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Sent: Monday, April 26, 2010 6:16 PM
To: secretary <secretary@CFTC.gov>
Cc: Baker, Richard H. <Richard@managedfunds.org>; Kaswell, Stuart <stuart@managedfunds.org>; Eric Vincent <eric.vincent@ospraie.com>
Subject: Proposed Federal Speculative Position Limits for Referenced Energy Contracts and Associated Regulations
Attach: MFA CFTC energy spec limits.4.26.10.pdf

Dear Mr. Stawick,

Managed Funds Association is pleased to submit the attached comments to the Commission's proposal on "Federal speculative position limits for referenced energy contracts and associated regulations."

Please feel free to contact me if you have questions or comments.

Regards,

Jennifer Han | *Assistant General Counsel* | jennifer@managedfunds.org

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Register for MFA's Forum 2010, June 8-9, 2010, The Drake Hotel, Chicago.
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April 26, 2010

Via Electronic Mail: secretary@cftc.gov

David A. Stawick
Secretary
Commodity Futures Trading Commission
1155 21st Street, N.W.
Washington, D.C. 20581

Re: Proposed Federal Speculative Position Limits for Referenced Energy Contracts
And Associated Regulations

Dear Mr. Stawick:

Managed Funds Association (“MFA”)¹ appreciates the opportunity to comment on the Commodity Futures Trading Commission’s (“Commission”) Notice of proposed rulemaking on Federal Speculative Position Limits for Referenced Energy Contracts and Associated Regulations (the “Notice”), which proposes to implement federal speculative position limits for futures and option contracts in certain energy commodities². MFA recognizes that there has been a great deal of public focus on commodity price increases and volatility, and energy prices in particular, and the role and impact of speculators. We further understand that some voices have called for the Commission to impose additional restrictions on speculators (beyond those imposed by futures exchanges) to address energy price volatility and restore confidence in the price discovery function of futures markets.

We appreciate the Commission’s efforts to respond to the concerns by publishing its Notice and seeking public comment. As longstanding market participants, we rely on fair, competitive, and transparent markets that respond to fundamental factors to conduct our businesses. MFA’s members play a vital role in the energy futures markets by assuming the price risk from commercial participants (hedgers) on both the long and short sides of the market, and by providing liquidity that facilitates risk transfer and price discovery for businesses around the world. Some of MFA’s members also invest in operating companies whose business involves the production, refining, merchandising or processing of energy and entities engaged in the development of energy market infrastructure (such as production, transportation or storage of energy)³, and thus have an interest in enabling such entities to access liquid price discovery and risk shifting markets. We understand the Commission has issued the Notice to address the perception of excessive speculation causing an undue impact on energy prices.

¹ MFA is the voice of the global alternative investment industry. Its members are professionals in hedge funds, funds of funds and managed futures funds, as well as industry service providers. Established in 1991, MFA is the primary source of information for policy makers and the media and the leading advocate for sound business practices and industry growth. MFA members include the vast majority of the largest hedge fund groups in the world who manage a substantial portion of the approximately \$1.5 trillion invested in absolute return strategies. MFA is headquartered in Washington, D.C., with an office in New York.

² 75 Fed. Reg. 4144 (Jan. 26, 2010) (the “Notice”).

³ “The IEA [International Energy Agency], in its 2009 report, estimates \$25 trillion must be spent just in energy supply infrastructure between now and 2030.” Prepared Statement Before the Commodity Futures Trading Commission of Kevin Norrish, Managing Director of Commodities Research, Barclays Capital (March 25, 2010) (“Norrish Testimony”), at 4.

Extensive studies have been undertaken by public and private institutions around the world on the energy price volatility of 2007-2008, seeking to identify and explain the underlying factors. The vast majority of reputable research has concluded that fundamental factors of supply and demand, along with economic factors such as the decline in the U.S. dollar, were responsible.⁴ There was no evidence to indicate that excessive speculation was to blame.⁵ In fact, longstanding research has shown, including by the Commission, that speculators perform essential functions to the energy markets by transferring risk from commercial participants, providing liquidity, reducing volatility, and contributing to the price discovery process, which benefits hedgers and all consumers and producers of energy.⁶ Restricting this important service, and without establishing the need or fully assessing the cost, could have a significant negative impact. Indeed, economic analyses suggest that the likely result of the proposed federal limits would be a reduction in market participants' ability to transfer risk and hedge against future prices, greater volatility in energy prices over the long term, a reduction in liquidity on U.S. futures markets, and a flight of capital to overseas futures markets coinciding with decreased U.S. competitiveness.⁷

As the Commission engages in rulemaking, we respectfully urge it to carefully examine all relevant data and options. Rulemaking should be empirically driven and not a response to popular sentiment or partial analyses. Otherwise, it can become a vehicle for costly, detrimental and unintended consequences, and can severely impair the efficient functioning and competitiveness of U.S. energy markets.

⁴ See, e.g., "With Better Data, Better Understanding" (January 27, 2009), Lawrence Eagles, J.P. Morgan; MFA Analysis and Recommendations, "The Investor in a Sound Futures Market" (July 2008); CFTC Inter-Agency Task Force on Commodity markets—Interim Report on Crude Oil (July 2008); CFTC Staff Report on Commodity Swap Dealers & Index Traders (September 2008); HM Treasury Global Commodities: A long term vision for stable, secure and sustainable global markets (June 2008); IMF World Economic Outlook (October 2008); GAO Briefings to the House Committee on Agriculture on Issues Involving the use of Futures Markets to Invest in Commodity Indexes (December 2008); International Organization of Securities Commission's Technical Committee (IOSCO) Final Report (March 2009); CME Group white paper "Excessive Speculation and Position Limits in Energy Derivatives Markets", available at <http://cmegroup.com/company/files/PositionLimitsWhitePaper.pdf>.

⁵ See, e.g., "Commodity Price and Futures Positions" (December 16, 2009), Ruy Ribero, Lawrence Eagles and Nicholas von Solodkoff, J.P. Morgan; "We can safely say there is no indication in this data of the fact speculators are pushing the price of oil," Christophe Barret, global oil analyst at Credit Agricole, quoted in Energy Risk (April 13, 2010), available at <http://www.risk.net/energy-risk/news/1600919/cftc-speculators-influence-commodity-markets>; Prepared Testimony of Philip K. Verleger, Jr., Haskayne School of Management, University of Calgary, PKVerleger LLC, to U.S. Commodities Futures Trading Commission on The Role of Speculators in Setting the Price of Oil (August 5, 2009); "Speculators Cleared in U.K. Oil Volatility" (July 28, 2009), The Wall Street Journal; and "Interagency Task Force on Commodity Markets, Interim Report on Crude Oil" (July 22, 2008).

