going to need to request an exemption level.

On the exchange side, through our market surveillance practices, the same ones that Joe discussed, we will review the strategy to make sure it meets the criteria for hedging. We'll look at the underlying exposure and make a determination on -- I guess what I would say is -- what's the justifiable exposure. That is, someone might come to us and say, explain their strategy, tell us they have 10,000 lots of exposure. We'll look at it and see if we feel that all 10,000 lots really meet the strategy, so I guess we'll call that the justifiable exposure. We'll make a determination on what that exposure is, and then the third part, which is similar for the enumerated process -- we'll make a determination on what exemption level should be granted based on that exposure and that could be less than your exposure. And we'll look at market conditions, the size of the company, for certain products the stock for deliverable products, and try to ensure that no one market participant, whether you're commercial or not, can exert influence in the market. Again, that process would not differ greatly from the existing exemption process.

What this does bring in is the idea that a hedger that's granted an exemption from the exchange for a non-enumerated strategy, as opposed to through a CFTC rule, will be able to rely on the exchange exemption for that non-enumerated strategy -- to base their OTC hedging off of. And that's getting, again, into this non-enumerated section, which is a little different from the current process, but we believe that if we're going to review this non-enumerated strategy and make a determination on the exposure and whether it qualifies - to alleviate, I guess, another burden from this overall process - it would [have to] be that this hedger could then rely on our determination that this is a legitimate hedging strategy under a non-enumerated rule and they could rely on our approval for OTC or swaps hedging if so be it.

And then finally, the other idea that we think would need to come out of this would be that the exchanges would submit to the Commission all of our approvals and determinations for non-enumerated strategies. It would have to be done on a timely basis just to ensure the Commission is working with the freshest data from exchanges or any other SEF that's granting non-enumerated exemptions.

With this, the Commission then maintains the responsibility for ongoing surveillance of federal limit and the OTC markets, but what we've accomplished is the exchanges have used our expertise to make a determination. We've kind of done the leg work of weeding out the non-enumerated exemption application, determining whether it's legitimate, what the underlying exposure should be, and that, as we provide this information to the Commission, it aids in the Commission's responsibility for overseeing a federal limit and OTC exposure because they know what we've determined is the justifiable exposure, and they can compare any entity's position verse the level we've determined.

With this, too -- because non-enumerated exemptions can be one-off and we'd like to -- once we make a determination on allowing a non-enumerated strategy, we feel the transparency of that - the general nature of that strategy is important, so we would agree to post on our website the general nature of non-enumerated strategies that we've granted. There would be no identifying information based on anyone who received it, but just letting the market, the Commission, know types of -- the general natures of strategies that we've granted under this. Exchanges -- we would agree to try and classify those strategies similarly so that it's clear to everyone what's been approved and so other folks could rely on that same type of exemption.

And again, it falls into the final point here is that we believe the Commission obviously has its obligation to review the market, but also their oversight of the exchanges through this process -- they can come to us at any time or through the rule enforcement review process to review any approvals or denials that we've made, check our work, communicate across exchanges. They can oversee this whole process and help give guidance where it's needed.

Moving on, I guess, from the non-enumerated discussion is a point we want to emphasize about a one-size-fits-all approach to limits. I think it's been mentioned a few times. It's been mentioned at other committee meetings and, specifically for ICE, we'd like to note the accountability versus levels an all-months limits concept, again, and note that single and all-month accountability levels allow the market surveillance departments and processes to really manage and review large positions. Accountability rules can be more effective at times than limits given that accountability levels give the exchange an easy way to force the market participants to either liquidate or hold their position.

Without accountability, if it's just under the position limit rule, as it is, exchanges would have a much longer process to get a participant to automatically decrease. Accountability gives us more flexibility to work with that person on managing the expectations of their position, and the data that we've seen shows accountability is an effective tool and oftentimes can be more effective than single and all month limits out the curve.

Just touching on the ICE futures U.S. products, cotton has federal limits. The rest of our products all have spot month exchange limits. OJ and sugar are domestic products and they'll have single and all month limits, but cocoa, coffee, and sugar are international commodities and, per Commission rule, have had single and all month accountability levels for over a decade, and what we'd like to point out is that cocoa, which has a spot month limit, but out the curve, has single and all month accountability levels. What we have here is that the price graph for the prompt month futures contract over the past five years. Price has gone up four percent and the red reflects the day-to-day settlement price percentage change, and so during this period the average change per day is one percent, so you can have one percent change from prior day settle to the next day's settlement, and the vast majority of these changes falling between plus or minus four percent on a daily basis, so not extremely volatile. You don't see wide changes on a daily basis.

