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COMMENT
CL-08328

From: Jung Lee <junglee211@gmail.com>
Sent: Monday, April 26, 2010 4:00 PM
To: secretary <secretary@CFTC.gov>
Cc: Greenberger, Michael <mgreenberger@law.umaryland.edu>
Subject: Proposed Federal Speculative Position Limits for Referenced Energy Contracts and Associated Regulations
Attach: CFTC Comment_Letter_for_Speculative_Postion_Limits.pdf

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Dear Mr. Stawick,

I am submitting the attached comment letter on behalf of Professor Michael Greenberger. Thank you.

Sincerely,

Jung Lee
Candidate for JD, CPA, CFA
University of Maryland School of Law, 2010
Tel: (347) 885-2563
junglee211@gmail.com

April 26, 2010

David Stawick
Secretary
United States Commodity Futures Trading Commission
1155 21st Street, NW
Washington, DC 20581

Re: Proposed Federal Speculative Position Limits on Referenced Energy Contracts and Associated Regulations

Dear Mr. Stawick:

I am pleased to submit this comment letter on the Commission's proposal to implement speculative position limits.[1]

In recent months and as the country has tried to fight its way out of the most serious financial crisis since the Great Depression, the personal finances of most Americans have taken a an added and serious beating because of destabilizing price spikes in traditional physical commodities, such as oil, gasoline, heating oil, and basic food staples. As one prime example, we have seen dizzying volatility in crude oil prices during the last 24 months: with no underlying change in supply and demand. The price of crude oscillated from $65 per barrel in June 2007 to $147 in July 2008 to $30 in December 2008 and back up to $89 in April 2010.[2]

On September 22, 2008, the price of a barrel of crude oil posted a single day record rise of $18.56 and then dramatically dropped $14.75 the very next day, eventually dropping to near $30 a barrel by December 2008.[3] The September 22 single day crude oil price *increase* of over

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[1] Federal Speculative Position Limits for Referenced Energy Contracts and Associated Regulations, 75 Fed. Reg. 4144 (Jan. 26, 2010).

[2] *See* Organization of Petroleum Exporting Countries, World Oil Outlook 2009, *available at* http://www.opec.org/opecna/Speeches/2009/attachments/WOO09presentation.pdf (last visited April 23, 2010); Gordon Brown and Nicolas Sarkozy, *Oil Prices Need Government Supervision: Producers and consumers benefit from stability*, WALL ST. J., July 8, 2009, *available at* http://online.wsj.com/article/SB124701217125708963.html (last visited April 18, 2010); INTERNATIONAL MONETARY FUND, *REGIONAL ECONOMIC OUTLOOK: MIDDLE EAST AND CENTRAL Asia*, 27-28, May 2008, *available at* http://www.imf.org/external/pubs/ft/reo/2008/MCD/eng/mreo0508.pdf (last visited April 18, 2010); Price data for Cushing, OK WTI Spot Price FOB (Dollars per Barrel), ENERGY INFORMATION ADMINISTRATION, *available at* http://tonto.eia.doe.gov/dnav/pet/hist/rwtcd.htm (last visited April 18, 2010).

[3] Data for Cushing, OK WTI Spot Price FOB (Dollars per Barrel), published by The Energy Information Administration, *available at* http://tonto.eia.doe.gov/dnav/pet/hist/rwtcd.htm (last visited April 18, 2010).

$18 must be put into the saddening context that as recently as January 2002 the *entire* price of a barrel of crude was only $18.[4]

As Michael Masters, in the context of the June 4, 2009 Senate hearings, observed, while oil prices fluctuated wildly, "U.S economic output was dropping during the first six months of 2008. During that time, worldwide supply of oil was increasing and worldwide demand for oil was decreasing. . . . According to the Energy Information Agency (EIA), the available supply of crude oil in the United States is at a 20-year high, while the demand for crude oil is at a 10-year low. The International Energy Agency (IEA) sees a similarly bleak supply and demand outlook for the world as a whole. *And, yet, despite this glut of unwanted oil, the price has risen an amazing 85% per barrel from the mid-$30s to mid-$60s. In fact, oil prices increased more in the month of May [2009] than in any other month for the last 10 years*."[5]

The recent run up in crude oil and gasoline prices, at the same time the country is attempting to recover from the worst financial crisis, presents a dire threat that the financial back of the American consumer will break as a result of further price spikes in everyday necessities. This is a phenomenon that will undoubtedly weigh down any potential economic recovery, leading to further and more sustained economic hardship. In light of this, I applaud the Commission's effort to implement speculative position limits to stabilize the commodities prices and to bring transparency to the markets.

I have prepared my comments on the following questions:

1. **Are Federal Speculative position limits for energy contracts traded on reporting markets necessary to "diminish, eliminate, or prevent" the burdens on interstate commerce that may result from position concentrations in such contracts?**

My short answer to this question is yes. One of the fundamental purposes of futures contracts is to provide price discovery in the "cash" or "spot" markets.[6] Those selling or buying commodities in the "spot" markets rely on futures prices to judge amounts to charge or pay for the delivery of a commodity.[7] Since their creation in the agricultural context decades ago, it has been widely understood that, unless properly regulated, futures markets unquestionably have the

[4] Jad Mouawad & Heather Timmon, *Trading Frenzy Adds to Jump in Price of Oil*, N.Y. TIMES, Apr. 29, 2006, *available at* http://www.nytimes.com/2006/04/29/business/29traders.html (last visited April 18, 2010).
[5] Testimony of Michael Masters, U.S. Senate Comm. on Agriculture, Nutrition, and Forestry at 3-4, June 4, 2009 (emphasis added and interior citations omitted), *available at* http://216.40.253.202/~usscanf/index.php?option=com_events&task=view_detail&agid=32&year=2009&month=06&day=04&Itemid=44 (last visited April 18, 2010).
[6] The Economic Purpose of Futures Markets and How They Work, COMMODITY FUTURES TRADING COMMISSION, http://www.cftc.gov/educationcenter/economicpurpose.html (last visited April 18, 2010).
[7] *See* Platts Oil Pricing and Market-on-Close Methodology Explained, Platts (July 2007) at 3, *available at* http://www.platts.com/IndustrySolutionPapers.aspx (last visited April 18, 2010).

potential to distort the economic fundamentals of price discovery (*i.e.*, cause the paying of unnecessarily higher or lower prices) through, *inter alia*, excessive speculation.[8]

As the 1935 Report of House Agriculture Committee stated: "The fundamental purpose of the measure [*i.e.*, what was to become the Commodity Exchange Act of 1936 ("CEA")] is to insure fair practice and honest dealing on the commodity exchanges and to provide a measure of control over those forms of speculative activity which *too often demoralize the markets to the injury of producers and consumers and the exchanges themselves*."[9]

Indeed, President Roosevelt, when introducing what became the CEA in 1934 said: "[I]t should be our national policy to restrict, as far as possible, the use of these exchanges for purely speculative operations."[10] In this regard, the House Agriculture Committee then stated: "This bill authorizes the Commission . . . to fix limitations upon purely speculative trades . . ."[11] As the telling colloquy between Chairman Gensler and General Counsel Dan M. Berkovitz at the July 28, 2009 hearing so accurately reflected, the Commodity Exchange Act today, 74 years later, continues to provide that it is the duty of the Commission to guard against "excessive speculation" that destabilize markets under this agency's jurisdiction.