⁶ See, e.g., "A Review of Recent Hedge Fund Participation in NYMEX Natural Gas and Crude Oil Futures Markets", New York Mercantile Exchange, March 1, 2005; "Price Dynamics, Price Discovery and Large Futures Trader Interactions in the Energy Complex, Working Paper First Draft: April 28th 2005", Michael S. Haigh, Jana Hranaiova and James A. Overdahl, Office of the Chief Economist, U.S. Commodity Futures Trading Commission ("Commission Energy Complex Report"); Testimony of Craig Pirrong, Professor of Finance, Director, Global Energy Management Institute, Bauer College of Business, The University of Houston, Before the House Committee on Agriculture (July 7, 2008) ("Pirrong Testimony"); "Populists versus theorists: Futures markets and the volatility of prices" (June, 2006), Explorations in Economic History 44 (2007) 342-362, David S. Jacks ("Jacks Study"), available at www.sciencedirect.com.

⁷ See, e.g., Testimony of Todd E. Petzel, Ph.D., Chief Investment Officer, Offit Capital Advisors, CFTC Hearings to Discuss Position Limits, Hedge Exemptions and Transparency for Energy Markets (July 28, 2009); Testimony of Donald Casturo, Managing Director, Goldman, Sachs & Co., CFTC Hearings to Discuss Position Limits, Hedge Exemptions and Transparency for Energy Markets (July 29, 2009).

We also note that under Section 15(a) of the Commodity Exchange Act (the “CEA”), in considering or determining whether an action is necessary or appropriate to protect the public interest, the Commission must consider, in addition to the protection of market participants and the public, whether the action will promote efficiency, competitiveness and financial integrity of the market for listed derivatives.

In this case, in our view it appears that the empirical data do not support the need for federal speculative position limits in energy contracts, and that the proposed federal limits might harm U.S. energy markets through decreased liquidity and pricing efficiency, and greater transaction costs resulting from such decreased liquidity and wider bid-ask spreads. As a result, if the Commission does make a finding under CEA § 4a(a) that additional measures are needed, then we urge it to consider more effective alternatives, such as those suggested below in Section IV.G, including greater transparency, increased data gathering to identify market manipulation, and strict prosecution of abusive market practices.

I. EXECUTIVE SUMMARY

- Research and experience demonstrate that hard position limits have not reduced price volatility or prevented market manipulation. Commissioner O’Malia noted as much at the Commission’s January 26, 2010 hearing with respect to the agriculture markets.⁸ Thus, it is not clear how the proposed federal limits will achieve their intended purpose with respect to energy markets. In fact, MFA fears that the Commission’s proposals may actually undermine its intent to encourage market transparency and reduce systemic risks through centralized clearing, as participants may be forced to move their transactions to less transparent and non-cleared markets.
- Further, academic and governmental studies and real world examples show that policies restricting investor access to futures markets only impair commercial participants’ ability to hedge and restrict the use of risk management tools. The proposed federal limits will likely result in decreased market liquidity, which in turn will impair the ability of commercial market participants to hedge against rising prices. Proposed federal limits are also likely to increase the risk exposure of commercial participants and ultimately raise energy prices over the long run.
- Restricting trading on U.S. futures markets may drive trading overseas, reducing the competitiveness of U.S. markets. In light of the global nature of energy commodity markets, the portability of trading capital and resources across borders, and the existence of a robust OTC energy market, before acting on its own the Commission should reach agreement with its counterparts in other G-20 countries to arrive at a comprehensive, consistent, and effective approach across related markets.
- The Commission has not met its statutory burden in proposing the federal limits. It has not found as required by CEA § 4a(a) that the proposed federal limits are necessary to prevent the burdens of “excessive speculation” in the energy markets. Nor has the Commission demonstrated that: (1) excessive speculation exists or has been the cause of recent undue price volatility in the energy markets; (2) it has the legal authority to restrict hedgers that are relying on a hedge exemption from engaging in speculative trading in addition to their risk management activities; and (3) it could not achieve its goals through less burdensome and more flexible methods.

⁸ Notice, Concurring Statement of Commissioner O’Malia, at 4172.

- The costs of the proposed federal limits far outweigh the benefits. The Commission underestimates the number of affected parties, the costs to the market of compliance with the proposed rules and the potential unintended consequences. Such consequences are likely to include decreased liquidity and increased price volatility, resulting in higher transaction costs as the bid-offer spreads widen in the futures and OTC markets, and less market transparency and more systemic risk as participants move to less transparent trading venues and/or bilateral, non-cleared transactions. Other consequences include unnecessary constraints on corporate structures and the amount of capital available for investment in commodity operating companies and commodity infrastructure, and considerable administrative burdens and costs in monitoring and complying with multiple overlapping and inconsistent federal and exchange limits, position aggregation requirements, and hedge exemption procedures.
- MFA urges the Commission to consider the availability of alternative approaches. Such alternatives might include implementing aggregate position accountability levels, requiring more comprehensive reporting of positions by traders in all related trading venues, publishing more information about hedger and swap dealer positions in OTC and exchange markets, and using additional resources to expand its current monitoring and enforcement programs.

II. BACKGROUND

The Commission's stated purpose in considering the Proposed Federal Limits is to prevent the "unreasonable and abrupt price movements that are attributable to large or concentrated speculative positions"⁹ and to curb the purported impact of disruptive, excessive speculation by imposing "Federal speculative position limits for futures and options contracts in certain energy commodities and aggregate position limits that would apply across economically similar contracts, regardless of whether such contracts are listed on a single or on multiple markets."¹⁰

MFA agrees that any market participant intentionally creating artificial prices undermines the integrity of the futures markets. We fully support the Commission's efforts to combat market manipulation and protect the integrity of the market. Congress has granted the Commission broad authority to sanction persons who engage in manipulative behavior. Indeed, one of Congress' central goals in enacting the CEA was to prevent price manipulation and/or any other disruptions to market integrity.¹¹

MFA notes that Congress provided that this important goal is to be achieved through a "system of effective self-regulation of trading facilities, clearing systems, market participants and market professionals under the oversight of the Commission".¹² MFA also notes that Congress found that such regulatory imperative is intended to serve the "national public interest of providing a means for managing and assuming price risks, discovering prices, or disseminating pricing information through trading in liquid, fair markets".¹³

MFA believes that, when the Commission exercises its regulatory oversight authority, it must be cognizant of the effect of the proposed federal limits on the ability of futures markets to perform their

⁹ Notice, at 4148.