Cotton is an enumerated product. It has federal spot month, federal single, federal all month limits. It also has exchange-set spot-, single-, and all-months limits and cotton has daily price limits which lock in the -- the minimum/maximum that the price can move on any given day. Cocoa does not have that, but during that same time period, while the price of cotton has been down 24 percent, the average settlement change is one percent with the vast majority falling between plus or minus four percent.

So, the point we're really trying to make here is that with a set of products that don't have single and all month limits that have been managed through a market surveillance standpoint with accountability levels -- we have other products that have had single and all month limits for that same period - when you look at the trend in prices and settlement changes the two sets of products are indistinguishable.

The international softs which all have these single- and all-month accountability levels, which we would hope to maintain, do not exhibit the symptoms that single- and all-month limit are intended to protect. Implementing them would be a solution to a non-existent problem in these products. Again, we don't think a one-size-fits-all approach is appropriate for any markets, whether in-between asset classes or certain products in asset classes, and by implementing single and all-month limits, what we hope doesn't occur, but what we fear might occur, is that the people that we're going to force out of the market are the ones providing both price stability out the curve and liquidity, and doing so is only going to harm the market. That's our presentation. [I'm] happy to answer any questions.

MR. FORTENBERY: Thank you, panel. Questions or comments? Yes, sir.

MR. KOTSCHWAR: So, CMC is fully supportive, Mr. Chairman, of having the SRO, you know, the exchanges in their SRO capacity, handle this non-enumerated hedge function, and I think what Joe talked about is one of the biggest policy reasons why, which is, they don't just look at my company's application for a hedge exemption. They look at it in the context of the operation of their market. They're not always going to give me what I ask for, and so they're looking at it holistically, and I think it makes really good policy sense for them to keep this activity there.

MR. DIERLAM: I would concur. I would concur, as well, and I think that Joe, as well, made another comment, as well, that I think is important to be mindful of, and that's where the focus of the presentation, I think, was -- a process for non-enumerated hedges. One component of Joe's comment was getting the list of enumerated hedges right as well. And so I appreciate Joe's comments, both Joe and Erik's comments, in both regards. Number one is getting the list of enumerated hedges right in the first instance and then a good solid process on non-enumerated hedges, together, for the reasons that they spoke about and I also concur with Lance's comments.

MR. GALLAGHER: Joe, you were here earlier when I asked Tim a question. He punted it to you, so I'll ask again. If it gets back to if it was a series of swap transactions that were to hedge, as opposed to any futures or options that would be traded on your exchange, would you still be the entity that would determine whether that meets a non-enumerated hedge?

MR. HAWRYSZ: Right, and thank you for the preview of the question at the first panel. The proposal that we're outlining here would put that decision-making and that process -- continue to keep it within the exchange, right. Well, you've talked about if it were to occur -- if you're asking for -- in today's world in corn, right, you would go to the Commission for approval and not until you got that approval from the Commission could the exchanges review it and make a determination. We're talking that same thing in dairy, right, or in cattle for the non-enumerated [hedges].

Today we have the ability to evaluate everything I've said and approve it and with this proposal, or at least this idea, we would continue to do that, right, and even today the Commission ultimately will always have -- I mean they have a very unwritten role and that's oversight of the DCM and the SRO, right -- so they always have the ability through, you know, rule enforcement reviews or one-offs, again, if they feel very strongly about it to come back to us. But by and large that hasn't happened. I think it hasn't happened because, again, of the thoughtfulness and the thoroughness of what we do, and I think some in this room know what you -- I don't want to say it in a bad way -- what you go through, right, to get an exemption. It's not, as Brian mentioned, it's not send an application, look at numbers, and here's your approval. There's dialogue that goes on.

MR. GALLAGHER: So back to the other part of the question I had asked was...so if there are hedges that we do now that for whatever reason won't be enumerated -- that we're going to go pretty quickly before this thing gets implemented -- and ask you to opine on them and see if they would be non-enumerated.