While there has been a debate over whether excessive speculation has destabilized markets, I agree with experts on[12], and observers of[13], these markets, whose contention that that

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[8] *See, e.g.*, Jonathan Ira Levy, *Contemplating Delivery: Futures Trading and the Problem of Commodity Exchange in the United States, 1875-1905*, AMERICAN HISTORICAL REVIEW 307 (2006) ("'[T]he man who managed or sold or owned those immense wheat fields has not as much to say with the regard to the price of the wheat that some young fellow who stands howling around the Chicago wheat pit could actually sell in a day'"(quoting *Fictitious Dealings in Agricultural Products: House Comm. on Agric. Committee Hearing Reports* (1892)).

[9] Report No. 421, U.S. House of Representatives 74th Cong, Accompanying the Commodity Exchange Act, March 18, 1935 (emphasis added).

[10] President Franklin D. Roosevelt, Message to Congress, February 9, 1934.

[11] Report No. 421, U.S. House of Representatives 74th Cong., Accompanying the Commodity Exchange Act, March 18, 1935.

[12] *See, e.g.,* Edmund Conway, *George Soros: Rocketing Oil Price is a Bubble*, Daily Telegraph (May 27, 2008), *available at* http://www.telegraph.co.uk/finance/newsbysector/banksandfinance/2790539/George-Soros-rocketing-oil-price-is-a-bubble.html (last visited April 18, 2010) (quoting Mr. George Soros as stating "Speculation . . . is increasingly affecting the price"); Written Testimony of Michael Masters, *Hearing Before the Committee on Homeland Security and Governmental Affairs, U.S. Senate* 2 (May 20, 2008), *available at* http://hsgac.senate.gov/public/_files/052008Masters.pdf (last visited April 18, 2010) (quoting Michael W. Masters as stating "Are Institutional Investors contributing to food and energy price inflation? And my unequivocal answer is YES"); Giacomo Luciani, *From Price Taker to Price Maker? Saudi Arabia and the World Oil Market* 3 (Working Paper, 2009) (quoting Giacomo Luciani as stating "The inflow of liquidity, the increasing role played by the futures market (paper barrels) over the spot (wet barrels), and the proliferation of derivatives which encourage betting on price changes rather than on the absolute level of prices all contribute to worsen the situation, amplifying price oscillations"); Ke Tang & Wei Xiong, *Index Investing and the Financialization of Commodities* 23 (Working Paper, 2009), *available at* http://www.princeton.edu/~wxiong/papers/commodity.pdf. (stating "the financialization process of commodities precipitated by the rapid growth of index investment to the commodities markets, had "contributed significantly" to the volatility of commodity prices in oil and other non-energy commodities in 2008); Xiaodong Du, Cindy L. Yu & Dermot J. Hayes, *Speculation and Volatility Spillover in the Crude Oil and Agricultural Commodity Markets: A Bayesian Analysis* 13 (Center for Agric. & Rural Dev., Iowa State Univ., Working Paper No. 09-WP 491, 2009), *available at* http://www.econ.iastate.edu/research/webpapers/paper_13066.pdf (stating that noncommercial speculation in crude oil futures markets increases price volatility in a "significant manner.");

KENNETH B. MEDLOCK III & AMY MYERS JAFFE, JAMES A. BAKER III INST. FOR PUB. POLICY, RICE UNIV., WHO IS IN THE OIL FUTURES MARKET AND HOW HAS IT CHANGED? 5 (2009), *available at* http://www.bakerinstitute.org/publications/EF-pub-MedlockJaffeOilFuturesMarket-082609.pdf (noting that noncommercial players now constitute about "50 percent of those holding outstanding positions in the U.S. oil futures market" and state that the increase is "highly correlated with the run-up in oil prices."); Oral Testimony of Edward Krapels, Hearing Before the Committee on Energy and Commerce Subcommittee on Oversight and Investigations, U.S. House of Representatives, (June 23, 2008) (quoting Mr. Edward Krapels as stating "I think the amount of speculation is really substantial [within the crude oil market.]"); Oral Testimony of Roger Diwan, Hearing Before the Committee on Energy and Commerce Subcommittee on Oversight and Investigations, U.S. House of Representatives, (June 23, 2008) (quoting Mr. Roger Diwan, responding to Rep. Whitfield's question: So you're saying if we adopt these regulatory changes, we could almost cut the retail price of gas in half in a relatively short period of time? "I don't know how quickly it takes to get prices down, but it's clear that prices will reflect closer the marginal cost of producing oil."); Alejandro Lazo, Energy *Stocks Haven't Caught Up With Oil Prices*, WASH. POST, Mar. 23, 2008, *available at* http://www.washingtonpost.com/wp-dyn/content/article/2008/03/21/AR2008032103825.html (last visited April 18, 2010) (quoting Mr. Fadel Gheit as stating, "The largest speculators are the largest financial companies."); Michelle Foss, United States Natural Gas Prices to 2015, 34 (2007), *available at* http://www.oxfordenergy.org/pdfs/NG18.pdf (last visited Aug. 2, 2009) (asserting "The role of speculation in oil markets has been widely debated but could add upwards of $20 to the price per barrel."); Tim Evans, Citi Futures Perspective: PM Energy News & Views, at 2 (July 3, 2008) (quoting "With the latest push to the upside, we see the crude oil market becoming even more completely divorced from any connection to fundamental factors and becoming even more obsessed with the simple question, How high can it go?"); Advantage Business Media, *Economist Blames Subsidies for Oil Price Hike*, Chem.Info (2008), *available at* http://www.chem.info/ShowPR.aspx?PUBCODE=075&ACCT=0000100&ISSUE=0609&ORIGRELTYPE=DM&RELTYPE=PR&PRODCODE=00000&PRODLETT=M&CommonCount=0 (last visited April 18, 2010) (quoting Dr. Michelle Foss as stating "We have an overpriced commodity, and this is going to be around for a while."); Kenneth N. Gilpin, *OPEC Agrees to Increase Output in July to Ease Oil Prices*, N.Y. TIMES (June 3, 2004) *available at* http://www.nytimes.com/2004/06/03/business/03CND-OIL.html?ex=1401681600&en=5dbd50c5b369795b&ei=5007&partner=USERLAND (last visited April 18, 2010) (quoting Mr. Kyle Cooper as stating, "There is not a crude shortage, which is why OPEC was so reluctant to raise production."); Upstream, *Speculators 'not to blame' for Oil Prices*, UpstreamOnline.com (April 4, 2008), *available at* http://www.upstreamonline.com/live/article151805.ece (last visited April 18, 2010) (quoting Mr. Sean Cota as stating, "It has become apparent that excessive speculation on energy trading facilities is the fuel that is driving this runaway train in crude prices"); Mike Norman, *The Danger of Speculation*, FoxNews.com, *available at* http://www.foxnews.com/story/0,2933,166038,00.html (last visited April 18, 2010) (Mr. Norman stating "Oil prices are high because of speculation, pure and simple. That's not an assertion, that's a fact. Yet rather than attack the speculation and rid ourselves of the problem, we flail away at the symptoms."); International Monetary Fund, Regional Economic Outlook: Middle East and Central Asia 27-28 (May 2008) ("Producers and many analysts say it is speculative activity that is pushing up oil prices now. Producers in particular argue that fundamentals would yield an oil price of about US $80 a barrel, with the rest being the result of speculative activity."); *see also* Neil King Jr., *Saudi Arabia's Leverage In Oil Market Is Sapped*, WALL STREET J. (June 16, 2008), *available at* http://online.wsj.com/article/SB121355902769475555.html?mod=googlenews_wsj (last visited April 18, 2010) (quoting Saudi Oil Minister Ali Naimi as saying skyrocketing oil prices were "unjustified by the fundamentals" of supply and demand); Gordon Brown and Nicolas Sarkozy, *We Must Address Oil-Market Volatility*, Wall St. J., July 8, 2009, *available at* http://online.wsj.com/article/SB124699813615707481.html (last visited April 18, 2010); Michael W. Masters & Adam K. White, *How Investors Are Driving Up Food and Energy Prices*, July 31, 2008, *available at* www.accidentalhuntbrothers.com (last visited April 18, 2010); Michael W. Masters & Adam K. White, *Index Speculators Have Been a Major Cause of the Recent Drop in Oil Prices*, Sept. 10, 2008, *available at* www.accidentalhuntbrothers.com (last visited April 18, 2010).