¹⁰ Id. at 4149.

¹¹ CEA § 3(b).

¹² Id.

¹³ Id. and CEA § 3(a).

fundamental price discovery, risk transfer and risk management functions, which depend on the existence of liquid, fair and competitive markets. Therefore, any proposal that would tend to adversely affect the liquidity, fairness or competitiveness of the futures markets must be carefully scrutinized.

MFA respectfully suggests that the Commission may better achieve its goals by further developing and implementing its ongoing energy market transparency initiatives, such as: adopting aggregate position accountability levels across economically equivalent products on all related trading venues; requiring more comprehensive reporting of positions (both exchange-traded and OTC transactions) by large traders, swap dealers and hedgers; implementing more frequent collection of such information by the Commission; using such data to detect instances of manipulation or attempted manipulation; and bringing vigorous enforcement actions against participants who create artificial prices in the energy market.

III. THE PROPOSALS

The Commission's proposed rulemaking would:

- Establish federal speculative position limits on four "referenced energy commodities", specifically: Henry Hub natural gas, light sweet crude oil, New York Harbor No. 2 heating oil and New York harbor gasoline blendstock, and any other contract that is based on the referenced commodity (except for basis contracts and diversified commodity indexes)¹⁴;
- Apply to derivatives contracts in the referenced energy commodities traded on or subject to the rules of "reporting markets"¹⁵, i.e., derivatives contract markets ("DCMs"), such as the New York Mercantile Exchange Inc. ("NYMEX"), and exempt commercial markets that list significant price discovery contracts ("ECM-SPDCs"), such as ICE;
- Establish separate limits for the spot-month, any single month, and all-months-combined.¹⁶ The single month (outside of the spot-month), and all-months-combined limits would be set at both the reporting market level¹⁷ and as aggregate limits across all reporting markets (i.e., DCMs and ECM-SPDCs) listing the referenced energy commodities¹⁸;
- Set aggregate limits by reference to an open interest formula. The all-months-combined position limit would be 10% of the first 25,000 of open interest and 2.5% of open interest above 25,000 contracts.¹⁹ The single-month position limit would be set at 2/3rds of the all-months-combined limit²⁰;
- Establish a limit for the spot-month physically-settled contract at 25% of the estimated deliverable supply²¹, and a limit for cash-settled contracts in the spot-month of five times the limit of the physically-settled contract. However, if a trader holds a position in the physically-settled spot-month

¹⁴ Proposed Regulation § 151.1.

¹⁵ Proposed Regulation § 151.1 and § 15.00.

¹⁶ Proposed Regulation § 151.2.

¹⁷ Proposed Regulation § 151.2(b)(2).

¹⁸ Proposed Regulation § 151.2(b)(1).

¹⁹ Proposed Regulation § 151.2(b)(1)(i).

²⁰ Proposed Regulation § 151.2(b)(1)(ii).

²¹ Proposed Regulation § 151.2(a)(1).

contract, the applicable cash-settled limit would be the same as the limit fixed for the physically-settled contract (the “conditional limit”)²²;

- Require the CFTC to reset the limits by January 31st of each calendar year²³;
- Be in addition to, and not replace, position limits and position accountability levels established by DCMs and ECM-SPDCs²⁴;
- Provide for hedge exemptions from the limits for bona fide commercial hedgers²⁵;
- Provide for a limited risk management exemption (outside of the spot-month) for swap dealers establishing positions to offset customer initiated swap positions (with such exemption capped at two times the otherwise applicable single-month or all-months-combined limit)²⁶;
- Provide that a hedger or swap-dealer with an exemption could not also maintain speculative positions in the same contracts in which they have been granted an exemption (the “crowding-out provision”)²⁷;
- Provide that aggregation of positions would be required for position limit calculation purposes based upon common ownership of 10% or more, without any exception for independence of control of commonly owned accounts²⁸; and
- Require reporting to the Commission of certain cash and derivatives position data by all persons that (1) acquire positions in a referenced energy contract pursuant to the conditional-spot-month limit²⁹, (2) obtain bona-fide hedge exemptions³⁰, or (3) obtain a swap dealer exemption³¹.

The Commission has requested comment on all aspects of the proposed rulemaking, as well as on eighteen enumerated questions included in the Notice. MFA has numerous concerns with the proposed rulemaking, as we explain below.

IV. COMMENTS

A. The Proposed Federal Limits Are Unlikely To Achieve The Desired Result.

We believe that the hard position limits proposed in the Notice will neither keep energy prices from fluctuating in response to supply and demand factors nor promote market integrity. Rather, they will hinder commercial risk management.³² Speculators absorb risk from hedgers and provide liquidity.³³

²² Proposed Regulation § 151.2(a)(2).

²³ Proposed Regulation § 151.2(f).

²⁴ Notice, at 4145.

²⁵ Proposed Regulation §151.3(a)(1) and §20.01.

²⁶ Proposed Regulation §151.3(a)(2) and § 1.45.

²⁷ Proposed Regulation § 151.3(a)(1)(i), (ii), and (2).

²⁸ Proposed Regulation § 151.4(a)(1).

²⁹ Proposed Regulation § 20.00(b).

³⁰ Proposed Regulation § 20.01(b).

³¹ Proposed Regulation § 20.02(a) and (b).

³² See, for example, Pirrong Testimony, at 3.

Position limits, even purportedly generous ones, may impair the ability of markets to serve their essential risk shifting function, which would increase the cost of managing risk and harm hedgers, and ultimately consumers of energy products.³⁴ Studies have demonstrated that on prior occasions where trading by investors was restricted, such as by prohibiting futures transactions in certain commodities (Chicago onions, Berlin wheat), the result was significantly greater, and not less, price volatility.³⁵ Studies comparing price volatility in various commodities (wheat, cotton, oats, sugar, butter, eggs, rubber, silk, copper, silver, lead, zinc, soybeans, linseed, and hogs) before and after the establishment of futures markets for such commodities also demonstrate that futures markets are associated with lower price volatility.³⁶

Although position limits may reduce the ability of persons with market power to squeeze or corner the market, they have been described as a crude and inefficient tool.³⁷ This is because it is difficult to set the limits at a level that inhibits market manipulation without unduly affecting the ability of markets to efficiently transfer risk.³⁸ We recommend alternatives to using such a blunt instrument.

