May 15, 2020

Christopher Kirkpatrick
Secretary of the Commodity Futures Trading Commission
3 Lafayette Centre
1155 21st Street, NW Washington, DC 20581

Re: Position Limits for Derivatives'' and RIN 3038-AD99

Dear Mr. Kirkpatrick:

The Petroleum Marketers Association of America ("PMAA") submits these comments to the Commodity Futures Trading Commission ("CFTC" or "Commission") on its Notice of Proposed Rulemaking RIN 3038-AD99 regarding Position Limits for Commodity Derivatives.

I. Introduction

The Petroleum Marketers Association of America (PMAA) is a national federation of 47 state and regional trade associations representing independent petroleum marketing companies throughout the United States. Petroleum marketers represent a vital link in the petroleum distribution chain. Operating exclusively below the terminal rack, PMAA members supply 80 percent of all finished petroleum products sold nationwide including gasoline, diesel fuel, biofuels, heating fuel, jet fuel, kerosene, racing fuel and lubricating oils. Moreover, petroleum marketers represented by PMAA own and operate approximately 60,000 retail gasoline stations and supply heating fuel to more than 5 million homes and businesses nationwide.

For decades, petroleum marketers have been utilizing oil and refined product futures markets for their hedging needs to protect customers from volatility and price spikes. Well-functioning markets are critical to commodity price discovery and position limits will play a critical role in reestablishing market fundamentals. Therefore, it is in the interest of these companies and their consumers that these markets are as transparent and functional as possible, and we appreciate the opportunity to provide the CFTC with input on this matter.

II. CFTC Proposal

The CFTC is proposing new and amended regulations concerning speculative position limits to conform to the Wall Street Reform and Consumer Protection Act of 2010 (the Dodd-Frank Act) amendments to the Commodity Exchange Act. The proposal includes new and/or amended federal spot month limits for 25 physical commodity derivatives and physically-settled and linked cash-settled futures, options on futures, and economically equivalent swaps for such commodities. The proposal also includes certain exemptions from position limits, such as a revised definition of "bona fide hedging transactions or positions" and an expanded list of enumerated bona fide hedges to cover additional hedging practices. In addition, the proposal establishes a new process that would streamline requests for bona fide hedge

exemptions for both exchange-set and federal position limit requirements. The proposal also eliminates multiple duplicative reporting requirements for information currently available to the Commission from the exchanges.

III. PMAA Comments

It is well established that the CFTC's primary statutory mandate is to foster fair, open and efficient functioning of the commodity markets as a hedging and price discovery tool for bona- fide physical hedgers. Section 737 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Dodd-Frank Act") required the CFTC to establish speculative position limits for commodities that had been exempt under the Commodity Exchange Act. These "exempt commodities" include energy-related commodities (i.e., crude oil, refined products, natural gas and metals).

The Dodd-Frank Act acknowledged the potential harm of excessive speculation and reaffirmed the importance of position limits by providing the Commission with expanded authority to impose such limits aggregated across all markets, both regulated and unregulated. Congress directed the Commission to establish limits on the number of positions that may be held as it finds necessary to "(i) diminish, eliminate, or prevent excessive speculation; (ii) to deter and prevent market manipulation, squeezes, and corners; (iii) to ensure sufficient market liquidity for bona fide hedgers; and (iv) to ensure that the price discovery function of the underlying market is not disrupted."

Position Limits

PMAA strongly supports the immediate implementation of position limits to protect commodities markets participants and the public from undue burdens that may result from ''excessive speculation.'' Excessive speculation contributed to the oil price run up in the mid-2000s when prices soared to approximately $147 per barrel in July 2008, only to plunge to a low of $32 per barrel in December of the same year. More recently, excessive speculation may have contributed to the April 2020 dramatic drop in oil prices which sent the West Texas Intermediate (WTI) into negative territory for the first time. Contracts for May delivery were due to expire on April 21, putting maximum pressure the day before on traders whose contracts were coming due. For these traders, who have no physical storage capacity, selling at a steeply negative price, even below zero was their only option. PMAA believes the proposed position limits rule does not go far enough to limit excessive oil commodity speculation especially with respect to passive investments.

- ***Spot-Month Limits***

Unfortunately, the spot-month limit of 25 percent of deliverable supply is not sufficiently aggressive to deter excessive speculation. The Commission must consider lowering the stated spot month limit for energy futures and "economically equivalent" energy futures, options on futures, and swaps to a level that is more consistent with existing federal spot month limits for legacy agriculture contracts to prevent market manipulation.

- ***Delegation of Review Authority to the Exchanges***

PMAA believes that the determination of "estimated deliverable supply" should immediately be withdrawn from the Designated Contract Markets (DCMs) and that the CFTC should retain exclusive discretion in determining "deliverable supply" for the purposes of establishing speculative position limits. Instead, the Commission should consult with and solicit information from market experts, when

determining “deliverable supply” and formulating limits, including appropriate governmental entities (i.e., the Department of Energy’s Energy Information Administration and the U.S. Department of Agriculture) and academics, as well as representatives of industries that produce, refine, process, store, transport, market and consume the underlying commodity.