[13] INTERNATIONAL MONETARY FUND, REGIONAL ECONOMIC OUTLOOK: MIDDLE EAST AND CENTRAL ASIA, 27-28, (May 2008) ("Producers and many analysts say it is speculative activity that is pushing up oil prices now. Producers in particular argue that fundamentals would yield an oil price of about US $80 a barrel, with the rest being the result of speculative activity."), *available at* http://www.imf.org/external/pubs/ft/reo/2008/MCD/eng/mreo0508.pdf (last visited April 18, 2010). *See also* Neil King Jr., *Saudi Arabia's Leverage In Oil Market Is Sapped*, WALL STREET J. (June 16, 2008), *available at* http://online.wsj.com/article/SB121355902769475555.html?mod=googlenews_wsj (last visited April 18, 2010) (quoting Saudi Oil Minister Ali Naimi as saying skyrocketing oil prices were

outsized excessive speculation within the physical derivatives markets has caused unnecessary volatility, including unnecessary and substantial price increases that consumers pay for everyday staples, is supported by further independent and reasoned authority.

As I will demonstrate, whatever debate remains over the question whether excessive speculation (and not supply and demand factors) has been a principal source of price volatility should be put to rest completely by the last of a series of three bipartisan staff reports of the Senate Permanent Subcommittee on Investigations ("PSI"), which on June 24, 2009 (with the express endorsement of both PSI Chair Senator Carl Levin and Ranking Member Senator Tom Coburn[14]) demonstrated conclusively that:

- "[o]ver the past four years . . . increases in wheat prices were nearly as steep as the increases in the price of oil,"[15] during which period wheat prices rose "to record heights"[16];
- there is "significant and persuasive evidence that the large number of wheat futures contracts (long open interest) held by commodity index traders is a primary reason for the pricing problems in the wheat market . . . including . . . the disconnect between wheat futures prices and cash market fundamentals . . . during 2008;[17]"
- "commodity index instruments were, in essence, *speculative bets*;"[18]and
- "[t]he total value of the *speculative* investments in commodity indexes has increased an estimated tenfold in five years, from an estimated $15 billion in 2003, to around $200 billion by mid-2008."[19]

The PSI *Wheat Report* concluded "that the activities of the commodity index traders, in the aggregate, constituted 'excessive speculation' in the wheat market under the Commodity Exchange Act" and "that the CFTC [must] phase out existing exemptions and waivers that allow

"unjustified by the fundamentals" of supply and demand); Mahar Chmaytellin, *OPEC Calls for Curbing Oil Speculation, Blames Funds (Update2)*, BLOOMBERG, Jan. 28, 2009, *available at* http://www.bloomberg.com/apps/news?pid=20601013&sid=aVRKbFhcfdKM (last visited April 18, 2010).

[14] *See* Press Release, Sen. Carl Levin, Investigations Subcommittee Releases Levin-Coburn Report on Excessive Speculation in the Wheat Market (June 24, 2009), *available at* http://levin.senate.gov/newsroom/release.cfm?id=314947 (last visited April 18, 2010).

[15] PERMANENT SUBCOMMITTEE ON INVESTIGATIONS OF THE COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS, EXCESSIVE SPECULATION IN THE WHEAT MARKET (June 24, 2009) at 37 [hereinafter "Wheat Report"].

[16] *Id.* at 39.

[17] *Id.* at 120

[18] *Id.* at 94 (emphasis added).

[19] *Id.* at 5 (emphasis added).

some index traders to operate outside of trading limits designed to prevent excessive speculation."[20]

As such, the Commission should adopt and implement speculative position limits across all exchanges including OTC and FBOT in order to stabilize the markets and to protect producers and consumers against unjustifiably increased prices in commodities.

2. **Are there methods other than Federal speculative position limits that should be utilized to diminish, eliminate, or prevent such burdens?**

It is my opinion that Federal speculative position limits is the most effective method to diminish, eliminate, or prevent the burdens on interstate commerce that may result from position concentrations *providing that* speculative position limits apply to all currently regulated markets as well as OTC and FBOT.

The CFTC, because of the Commodity Futures Modernization Act of 2000, does not now oversee the trading of physical OTC derivative products that are exempt or excluded from its jurisdiction. Therefore, the Commission's proposal to apply speculative position limits to control excessive and destabilizing speculation in energy markets will at best have limited reach as the limits will only apply to those portions of the derivatives markets that the CFTC now oversees. Should CFTC supervised exchange trading become required by the new legislation working its way through Congress, the CFTC would be in a position to effectively guard against volatile and unnecessary price spikes in energy and food on a uniform, rather than partial, basis.

Indeed, all Commissioners have raised concerns about whether the CFTC lacks the regulatory authority to impose Federal speculative limits upon all similar energy contracts. Specifically, they are concerned that as the CFTC increases transparency in currently regulated markets, the proposed speculative position limits may undermine the Commission's efforts by allowing participants to turn to the less regulated and less transparent OTC or FBOT, which would be detrimental to the markets and to the public.[21]

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[20] *Id.* at 2-3.

