HEARING TO REVIEW IMPLEMENTATION OF PROVISIONS OF THE DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT RELATING TO POSITION LIMITS

HEARING

BEFORE THE

SUBCOMMITTEE ON
GENERAL FARM COMMODITIES
AND RISK MANAGEMENT

OF THE

COMMITTEE ON AGRICULTURE
HOUSE OF REPRESENTATIVES

ONE HUNDRED ELEVENTH CONGRESS

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WEDNESDAY, DECEMBER 15, 2010

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON GENERAL FARM COMMODITIES AND RISK MANAGEMENT,
COMMITTEE ON AGRICULTURE,
Washington, D.C.

The Subcommittee met, pursuant to call, at 10:00 a.m., in Room 1300, Longworth House Office Building, Hon. Leonard L. Boswell [Chairman of the Subcommittee] presiding.

Members present: Representatives Boswell, Schrader, Kissell, Peterson (*ex officio*), Marshall, Murphy, Moran, Johnson, Conaway, Luetkemeyer, Lucas (*ex officio*), and Neugebauer.

Staff present: Aleta Botts, Liz Friedlander, John Konya, Clark Ogilvie, Rebekah Solem, Tamara Hinton, Kevin Kramp, Josh Mathis, Jamie Mitchell, and Sangina Wright.

OPENING STATEMENT OF HON. LEONARD L. BOSWELL, A REPRESENTATIVE IN CONGRESS FROM IOWA

The CHAIRMAN. The hearing of the Subcommittee on General Farm Commodities and Risk Management to review implementation of provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act relating to position limits will come to order.

I would like to thank everybody for joining us today as we review where we are at on the implementation provisions of the Dodd-Frank regulatory reform law relating to position limits.

This hearing is very timely, as just recently the CEO of Sanderson Farms said it was delaying forward purchase of feed until the CFTC had issued position limit rules, and that he doesn't like to buy grain when "index funds own 25–30 percent of the crop." So I wouldn't say that is why we are here today. I would like to review where we are at on this.

I see that Chairman Peterson has joined us and I would like to take a moment, if I could, and divert from the hearing and recognize the outstanding work and dedication of Chairman Collin Peterson for leading this Committee through some of the most challenging times that the agriculture community has faced since the farm crisis of the 1980s. Specifically, he has championed the bringing of oversight and transparency to the derivatives market to protect end-users. And if everyone will indulge me, I would like to take a moment and thank Chairman Peterson. Thank you, Collin Peterson.

We have Members who will be leaving us for different reasons, and we are going to give them a sad farewell as we work through this process today. And I am sure I will have an opportunity to recognize Mr. Moran, as he is going on to his new endeavors, and all the rest to their new endeavors.

I might just at this moment add that my very special assistant, Alexis Taylor, from east Iowa, is going to be leaving our office and going over to the Senate. She is going to be the legislative assistant for Senator Baucus. So we congratulate her on her, I guess we could say, promotion. She will be very involved there for the next farm bill and that is good. We wish her well.

Congress required the establishment of enforcement of position limits to ensure that no single entity holds too much power over the marketplace. Position limits are essential to the function of effective and efficient markets, and to inject confidence in the markets by providing reliable and transparent price signals.

Some will argue that the very existence of position limits operates contrary to the principles underlying a free market; however, limits ensure that speculative positions are not in control of a contract, enhance a market, and make price signals a more accurate representation of the true market price.

There is a strong need to ensure that the market is not being manipulated by a few players, and we are closely watching the pace of rulemaking on the Dodd-Frank Wall Street Reform and Consumer Protection Act, especially the rule relating to position limits.

I think that all of us on the Subcommittee would agree that the Commission must take the time to get this right. However the Commission also must move quickly to ensure the individuals that use the markets for *bona fide* hedging purposes have the confidence that these markets are fair markets. Confidence by hedgers in these markets is critical, to say nothing of the importance of the confidence by the Congress in the Commission's ability to implement all the regulations required by the Act.

Back in March, this Subcommittee held a hearing on rulemaking pertaining to the implementation of Commodity Exchange Act provisions contained in the 2008 Farm Bill. At the time, the rule on provision limits was pending for several energy contracts. That rule was withdrawn after the Dodd-Frank Act made further changes. I understand this issue is on tap for discussion at tomorrow's Commission meeting. So I hope that our hearing today will provide some valuable input into the forum along with a chance to review what the Commission's plans are on this topic.

I am looking forward to hearing today from Chairman Gensler who has used his leadership on the Commission to be a powerful advocate for limits, and to ensure the Commission is on a speedy though challenging path towards full implementation of the law.

I am also pleased to welcome Commissioner Chilton to the Committee. Mr. Chilton has expressed concerns about the pace of the regulatory process, and we look forward to discussing these concerns in more detail.

Additional reactions from the witnesses on the second panel on the pace of the rulemaking and the content of regulations on position limits will be important to assessing the needs to move this issue along in the Commission's priority list.

Before I turn to my good friend and future Senator from Kansas, Jerry Moran, for an opening statement, Jerry, I just want to thank you for the knowledge and support in working together. You have been a good colleague on this, and I appreciate the service you have given to us here on the House Agriculture Committee and we look forward to having a friend over there in the Senate. We wish you Godspeed in your work over there and much success.

