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Textualism Gone Astray: A Reply to Norris, Davison, and May on Hedge to Arrive Contracts

by

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TEXTUALISM GONE ASTRAY: A REPLY TO NORRIS, DAVISON, AND MAY ON HEDGE TO ARRIVE CONTRACTS

*Edward M. Mansfield**

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I. INTRODUCTION

In their recent well-written article,[1] Glenn L. Norris, George F. Davison, Jr., and David N. May criticize decisions that have placed "Hedge to Arrive" (HTA) contracts between farmers and grain elevators within the "cash forward" exclusion of the Commodity Exchange Act (CEA).[2] Their concern is not purely academic. Since 1996, their firm has ably represented many farmers in HTA contract disputes. Norris and his colleagues have sought repeatedly to have these

* Member, Belin Lamson McCormick Zumbach Flynn, Des Moines, Iowa; B.A., 1978, Harvard; J.D., 1982, Yale. The author represents several grain elevators in HTA contract disputes and litigation. The views expressed in this Article are solely those of the author.

1. Glenn L. Norris et al., *Hedge to Arrive Contracts and the Commodity Exchange Act: A Textual Alternative*, 47 DRAKE L. REV. 319 (1999).

2. Andersons, Inc. v. Horton Farms, Inc., 166 F.3d 308, 322 (6th Cir. 1998); Lachmund v. ADM Investor Servs., Inc., 26 F. Supp. 2d 1107, 1119 (N.D. Ind. 1998); Johnson v. Land O' Lakes, Inc., 18 F. Supp. 2d 985, 996-97 (N.D. Iowa 1998); Barz v. Geneva Elevator Co., 12 F. Supp. 2d 943, 954-57 (N.D. Iowa 1998); Top of Iowa Coop. v. Schewe, 6 F. Supp. 2d 843, 858 (N.D. Iowa 1998); Oeltjenbrun v. CSA Investors, Inc., 3 F. Supp. 2d 1024, 1044-45 (N.D. Iowa 1998); Andersons, Inc. v. Crotser, 7 F. Supp. 2d 931, 933-36 (W.D. Mich. 1998); *In re* Grain Land Coop., 978 F. Supp. 1267, 1273 (D. Minn. 1997). *But see* Eby v. Producers Co-op, Inc., 959 F. Supp. 428, 433 (W.D. Mich. 1997) (denying a motion to dismiss an illegality claim).

contracts declared illegal under the CEA, so far without great success in the federal courts.[3] But their arguments are serious and deserve a serious response.

Norris and his colleagues make three basic points. First, they contend that recent decisions have erred in upholding HTA contracts based on the cash forward exclusion.[4] Second, they maintain that the current "erroneous" view of the exclusion stems from the 1982 decision by the Ninth Circuit in *Commodity Futures Trading Commission v. Co Petro Marketing Group, Inc.*,[5] which dissected the legislative history of the exclusion.[6] Norris and his colleagues argue that *Co Petro* "infected the DNA" of later decisions with its conclusion that "'a cash forward contract is one in which the parties contemplate physical transfer of the actual commodity.'"[7] Third, and most importantly, Norris and his colleagues advance a "textual alternative" to the delivery-based analysis in *Co Petro*.[8] Under their "textual alternative," only "sales" under Article 2 of the Uniform Commercial Code (UCC) could qualify for the cash forward exclusion.[9] In their view, this would limit lawful HTA contracts to the circumstances where the farmer had already planted the crop at the time of contracting.[10]

While perhaps superficially appealing, Norris and his colleagues' analysis is simply wrong. As this Reply will show, their textual exegesis is unsound and unconvincing, ignoring provisions of both the CEA and the UCC. Furthermore, their criticisms of *Co Petro* are misplaced because that decision did not stake out new ground but, instead, correctly interpreted both the legislative history and the policies behind the cash forward exemption. Finally, Norris and his colleagues' criticisms of recent decisions upholding the legality of HTA contracts are unjustified. Failing to do justice to the thoroughness of many of these opinions, they attack a strawman when they suggest that these decisions have turned solely on whether the HTA contract contained an obligation to deliver.

Ultimately, the Norris Article is a case study in textualism gone astray. Far from being true textualism, their Article is an effort to shoehorn mismatched legal definitions from one statute into another, while disregarding the very different purposes of each statute. The result of this misguided breeding attempt

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3. Norris and his colleagues are counsel of record for the farmers in the *Johnson* and *Barz* cases. Johnson v. Land O' Lakes, Inc., 18 F. Supp. 2d at 988; Barz v. Geneva Elevator Co., 12 F. Supp. 2d at 945.

4. *See* Norris et al., *supra* note 1, at 328-30.

5. Commodity Futures Trading Comm'n v. Co Petro Mktg. Group, Inc., 680 F.2d 573 (9th Cir. 1982).

6. *Id.* at 579-82.

7. *See* Norris et al., *supra* note 1, at 330-34 (quoting Commodity Futures Trading Comm'n v. Co Petro Mktg. Group, Inc., 680 F.2d at 578).

8. *Id.* at 334-40.

9. *Id.* at 336-40.

10. *Id.* at 339-40.

is, unsurprisingly, a *reductio ad absurdum* in itself. This Reply will discuss the flaws in Norris and his colleagues' analysis, and then close by urging a textual approach that is far more consistent with the language, the legislative history, and the policies and economics of the CEA. This approach focuses on whether the transaction involves "cash grain" (*i.e.*, actual grain) rather than on technical questions of whether the transaction is a "sale" under the UCC.