[21] *See* Concurring Statement of Commissioner Scott D. O'Malia, on Proposed Federal Speculative Position Limits for Referenced Energy Contracts and Associated Regulations, CFTC, January 14, 2010, *available at* http://www.cftc.gov/ucm/groups/public/@newsroom/documents/speechandtestimony/omaliastatement011410.pdf (last visited April 16, 2010); Statement of Commissioner Bart Chilton, on Notice of Proposed Rulemaking for Speculative Position Limits for Referenced Energy Contracts, CFTC, January 14, 2010, *available at* http://www.cftc.gov/ucm/groups/public/@newsroom/documents/speechandtestimony/chitlonstatement011410.pdf (last visited on April 18, 2010) (noting that "there would be a possibility that trading migration could take place, transferring traders to over-the-counter markets or overseas exchanges. […] Hundreds of trillions of dollars are traded in these dark markets and they can influence the price that consumers pay for everything from gasoline, to a loaf of bread, to a home mortgage."); Closing Statement of Commissioner Michael V. Dunn, on Meeting on Energy Position Limits and Hedge Exemptions, CFTC, January 14, 2010, *available at* http://www.cftc.gov/ucm/groups/public/@newsroom/documents/speechandtestimony/dunnstatement011410.pdf (last visited on April 18, 2010) ("I am concerned that the adoption of this proposed regulation, without the corresponding OTC regulatory authority and similar undertakings by other nations' regulators, may result in less

Accordingly, legislative authority is needed to allow the CFTC to utilize and implement overarching limits across all markets by all trading done within a control entity whether the trading venue is directly regulated or not. In this respect, I fully support the bill reported out of Senate Agriculture, Nutrition, and Forestry Committee last week. If that bill, The Wall Street Transparency and Accountability Act of 2010,[22] is enacted, it will be required that most derivative contracts be traded on a public exchange and cleared through a third party to guarantee payment.

Another issue is whether ICE Futures Europe, which trades a cash settled crude oil WTI futures contract linked to NYMEX WTI contracts on U.S.-based trading terminals, can or will be subject to new CFTC position limits and hedge exemption policies. NYMEX is a U.S. designated contract market directly regulated by the CFTC. Position limits affecting NYMEX's traditional physical futures trading is squarely within the CFTC's jurisdiction. ICE Futures Europe, however, operates its WTI crude oil derivatives futures contract trading under a 1999 CFTC staff no action letter issued to a predecessor U.K. exchange, the International Petroleum Exchange, which places ICE Futures Europe's substantial U.S. terminal trading under the direct regulatory supervision of the U.K.'s Financial Services Authority.[23]

There has been substantial debate over the propriety of labeling ICE Futures Europe a U.K. regulated company while at the same time permitting it to offer U.S. citizens trading privileges on U.S. terminals in a futures contract denominated in U.S. dollars and premised on the U.S. benchmark WTI contract. No doubt in response to that valid Congressional concern, on June 17, 2008, the CFTC staff amended ICE Futures Europe's no action letter to impose four new requirements on ICE Futures Europe- conditioning its ability to maintain its status as a U.K. regulated entity. These four conditions include, *inter alia*, a requirement that ICE Futures Europe adopt the position limits used by its principal U.S. competitor in energy futures trading, NYMEX.[24] Therefore, any CFTC mandated changes in WTI position limits applicable to NYMEX would also indirectly be applicable to ICE Futures Europe.

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transparency in the futures markets if those presently trading on exchange move to OTC and other opaque markets to circumvent these proposed position limits."); Dissenting Statement of Commissioner Jill E. Sommers, on Proposed Federal Speculative Position Limits for Referenced Energy Contracts and Associated Regulations, CFTC, January 14, 2010, available at http://www.cftc.gov/ucm/groups/public/@newsroom/documents/speechandtestimony/sommersstatement011410.pdf (last visited on January 18, 2010) (noting that "I am concerned that hard positions limits may be imposed on exchange trading without similar limits in place for OTC markets. […] Likewise, I am concerned that, without global standards, trading will move to other financial centers around the world").

[22] The Wall Street Transparency and Accountability Act of 2010, S.___, 111th Cong. (2010).

[23] International Petroleum Exchange of London Limited, CFTC No-Action Letter, CFTC Letter No. 99-69, *available at* http://www.cftc.gov/tm/letters/99letters/tm99-69.htm (last visited April 18, 2010).

[24] International Petroleum Exchange (now ICE Futures Europe), CFTC No-Action Letter, CFTC Letter No. 08-09, *available at* http://www.cftc.gov/stellent/groups/public/@lrlettergeneral/documents/letter/08-09.pdf (last visited April 18, 2010).

While the CFTC therefore has an indirect method for establishing its position limit and hedge exemption regime upon ICE Futures Europe, there continues to be considerable discussion about why the CFTC does not simply terminate ICE Futures Europe's no action letter (as that letter and amendments to its expressly allow) as the no action license applies to trading of ICE Future Europe's contracts in the U.S., thereby bringing that exchange under CFTC day-to-day supervision.

Some adopt the position that, because § 4 (a)'s registration requirements do not apply to any exchange "located outside the United States" and § 4 (b) does not allow CFTC rules to "govern in any way" foreign exchanges, ICE Futures Europe's trading of the U.S. benchmark WTI contract on U.S. trading terminals with U.S. servers in U.S. denominated dollars is outside the reach of the CFTC.

Even if this were a correct reading of § 4, the trading on ICE Futures Europe's U.S.-based terminals can not in any sense be deemed "foreign."(And, this argument would remain true even if pending legislation in Congress authorizes the CFTC to impose position limits and other regulatory controls on the U.S. trading of *foreign* boards of trade.) In this regard, ICE Futures Europe is the wholly owned subsidiary of a U.S. holding company, the Intercontinental Exchange ("ICE"), which is a Delaware corporation located in Atlanta, Georgia. ICE operates exempt commercial markets and regulated contact markets in the U.S. ICE Futures Europe has trading terminals in the U.S.; its trading engines are in Chicago, Illinois; and it has traded a considerable portion of U.S. WTI crude oil futures market. Whatever protection § 4 (or future legislation) has for exchanges "located outside the United States," ICE Futures Europe, insofar as it trades the U.S. benchmark crude oil futures contract in the United States with U.S. trading engines and terminals is very much located here.

Moreover, the underlying premise of the no action letter on which ICE Futures Europe relies is that, but for the no action letter, exchange would be fully subject to U.S. CFTC regulation when it brings its trading terminals physically into the U.S. That was true when the no action letters were first issued in 1999;[25] when the CFTC issued its 2006 Policy on this subject;[26] and it is evidenced by the CFTC staff's June 17 2008 letter to ICE Futures Europe expressly stating that the failure to comply with the four new conditions, including position limits, imposed by the CFTC staff at that time would lead to a recommendation to "institute

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[25] The no action letters at issue originated from a rulemaking proceeding, that by it very terms, provided that permission to put terminals in the U.S. derived from Section 4 (c)'s exemption from U.S. contract market registration requirements and not from a statutory prohibition from regulating foreign exchanges "outside of the United States." *See* LIFFE Administration & Management, CFTC No-Action Letter, 1999 CFTC Ltr. LEXIS 38, 3 n. 4 (July 23, 1999); Access to Automated Boards of Trade (proposed rules), 64 Fed. Reg. 14,159, 14,174 (Mar. 24, 1999).