The Commission states that it has modeled the proposed federal limits after the current federal speculative position limits applicable to agricultural commodities. However, the Commission offers no empirical support for the proposition that hard position limits have reduced undue price volatility in agricultural commodities or will reduce volatility in energy markets.³⁹ As Commissioner O'Malia observed at the Commission's January 26, 2010 hearing, it is not clear that hard position limits in the agricultural markets have prevented price spikes in those markets.⁴⁰ Moreover, the Commission does not explain why the agricultural model would be correctly applied to energy in view of the different characteristics that distinguish these markets. For example, the energy markets are more global, energy commodities are more fungible, supplies of energy commodities are much greater and production is subject to less seasonal variation than with agricultural commodities.

³³ "The short hedgers and long investors provide liquidity for each other by using futures markets to serve their respective interests in a open, transparent and efficient manner. Liquidity will be essential to make sure each can achieve their objectives at an efficient price. Artificial limits on that liquidity should not be imposed. There are numerous ways to further the objectives of enhanced transparency and reduced systemic risk that do not involve reductions in much needed liquidity." Norrish Testimony, at 4.

³⁴ Id. See, also "Streetwise Professor: Now I Know How Sisyphus Felt" (July 8, 2009), by Dr. Craig Pirrong, at 4, available at <http://streetwiseprofessor.com/?p=2099>; see also, "Commodities and Speculators: Argument for Position Limits Non-Existent" (October 5, 2009), in Hard Assets Investor, interview of Dr. Craig Pirrong by Associate Editor Lara Crigger, available at <http://seekingalpha.com/article/164814-commodities-and-speculators-argument-for-position-limits-non-existent>.

³⁵ "At a minimum, there is no evidence for the claim that futures markets are associated with higher price volatility. Indeed, the results presented in this paper strongly suggest the opposite: futures markets were associated with, and most likely caused lower commodity price volatility." Jacks Study, at 357.

³⁶ Jacks Study, at 352.

³⁷ Pirrong Testimony, at 5.

³⁸ Id.

³⁹ "[W]e do not believe a case has been made which demonstrates that prices of commodities, or other financial derivatives, can be effectively controlled through the mandatory operation of regulatory tools such as position limits, whether on exchange or OTC. Analysis of market data where position limits are already in use suggests this has not shown a reduction in volatility or absolute price movements compared to contracts where they are not." Financial Services Authority & HM Treasury, Reforming OTC Derivative Markets, A UK perspective ("FSA & HM Treasury Report") (December 2009), at 34.

⁴⁰ Notice, at 4172.

Additionally, MFA respectfully questions whether the Commission's approach will promote the goal of preserving market integrity. As the imposition of hard limits on U.S. futures exchanges drives more trading to other markets, the Commission will have more difficulty conducting effective market surveillance and preventing potential price manipulation. Moreover, it is currently a fundamental part of the proposed financial markets regulatory reform effort promoted by the Commission to encourage clearing of derivatives transactions through central counterparties to increase market transparency, promote financial integrity and reduce systemic risks.⁴¹ We believe the proposed federal limits will have just the opposite effect, as participants will be induced to effect trades in less transparent OTC markets and settle such trades on a bilateral basis.

We believe there are better alternatives than hard position limits to deter market manipulation. Corners, squeezes and other forms of manipulation can be detected. It is preferable, therefore, to use readily available market data and the Commission's existing statutory authority to investigate and prosecute aggressive traders that manipulate or attempt to manipulate the market, than to limit the trading activity of all other market participants through hard position limits.

B. The Proposed Federal Limits Will Reduce Liquidity On U.S. Futures Markets.

The Commission's own studies and other governmental studies have found that commodity trading advisors such as MFA's members, termed "managed money speculative traders," are an important source of futures market liquidity for energy commodities and help to act as a shock absorber for commercial (i.e., hedger) order flow.⁴² The proposed federal limits will generally reduce the liquidity provided by managed money traders. Aside from the overall imposition of hard limits, there are several aspects of the proposed rule that we believe will significantly impact liquidity in the energy futures markets.

1. Adverse Effect of Conditional Limit In The Spot Month

Under the proposed spot month conditional limit, a trader holding cash-settled contracts would be subject to a spot-month position limit of five times the level fixed for the cash-settled contract's physically-settled counterpart if the trader holds no physically-settled contracts in the spot month. But if the trader holds even one physically settled contract in the spot month, the trader in cash-settled contracts would be subject to the much lower limit fixed for a contract's physically-settled counterpart. MFA's members believe that the conditional limit is too low and will constrain liquidity. The conditional limit will cause spot month liquidity to collapse three days before contract expiry (or even earlier) by either forcing speculative traders out of physically-settled contracts in the spot month during the last three days of trading or restricting the cash-settled positions of those traders that choose to maintain some physically-settled contracts.

⁴¹ "We must bring all standardized over-the-counter derivatives onto transparent and regulated exchanges or similar trading venues to lower risk and improve pricing in the marketplace... to further lower risk, we must bring all standardized over-the-counter derivatives into central clearinghouses." Remarks of Chairman Gary Gensler, Over-the-Counter Derivatives Reform, Council of Institutional Investors, Washington, D.C. (April 13, 2010).

⁴² "[W]e observe that indeed, the largest speculative category [managed money traders] provides liquidity to the market and enhances the price discovery function." Commission Energy Complex Report at 25. "...[R]esults from DAG analysis suggest that it is the [managed money traders] that are providing liquidity to the large hedgers and not the other way around." *Id.*, at 38.

While it is too early to empirically demonstrate, MFA's members are concerned that the implementation by NYMEX in February 2010 of a rule that adopted the conditional limit methodology proposed by the Commission is having a negative impact on liquidity, and is causing increased volatility and wider price spreads in the spot month trading in NYMEX Henry Hub Natural Gas contracts. The Commission should study the effects of the conditional limit (on NYMEX and ICE) in consideration of the impact of the proposed rule. In doing so, it should also consider revising the current conditional limit methodology and raising the cash-settled limit to a more appropriate level, above five times the physical limit.

2. Adverse Effect of Crowding Out Provision on Liquidity

The "crowding out provision" of the proposed rules will also adversely affect liquidity. That provision, applicable to participants with a bona fide hedge exemption or swap dealer exemption, would prohibit such participants from holding speculative positions if they are relying on an exemption. Under the CEA, and under the hedge exemption and risk management exemption policies administered by U.S. futures exchanges, every participant, including hedgers and swap dealers, is permitted to hold speculative positions below the established speculative positions limits. And, in fact, many bona-fide hedgers and swap dealers also engage in speculative trading within the applicable speculative position limits and can be important sources of market liquidity.⁴³ In the Notice the Commission does not provide any support for the need to bar hedgers and swap dealers from engaging in speculative trading.