II. THE HTA CONTRACT CONTROVERSY

The CEA regulates "contract[s] for the purchase or sale of a commodity for future delivery,"[11] commonly known as "futures contracts." Essentially, the Act provides that these contracts must be executed on a board of trade by members of that board.[12] The stringency of this rule, however, is mitigated by the so-called "cash forward" exclusion, which provides that "[t]he term 'future delivery' does not include any sale of any cash commodity for deferred shipment or delivery."[13]

In the 1990s, HTA contracts became a popular way for some farmers to market their grain to elevators. As Norris and his colleagues correctly point out, certain HTA contracts contained only a tentative delivery date, with a corresponding ability of the farmer to "roll" the contract and thereby postpone delivery to the elevator.[14] Rolls typically resulted in a change to the contract price. In some cases, farmers entered into HTA contracts expecting to deliver on those contracts out of a future year's crop that had not yet been planted at the time of contracting.[15]

In the first half of 1996, current corn prices rose dramatically to historically unprecedented levels, providing an economic incentive for farmers not to deliver on HTA contracts that they had entered into in 1995 or earlier. Meanwhile, elevators, which had hedged these contracts by selling corn futures on the Chicago Board of Trade, found that they had to make substantial margin deposits in their futures accounts. These tensions led to disputes and ultimately litigation.[16] Typically, in HTA contract litigation, the elevators have alleged that the farmers

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11. Commodity Exchange Act, 7 U.S.C. § 6(a) (1994).

12. *Id.* § 6(a)(2).

13. *Id.* § 1a(11).

14. Norris et al., *supra* note 1, at 322-23.

15. *Id.* Norris and his colleagues are correct that generalizations about HTA contracts may or may not apply to a particular case. *Id.* at 322. For another helpful summary of the salient features of HTA contracts, which also acknowledges the existence of differences among these contracts, see Erik Asklesen, *Hedge-to-Arrive Contracts and the Commodity Exchange Act*, 7 KAN. J.L. & PUB. POL'Y, SPRING 1998 NO. II, at 122, 123-25.

16. For a similar, but more detailed, summary of the circumstances leading to the present controversy see Asklesen, *supra* note 15, at 125-26.

repudiated their contracts, while the farmers have defended on the ground that the contracts are illegal.

Hence, in HTA contract litigation, a fighting issue between farmers and elevators has been whether HTA contracts, which the parties entered into and which the farmers now want to invalidate, are "sale[s] of any cash commodity for deferred shipment or delivery" and, thus, exempt from CEA requirements.[17]

III. TEXTUAL FLAWS IN THE "TEXTUAL ALTERNATIVE"

Norris and his colleagues argue that the language "sale of any cash commodity for deferred shipment or delivery"[18]—perhaps less than clear at first glance[19]—was actually intended to draw a sharp legal distinction between "sales" and "contracts to sell."[20] That is, so-called "sales"—where title passes at the time of transaction—are exempt cash forward transactions, but "contracts to sell" are not. Their argument, however, falls apart on textual grounds, even before considering its flaws in other areas.

First, the CEA expressly rejects this distinction. According to another provision of the CEA, never mentioned by Norris and his colleagues in their Article, "[t]he term 'contract of sale' includes sales, agreements of sale, and agreements to sell."[21] But because a "contract of sale" is at least technically the same thing as a "sale,"[22] this means that "sales" include "contracts to sell." At a minimum, it would be difficult to argue that Congress intended to make a neat legal distinction between the two. The logical conclusion, rather, is that Congress meant to avoid legalistic line-drawing between various forms of delivery contracts for commodities.[23] Over forty years ago, a court of appeals adopted the same posi-

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17. 7 U.S.C. § 1a(11).

18. *Id.*; *see also* Norris et al., *supra* note 1, at 334-40.

19. The Fourth Circuit has characterized the CEA's distinction between regulated futures contracts and excluded forward contracts as "semantically subtle." Salomon Forex, Inc. v. Tauber, 8 F.3d 966, 971 (4th Cir. 1993). Nonetheless, the court maintains that it has an accepted meaning in the trade. *Id.*

20. *See* Norris et al., *supra* note 1, at 339.

21. 7 U.S.C. § 1a(6). This definition dates back to the original statute, the Future Trading Act. Future Trading Act, 42 Stat. 187 (1921) (superseded by the Commodity Exchange Act, ch. 369, § 1, 42 Stat. 998 (codified as amended at 7 U.S.C. §§ 1-26)).

22. For example, one treatise of that era states: "Correctly used, this term [contract of sale] would mean a sale as distinguished from a contract to sell. But by reason of its interchangeable use by various courts and authors it is at best an ambiguous term and to be avoided." IRVING B. MARIASH, A TREATISE ON THE LAW OF SALES § 7 (1930).

23. In *Dunn v. Commodity Futures Trading Commission*, the Supreme Court rejected this kind of legalistic line drawing in interpreting the CEA. Dunn v. Commodity Futures Trading Comm'n, 117 S. Ct. 915, 919 (1997). The question in *Dunn* was the scope of the so-called Treasury Amendment, which exempted "transactions in foreign currency" from the CEA. *Id.* at 917. The Commodity Futures Trading Commission (CFTC) argued that it nonetheless could

tion holding that the term "sale," as used in another provision of the CEA, "[o]bviously . . . does not mean a 'sale' in the technically legal sense of the word."[24]

Moreover, the Norris argument proves too much. Under the UCC, a "sale," as opposed to a "contract for sale," consists of the passing of title.[25] But under the UCC, unless otherwise explicitly agreed, title passes only on delivery.[26] Thus, a "sale" under the UCC generally requires immediate delivery. The cash forward exclusion, however, covers "any sale of any cash commodity for *deferred* shipment or delivery."[27] If the cash forward exclusion were artificially limited to UCC "sales," which require present delivery, essentially there would be no cash forward exclusion.