But things will come up over time that we haven't thought of yet that we're going to come to you. How - can you give us some sort of sense -- how quickly you may be able to get through a decision-making process?

MR. HAWRYSZ: Sure, and I agree. I mean non-enumerated [hedges] are always going to exist. They have to exist, right, because it's impossible to foresee the future. It's impossible to foresee every single situation. You can't list those all out, so to the degree that would happen -- I guess I'll answer it this way, all right. There's a bunch of factors that go into it, right, but let's look at it in a vacuum. Let's say you're the only one that comes to me in dairy so we'll talk a one-off. Obviously if everyone in this room comes to me on the same day, the number is going to change from a pure resource perspective. But, to the degree you come to us, we will by and large interact with you because it may be something new and unique which is why it's coming to us. There will be some dialogue back and forth. I would say within probably a couple of days -- assuming there's no miscommunications, right, assuming we get the information that we've asked for -- that we can make that determination, but I will preface it by saying again, it all depends on how many are in at any given point in time where that two days, you know, you might be two days and if you're like the tenth person in, in the same asset class, it obviously can stretch out.

MR. WESTON: I wanted to basically concur with Lance and Brian, and want to thank you for your presentation, both of you. I think that was very helpful. I know, Chairman, at the beginning you made some comments on this panel, and I would like to thank you and the other commissioners for conducting this. This has been something that's been important to the sugar industry. Some of you have met with David Perlman and some of my member companies. I appreciate your time doing that. We've been concerned that if we go forward with the delegation to the exchanges -- that to then have the extra burden of regulation on the hedging side -- that was going to be something where we might actually have extra regulation added to us.

I would say on the sugar side we are an interesting product. We have the farmers and then the farmers own the mills and refineries pretty much all the way through, so we're the producer group and we're the agri-business side of the group, so our work goes all the way through from the crop to the white sugar you see either in a product or being sold to all the companies that use our product, so we go past the traditional 12-month period. When you plant sugar cane you're going to have a crop for at least three more years, maybe four or five, so we're in that for the long haul.

We don't do hedges that are not bona fide -- we're not speculators. We're in the business, so this is something, I think -- as we look at the presentation such as this -- this is very helpful, and if we ever have to answer any more detailed questions we'd be happy -- David, I could come in and if -- I know you guys have traveled around. We'd be happy to have any of you or your staff come to any of our mills down in Florida, if you have meetings down there. We start harvest in November and we'll basically go through March.

MR. MAY: Thank you. Just a few comments from the cotton-trading community. The Dodd-Frank Act required the CFTC to adopt positon limits on an expanded scope of futures contracts as well as economically equivalent swap contracts, if needed to prevent excessive speculation. This is generally an exercise that our members supported during the Dodd-Frank debate. However, proposals to date have included provisions that would restrict the hedging activities of commercial end-users, such as my members.

We do not think that result was, in any way, intended by the Congress. We've written multiple comments letters to this effect and our members have testified before the Commission and the Congress on these points. It is extremely important that the Commission modify its proposal to allow hedgers to hedge, and we are hopeful that these points are recognized prior to the rule finalization. The consequences of not making the necessary changes are all bad. Hedging programs are responsible risk-management initiatives that can give producers better prices for their crops and consumers better prices for finished goods.

MR. GALLAGHER: I'd ask a little more

dialogue on one part of your proposal. It says "exchange maintains responsibility for ongoing surveillance on its market, but CFTC takes responsibility for OTC monitoring and for federal limits." Can you talk to us a little bit more about why you decided to have the CFTC do the monitoring on the OTC stuff as opposed to the exchanges doing the monitoring?

MR. HAWRYSZ: I guess the answer is pretty straightforward in that we don't see the OTC positions. The Commission is the only one who'll see all the OTC because of all the stuff's out there, so we don't -- we wouldn't even have the ability -- as we do in the futures, right, we see everything. We can review what's on our exchange. We just don't have the data on the OTC side.

MR. GALLAGHER: So I don't know who I could fairly ask this question to but maybe Mark, maybe. Are you guys -- are you -- I don't - just because you're on staff. Are you guys set up to be able to do the monitoring of something like dairy?

MR. FAJFAR: Yes, but it's -- Frank, that's not my -- I'm not (inaudible).

MR. GALLAGHER: Yes, okay. So not a fair question for you either?