- ***Non-Spot Month Limits***

PMAA is concerned about the proposals failure to adopt non—spot month limits on energy commodity positions. PMAA believes the Proposal largely defers to the DCMs to address excessive speculation in the non—spot -month for the energy futures contracts. History has shown on a number of occasions that large trades in non-spot months can distort markets and increase volatility. Unfortunately, the proposal instead finds accountability limits to be sufficient to manage speculation. Section 4a(a)(3) of the Commodity Exchange Act (CEA) expressly directs the Commission to set limits on positions in both spot-months and non-spot months where appropriate. However, there is no data or discussion provided in the proposal indicating why the Commission believes limits for non-spot months are not appropriate. PMAA supports applying the traditional 2.5% limit formula to energy contracts and economically equivalent energy futures, options, and swaps in non-spot months as a reasonable and effective way to manage speculation and urges the Commission to adopt such limits to prevent market manipulation.

- **Passive Investments**

PMAA is also concerned that the proposed rule does not in any way address the growing issue of passive long traders. Such funds and investment vehicles share a common characteristic that interferes with and distorts the normal functioning of the futures markets - they buy without regard to current supply and demand fundamentals and thus without regard to price. Their trading strategies are premised on factors unrelated to the physical market, but in executing them, they compete with physical commodity consumers and producers and, in turn, distort the market and make hedging more uncertain and, consequently, expensive. In short, their presence upsets the price discovery function.

There is ample evidence that passive long only investment began to surge in 2006, peaked in mid-2008, plummeted in the second half of 2008, and then began to rise again in early 2009. In the early to mid-2000s, financial institutions began receiving permission to create and market new kinds of securities linked to commodities and commodity indexes. These included indexes based partly, or predominantly, on energy and energy derivatives. By 2006, the SEC had approved the first exchange-traded fund that was based exclusively on energy derivatives. These and other commodity-based funds -- which are heavily weighted toward energy futures -- have been aggressively marketed as a way for investors to diversify portfolios and speculate on commodity prices.

Fast forward to today, passive investments could be playing an even a larger role in the oil futures market. Although a combination of reduced demand, oversupply and disputes between Saudi Arabia and Russia over production cuts helped contribute to the dramatic plunge in oil prices, passive investments in the oil futures market only made matters worse. For instance, “the United States Oil Fund and the Samsung S&P GSCI Crude Oil ER Futures ETF sold about 110,000 contracts in the most-liquid June WTI futures on Tuesday, according to Bloomberg calculations based on the funds’ filings -- equivalent to 19% of the total open interest in the contracts at the end of the previous day. The data point to one reason for Tuesday’s collapse in June WTI prices, which tumbled by as much as 68% to touch a low of $6.50 a barrel. At the same time, its discount to later-dated contracts -- known as

contango -- also widened dramatically, with the spread between June and July almost doubling to a contango of as much as $10.99 a barrel.[1]

Therefore, the Commission should consider setting separate speculative position limits specifically for passive long traders in the referenced contracts and should consider setting those limits to be lower than the limits that apply to active speculative traders. Positions of passive long speculators should be aggregated to the extent the positions are held or controlled by passive long speculators who follow the same trading strategies. Position limits should be strengthened to ensure that multiple accounts or pools with identical trading strategies be aggregated regardless of whether their positions are held or controlled by the same trader to shield the futures markets from the cumulative impact of multiple passive long speculators who follow the same trading strategies.

If the Commission is of the view that it does not have sufficient information on which to act in response to the issue of the role, effect and mitigation of the effect of passive long traders, it should commit to conducting a study to analyze and determine appropriate position limit levels for passive long traders. In light of the latest oil market volatility, the CFTC should commit to completing the study within a time period to be determined by the CFTC during the next six months.

Bona Fide Hedge Activities

PMAA welcomes the elimination risk of management exemptions as bona fide hedges for physical commodities. PMAA believes that the exemption allowed parties, including swap dealers to solicit wealthy investors to bet on the upward price of commodities and create a potential for significant volatility in the market. While the Proposal improves the definition of bona fide hedge activities, it also delegates to Exchanges far too much discretion to determine whether a position constitutes a bona fide hedge under the Commission's new definition. PMAA believes this broad discretion opens the door to a potentially unlimited universe of new unenumerated exemptions for speculative positions that could have an adverse impact on markets. The commission must adopt well defined criteria for Exchanges to follow that would avert the predictable explosion in the number of exemptions with the potential to promote undue speculation. Market participants would also benefit from defining criteria for unenumerated exemptions as a way to provide legal certainty over what constitutes a bona fide hedge.

PMAA is also concerned that the Proposal does not determine the validity of unenumerated hedge exemptions through the normal public notice and comment process. Instead, the Proposal allows the Exchange to make the determination followed by a 10-day retrospective review period by the Commission. This undercuts the ability for the public to comment on the exemption under review in any meaningful way. PMAA believes that determining the validity of unenumerated hedge exemptions lies with the Commission itself. In fact, the Dodd-Frank Act specifically assigns to the Commission responsibility for the legal and policy determination of what constitutes a bona fide hedge. The Commission is uniquely qualified to make these determinations and the authority to do so should not be delegated to the Exchanges.

IV. Conclusion

[1] How ETFs, New Whales of the Oil Market, Are Roiling Prices; https://www.bloomberg.com/news/articles/2020-04-22/how-etfs-new-whales-of-the-oil-market-are-roiling-crude-prices?sref=PhHgVmzr

PMAA urges the Commission to adopt the positions outlined in these comments. PMAA has significant concerns with a market structure that seemingly no longer serves a valid price discovery function. Massive positions held by passive speculators have contributed to price volatility that is simply unrelated to supply and demand fundamentals. The commodity markets were created to serve bona fide commercial hedgers as a tool for risk mitigation and to serve a price discovery function that is reflective of real-world supply and demand fundamentals.

PMAA thanks the Commission for the opportunity to submit these comments. Please feel free to contact me should you have any additional questions or require additional information.

Sincerely,

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