[26] "In the absence of no-action relief, a board of trade, exchange or market that permits direct access by U.S. persons might be subject to Commission action for violation of, among other provisions section 4 (a) of the CEA, if it were not found to qualify for the exclusion from the DCM designation or DTEF registration requirement." 71 Fed. Reg. 64,443, 445 n.23 (Nov. 2, 2006).

enforcement action against [ICE Futures Europe] based on a failure to seek contract market designation or registration as a DTEF under Sections 5 and 5a of the Act."[27]

The CFTC's stance in its June 17 letter to ICE Futures Europe is in keeping with a host of federal cases and CFTC enforcement actions making it clear that the prohibitions on the CFTC with regard to foreign exchanges within § 4 only apply when *foreigners* trade foreign futures contracts in *foreign* countries on *foreign* exchanges that do not significantly impact U.S. markets.[28]

As evidenced by the June 17, 2008 CFTC staff letter establishing further conditions on ICE Futures Europe's U.S. trading operations, it appears that the CFTC is trying hard to create indirectly *equivalency* between what is required of a U.S. exchange directly regulated by it and a direct competitor exchange, ICE Futures Europe, in the latter's present capacity as a UK regulated exchange for purposes of its substantial futures trading in the U.S.

In so doing, the CFTC is dependent on data flowing smoothly from the U.K's regulator. Media reports have suggested that in important instances data of this nature has not always flowed as effectively as the CFTC would have hoped. As a result of the CFTC's dependency on the FSA for trading done by ICE Futures Europe in the U.S., despite the CFTC's hard work in gaining equivalency through its staff with regard to direct competition in the U.S. between U.S. DCMs and ICE Futures Europe, important regulatory measures applicable in the U.S. still do not apply to ICE Futures Europe. At the very least, the self regulation required of U.S. DCMs *in practice* is much more demanding here than that found in the U.K. Also, § 8a (9)'s important grant of emergency powers to the CFTC to take strong action and direct action in markets under its jurisdiction does not apply to those exchanges falling under the FSA's authority. As a matter of prudence, the CFTC should assume direct supervision over substantial futures trading done in the U.S. by U.S. citizens on important U.S. benchmark crude oil futures contracts. This trading, over which CFTC should assume direct supervision, is clearly and unambiguously in direct competition in the U.S. with a U.S. regulated exchange. Failure to assume such responsibility is unreasonable.

5. **Under proposed regulation 151.2(b)(1)(i), the Commission would establish an all-months-combined aggregate position limit equal to 10% of the average combined futures and option contract open interest aggregated across all reporting markets for the most recent calendar year up to 25,000 contracts, with a marginal increase of 2.5% of open interest thereafter. As an alternative to this approach to an all-**

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[27] *See* International Petroleum Exchange (now ICE Futures Europe), CFTC No-Action Letter, CFTC Letter No. 08-09, *available at* http://www.cftc.gov/stellent/groups/public/@lrlettergeneral/documents/letter/08-09.pdf (last visited April 18, 2010).

[28] See the discussion of relevant cases in Written Testimony of Professor Michael Greenberger, *Energy Speculation: Is Greater Regulation Necessary to Stop Price Manipulation? – Part II: Hearing Before the House Energy and Commerce Subcomm. on Oversight and Investigations* 9-12 (June 23, 2008), *available at* http://www.michaelgreenberger.com/files/June_23_2008_testimony.pdf (last visited April 18, 2010).

months-combined aggregate position limit, the Commission requests comment on whether an additional increment with a marginal increase larger than 2.5% would be adequate to prevent excessive speculation in the referenced energy contracts. An additional increment would permit traders to hold larger positions relative to total open positions in the referenced energy contracts, in comparison to the proposed formula. For example, the Commission could fix the all-months-combined aggregate position limit at 10% of the prior year's average open interest up to 25,000 contracts, with a marginal increase of 5% up to 300,000 contracts and a marginal increase of 2.5% thereafter. Assuming the prior year's average open interest equaled 300,000 contracts, an all-months-combined aggregate position limit would be fixed at 9,400 contracts under the proposed rule and 16,300 contracts under the alternative.

I fully support the Commission's proposal to establish an all-months-combined aggregate position limit equal to or less than 10% of the average combined futures and option contract open interest aggregated across all reporting markets, OTC, and FBOT.

6. **Should customary position sizes held by speculative traders be a factor in moderating the limit levels proposed by the Commission? In this connection, the Commission notes that current regulation 150.5(c) states contract markets may adjust their speculative limit levels "based on position sizes customarily held by speculative traders on the contract market, which shall not be extraordinarily large relative to total open positions in the contract * * *"**

I agree with PMAA's comment letter that the Commission should revise the proposed limit levels downward to ensure fair and orderly markets and prevent a small handful of speculators from holding a controlling percentage of the open interest in any of these contracts. At the levels being proposed, PMAA is concerned that the position limits will have little, if any impact, on market concentration. More restrictive position limits would help restore the balance that historically has existed between speculative traders and commercial users of these markets and help prevent price distortions that can result from unduly large speculative positions.[29]

7. **Reporting markets that list referenced energy contracts, as defined by the proposed regulations, would continue to be responsible for maintaining their own position limits or position accountability rules. The Commission seeks comment on whether it should issue acceptable practices that adopt formal guidelines and procedures for implementing position accountability rules.**

Given the powerful nature of the position limits in tamping down highly price distorting excessive speculation and the fact that position limits are a tool mandated by Congress to prevent excessive speculation in physical futures markets, the time has come for the Commission to take back from the exchanges their authority to set position limits on non-agricultural physical futures trading. Moreover, the Commission must carefully weigh the effectiveness of the existing

[29] *See* Comment Letter of Petroleum Marketers Association America (PMAA), Federal Speculative Position Limits for Referenced Energy Contracts and Associated Regulations.

position limits for those agricultural products the Commission itself now sets. Also, in determining whether to deploy as its own those spot month position limits presently set by the exchanges, the Commission must carefully examine the effectiveness of those limits set up until this point because the Commission clearly has existing legislative authority to take all of these actions.

The first proposition must be that the Commission itself –not the Commission staff or the exchanges—must be the final decision maker about the propriety and effectiveness of those limits. I understand that there may be a fine line between encouraging enough speculation to accommodate liquidity, but not allowing so much that speculation is excessive. However, the Commission has the experience of setting those limits for agricultural products. It has regulations that broadly govern and direct the methodology for position limit establishment.[30] I agree with those who have recommended that physical hedgers be very actively involved in that process. Indeed, I would recommend that hearings be established to allow a broad array of participants to offer on a transparent basis technical guidance to the Commission about the establishment of these controls.