MR. MASSAD: It's a good question. I think where we are today is a follow-on. We have two dozen SEFs. The law has language about them adopting position limits. The data on what's happening on each SEF is being reported to a swap-data repository. We still have a lot of work to do, I think, to have an overall data-reporting regime that gets us to where we want to be. I often talk about this issue and think of it kind of like a big infrastructure project. You can't just write some rules and expect us to go from zero reporting on the OTC swap market to a perfect system where we can look at exactly what we want and measure it instantly. We're talking about creating a data-reporting system that involves lots of participants, lots of different contracts, but I think what we as a commission have to think about is how do you integrate monitoring the SEFs with monitoring the exchanges, and that's going to be some combination of what an individual SEF can do and perhaps what we see in the SDR data.

MR. FORTENBERY: Let me just check in and see if we have any questions or comments from remotely connected members. Okay, go ahead.

MR. STRONG: Joe or Erik, a little more color on the comment that Ed was talking about on page nine about publishing the approvals on our website? How detailed?

MR. HAWRYSZ: Well, certainly we would not be publishing names. We would not be publishing company names, and it's an excellent question, right, and we've talked a lot about that. We would publish it in a manner that wasn't detailed enough to, kind of, disclose proprietary strategies. So for example it might be a storage hedge or it may be a cross hedge, but it would be, I'll say, more generically like that. And when that's on the website, you know, as a user, a participant, it wouldn't mean -- it doesn't mean it's enumerated. Alright, you would still have to come to us for an application, but it would at least give some transparency to -- okay, they are approving types like this, cross hedges, anticipatory merchandising, if it unfortunately doesn't get enumerated, right -- then you would come to us. So yes, we would not be disclosing participant names, and we would also be very, very careful, you know, not to disclose any detail that would make transparent proprietary information.

MR. CORDES: It's a little bit of a pile on to Lance and everyone else, but we've been pretty outspoken about the bona fide hedge. I think the ability to take a look at what is an enumerated hedge has opportunity to solve a lot of our heartburn to -- easier said than done and it'll probably require some elegance, but I think that has the potential to -- be a good solution.

MR. FORTENBERY: Any other questions or comments related to the position limit presentations?

MR. WESTON: I would just like to note

that it's nice to see that the farm side and the agri-business side are actually agreeing on something. This is a very important issue for most of us to deal with, you know. Any new regulation could be burdensome, and this is a very important thing to make sure we get the best price we can in a very tough market. As I think a couple of you noted in your opening statements, it's going to be a pretty rough couple of years possibly for farmers.

MR. M. J. ANDERSON: May be expected but any kind of timeline or timeframe?

MR. MASSAD: We haven't made a decision on whether we would go forward with this. Something we're thinking about. Meetings like this are very helpful to get input so that we can reflect on that and we'll be thinking about it. Staff is thinking about it in the days ahead.

MR. FORTENBERY: Anything else on this topic? Go ahead, yeah.

MR. OWEN: Excuse me. I would just caution the Commissioners about the unintended consequences of over- regulation. And if it becomes more difficult to obtain hedging exemptions, I'm afraid you're going to slow things down, you're going to take us potentially down the road. As a farmer, the worst thing that can happen is the market dries up -- there's not a bid, or if the commercial cannot transfer risk through the futures market. The only way [the farmer] is going to be able to transfer [risk] is through basis and that comes down to the farmer, and that really harms me.

And also if you have basis that becomes way out of line with the futures market, then people begin to lose confidence in the futures contract. I work with rice. We have a very thinly traded contract. In the past I can remember when basis was 20 percent of the value of the underlying contract, and it's difficult to get any volume in that situation because there's so much risk. You have basis risk that's unacceptable, so you move toward a cash market. So I would ask that you move cautiously towards anything that would possibly hurt market liquidity, and I'm very confident in CME's ability to grant hedging exemptions. I think they've done a good job in the past, and I think they will do so in the future. Thank you.

MR. FORTENBERY: Any other questions or comments? So, if you look at the agenda the last item for discussion is new business and/or any comments you might have about other panels that we had earlier today.

I just want to make a couple points though. I was handed a note that suggests that I remind you that today might be a high-traffic volume day; that I guess they're going to shut down 395 in both directions starting, I guess, 1:00 p.m. it says. So I guess that's already happened. Is that right? Do I have that right?