For example, take the farmer who on July 4 enters into a contract to deliver 10,000 bushels of his or her crop, for a fixed price, to an elevator in the first half of December of the same year. Norris and his colleagues appear to agree that this is a legal forward contract. Yet under their UCC argument, this contract would be illegal because title to the grain does not pass until delivery in December. (If hail destroys the crop in August, that is the farmer's problem, not the elevator's.) In short, a UCC "sale" generally does not occur until delivery, but the cash forward exclusion is for sales for "deferred shipment or delivery," so using the former to define the latter would eliminate the exclusion.

A recent Iowa Supreme Court decision[28] illustrates this point while highlighting the weaknesses of Norris and his colleagues' analysis. The court,

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regulate trading in currency options, because only the actual exercise of an option created a "transaction in foreign currency." *Id.* at 918. The Supreme Court unanimously rejected this view, reasoning that the term "transactions in foreign currency" was broad enough to encompass option transactions. *Id.*

24. Corn Prods. Refining Co. v. Benson, 232 F.2d 554, 562 (2d Cir. 1956) (interpreting the term "sale," as it was then used, in the bona fide hedging exemption from trading limits). Also, in 1921, as today, there is evidence that the term "sale" was frequently used with less than rapier-like precision. *See* 1 FLOYD R. MECHEM, A TREATISE ON THE LAW OF SALE OF PERSONAL PROPERTY § 5, at 7 (1901) ("[P]recision of meaning is a condition rather to be desired than as yet actually attained, for it seems impossible for courts and text-writers to agree either as to the meaning of the word or as to the essential elements of the idea it represents. According to some the sale is the *transfer* of title; according to others, it is the *agreement* to transfer.").

25. U.C.C. § 2-106(1) (1989). The pre-UCC law of sales generally adhered to the same framework. *See* MARIASH, *supra* note 22, at §§ 3-6. Section 1 of the Uniform Sales Act distinguished between "contracts to sell" and "sales," with only the latter involving a present transfer of title. *Id.* § 4. A "sale" thus involved three acts: (a) transfer of title; (b) delivery of the article; and (c) payment of the price. *Id.* § 5. Strictly speaking, a "sale" occurred "only when the parties intend[ed] immediate transfer of title." *Id.*

26. U.C.C. § 2-401(2).

27. 7 U.S.C. § 1a(11) (1994) (emphasis added).

28. Production Credit Ass'n v. Farm & Town Indus., Inc., 518 N.W.2d 339 (Iowa 1994).

resolving a priority of liens dispute, held that a grain dealer's purchase of a farmer's 1991 crop in August 1991, when it was planted and growing, did not involve a present sale under the UCC.[29] The court noted that a sale requires either delivery of the goods or an express agreement that title will pass when the contract is executed.[30] Because neither had occurred in August, there was no sale at that time, and an institutional lender, who gave the grain dealer written notice of his security interest before delivery occurred, had a superior interest in the crop.[31] The court further noted that the specific corn to be sold had not been identified in August, and, therefore, the dealer's "sale" argument failed for an additional reason.[32] One suspects that the contract involved in this case was hardly unusual, and only rarely will a commercial sales agreement between a farmer and an elevator pass title before delivery occurs.

Indeed, it is not difficult to find numerous examples of standard farm contracts that would be rendered "illegal" by the Norris analysis. Nearly 120 years ago, the Iowa Supreme Court held that a farmer who had contracted to deliver 1600 bushels of "dry, sound, shelled" corn to an elevator in May, June, and July 1881, was responsible for damage to the corn prior to delivery.[33] The court noted that no "sale" had occurred at the time of contracting, and, therefore, risk of loss remained with the farmer.[34] Yet, this forward contract would now be an illegal arrangement if a court adopted Norris and his colleagues' view of the cash forward exclusion.

No one, including the Commodity Futures Trading Commission (CFTC)—the agency charged with administering the CEA—has previously suggested that a grain contract must involve a "present sale" and an immediate transfer of title to qualify for the cash forward exclusion. Norris and his colleagues' so-called textualism would turn the grain world upside down.

IV. THE "TEXTUAL ALTERNATIVE" CANNOT BE RECONCILED WITH THE LEGISLATIVE HISTORY OF THE CASH FORWARD EXCLUSION

Significantly, Norris and his colleagues do not claim that their "sale"-"contract to sell" distinction is supported by the legislative history.[35] The legis-

29. *Id.* at 346-47.
30. *Id.* at 347.
31. *Id.*
32. *Id.*
33. Davis v. Budd, 60 Iowa 144, 147 (1882).
34. *Id.* at 146-47.
35. For another discussion of the CEA's legislative history, see William L. Stein, *The Exchange-Trading Requirement of the Commodity Exchange Act*, 41 VAND. L. REV. 473, 486-91 (1988). The CFTC's General Counsel also prepared a helpful legislative history memorandum relatively early in the agency's existence. *See* Regulation of Leverage Transactions as Contracts

lative history shows that Congress did not intend to use the term "sale" in the narrow legal sense; that Congress always intended to exclude transactions in grain "to be grown" from the purview of its regulatory scheme; and that Congress believed from the very beginning that transactions in actual grain should be exempt.[36] Norris and his colleagues' "textual" interpretation cannot be squared with any of these facts.