Because hedging and risk management is generally performed on a portfolio basis, and not on a position by position basis, on a practical level it will be very difficult, if not impossible, for bona fide hedgers and swap dealers to monitor and comply with the provision barring them from holding any speculative futures positions. This will almost certainly result in a loss of liquidity on U.S. futures markets as trading will migrate to markets where no such restrictions apply.

Our understanding of the policy administered by the Chicago Mercantile Exchange ("CME"), Chicago Board of Trade ("CBOT") and NYMEX is that every participant is entitled to a position up to the applicable speculative position limit, unless there is market congestion. In such case a smaller limit may be imposed. Bona fide hedgers may apply to the exchange for an exemption to hold a position greater than the speculative limit. The application requires a demonstration of risk exposure at the time the request for exemption is made. If the demonstration is sufficient, the exchange approves the request. The "extra" hedge or risk management position size is permitted for hedging purposes, on top of the speculative limit, with the following qualification. In all cases, for all commercial hedgers and all other entities (such as swap dealers) who are accorded any kind of risk or spread exemptions, the approval of an exemption carries the condition that the firm must be able to demonstrate, at any point in time, that its current position in excess of speculative limits, by any amount, is demonstrably equivalent to its actual current risk exposure. If not, then the firm is subject to position limit rule enforcement procedures, and possible revocation of its exemption. We believe that this exchange policy is appropriate to prevent a trader with an exemption from abusing that privilege and the Commission should consider it in lieu of its proposed crowding out provision.

⁴³ "Swap dealers perform a critical risk-warehousing function in these markets...providing long-term liquidity where there would otherwise be none, even for very standard products such as oil and natural gas." Norrish Testimony, at 4.

3. Adverse Effect of Aggregation Policy on Liquidity

a. Disaggregation Of Independent Account Controllers Has Been The Longstanding Policy Of The Commission

The limitation on disaggregation of independent account controllers in the proposed rules will also adversely affect liquidity. Disaggregation based upon independence of control has been a longstanding policy of the Commission and U.S. futures exchanges.⁴⁴ The Commission has historically required aggregation of positions on the basis of ownership of positions or control of trading decisions. For this purpose, a trader holding accounts or positions in which the trader directly or indirectly has a 10% or greater ownership or equity interest generally must aggregate all such accounts or positions. Over the years, by regulation and interpretative letters, the Commission has provided relief from having to aggregate accounts or positions on the basis of ownership where discretion over trading is granted to an independent third party. The premise of such relief is that the beneficial owner in these cases does not directly or indirectly control the trading of the accounts or positions involved.

Under Commission Rule 150.3(a)(4), a commodity pool operator (“CPO”), commodity trading advisor (“CTA”), bank or trust company, an insurance company, or the operator of trading vehicle that is excluded or has qualified for an exemption under Commission Regulation 4.5 (each, an “eligible entity”) need not aggregate positions carried for it by an “independent account controller”⁴⁵ except in the spot month if there is a spot month limit. If an independent account controller is affiliated with the eligible entity or another independent account controller trading on behalf of the eligible entity, each of the affiliated entities must: (1) maintain written procedures to preclude them from having knowledge of, or gaining access to, trades of the other, including document and order routing arrangements or separate physical locations; (2) trade such accounts pursuant to separately developed and independent trading systems; (3) market such trading systems separately; and (4) solicit such funds by using separate disclosure documents (where such documents are required under Commission rules).

Under Commission Rule 150.4(b), a trader who is a limited partner or shareholder in a commodity pool (other than the pool’s CPO) with an ownership or equity interest of 10% or more in the pool generally need not aggregate the pool’s positions so long as such trader does not control the trading

⁴⁴ See e.g., the Aggregation Policy (exemption from aggregation for futures commission merchant managed account programs utilizing independent commodity pool operators); Adoption of Commission Regulation 150.3(a)(4), 53 Fed. Reg. 415653 (October 24, 1988)(extending the Aggregation Policy exemption for multi-advisor commodity funds); Exemption From Speculative Position Limits for Positions Which Have a Common Owner, But Which Are Independently Controlled, 56 Fed. Reg 14308 (April 9, 1991) (extending the exemption to commodity trading advisors); Amendment of Commission Regulation 150.3, 57 Fed. Reg. 44492 (September 28, 1992) (making the exemption for eligible entities self-executing); CFTC Interpretative Letter No. 92-15 (where an FCM is one of the components of a larger organization, the Aggregation Letter exemption would apply, even where the CPO/CTA were being operated as a separate subsidiary of a common parent); Amendment of Commission Regulation 150.1(d) and 150.4, 64 Fed. Reg. 24038 (May 5, 1999) (to expand the categories of eligible entities that authorize independent account controllers to trade on their behalf to the separately organized affiliates of an eligible entity); and CFTC Regulation 150.4(c) (disaggregation for ownership by limited partners, shareholder or other pool participants). Also, see NYMEX Rule 559.E.

⁴⁵ For this purpose an independent account controller is defined as a person who: trades independently on behalf of an “eligible entity” such as a CPO or CTA; over whose trading the CPO or CTA maintains only such minimum control consistent with its duty to supervise diligently the trading done on its behalf; who has no knowledge of any trading decisions by any other independent account controller acting on its behalf; and who is separately registered as a CTA or an associated person of a CTA. Commission Regulation 150.1(d).

of such pool. Moreover, under Commission Regulation 150.4(c)(2) if the trader who is a limited partner or shareholder with an equity or ownership interest of 10% or greater in the pool is an affiliate of the pool's CPO, the trader need not aggregate the pool's positions, provided that: (1) the pool's CPO maintains written procedures to preclude the trader from having knowledge of, or gaining access to, the pool's trading or positions; (2) the trader does not have direct, day-to-day supervisory authority or control over the pool's trading decisions; and (3) if the trader is a principal of the pool's CPO, the trader maintains only such minimum control consistent with its responsibilities as a principal and its duty to supervise the pool's trading activities.

Additionally, Commission staff has provided no-action relief from having to aggregate positions on the basis of taking a 10% or greater ownership or equity interest in another entity on a case-by-case basis, where, among other things, trading is conducted separately and independently by or on behalf of the two affiliated entities.

