FarmPolicy.com Interview with House Agriculture Committee Chairman Collin Peterson- Financial Reform Bill July 1, 2010

Q: In the fall of 2008, the U.S. faced the biggest financial crisis since the Great Depression. Nearly two years later, it appears that Congress will pass a financial reform bill that seeks to address some of the shortfalls that led to this near disaster. As I look at the record of congressional activity, it appears that you were the first in Congress to take legislative action. Shortly after the crisis began to unfold, back in July of '08, you introduced a reform bill that sought to bring greater transparency to commodity markets.

A bill passed the full House in September of '08, but was never acted on by the Senate. That set the stage for the new legislation that you reported from your committee in February of 2009, which was eventually incorporated in the Financial Services Committee and passed the House in December of 2009. With that background in mind, my question is why were you so far ahead of the rest of Congress in pushing for reform legislation?

A: Well, I don't know. Well, we had jurisdiction in the area that first got on people's radar screen, and that was a couple of things. One was the situation that happened in the cotton market, where we had a bunch of money come into the market and the market got fouled up. And then with the oil prices going up the summer of '08, and at the time that was going on, at the peak of that, we ended up having 70% of the money in the oil market was long only financial money that was not intended, was never going to buy any oil. And so we got to looking at the hedge exemption that was given by the CFTC to allow these index funds and others to get into these markets without the normal speculation limits that are applied to everybody else.

And so that's what got us looking into this in the first place. And then, you know, as part of that process, I was educated. Other members were educated about some of these other issues that we came to believe were partly responsible for the financial problems that we ran into. So I guess the fact that we got to looking into these markets and spending a lot of time studying this, we probably were a little ahead of the curve, maybe more knowledgeable, and understood what had happened before other people understood. And so that background led us to put a more comprehensive bill together and move that in early 2009.

Q: More specifically with respect to the legislation, how did the legislation seek to remedy some of those root causes of the financial meltdown, some of the things that you outlined there?

A: Okay, well, in the speculation, what we did, and what is in this bill that passed the House, you know, was part of what was, at the time, HR 977, we will eliminate the hedge exemption for these big index funds and hedge funds and so forth, and they're going to be…there's going to be position limits applied to them, so that is how that part of it was dealt with.

We're also going to require that all of the over-the-counter market has to be reported to the regulators, which was not done before. And we put in new definitions on who is a major swap participant, major swap dealers, which are the primary folks that are in this market, and require that there be margins and collateral placed on any of these swaps that are done by major swap participants and dealers so that… You know, the easy way to say that is that they're going to have to put up money to stand behind the deals that is adequate in case the deal turns out to be a risky situation.

And we…you know, we're trying to make most of these swaps go through clearinghouses. Now, they won't all be able to be cleared because some of them are very customized swaps, but the whole incentive of the system is to push things towards clearing. And at the end of the compromise, some things that are built into the system, it'll be actually cheaper to do business if it's cleared than if it isn't cleared. So we're trying to get as many of these swaps through the clearing process as possible, which mitigates the risk, and make all of it transparent. And if it's not cleared, then the CFTC and the SEC has the authority to put margin and capital requirements on these major swap positions with the dealers that are involved in this.

Q: You've outlined the specific legislative remedies. What kind of resistance did you encounter to some of those proposals along the way?

A: Well, along the way, because we had defined these dealers and participants, their people that were physically hedging became concerned that they might get caught up in this and that they would be required to put up cash, you know, margin and capital, which was contrary to what they normally do. And so we did carve out exemptions for people that are using these markets for physical hedging, which are basically the ag folks, energy, people that are using these markets for the right reasons and not all of these derivatives and, in a lot of cases, in my opinion, gambling that was going on.

So we carved out exemptions that said if you're using…you know, these people didn't cause any of this problem, and if you're using some other type of collateral, that is permissible under this legislation. So in the case of ag, they're probably using the ag products as a backup. In the case of energy, they're using future oil, they're using oil wells or oil finds that they have as collateral. In the case of electricity, they're using the future electric revenue where they have contracts that they can rely on and so forth.

But in that process, we found the big Wall Street firms that are generally the counterparties in these transactions, they tried, right up to the end, to get an exemption for their side of the transaction. [*Laughs*.] You know, I think what happened is they went to the physical hedges and said, well, if we have to start putting money up for our side of this, then we're going to have to charge you more. And so they had the physical hedgers coming and trying to get an additional exemption from the major swap participant language, which I did not agree to. Because the risk is in these big guys that are doing the majority of the stuff, and I was not about to give them an exemption. That's what got us into this problem on the speculation issue in the first place, so…

So there was heavy lobbying going on right up to the end, I mean, up to 5:30 in the morning on the day we set it out. And then when they had to go in and change the [pay fors], I must have had 15 members come up to me with amendments that they were trying to get me to bring into the conference committee, mostly to try to get the big Wall Street guys additional exemptions.

Q: And that was last Friday, right, the 25^{th}?

A: Right.

Q: The night of the 24^{th}, I guess, into the morning?

A: Right.

Q: The new law will be aggressively implemented -- I mean, do you feel that the new law will be aggressively implemented? It seems like a great deal of discretion is going to be left to regulators. What's your thoughts on that?

A: Yeah. Well, yeah, and we debated that. And frankly, we just felt we didn't have the expertise or the time. I mean, you know, it just wouldn't have been smart to try to put some of this stuff in [statute] in terms of what level of margin should be, and capital, and so forth, so we really didn't have any choice but to leave it to the regulators in a lot of those cases. I just got off the phone with Chairman Gensler, and he was calling to thank me for working through this with them and Treasury, and so forth.

And we talked about this very thing, about the rule making and regulations, and it's going to be a huge amount of work here to get this in place. And I told him and warned him that we will be doing extremely aggressive oversight over that process, and we will be meeting on a regular basis to oversee that process and to oversee the decisions that are made to make sure that we make that the risks are being adequately mitigated in whatever they finally come up with.

And that was, frankly, one of our faults, in my opinion, on the Ag Committee. The CFMA, at the time we passed that, it was conventional wisdom on everybody's part -- Greenspan and Rubin and Summers, and everybody that was involved, except for Brooksly Born were saying that this was the right thing to do.

These are a bunch of rich people and then have $10 million minimum to get into this business and so they're just dealing their own money, and it's nobody's business what they're up to.

And that was the arguments, and we didn't do any oversight over what was going on. And of course I wasn't, you know, we were in the minority at that time. That was a mistake. And I can guarantee you that will not happen going forward. Gensler is going to be very aggressive in moving these regulations through the process. We will be on top of that every step of the way, and that's the way it should be.

Q: Well, as you noted, the bill did pass the House yesterday and is now, I guess, awaiting Senate action, which is forthcoming, I think, after the break, is that your understanding?

A: Yeah.

Q: Well, very good. I know it's been a very busy week, and I certainly appreciate you making time to speak with me. It's a very interesting conversation, and thank you very much.

A: All right, thank you.

Q: Bye-bye.

A: Yeah, see ya.

[*End of recording.*]