On several occasions, the CFTC has discussed the genesis of the cash forward exclusion.[37] The exclusion dates back to 1921, when Congress enacted the Future Trading Act to regulate grain futures transactions by prohibitively taxing them when they were not conducted on a recognized board of trade.[38] The House-passed version of the Act (House Resolution 5676) contained an express exemption for contracts where one party was "the grower thereof, or . . . the owner or renter of land on which the [grain] is *to be* grown."[39] Thus, from the very beginning, an exemption for transactions in grain "to be grown" existed. As one representative stated in the floor debate: "This allows anyone who is the actual owner or who is the actual producer or prospective producer to sell his prospect or possession and allows anybody with no limitation to buy."[40]

When it considered House Resolution 5676, the Senate Committee on Agriculture and Forestry strengthened the exclusions by adopting one witness's suggestion to add an exclusion for "sales of cash grain for deferred shipment," substantially the same language as exists today.[41] No importance was attached to the word "sale." Indeed, the official committee report explained that this exemp-

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for Future Delivery or Otherwise, 44 Fed. Reg. 13,494, 13,498-501 (1979) (memorandum dated September 5, 1978, as amended September 11, 1978) (codified at 17 C.F.R. ch. 1 (1998)).

36 Stein, *supra* note 35, at 486-92.

37. Regulation of Leverage Transactions as Contracts for Future Delivery or Otherwise, 44 Fed. Reg. 13,494, 13,498-501 (1979) (codified at 17 C.F.R. ch. 1 (1998)); Characteristics Distinguishing Cash and Forward Contracts and "Trade" Options, 50 Fed. Reg. 39,656, 39,657-58 (1985) (codified at 17 C.F.R. ch. 1 (1998)).

38 *See* H.R. 5676, 67th Cong. § 1 (1921).

39 *Id.* § 4(a) (emphasis added).

40. 61 CONG. REC. 1374 (1921) (statement of Rep. Hardy). Representative Tincher, the House sponsor, gave a similar explanation during the House hearings: [P]ersons, who at the time of the making of the contract, regularly engaged in the business of growing, dealing in, or manufacturing grain or grain products may enter into contracts for future delivery . . . ." *Future Trading in Grain: Hearings on H.R. 2363 Before the House Comm. on Agric.*, 67th Cong. 17 (1921) (statement of Rep. Tincher).

41. *Future Trading in Grain: Hearings on H.R. 5676 Before the Senate Comm. on Agric. and Forestry*, 67th Cong. 214, 402 (1921) (suggestion of George McDermott of Topeka, Kansas, representing the Kansas Grain Dealers' Association). As Secretary of Agriculture Wallace indicated at the close of the Senate hearings, the legislation needed "to preserve the right of an individual or desire of individuals to make a contract for future delivery for the sale of grain which did not exist but which would exist in time for delivery" without going on a Board of Trade. *Id.* at 462 (statement of Sec. of Agric. Wallace).

tion had been added "in order that *transactions* in cash grain when made for deferred shipment or delivery would not fall within the provisions for taxing imposed in section 4 of the bill."[42] The Senate sponsor, Senator Capper, reiterated on the floor that "[t]he bill does not touch any transaction in cash grain, for it is expressly provided in the definition section that it shall not include any cash grain for deferred shipment."[43] The Act eventually passed both Houses with both of these exclusions intact.[44]

The Supreme Court struck down the Future Trading Act in 1922 as an impermissible exercise of taxing authority.[45] The statutory scheme was reenacted as a direct prohibition on off-board futures transactions later that year.[46] In 1936, Congress broadened the Act and renamed it the Commodity Exchange Act.[47] At that time, the exception for growers and owners/ renters of land on which crops are "to be grown" was eliminated as confusing and unnecessary in light of the additional exemption for sales of cash grain—now broadened to "cash commodities"—for deferred shipment or delivery.[48] In 1974, Congress enacted the Commodity Futures Trading Commission Act which established the CFTC, but the operative language of the cash forward exclusion remained the same.[49]

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42. S. REP. NO. 212, at 33 (1921) (emphasis added).

43. 61 CONG. REC. 4762 (1921) (statement of Sen. Capper). Senator Capper elaborated:

> Let me repeat that the bill does not concern itself at all with the sale or purchase of actual grain, either for present or future delivery. The entire business of buying and selling the actual grain, sometimes called "cash" or "spot" business, is expressly excluded. It deals only with the "future" or "pit" transaction, in which the transfer of actual grain is not contemplated.

Id.

44. Future Trading Act, ch. 86, 42 Stat. 187 (1921) (superseded by the Commodity Exchange Act, ch. 545, § 1, 49 Stat. 1491 (1936) (codified as amended at 7 U.S.C. §§ 1-26 (1994)).

45. Hill v. Wallace, 259 U.S. 44, 68 (1922).

46. Grain Futures Act, ch. 369, § 1, 42 Stat. 998 (1922). The Supreme Court upheld the constitutionality of the Grain Futures Act in *Board of Trade v. Olsen*, 262 U.S. 1, 43 (1923).

47. Commodity Exchange Act, ch. 545, § 1, 49 Stat. 1491 (1936).

48. H.R. REP. NO. 74-421, at 4-5 (1935). As Senator Pope, the floor manager in the Senate, put it: "As I construe the amendments in section 4, they simply make more accurate the language, but do not change the meaning or effect of the original Grain Futures Act." 80 CONG. REC. 7852 (1936) (statement of Sen. Pope).

49. Commodity Futures Trading Commission Act of 1974, Pub. L. No. 93-463, 88 Stat. 1389.

V. EMPHASIS ON DELIVERY DID NOT BEGIN WITH THE NINTH CIRCUIT'S 1982 *CO PETRO* DECISION

Norris and his colleagues argue that emphasis on the delivery criterion originated with the Ninth Circuit's 1982 decision in *Co Petro*.[50] However, they are incorrect. In fact, the CFTC's own seminal 1979 decision in *In re Stovall*[51] followed the same principles, derived from the same legislative history.