The Commission now proposes to prohibit previously eligible entities from disaggregating positions pursuant to the Commission's longstanding independent account controller framework. Under proposed Regulation 151.4(a)(1) aggregation would be required based upon common ownership of 10% or more, without any exception for independence of control. In addition, under proposed Regulation 151.4(b), a passive limited partner or shareholder with an ownership of 25% or more in a commodity pool, with no ability to control the trading of the pool, would be required to aggregate the pool's positions.

b. Many Asset Managers Use Independent Account Controllers.

An asset manager may legitimately access multiple active and passive trading programs that are independently managed by independent account controllers. Some programs involve short-term trading strategies, some are long-term, some are based on market fundamentals and some are based on technical signals. Asset managers may also invest through "funds of funds" structures which allow their investors to have access to various and diversified independently managed investment approaches. An asset management firm may also own, in whole or in part, or through private equity investments, utilities, producers of energy or other energy companies, and need to hedge those exposures independently from other trading strategies.

In all of the foregoing scenarios there is the possibility that these independently controlled accounts will be 10% or more commonly owned. The proposed aggregation rule would require that all such accounts be aggregated for position limit purposes, notwithstanding the independence in trading control. All of the above-described investment approaches provide (and require) different types of market liquidity, and if such investments are independently controlled, we can see no reason nor has the Commission given any reason to depart from its long-standing exception for independently controlled accounts from its aggregation policy.⁴⁶ By preventing asset managers from disaggregating independent account controllers for purposes of position limits, asset managers and/or independent account controllers to whom they allocate assets may be compelled to reduce their participation in US energy futures markets, and/or shift their business to other venues, resulting in a reduction of market liquidity on U.S. futures exchanges. Furthermore, it would undermine their ability to invest, in whole or in part, in a range of energy and energy-related projects vital to the economy.

⁴⁶ Statement of Aggregation Policy and Adoption of Related Reporting Rules, 44 Fed. Reg. 33839 (June 13, 1979) (the "Aggregation Policy").

Asset managers and corporate enterprises should be free to allocate capital efficiently across all types of business lines, including speculative trading ventures and commercial enterprises without fear that the independent trading operations of various commonly owned but independently operated businesses will be subject to aggregated limits, possibly affecting the ability of two or more independently controlled, but commonly owned businesses to trade in a particular market. We also note that the proposed rule would effectively require otherwise independent trading operations of commonly owned enterprises to communicate with each other as to their trading positions and intentions so as to avoid violating position limits. Such communications would actually raise the potential for trading in concert, which is precisely the sort of behavior that the proposed rules seek to avoid.

c. The Lack of Disaggregation Relief Will Significantly Impact Asset Managers and Market Liquidity.

The absence of independent account controller relief from aggregation, combined with the proposed crowding out provision prohibiting hedgers or swap dealers from engaging in speculative trading may require commodity trading advisors that invest in multiple lines of business (i.e., production, processing, merchandising, commercial use, dealing in swaps and/or speculation in commodities) to either sell or spin off ongoing businesses or refrain from hedging in US futures markets, adversely impacting the price discovery function of such markets and reducing liquidity in futures markets.

As noted above, some asset managers have investments in operating companies engaged in the production, processing, commercial use or merchandising of commodities or in energy commodity infrastructure companies. Aggregation of independent account controllers in 10% or more commonly-owned enterprises will have the effect of limiting the amount of capital available to invest in such enterprises and will have a detrimental effect on the development of energy commodities infrastructure.⁴⁷

Energy commodities should not be treated differently from agricultural (or any other commodities) with respect to the Commission's aggregation policy. The need to comply with two different aggregation regimes will create significant confusion and administrative burdens. Moreover, the Commission's adoption of a more restrictive aggregation policy for referenced energy commodities is likely to spill over to other energy products and to other non-energy commodities because exchanges tend to take their cue from the Commission in applying and interpreting their aggregation policies. Because it will be burdensome for exchanges and carrying brokers to administer two different aggregation policies, the end result may be that all energy commodities and all other commodities will be subject to an aggregation policy that is more restrictive than is necessary.

d. The Solution Is To Audit and Enforce Independent Account Controller Information Barrier Policies and Procedures.

With respect, the Commission has not pointed to any problems or abuses in energy commodity markets arising out of the application of the current independent account controller exemption permitting disaggregation that would require a different rule in the energy market. If the Commission is concerned that the information barriers constructed between commonly owned enterprises are inadequate for the purposes of maintaining true independence among account controllers, it would seem to us that an appropriate regulatory response would be to audit for the adequacy of, and compliance with, such

⁴⁷ "Given the vast scale of capital spending needs, deep and liquid markets are essential to help facilitate the hedging of price risk inherent in these investments, stabilizing cash flows to support financing and construction." Norrish Testimony, at 4.

information barrier policies and procedures, rather than to automatically require aggregation. The Commission already has access to information regarding cross-ownership of traders through its Statement of Reporting Trader forms and may use this information to ensure segregation of trade information.

While we acknowledge the difficulty of quantifying in advance the potential individual effect of each of the impacts on market liquidity noted above, there can be no denying that the cumulative impact is likely to be significant.

C. The Proposed Federal Limits Will Hurt the Competitiveness of Commission Regulated Markets and U.S. Energy Markets.

MFA fears that the Commission's unilateral imposition of aggregate position limits on contracts traded on U.S. exchanges and trading facilities will drive business offshore or to OTC markets, adversely affecting the liquidity, transparency and competitiveness of U.S. futures markets, and thus impacting the price discovery and risk shifting purposes of such markets. There is no consensus among foreign regulators that strict position limits are necessary or desirable.⁴⁸

The flight to foreign and OTC markets has already begun. United States Oil Fund has been moving a considerable portion of its energy futures trading from NYMEX to London and to OTC markets.⁴⁹ Additionally, Standard & Poors recently announced the launch of a commodity index that excludes all US exchange-traded commodities, instead choosing as index components contracts listed on foreign commodity markets.⁵⁰

In light of the global nature of energy commodity markets, the portability of trading capital and resources across borders, and the existence of robust OTC derivatives markets, MFA believes that before acting on its own the Commission must reach agreement with its counterparts in the G-20 countries to arrive at a comprehensive, consistent, and effective approach across related markets. The failure to do so threatens to send significant liquidity overseas, harming the price discovery and risk shifting capacity of U.S. energy markets.