However, action of this nature must be done expeditiously with the recognition that the Commission has authority to fine tune limits it sets. The Commission may also consider prioritizing its actions for those physical markets about which it has particular concern. It should also consider using emergency agency decision making authorities afforded by the Administrative Procedures Act or, where appropriate, the express emergency authority within § 8a (9) of the CEA to expedite its processes. The latter provision expressly authorizes both the establishment of temporary emergency margining and/or position limits if the Commission finds that there is a "major market disturbance which prevents the market from accurately reflecting the forces of supply and demand for such commodity."

8. **Proposed regulation 151.3(a)(2) would establish a swap dealer risk management exemption whereby swap dealers would be granted a position limit exemption for positions that are held to offset risks associated with customer initiated swap agreements that are linked to a referenced energy contract but that do not qualify as bona fide hedge positions. The swap dealer risk management exemption would be capped at twice the size of any otherwise applicable all-months-combined or single non-spot-month position limit. The Commission seeks comment on any alternatives to this proposed approach. The Commission seeks particular comment on the feasibility of a ``look-through'' exemption for swap dealers such that dealers would receive exemptions for positions offsetting risks resulting from swap agreements opposite counterparties who would have been entitled to a hedge exemption if they had hedged their exposure directly in the futures markets. How viable is such an approach given the Commission's lack of regulatory authority over the OTC swap markets?**

[30] 17 C.F.R. § 1.3(z) and Part 150.

Although I generally support the Commission proposal to adopt a *bona fide* hedging exemption for traders hedging commercial risks to the extent of their demonstrated needs,[31] the Commodity Exchange Act requires the Commission impose a strict standard for granting such exemption.

The PSI *Wheat Report* has posed the question whether the statutory definition of "bona fide hedging transaction" (*i.e.*, a transaction not subject to position limits) should include the hedging of financial risk, *e.g.*, index commodity swap traders offsetting their exposure to their swaps customer by buying corresponding physical futures contracts on a regulated exchange.

For purposes of wheat futures, the PSI *Wheat Report* recommends the phasing out of hedge exemptions of this nature for commodity index traders. Again, it must be remembered that only 5.2% of the Goldman Sachs Commodity Index is composed of Chicago wheat. The other 94.8% of the physical commodities referenced within that index similarly require hedging by commodity index traders in the corresponding agricultural, crude oil, and natural gas futures contracts. The *Wheat Report*'s findings on commodity index trading on wheat prices corroborates the abundance of information described above that price spikes in other physical commodities trace their origins to hedge exemptions from position limits on all exchange traded futures markets that correspond to the commodity index physical products makeup.

Until the Commission is convinced that these physical futures markets have returned on a stable basis to economic fundamentals, it cannot lawfully grant any hedge exemptions to hedge financial risk and it should phase out all existing exemptions of this nature. Again, as mentioned above, Congress has not mandated that those hedging financial risk be deemed "bona fide hedgers." By a 1987 *interpretation* only (and not even by a substantive rule), the Commission has afforded itself the *discretion* (not the *obligation*) to grant such exemptions. It must exercise that discretion with great prudence and with an eye towards the fact that there overwhelming evidence that the present speculative activity in the regulated futures markets have destabilized prices (unmooring them from economic fundamentals) and that commercial hedgers have been driven from the regulated futures markets because of the unpredictable volatility caused by excessive speculation.

It should be noted that experience may very well demonstrate that the elimination of hedge exemptions to offset financial risk may, in and of itself, cure problems with the setting of position limits. For example, the PSI *Wheat Report* first recommended the abolition and phasing out of troublesome speculative hedge exemptions and then only, secondarily, suggested that consideration be given by the Commission to lowering the spot month limit for Chicago wheat from 6500 contracts to 5000 contracts where it had previously been.[32] This suggestion implicitly recognizes that the problem may not be with the setting of spot month position limits, but with the unwise granting of hedge exemptions for financial risk management from those limits.

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[31] Proposed Regulation 17 C.F.R. §151.3(a)(1).

[32] Wheat Report, *supra* note 14, at 13-14.

9. **Proposed regulation 20.02 would require swap dealers to file with the Commission certain information in connection with their risk management exemptions to ensure that the Commission can adequately assess their need for an exemption. The Commission invites comment on whether these requirements are sufficient. In the alternative, should the Commission limit these filing requirements, and instead rely upon its regulation 18.05 special call authority to assess the merit of swap dealer risk management exemption requests?**

I oppose any exemption for swaps dealers, e.g., for Goldman Sachs and Morgan Stanley. An exemption of this kind is in violation of the plain language of the law, which cannot be subsumed by "interpretations" or isolated legislative passages. In any event, exemptions of this sort would be arbitrary and capricious under the Administrative Procedures Act because of the overwhelming factual basis that demonstrates that the existing exemptions granted to swap dealers have caused unnecessary financial hardship worldwide by needlessly driving up the price of energy and food far beyond what market fundamentals dictate.[33] A vote by a Commissioner for swaps dealer exemptions is a vote to maintain the status quo where hard working Americans whose taxes bailed out those institutions that are swaps dealers and who are fighting the joblessness (one out of every six Americans is unemployed or underemployed) and insecurity of the Great Recession must carry the added burden of paying yet again a premium for their energy and food needs to bailed out Wall Street banks– a premium that bears no relationship to the production of food and energy, but only lines the pockets of passive speculators in these markets.

If there is to be a "swaps dealer" exemption for banks such as Goldman Sachs and Morgan Stanley, I would fully support the proposed regulation 20.02 that requires swap dealers to file with the Commission certain information in connection with their risk management exemptions to ensure that the Commission can adequately assess their need for an exemption. Relying on the Commission's special call authority pursuant to its regulation 18.05 would impose an unnecessary burden on the Commission and would waste the Commission's valuable administrative resources.

12. **As discussed previously, the Commission has followed a policy since 2008 of conditioning FBOT no-action relief on the requirement that FBOTs with contracts that link to CFTC-regulated contracts have position limits that are comparable to the position limits applicable to CFTC-regulated contracts. If the Commission adopts the proposed rulemaking, should it continue, or modify in any way, this**

[33] Congressman Bart Stupak, Testimony Before the Commodity Futures Trading Commission on Energy Position Limits and Hedge Exemptions 3 (July 28, 2009), *available at* http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/hearing072809_stupak.pdf (reporting that according to congressional investigation, the oil futures market had been "taken over by swap dealers and speculators").

policy to address FBOT contracts that would be linked to any referenced energy contract as defined by the proposed regulations?

Please see my comment for Question 2.