Stovall was an enforcement proceeding against an individual who offered to set up commodities accounts for the general public.[52] Typically, the customer would open the account and, thereafter, exercise no control over it, remaining unaware of what commodities, in what quantities, were bought and sold.[53] With one exception, delivery of the commodity never occurred.[54]

After considering the legislative history of the cash forward exemption, the CFTC readily concluded that Stovall's contracts did not qualify.[55] The CFTC cited several statements in the legislative history to the effect that the CEA was not intended to interfere with "cash grain," or "actual grain."[56] It referred to the exclusion as the "cash commodity" exclusion.[57] And, it noted that a "major difference" between an excluded cash forward contract and a regulated futures contract was "the generally fulfilled expectation that the contract will lead to the exchange of commodities for money."[58] Thus, *Co Petro* did not create the delivery test; the CFTC, the agency responsible for administering the CEA, had applied the same standard several years before in its first decision interpreting the cash forward exemption.[59] Nor did the Ninth Circuit embark in a new direction

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50. *See* Norris et al., *supra* note 1, at 330-34; Commodity Futures Trading Comm'n v. Co Petro Mktg. Group, Inc., 680 F.2d 573 (9th Cir. 1982).

51. *In re* Stovall, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941 (Dec. 6, 1979).

52. *Id.* at 23,778.

53. *Id.*

54. *Id.* at 23,779.

55. *Id.* at 23,782-83.

56. *Id.* at 23,777.

57. *Id.* at 23,778.

58. *Id.*

59. Pursuant to the Commodity Futures Trading Commission Act of 1974, Pub. L. No. 93-463, 88 Stat. 1389, the CFTC gained responsibility for enforcing the CEA in 1975, *id.* at 1392. The administrative law judge's (ALJ) decision in *Stovall* appears to be the first CFTC proceeding discussing the cash forward exemption. *In re* Stovall, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,420, at 21,677 (May 6, 1977) (Campbell, ALJ). The CFTC's analysis in *Stovall* is also largely consistent with an early legislative history memorandum authored by the agency's general counsel. *Compare id.*, *with* 44 Fed. Reg. 13,494, 13,498-501 (1979) (memorandum dated September 5, 1978, as amended September 11, 1978) (codified at 17 C.F.R. ch. 1 (1998)).

when it combed the legislative history of the cash forward exclusion as an aid to interpretation; the CFTC had done the same thing three years earlier.[60]

Courts applying this established law overwhelmingly have found HTA contracts lawful.[61] Contrary to Norris and his colleagues' suggestion, these courts have not simply looked for a "scintilla of a delivery obligation."[62] Rather, they have applied multi-factor tests, including: (1) whether the contracting parties are in the business of producing and receiving grain; (2) whether they have the capacity to deliver grain; and (3) whether delivery had occurred in past dealings.[63] Thus, while judicial inquiry has focused on whether actual, physical delivery of grain was contemplated, by no means have the decisions been as simplistic as Norris and his colleagues suggest. Contemplation of delivery means more than just the existence of some delivery obligation in the contract.[64]

Norris and his colleagues also overstate the degree of conflict between the CFTC's current HTA contract enforcement policy and court decisions. The CFTC has brought several enforcement proceedings since 1996 against marketing advisors and elevators that offered HTA contracts.[65] Yet a common thread running through these proceedings is the CFTC's assertion that the contracts did not contemplate delivery of physical grain, typically because they contained a regularly exercised buy-out clause.[66] Whether one agrees with the CFTC's

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60. Not surprisingly, the CFTC has endorsed the *Co Petro* standard on several occasions. *See* 50 Fed. Reg. 39,656 & 39,657 (1985); 52 Fed. Reg. 47,022 & 47,027 (1987); 55 Fed. Reg. 39,188 & 39,190-91 (1990).

61. *See supra* note 2.

62. Norris et al., *supra* note 1, at 328.

63. Andersons, Inc. v. Norton Farms, Inc., 166 F.3d 308, 320 (6th Cir. 1998); Johnson v. Land O' Lakes, Inc., 18 F. Supp. 2d 985, 994 (N.D. Iowa 1998); *In re* Grain Land Coop., 978 F. Supp. 1267, 1273-74 (D. Minn. 1997).

64. Indeed, if anyone, Norris and his colleagues have followed an overly simplified approach tied to the literal language of the HTA contracts. *See* Norris et al., *supra* note 1, at 330-42. For example, they provide a *reductio ad absurdum* example of a hypothetical HTA contract that could be rolled until the year 2235. *Id.* at 330. But arguments based on the literal language of the contract must work both ways. If a mere delivery obligation in the contract does not establish "cash forward exemption" status, so too the hypothetical ability to roll for 36 years without delivering does not negate that status. Courts must focus on what was realistically contemplated at the time the contract was originally executed.

65. *In re* Competitive Strategies for Agric., Ltd., CFTC No. 98-4 (Aug. 24, 1998) (settlement); *In re* Grain Land Coop., CFTC No. 97-1 (Nov. 6, 1998) (ALJ decision); *In re* Farmers Coop. Co., CFTC No. 99-6 (Jan. 12, 1999) (complaint); *In re* Andersons, Inc., CFTC No. 99-5 (Jan. 12, 1999) (settlement).