D. The Commission Has Not Met Its Statutory Burden In Proposing The Federal Limits

The Commission has not made the required statutory findings to support adoption of the proposed rules. CEA § 4a(a) provides that the Commission must make a finding that its position limit rules are necessary to diminish, eliminate or prevent the burden on interstate commerce caused by sudden, unreasonable or unwarranted price fluctuations arising out of excessive speculation in contracts for future delivery traded on contract markets or electronic trading facilities. The Commission's Notice focuses on the prevention of undue concentration of positions, but ownership of a concentrated position, standing alone, is not the same as excessive speculation.

⁴⁸ "As we have outlined the current broad position management approach adopted in the UK is effective in combating market manipulation and so we see no need to introduce position limits for this purpose. With regards to controlling or limiting price movement we have not seen evidence that a position limits regime is needed." FSA & HM Treasury Report, at 36.

⁴⁹ "US watchdog probes ETF's oil contract stake", article by Javier Blas and Joanna Chung, The Financial Times (February 27 2009).

⁵⁰ "S&P index seeks to bypass US clampdown", article by Chris Flood, The Financial Times (March 18, 2010).

Respectfully, the Commission has ignored the studies of its own economists (as well as third parties) concluding that there was no link between speculative trading and the price spikes in energy contracts in 2008 and in prior years.⁵¹ Moreover, the Commission has not provided any evidence that the proposed rule will help reduce price fluctuations nor could it. Rather, studies indicate that hard position limits have not been shown to alleviate undue price volatility. If the Commission proceeds with this rulemaking it is obliged to present empirical evidence: (1) of excessive speculation in the relevant energy markets; (2) that such excessive speculation caused sudden, unreasonable or unwarranted price fluctuations; and (3) that its rules are the most appropriate means of diminishing, eliminating or preventing the burden caused by such price fluctuations.

Nor do we believe that the Commission has the authority to condition the grant of a hedge or swap dealer exemption on the recipient of such relief being required to refrain from speculative trading (the crowding out provision). CEA § 4a(c) states that “No rule, regulation, or order issued under subsection (a) of this section shall apply to transactions or positions which are shown to be bona fide hedging transactions or positions....” We read this to effectively provide a hedger with an exemption from speculative position limits authorized under CEA § 4a(a) for all positions that qualify as bona fide hedges. By counting a hedger’s bona fide hedge positions against such trader’s speculative position limit, the Commission’s crowding out provision would effectively convert bona fide hedge positions into speculative positions, which is inconsistent with CEA § 4a(c). As noted above, the futures exchanges do not apply such a policy in their administration of their hedge exemptions and we would urge the Commission to adopt an approach consistent with that implemented by the exchanges.

E. The Purported Benefits Of The Proposed Federal Limits Are Far Outweighed By The Costs.

MFA has several concerns regarding the potential costs and burdens on market participants of compliance with the proposed federal limits. The Commission’s cost/benefit analysis underestimates the substantial costs and burdens that would be imposed by the proposed rules. The proposed federal limits are complex and must be layered on top of existing exchange position limits and position accountability levels. Traders will be required to compute and aggregate their positions across contract types and across trading platforms on a real time basis so as to permit effective compliance with the multiple layers of individual and aggregated position limits. Additionally, traders operating in commonly owned entities will also be required to perform these calculations across all related entities. We are not aware of any existing automated system that is readily available to the commodity trading advisor community to perform this task. The systems development burdens and costs of accomplishing this task are not insignificant.

In addition, the Commission’s estimate that the rulemaking will affect “possibly 10 traders”⁵² does not take into account the number of entities that will be affected by the Commission’s aggregation

⁵¹ For example, the Commission Energy Complex Report explored the relationship between futures prices and the positions of managed money traders (MMTs), commonly known as hedge funds, for the natural gas and crude oil futures markets and examined the relationship between the positions of MMTs and positions of other categories of traders (e.g., floor traders, merchants, manufacturers, commercial banks, dealers) for the same markets. The results of the study found “no evidence of a link between price changes and MMT positions (conditional on other participants trading) in the natural gas market, and find a significantly negative relationship between MMT position changes and price changes (conditional on other participants trading) in the crude oil market....”

⁵² Notice, at 4165.

rule and the significant burdens that such rule will impose. Nor does it take into account the effect that the reduced liquidity on U.S. energy futures markets will have on market participants in general.

MFA is concerned that the Commission underestimates the costs of compliance with the proposed federal limits, and that the potential unintended consequences of the rules will greatly outweigh any purported benefits. Such consequences are likely to include decreased liquidity and increased price volatility, resulting in higher transaction costs as the bid-offer spreads widen in the futures and OTC markets and less market transparency. In addition, the Commission does not appear to have considered either the constraints on corporate structures, the amount of capital available for investment in commodity operating companies and commodity infrastructure, or the considerable administrative burdens and costs in monitoring and complying with multiple overlapping and inconsistent exchange and federal limits, position aggregation requirements, and hedge exemption procedures.

MFA respectfully believes that many of these costs and burdens could be alleviated if the Commission were to adopt an approach that is more consistent with the framework currently implemented by U.S. futures exchanges.

F. Other Significant Concerns With The Proposed Federal Limits

In the following section MFA outlines several additional concerns regarding the proposed rules.

1. The Commission should provide greater detail as to the purpose and rationale of the proposed rules, the specifics on its computations, and the data it used to calculate aggregate open interest and deliverable supply.

a. Particularly with respect to options, the Commission has not explained whether option open interest is calculated on a gross basis or a net basis (i.e., are long calls and long puts at the same strike price calculated on a net or gross basis) and the rationale for its option methodology.

b. Transparency into the calculation methodology (and the actual underlying numbers used by the Commission in its open interest calculations) is important to allow interested persons to judge the validity of the assumptions underlying the proposed limits and to permit compliance by market participants on an ongoing basis if the rules are adopted. For example, we note a significant discrepancy between the prospective all-months-combined limits published in the Notice and the limits presented by the CFTC at its open hearing discussing the proposed federal limits.⁵³ We also note that it is difficult to obtain timely and complete options open interest data from the exchanges. For example, it has been difficult to obtain open interest information broken down by option strike prices. Thus, participants that wish to independently forecast the positions limits in the next year and manage their portfolios effectively will have difficulty doing so. An opaque process without timely and transparent access would disrupt trading activity and increase the potential for non-fundamental or political factors being introduced.

c. The Commission's proposed spot month limits will be based upon the deliverable supply of the underlying commodity. While that approach may have some justification for physically-settled

⁵³ For example, on page 6 of the Statement of Steve Sherrod, Acting Director of Surveillance, Division of Market Oversight, Commodity Futures Trading Commission (January 14, 2010), the prospective All Months Combined Speculative Position Limits were listed as 98,200 for Crude Oil, 8,900 for Harbor Gasoline Blendstock, 13,100 for Heating Oil and 117,300 for Natural Gas, whereas in the Notice, the proposed limits were 98,100 for Crude Oil, 9,000 for Harbor Gasoline Blendstock, 9,000 for Heating Oil, and 132,700 for Natural Gas (Notice, at 4162).

contracts, there is no economic relationship or rationale for linking position limits on cash-settled contracts to deliverable supply. The Commission has not explained its rationale for doing so. Nor has the Commission disclosed the source of its deliverable supply statistics and whether those statistics are readily available to the public. How these statistics are gathered may have a significant impact on overall numbers and contract liquidity.