13. **The Commission notes that Congress is currently considering legislation that would revise the Commission's section 4a(a) position limit authority to extend beyond positions in reporting market contracts to reach positions in OTC derivative instruments and FBOT contracts. Under some of these revisions, the Commission would be authorized to set limits for positions held in OTC derivative instruments and FBOT contracts. The Commission seeks comment on how it should take this pending legislation into account in proposing Federal speculative position limits.**

Because the hardship Americans incur in paying a speculator's premium to banks such as Goldman Sachs and Morgan Stanley, this Commission should not await the passage of any new legislation to impose limits on speculators. Moreover, even if the legislation does pass, the implementation of the new legislation will take many months. Position limits controls cannot wait for that implementation to be completed. The Commission should act promptly to use existing authorities to impose tight speculative controls on Wall Street banks as an aid to the American taxpayer, who has already paid too high a price because of financial and commodity speculations orchestrated by the very Wall Street institutions the American taxpayer has had to bail out. Those bailed out institutions are now thriving while the average American is either jobless, under employed, or worried about his or her economic future. The Commission has the power to help American consumers. It is required by the Commodity Exchange Act to act immediately or explain to the American public why existing statutory mandates are being ignored.

15. **Concerns have been raised about the impact of large, passive, and unleveraged long-only positions on the futures markets. Instead of using the futures markets for risk transference, traders that own such positions treat commodity futures contracts as distinct assets that can be held for an appreciable duration. This notice of rulemaking does not propose regulations that would categorize such positions for the purpose of applying different regulatory standards. Rather, the owners of such positions are treated as other investors that would be subject to the proposed speculative position limits.**

    a. Should the Commission propose regulations to limit the positions of passive long traders?

    b. If so, what criteria should the Commission employ to identify and define such traders and positions?

    c. Assuming that passive long traders can properly be identified and defined, how and to what extent should the Commission limit their participation in the futures markets?

    d. If passive long positions should be limited in the aggregate, would it be feasible for the Commission to apportion market space amongst various traders that wish to establish passive long positions?

    e. What unintended consequences are likely to result from the Commission's

implementation of passive long position limits?

There is overwhelming support for the proposition that *excessive* speculation is a culprit causing unfair and dysfunctional markets. Underlying this contention is a fundamental understanding that futures markets are designed not to raise capital for, or provide lending to, business interests.[34] The entire rationale of these markets is to provide risk shifting vehicles to commercial producers and consumers. The tension between commercial producers and consumers trying to achieve fair prices for the sale and/or purchase of physical commodities through the public transparent hedging process moors these price discovery futures markets to economic fundamentals and, correspondingly, ensures fair market prices to the ultimate consumers of these commodities.

Speculators have a role to play in the hedging function *when* they are needed to ensure that the market has liquidity, *i.e.,* physical hedgers are almost always not numerous enough to ensure that contracts may be traded expeditiously among them, thereby ensuring much needed liquidity within these markets. However, President Roosevelt, in his 1934 message to Congress urging the passage of the CEA, considered it axiomatic that speculation cannot be "excessive," because, as the farmers learned to their dismay in the early 20th century, too much speculation, *i.e.*, more speculation than is needed to provide hedgers with liquidity, will unmoor the market from the competing tensions between consumers and producers when there is an overriding speculative influence.

Speculators' motivations do not include ensuring fair prices. They are simply betting on the direction of the market and their sole interest is that the markets go as high or as low as possible in support of their betting strategy. To the extent the speculator is providing liquidity for physical hedgers, the speculator is serving a public interest by assisting in the hedging function (*i.e*., providing enough counterparties for physical hedgers) even though it is pocketing gains.

When speculation is "excessive," however, those market "bets," as shown in PSI's *Wheat Report* described above, unmoor the market from fundamentals, causing prices to vary from supply and demand principles, and, correspondingly, drive the hedger from the markets because of volatility and unpredictability. If commercial interests cannot hedge in a fair and orderly market, they and their ultimate consumers, the public at large, are left to the mercy of volatile markets that undercut the hedging function. A contract market dominated by speculators changes the market from one that constructively shifts risk into a casino-like atmosphere consisting of bets on market direction unmoored from real world market responsibilities.

[34] Support for observations within this and the succeeding two paragraphs of this testimony can be found, *inter alia*, in the within the Wheat Report at pages 50-75, where there is a thorough and scholarly explanation of the purpose and beneficial hedging role of properly functioning futures markets, including observations about the proper role of speculation and the controls that must be imposed by the CFTC on speculation to keep it from becoming "excessive" and dysfunctional.

The PSI found that unchecked excessive speculation by passive commodity index funds led to substantial price dysfunctions within the wheat markets, including the price of wheat climbing by mid-2008 to "record heights" and "then falling sharply during the latter half of 2008."[35] The PSI report explains that commodity indexes offer investors the purchase of a "financial instrument whose value is linked to a commodity index enable[ing] an investor to get broad exposure to commodities without having to actually purchase quantities of each commodity or manage a portfolio of commodity investments."[36]

A chart of the popular S&P Goldman Sachs Commodity Index ("GSCI") as of March 2009 shows, for example, that crude oil futures make up over 44% of that commodity index, and all energy commodities over 65%, while all agricultural products make up about 18% of the index with Chicago wheat (CME wheat) composing 5.2% of the index on its own.[37] The *Wheat Report* states: "Financial institutions have devised several types of financial instruments to enable investors to gain exposure to the value of a commodity index."[38] The Report further notes: "The most common type of commodity index instrument is a . . . 'swap' whose return is based upon the performance of a specified index. . . If the value of the commodity index increases, the value of the swap to the purchaser will increase by a corresponding amount."[39] The swaps are sold by swaps dealers "'over the counter,' outside of the statutory and regulatory framework that applies to futures exchanges."[40]

Because most investors in commodity index swaps are going "long," *i.e.*, they wish to profit from an increase in the basket of commodities, the swaps dealer which holds the other side of the transaction "short" the basket of commodities and, if not hedged, it will lose money if the commodities gain in value. To eliminate that exposure to their swaps customers, "swaps dealers frequently use the futures markets for the purpose of obtaining . . . hedges or offsets,"[41] *i.e.*, laying off the risk to their customers by buying offsetting futures contracts on the futures exchanges reflecting commodity holdings in the index "basket."

Investments in commodity indexes are "purchased mainly by financial institutions, insurance companies, pension funds, foundations, hedge funds and wealthy individuals[.]"[42] According to the *Wheat Report*, the value of these investments "has grown more than tenfold in five years, from an estimated $15 billion in 2003, to at least $200 billion in mid-2008. The

[35] Wheat Report, *supra* note 14, at 37.
[36] *Id.* at79.
[37] *Id.* at 81.
[38] *Id.* at 83.
[39] *Id.* at 83.
[40] *Id.* at 83.
[41] *Id.* at 84.
[42] *Id.* at 76.

purchases of these index instruments have resulted in the injection of billions of dollars in passive, long investments into the agricultural, energy, and metals futures markets."[43]

The *Wheat Report* refers to articles appearing in 2006 indicating "that purchases of commodity index instruments were, in essence, *speculative bets* on the structure of the commodities futures markets rather than a risk-free technique for portfolio diversification."[44] Another analyst "left his readers with the following advice: 'The next time someone tries to sell you a commodities fund based on the Goldman Sachs Commodities Index, smile and say, 'Sorry, but I'm from Earth, and you're from planet *I Love Lucy*. Let's revisit this discussion in an alternate universe.'"[45]

Section 4a(c) of the CEA grants an exemption from position limits for "bona fide hedging transactions," leaving to the CFTC the discretion to define that term "consistent with the purposes" of the CEA to "permit" futures market users "to hedge their legitimate anticipated business needs . . . ."