66. *In re* Competitive Strategies for Agric., Ltd., CFTC No. 98-4, at *7 ("Perhaps most significantly, the contract provided an effective means of discharge or offset that was, in practice, used routinely to liquidate the contract for cash with no delivery of grain required. . . . In addition, the contract was marketed, entered into and structured as a means of capturing price movements in the futures markets, not as a vehicle for delivery. . . . Indeed, the contract even was offered to parties with no practical ability to deliver."); *In re* Grain Land Coop., CFTC No. 97-1, at *24 ("[T]he

application of the delivery standard in these proceedings or not,[67] the CFTC clearly shares the widely-held viewpoint[68] that expectation of delivery should be the fundamental test. Hence, the claimed split between the views of the CFTC and those of most district courts may be nonexistent.[69] Rather than carefully examining the actual enforcement actions brought by the CFTC, Norris and his colleagues give undue weight to a non-precedential 1996 CFTC staff "statement of policy" that did not purport to take a position on the validity of any HTA contracts but simply discussed methods of prudent risk-reduction for grain elevators and farmers.[70]

To put it simply, the CFTC has challenged only a few HTA contracts, in special circumstances where delivery was allegedly not contemplated because of routinely invoked buy-out clauses in the contract. Moreover, the CFTC's Chairperson recently announced that no further HTA cases are presently anticipated.[71]

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contractual terms of respondent's Flex HTA contracts, consistent with the way they were marketed, readily allowed a producer to unilaterally and unequivocally avoid delivery for any reason. This 'privilege' is fundamentally at odds with the rationale underlying a cash forward contract—the desire to dispose of or acquire grain."); *In re* Farmers Coop. Co., CFTC No. 99-6, at *3 ("Farmers Co-op permitted producers to 'buy-back' their HTA contracts at any time before delivery was required under the contract and thereby extinguish their delivery obligations by means other than the actual delivery of grain."); *In re* Andersons, Inc., CFTC No. 99-5, at *4-5 ("Most significantly, the contract provided an effective means of liquidating the contract for cash. In addition, the contract was offered, entered into and structured as a means of capturing price movements in the futures markets, not as a vehicle for delivery of grain to Andersons. Indeed, the contract even was offered to some parties who had no practical ability to deliver.")

67. It may be difficult to reconcile some of the CFTC's recent actions regarding HTA contracts with the CFTC's 1990 statutory interpretation that 15-day Brent oil contracts were subject to the cash forward exclusion, even though they were routinely settled by means other than delivery. Statutory Interpretation Concerning Forward Transactions, 55 Fed. Reg. 39,188 & 39,191-92 (1990).

68. For a recent discussion of the cash forward exclusion outside the HTA contract area that employs a similar mode of analysis, see *MG Refining & Marketing v. Knight Enterprises*, 25 F. Supp. 2d 175, 182-85 (S.D.N.Y. 1998).

69. *See* Norris et al., *supra* note 1, at 329.

70. CFTC Interpretive Ltr. No. 96-41 (Division of Economic Analysis Statement of Policy in Connection with the Unwinding of Certain Existing Contracts for the Delivery of Grain and Statement of Guidance Regarding Certain Contracting Practices), Comm. Fut. L. Rep. (CCH) ¶ 26,691 (May 15, 1996). Courts have declined to rely on this statement of policy. Oeltjenbrun v. CSA Investors, Inc., 3 F. Supp. 2d 1039, 1043 (N.D. Iowa 1998) (noting that the interpretive letter does not have the force and effect of law); *In re* Grain Land Coop., 978 F. Supp. 1267, 1277 (D. Minn. 1997) ("[W]hile the principles set forth by the [CFTC Division of Economic Analysis] may be helpful and informative to future parties in minimizing contractual risk, the Guidance Statement is of no value to this Court in its present inquiry.").

71. Testimony of Brooksley Born, CFTC Chairperson, Before the Subcomm. on Agric., Rural Dev., FDA, and Related Agencies of the House Comm. on Appropriations, March 4, 1999, at 4.

Not only the CFTC and courts, but a number of commentators, have approved a rule exempting contracts from the CEA where delivery on the contracts was originally anticipated.[72] Several careful analyses of the forward contract exclusion have preceded the Norris Article, and almost without exception they have found the "contemplation of delivery" standard to be well-grounded in the CEA's language and legislative history.[73]

VI. There Are Sound Policy Reasons for Focusing on Expectation of Delivery

Expectation of delivery is not simply a useful and well-established dividing line; it reflects policy considerations long known to Congress. The CEA and its predecessors were not intended to purge all risk from grain transactions; they were intended to eliminate market manipulation. Nothing in the legislative history suggests that Congress intended to eliminate *marketing* risk; that is, the risk that arises whenever a farmer chooses or fails to choose a particular method of marketing his or her grain. To the contrary, the contemporary debate in the early 1920's pitted farmers against large speculators who allegedly manipulated and, thereby, artificially depressed farm prices, preventing the exchanges from functioning properly and farmers from receiving a fair price for their crops.[74] The Act's proponents sought to liberate farmers from the ill effects of this specula-

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72. *See, e.g.*, Mark D. Young & William L. Stein, *Swap Transactions Under the Commodity Exchange Act: Is Congressional Action Needed?*, 76 GEO. L.J. 1917, 1923-24 (1988) (noting that parties to regulated futures contracts, as opposed to exempt cash forward contracts, "do not actually perform their contractual obligations nor do they ever intend to perform").

73. *See, e.g.*, 1 THOMAS A. RUSSO, REGULATION OF THE COMMODITIES AND FUTURES AND OPTIONS MARKET § 9.07, at 9-13 (1991) (noting that the basic policy behind the forward contract exclusion is that "regulation is not required for commodity sale contracts made principally among merchants where delivery is contemplated and where shipment or delivery of the commodity is deferred for reasons of commercial convenience or necessity"); David J. Gilberg, *Regulation of New Financial Instruments Under the Federal Securities and Commodities Laws*, 39 VAND. L. REV. 1599, 1605 (1986) ("Congress clearly intended to exclude standard agreements between commercial entities involving delivery of physical commodities at a later date from the prohibition on off-exchange futures trading."); Stein, *supra* note 35, at 492 ("Congress apparently concluded that cash deferred contracts, which contemplate the transfer of actual ownership of a commodity, could not be used to manipulate prices.").