This lack of accessibility to the Commission's data that underlie important portions of the proposed rules makes it difficult, if not impossible, for affected market participants to evaluate and meaningfully comment on significant aspects of the proposal.

2. The annual recalculation methodology is flawed because it contains a built-in bias towards lower annual limits.

Given the potentially severe consequences of violating a position limit, many traders currently build in a cushion to stay under position limits. This cushion typically may be 10% or more. As a result, assuming that no new investors enter the markets, the result will be overall lower open interest. Because the position limit levels will be reset annually by looking back at prior open interest levels, this may result in the following year having a lower position limit level and create a self-reinforcing cycle of lower open interest and lower position limits in successive years.

In addition, open interest can change dramatically from year to year depending on external events such as conflict in the Middle East or significant changes in weather that impact prices. If a slow year is followed by a more active year due to these events, the hard position limits will limit liquidity when it is most needed.

3. The Commission should provide an exemption for inter-commodity spread positions.

The Commission found it appropriate to provide for an exemption from speculative position limits for calendar spreads, presumably because such spreads reflect a relationship between two contract months rather than an outright directional trade in each component of the calendar spread. We suggest that the Commission should also provide for an exemption for intercommodity spreads, which similarly reflect a relationship between two commodities rather than an outright directional position in the spread components. For example, a market participant may purchase electricity from a producer while simultaneously selling natural gas. The participant is expressing a view as to the relative value of each commodity (given their fixed relationship—natural gas is used in the generation of electricity) while hedging its overall risk and providing liquidity to both markets.

G. Alternative Actions

MFA agrees with the Commission's goals of bolstering confidence in the market and preventing market disruptions. MFA believes, however, that the Commission should consider other approaches to achieving these goals. As a first step, the Commission should build on its recent information gathering initiatives regarding index investors and provide the public with greater transparency with respect to OTC markets related to energy futures markets through the publication of additional data.⁵⁴ For example, we

⁵⁴ The Commission began publishing a Disaggregated Commitments of Traders (Disaggregated COT) report on September 4, 2009. The Disaggregated COT report increases transparency from the legacy COT reports by separating traders into the following four categories of traders: Producer/Merchant/Processor/User; Swap

believe the public would benefit from the compilation and publication of the size of various OTC energy swap markets, the value of positions that are internally netted by swap dealers, and the volume of futures market trades that are effected by swap dealers to offset risk, among other things. More transparency tends to support price discovery and market integrity. In addition, should the Commission conclude that it lacks sufficient information about the energy markets, the implementation of aggregate position accountability levels would enable the Commission to better gather information about and monitor position concentrations. Accountability levels will not have the same negative effects as the imposition of hard speculative limits since reporting, as opposed to automatically curtailing trading, will not tend to decrease liquidity in the markets. Similarly, the Commission should re-examine the hedge exemption process and ensure that exemptions are not being used beyond their intended, legitimate purposes. The Commission should also utilize its increased information technology and data gathering capacity to support its ongoing efforts to identify and prosecute market manipulation.⁵⁵ Likewise, we would support Congress appropriating increased funds to the Commission to ensure that it has the necessary enforcement and surveillance staff resources to oversee futures markets and prosecute market manipulation and other abusive market practices, as this would achieve the Commission's objectives in the way least likely to reduce market liquidity and cause other unintended consequences.

V. CONCLUSION

Our domestic regulated futures markets play a leading role in price discovery and risk transference in both the U.S. and worldwide. We share the Commission's desire to preserve and enhance the integrity of our markets. However, we believe the Commission has not fully addressed the costs to these markets and their participants of the proposed federal limits. Such costs include reduced liquidity and a corresponding decline in the competitiveness of U.S. futures markets as business migrates overseas or to the OTC markets.

MFA is concerned that the Commission has not established the need for the proposed federal position limits and in any case overestimated their potential effectiveness. Additionally, even if such limits could be proven to be necessary or effective, unilateral imposition of aggregate position limits by the Commission on contracts traded on U.S. exchanges and trading facilities without international coordination would impair the liquidity and competitiveness of U.S. energy markets. The Commission would not achieve its goal of preserving market integrity and would only reduce the price discovery and risk shifting functions of U.S. markets.

MFA respectfully suggests that the Commission reassess its approach. Additional discussions with foreign regulators regarding a coordinated approach should also be undertaken if the Commission's goals are to be achieved. We believe that the Commission can most effectively further its goals by taking such tangible and meaningful steps as: implementing aggregate position accountability levels across economically equivalent products and all related trading venues; requiring more comprehensive reporting of positions (both exchange-traded and OTC transactions) by large traders, swap dealers and hedgers; collecting and publishing such information more frequently as part of its COT report; examining the hedge exemption process; and using the expanded data to detect and prosecute those who attempt to

Dealers; Managed Money; and Other Reportables. This impetus for providing market transparency arises from the recommendation to disaggregate the existing "commercial" category in the Commission's September 2008 Staff Report on Commodity Swap Dealers & Index Traders.

⁵⁵ "Aggressive use of the Commission's surveillance authority in partnership with the exchanges should be sufficient to closely monitor and protect the integrity of the markets." Commissioner Sommers dissent, Notice, at 4171.

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manipulate the market. MFA believes that this type of approach addresses the Commission's valid public policy concerns regarding the integrity of the futures markets, while at the same time preserves the liquidity, transparency and competitiveness of U.S. energy markets.

We would be happy to discuss our comments or any of the issues raised by the Proposed Federal Limits at greater length with the Commission or its staff. If staff has any questions, please do not hesitate to call Jennifer Han or the undersigned at (202) 367-1140.

Respectfully Submitted,

/s/ Richard H. Baker

Richard H. Baker
President and CEO

cc:

The Honorable Chairman Gary Gensler
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