As the PSI aptly states: "While there has been longstanding, broad consensus on the need to grant hedge exemptions [from speculative position limits] for commodity producers, merchants, and end users to manage price risks, granting similar exemptions to *financial* firms . . to manage their *financial* risks has been the subject of longstanding debate and controversy."[46]

Based on the interpretation of various Congressional *reports* (but not legislative directives), the CFTC in 1987 "issued a new *interpretation* of bona fide hedge transactions to permit exchanges to grant hedge exemptions for various [*financial*] risk management transactions."[47] Pursuant to that 1987 interpretation, "in 1991 the [CFTC] staff granted a . . . hedge exemption to a swap dealer who was seeking to manage price risk on its books as a result of swaps it planned to enter into with various investors [in] commodity indexes. Similar hedge exceptions were subsequently granted . . . where the futures positions offset risks related to swaps or similar OTC positions involving both individual commodities and commodity

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[43] *Id.* at 76 (emphasis added).
[44] *Id.* at 94 (emphasis added); *See* also DAVID GREELY & JEFFREY CURRIE, GOLDMAN, SACHS & CO., COMMODITIES: SPECULATORS, INDEX INVESTORS, AND COMMODITY PRICES 4 (2008); GOLDMAN SACHS INV. STRATEGY GROUP, COMMODITIES: A SOLUTION IN SEARCH OF A STRATEGY 7 (2010) (noting that in January 2010, Goldman Sachs Investment Strategy Group advised Goldman's Private Wealth Management Clients in a highly detailed report that "We [Goldman Sachs] have concluded that there is no consistent and reliable argument for a strategic allocation to a commodity futures index in a well-diversified portfolio.").
[45] *Id.* at 102 (emphasis added and citations omitted).
[46] Wheat Report, *supra* note 14, at 74 (emphasis added).
[47] Testimony of General Counsel Dan M. Berkovitz, Before the Commodity Future Trading Commission on Energy Positions Limits and Hedge Exemptions at 13-14, *available at* http://www.cftc.gov/stellent/groups/public/@newsroom/documents/speechandtestimony/berkovitzstatement072809.pdf (last visited on April 18, 2010) (emphasis added).

indexes.[48] On two occasions, CFTC staff has approved no action letters to managers of commodity index ETFs from the CFTC established position limits for agricultural commodities.

The CFTC has, since 2005, granted hedge exemptions for four swaps dealers for wheat futures trading on the Chicago futures exchange to allow those dealers to hedge their exposure to their commodity index swaps investors. The *Wheat Report* states: "Those exemptions permit the swaps dealers to hold up to 10,000, 17,500, 26,000, and 53,000 wheat futures contracts."[49] Adding CFTC staff hedge exemptions granted to ETFs, those "six index traders . . . hold a total of up to almost 130,000 wheat futures contracts in any single month and in all months combined" measured against an allowable limit of 39,000 contracts in the absence of the hedge exemptions.[50]

Thus, those six commodity index traders "may have held as much as 60% of the long open interest in" CME wheat futures contracts.[51] Further, the *Wheat Report* states: "If each swap dealer were restricted to holding no more than 6,500 wheat futures contract at any given time [*i.e.*, limited to the spot month CFTC-established position limit] these swaps dealers would have had to find another way to offset their financial exposure to the commodity index swaps they sold, or to assume the outright risk from those swaps."[52]

Accordingly, PSI found that the excessive speculation in the wheat futures market caused "unwarranted changes and unreasonable fluctuations" in the price of wheat futures contracts, and thus an "undue burden on interstate commerce." [53] It therefore recommended phasing out existing hedge exemptions for wheat futures for index traders and the possible consideration of reducing position limits on those markets from 6,500 to 5,000 contracts. It also recommended that the CFTC study other agricultural commodity markets and strengthen data collection of the impact of index traders on non-agricultural commodities, "especially crude oil and other energy commodities."[54]

17. **Under the proposed regulations, a swap dealer seeking a risk management exemption would apply directly to the Commission for the exemption. Should such exemptions be processed by the reporting markets as would be the case with bona fide hedge exemptions under the proposed regulations?**

The markets are now so unmoored from market fundamentals that commercial hedgers are being driven from them while prices far exceed market fundamentals. This is a time when the Commission – not the exchanges- owes it to the American taxpayer and consumer to take over all decision making power as to the imposition of position limits and exemptions from the exchanges. The existing position limits system as governed by the exchanges has been a

[48] *Id.* at 18.
[49] Wheat Report, *supra* note 14, at 105.
[50] *Id.* at 105.
[51] *Id.* at 106.
[52] Wheat Report, *supra* note 14, at 104, n. 187.
[53] *Id.* at 157.
[54] *Id.* at 16.

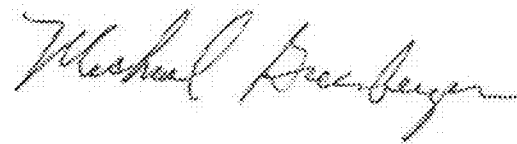
complete failure. Americans have needlessly paid prices for energy and food that far exceed those dictated by supply and demand fundamentals to line the pockets of speculators. The Commissioners owe those Americans a duty to take over the position limits system until the futures markets return to the status quo ante - smooth operation consistent with supply and demand fundamentals.

18. In implementing initial spot-month speculative position limits, if the notice of proposed rulemaking is finalized, should the Commission:
   a. Issue special calls for information to the reporting markets to assess the size of a contract's deliverable supply;
   b. Use the levels that are currently used by the exchanges; or
   c. Undertake an independent calculation of deliverable supply without substantial reliance on exchange estimates?

The Commission should undertake an independent calculation as well as issue special calls for information to the reporting markets and OTC to assess the size of a contract's deliverable supply. In doing so, the Commission should consider the levels that are currently used by the exchanges as a standard for assessment.

I applaud the Commission's effort to stabilize and restore faith in the market. I would like to express my confidence in the Commission's great capacity for monitoring, trading, and implementing remedial matters across interconnected commodity futures and open markets. I appreciate the opportunity to comment on the proposed rules.

Sincerely,



Michael Greenberger
Law School Professor
University of Maryland
500 W. Baltimore Street
Baltimore MD 21201
(o) 410-706-3846
mgreenberger@law.umaryland.edu