74. "Congressional committees and sponsors of the ill-fated 1921 legislation devoted most of their eloquence to injuries suffered by producers at the hands of wicked speculators . . . ." Leist v. Simplot, 638 F.2d 283, 304 (2d Cir. 1980) (finding an implied private right of action under the CEA), *aff'd*, 456 U.S. 353 (1982). For an extraordinarily thorough discussion of the interplay of political forces that led to the enactment of the Future Trading Act, see generally Roberta Romano, *The Political Dynamics of Derivative Securities Regulation*, 14 YALE J. ON REG. 279 (1997).

tion, not to restrict farmers.[75] Thus, Senator Capper explained on the Senate floor that the Act "is not a regulation of business in the sense in which that term is usually employed."[76]

The risk of making a bad bargain can occur in any transaction, and there is no reason why grain or commodities should be singled out for special treatment.[77] Historically, state law protections have been viewed as a sufficient backstop against agreements that were merely imprudent or unwise. As Representative Tincher stated during the House hearings, "I do not think any good-thinking man in the United States is in favor of preventing the farmer from selling his wheat for future delivery."[78] Thus, the CEA and its predecessors should not be viewed as an attempt to control the *primary* transaction between parties that expect to transfer physical grain or other commodities, but to give farmers better prices by ending market manipulation.

Norris and his colleagues argue that if delivery is the controlling factor, then the courts are really making an archaic distinction between legal contracts and illegal gambling contracts.[79] But there is powerful evidence in the legislative history that Congress was concerned about gambling.[80] Congress's innovation was to try to regulate gambling rather than prohibit it altogether. Congress believed that some "gambling" was essential to the smooth operation of a market on which farmers and elevators could price and hedge but, at the same time, Congress also was concerned about market manipulation.[81] Thus, the Act's purpose was not oversight of farmers' decisions on how to sell their grain, but to prevent market manipulation by confining futures transactions to recognized boards of trade and requiring written records to be kept of those transactions.[82] It is ironic indeed for Norris and his colleagues to take the position that legislation

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75. Romano, *supra* note 74, at 315-16; *see* Grain Futures Act, ch. 369, § 3, 42 Stat. 998 (1922) (statement of purpose of the Grain Futures Act) (superseded by the Commodity Exchange Act, ch. 545, 49 Stat. 1491 (1936) (codified as amended at 7 U.S.C. §§ 1-26 (1994)).

76. 61 CONG. REC. 4762 (1921) (statement of Sen. Capper).

77. In the words of one commentator, "Farmers and elevators are free to select any pricing mechanism, regardless of how inane, to set the contract price on a cash forward contract." Nicholas P. Iavarone, *Understanding the Hedge-to-Arrive Controversy*, 2 DRAKE J. AGR. LAW 371, 395 (1997).

78. *Future Trading in Grain: Hearings on H.R. 2363 Before the House Comm. on Agric.*, 67th Cong. 7 (1921) (statement of Rep. Tincher).

79. *See* Norris et al., *supra* note 1, at 331-32 n.53.

80. 61 CONG. REC. 1312-14 (1921) (statement of Rep. Tincher); *Future Trading in Grain: Hearings on H.R. 2363 Before the House Comm. on Agric.*, 67th Cong. 9, 16-17 (1921) (statement of Rep. Tincher); 61 CONG. REC. 4762 (1921) (statement of Sen. Capper).

81. As Senator Capper put it: "This legislation does not destroy the hedge; but on the contrary its object is to improve the hedge." 61 CONG. REC. 4762 (1921) (statement of Sen. Capper).

82. Future Trading Act, ch. 86, § 4, 42 Stat. 187 (1921) (superseded by the Commodity Exchange Act, ch. 545, § 1, 49 Stat. 1491 (1936) (codified as amended at 7 U.S.C. §§ 1-26 (1994)).

intended to relax an earlier tradition that viewed all non-delivery-related grain transactions as a form of illegal gambling[83] could invalidate even transactions where delivery of the physical grain was anticipated.

VII. A VIABLE TEXTUAL APPROACH

A textual analysis of the cash forward exclusion should focus on the phrase "cash." "Cash grain" is a common term in the grain industry, albeit a sometimes ill-defined one.[84] As one respected commentator has said,

> [B]oth the trade and the commentators understand "cash" to be an adjective having no relation to the timing of delivery, sale, payment, shipment, or transfer of title. Cash transactions comprise the universe of commercial transactions in commodities after the very narrow category of highly stylized transactions called "futures" is either excluded or excepted.[85]

While Norris and his colleagues criticize existing HTA contract case law for failing to give effect to the words of the statute, their textual alternative completely ignores the term "cash."[86] Under their interpretation, "cash" is excess baggage.

But that was not Congress's view at the time. During the House hearings, Representative Tincher gave the example of the farmer who thinks he is going to produce 2000 bushels of wheat, whether he ultimately does so or not.[87] "That is cash wheat for future delivery."[88] He explained, "I do not think that transaction ought to be interfered with at all."[89]

83. *See, e.g.*, R.N. Kelly Cotton Merchant, Inc. v. York, 494 F.2d 41, 42 n.2 (5th Cir. 1974) (citing GA. CODE ANN. § 20-601 (1965) (declaring any commodity contract unlawful when it was "not in good faith intended by the parties that an actual delivery . . . be made")).