MR. CLAUSSEN: Yes, it was just going to be from -- I got word that it was going to be -- from 14th Street to Anacostia Bridge which actually isn't that big of a stretch, but just as a reminder there are a few folks who had to get flights, so there's really no need to rush out, but we just wanted to give people an opportunity to leave without feeling bad about it.

MR. FORTENBERY: Right, so we don't want to encourage you to leave, but we don't want to have you miss your flight either if it looks like it's cutting it close. So, I guess I'll ask are there new business items that you would like to discuss? Would anybody want to circle back around some of the panel discussion we had earlier today before we adjourn?

MR. DIERLAM: I thought I might just add a couple comments. Layne from the Minneapolis Grain Exchange mentioned earlier the issue of equivalency -- I think he used the word parity -- between the various wheat contracts. and I would just note I tried to look up a list so I could have the list for you, but I would just note that a number of industry groups -- I know the CMC; I'm not certain about NGFA, but okay, I'm getting nod now, NGFA; I know Cargill did -- many industry groups in their comments did comment about the need for equivalency or parity between the wheat contracts, so I'll just note that that should be clearly communicated in the comments that were received on that issue. There should be plenty of comments in support for that -- for the position -- that he spoke about today.

MR. JOHN ANDERSON: Yeah, I don't know if this is new business or if this is circling back to the FCM discussion or maybe a little bit of both, but we talked a lot in that discussion of market trends about customer protections, and I guess my question is, or the general issue that I want to raise is, what is CFTC doing? Or maybe [what] can CFTC do to help with monitoring of customer protections? We have these new rules and we've talked about the costs associated with those. What are we getting for that cost and how effective are these new processes and new rules working out to be, and so I'll raise that as maybe an issue that we might come back around to at a future meeting, but any guidance I think the CFTC can give us on how effective these customer protections are and what kind of oversight is CFTC involved in to ensure that these new customer protections are actually being effective given both the new rules that we have in place and the changing structure of that market, I think, would be a really important issue for us to look at.

MR. MASSAD: I think that's a very good topic, and I could certainly spend more time on it at a future meeting. Let me just note one example though. We had a discussion earlier that touched on the segregation rules regarding customer funds. The procedures that have been put in place today require not only looking at what the clearing member says but we also get daily confirmation I believe from the depository of what the amount of segregated funds is so that we reconcile what the depository is saying with what the clearing member is saying. We work with the NFA on that. That's a quantum leap from where we were before.

MR. KADLEC: Yes, I would concur. If we're one minute late on sending our seg in to the exchange and to the CFTC we get calls, and it's not a pretty picture. I think the -- at most FCMs, at least at our FCM -- we had eight different eyes and six different officers monitoring seg on a daily basis. That can only help the process, and I think the third party -- it's important to note that there's independent verification of the Chairman's comments. They have data from all of our depositories, and that is confirmed on a daily basis. That is very, very high standard and there's no other industry that I believe that has as high a standard as far as monitoring. I'd also say that I sit on the CME Clearinghouse Committee, and we monitor that. It's part of every audit, and there's no FCM that would want to be walked in front of that committee and have any type of seg violations. The fines are very high, and the perception of industry standing is a very -- we just -- FCMs do not want to go there, and I think that's critically important.

MR. FORTENBERY: Any other comments or suggestions?

MR. MASSAD: Let me just say thanks again to everyone for being here. This has been a very, very helpful and informative session. We really appreciate you traveling in, for those of you that traveled in, and want to get you out so you get your planes on time. Thanks.

MR. FORTENBERY: Let me just check in one more time with the remote. Okay, at this point I'll adjourn the 38th meeting of the Ag Advisory Council. Thank you for traveling and travel safely home.

(Whereupon, at 3:56 p.m., the PROCEEDINGS were adjourned.)

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CERTIFICATE OF NOTARY PUBLIC

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I, Carleton J. Anderson, III, notary public in and for the District of Columbia, do hereby certify that the forgoing PROCEEDING was duly recorded and thereafter reduced to print under my direction; that the witnesses were sworn to tell the truth under penalty of perjury; that said transcript is a true record of the testimony given by witnesses; that I am neither counsel for, related to, nor employed by any of the parties to the action in which this proceeding was called; and, furthermore, that I am not a relative or employee of any attorney or counsel employed by the parties hereto, nor financially or otherwise interested in the outcome of this action.

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