84. Powell v. McCord, 12 N.E. 262, 264 (Ill. 1887) (stating cash grain means grain to be actually delivered). According to a glossary attached to House Report No. 93-975 on the Commodity Futures Trading Commission Act, a "cash commodity" is "[t]he physical or actual commodity as distinguished from the 'futures.'" H.R. REP. NO. 93-975, at 161 (1974). It should be noted, though, that the glossary is attached to the report with the disclaimer that it does not constitute a guide to interpretation of the Act. *See id.* During the 1921 Senate hearings, Senator Capper likewise referred to cash grain as "the actual grain," although a witness described it as grain that is actually in existence. *Future Trading in Grain: Hearings on H.R. 5676 Before the Senate Comm. on Agric. and Forestry*, 67th Cong. 463 (1921) (statement of Sen. Capper).

85. Glenn Willett Clark, *Genealogy and Genetics of "Contract of Sale of a Commodity for Future Delivery" in the Commodity Exchange Act*, 27 EMORY L.J. 1175, 1189-90 (1978).

86. Norris et al., *supra* note 1, at 330-34.

87. *Future Trading in Grain: Hearings on H.R. 2363 Before the House Comm. on Agric.*, 67th Cong. 8 (1921) (statement of Rep. Tincher).

88. *Id.*

89. *Id.*

Indeed, once one recognizes that Congress meant to use "cash" as a term of art, the apparent paradox identified by Norris and his colleagues becomes readily understandable. Norris and his colleagues maintain that it makes no sense to use the presence or absence of a delivery expectation to distinguish between two kinds of transactions that both contain the term "delivery"—*i.e.*, regulated "contract[s] for the purchase or sale of a commodity for future delivery" and unregulated "sale[s] of any cash commodity for future shipment or delivery."[90] However, because "cash" grain includes both immediate delivery or "spot" transactions and transactions where delivery is deferred, Congress needed to incorporate the term "future shipment or delivery" in the cash forward exclusion. Otherwise, a reader could get an erroneous impression from unnecessarily broad language in the exclusion that *the Act itself* affected grain sales for immediate delivery. Simply stated, from the broader universe of "contract[s] . . . for future delivery," Congress needed to extract "sale[s] of [cash grain] for future . . . delivery," *i.e.*, sales where movement of the actual grain was anticipated.[91] The meaning of the exclusion is clear.

Finally, if there is any doubt, the exclusion should be interpreted broadly, particularly as applied to growers of grain who had their own exemption in the original statute.[92] The mantra that the cash forward exemption is "narrow" provides a good example of an unsupported statement that slipped into case law and then procreated.[93] There is no logical reason why the cash forward exclusion

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90. Norris et al., *supra* note 1, at 332 (quoting 7 U.S.C. §§ 1a(11), 6(a) (1994)).

91. *Id.* Although "contract[s] for the purchase or sale of a commodity for future delivery" and "sale[s] of any cash commodity for deferred shipment or delivery" are sometimes viewed as mutually exclusive categories, *see id.*, it should be remembered that the cash forward exclusion, like other statutory exemptions, is really a trump card. In other words, even if a commodity contract meets the literal definition of a futures contract under the CEA, it nonetheless falls outside the coverage of the Act if it qualifies for the cash forward exclusion. *See In re* Bybee, 945 F.2d 309, 312-15 (9th Cir. 1991) (finding that precious metal contracts were futures contracts under the CEA, but that they also qualified for the cash forward exclusion).

92. As noted above, that exclusion was removed in 1936 because it was viewed as superfluous. *See supra* note 48 and accompanying text.

93. The Ninth Circuit may have started the trouble in *Co Petro* when it referred to the "narrowness" of the exclusion. Commodity Futures Trading Comm'n v. Co Petro Mktg. Group, Inc., 680 F.2d 573, 578 (9th Cir. 1982). A year later, a CFTC ALJ, while making the puzzling comment that the legislative history provides "little guidance" on the cash forward exclusion (despite the full Commission's detailed recital of that legislative history four years before in *Stovall*), described the exclusion as a "very narrow one." *In re* First Nat'l Monetary Corp., Comm. Fut. L. Rep. (CCH) ¶ 21,707, at 26,779 (Apr. 29, 1983). That same year, a district court again described the exemption as "narrow." NRT Metals, Inc. v. Manhattan Metals (Non-Ferrous) Ltd., 576 F. Supp. 1046, 1050 (S.D.N.Y. 1983) (citing Commodity Futures Trading Comm'n v. Co Petro Mktg. Group, Inc., 680 F.2d at 578). These kinds of statements have now become commonplace in opinions discussing the cash forward exclusion, with the courts generally citing *Co Petro*. *See, e.g.*, Commodity Futures Trading Comm'n v. Noble Metals Int'l, Inc., 67 F.3d 766, 772 (9th Cir. 1995); Oeltjenbrun v. CSA Investors, Inc., 3 F. Supp. 2d 1024, 1035 (N.D. Iowa 1998); *In re* Grain

should be "narrow." Without it, the CEA would be an extraordinarily overreaching and paternalistic statute. Sometimes described as a prohibition on off-exchange trading, it is really a prohibition on *contracting*. Indeed, only the cash forward exclusion makes the popular perception somewhat accurate, because it limits the prohibition to contracts expected to be offset by other contracts, or, in common vernacular, "traded."

A rule that a farmer and an elevator cannot legally agree that the farmer will deliver to the elevator the next year's crop, or several years' crops, belongs in the nineteenth century, not the twenty-first. Such an intrusion in the farm economy needs a far stronger legal basis than Norris and his colleagues have furnished in their Article.

Land Coop., 978 F. Supp. 1267, 1277 (D. Minn. 1997); Transnor (Bermuda) Ltd. v. BP N. Am. Petroleum, 738 F. Supp. 1472, 1490 (S.D.N.Y. 1990). Thus, *Co Petro* may have contaminated the gene pool, but not in the manner described by Norris and his colleagues.