[The prepared statement of Mr. Boswell follows:]

PREPARED STATEMENT OF HON. LEONARD L. BOSWELL, A REPRESENTATIVE IN CONGRESS FROM IOWA

I would like to thank everyone for joining us here today as we review the state of the implementation provisions of the Dodd-Frank regulatory reform law relating to position limits. This hearing is very timely as just yesterday, the CEO of Sanderson Farms said it was delaying forward purchases of feed until the CFTC had issued position limit rules and that he doesn't like to buy grain when "index funds own 25–30% of the crop."

I would especially like to thank our witnesses. The Committee looks forward to hearing your valuable insight.

I would like to take a moment and divert from the hearing and recognize the outstanding work and dedication of Chairman Colin Peterson for leading the Agriculture Committee through some of the most challenging times the agriculture community has faced since the farm crisis of the 1980's. Specifically he has championed bringing oversight and transparency to the derivatives markets to protect end-users. If everyone would indulge me to please take a moment and thank Chairman Peterson.

Thank you for that indulgence. Congress required the establishment and enforcement of position limits to ensure that no single entity holds too much power over the marketplace. Position limits are essential to the function of effective and efficient markets and to inject confidence in the markets by providing reliable and transparent price signals. Some argue that the very existence of position limits operates contrary to the principles underlying a free market. However, limits that ensure that speculative positions are not in control of a contract enhance the market and make price signals a more accurate representation of the true market price.

There is a strong need to ensure that a market is not being manipulated by a few players, and I am closely watching the pace of rulemaking on the Dodd-Frank Wall Street Reform and Consumer Protection Act, especially the rules relating to position limits. I think that all of us on this Subcommittee would agree that the Commission must take the time to get this right. However, the Commission also must move quickly to ensure that individuals that use these markets for *bona fide* hedging purposes have the confidence that these markets are fair markets. Confidence by hedgers in these markets is critical, to say nothing of the importance of the confidence by the Congress in the Commission's ability to implement all of the regulations required by the Act.

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Before I turn to my good friend and future Senator from Kansas, Jerry Moran for an opening statement I would like to thank him for his knowledge and constant support of agriculture in the House.

The CHAIRMAN. And at this time, I would like to recognize Mr. Moran for whatever you would like to say.

OPENING STATEMENT OF HON. JERRY MORAN, A REPRESENTATIVE IN CONGRESS FROM KANSAS

Mr. MORAN. Mr. Chairman, thank you very much. I appreciate the friendship that you and I have encountered now for a long time in the House of Representatives, and I appreciate the leadership that you provide on this Subcommittee and our full House Agriculture Committee. The House Agriculture Committee has really been my home during my time as a Member of the House of Representatives, and this is a significant part of what I enjoy the most about serving in Congress.

In regard to today's hearing, Mr. Chairman, I certainly believe that Congressional oversight is a good thing. And while I will not be here in the new year to chair this Subcommittee, I believe that my successor, and the incoming full Committee Chairman, Mr. Lucas, will readily exercise the House Agriculture Committee's oversight authority over the Commodity Futures Trading Commission.

In regard to the topic of position limits under the Dodd-Frank Act, however, I believe it is premature to hold an oversight hearing, because the CFTC has yet to release a proposed rule. Thus we are left to hold a hearing based on hearsay, a few exchanges between CFTC's Commissioners during a hearing on another issue, and a speech and an opinion editorial released to the press by Commissioner Chilton. Having said that, I am concerned about where the Commission's position on position limits discussion is going.

First, I would like to note that early on in the legislative process, both I as Ranking Member, and the Ranking Member, Mr. Lucas, of the full Committee, and other Members of the House Agriculture Committee, introduced amendments to place limits on the authority of the CFTC to impose position limits. During that debate, we were clear that the commodity futures market needed greater transparency, and we were in favor of creating mandatory reporting requirements. We were hesitant, however, to give the CFTC broader powers to impose position limits until we had adequate information about the over-the-counter markets. We felt that Congress needed to know who was trading on the OTC market, the size of the OTC market, and whether the OTC market was or was not having an adverse effect on exchange-traded markets before bestowing greater position limit authority on the Commission.

Unfortunately, those amendments did not pass, and we now have a situation where a regulator may be contemplating imposing position limits without having access to the information necessary to determine the appropriate position limits, or to enforce such position limits once they are set.

Despite what some believe is a mandate for the Commission to set position limits within a definite period of time, the Dodd-Frank legislation actually qualifies CFTC's position limit authority. Section 737 of the Dodd-Frank Act amends the Commodity Exchange Act so that section 4a(a)(2)(A) states: "The Commission shall by rule . . . establish limits on the amount of positions as appropriate . . . ."

The Act then states in subparagraph (B) for exempt commodities, the limit required under subparagraph (A) shall be established within 180 days after the date of enactment of this paragraph.

When subparagraphs (A) and (B) are read in conjunction, the Act states that when position limits are required under subparagraph (A), the Commission shall set elements within 180 days under paragraph (B). Subparagraph (A) says the position limit rule should be only prescribed when *appropriate*. Therefore, the 180 day timetable is only triggered if position limits are appropriate.

In regard to the word *appropriate*, the Commission has three distinct problems. First, the Commission has never made an affirmative finding that position limits are appropriate to curtail excessive speculation. In fact, to date the only reports issued by the Commission or its staff failed to identify a connection between market trends and excessive speculation. This is not to say that there is no connection, but it does say the Commission does not have enough information to draw an affirmative conclusion.

The second and third issues related to the appropriateness of position limits are related to adequacy of information about OTC markets. On December 8, 2010, the Commission published a proposed rule on Swap data record-keeping and reporting requirements. This proposed rule is open for comment until February 7, 2011, and the rule is not expected to be final and effective until summer at the earliest.

Furthermore, the Commission has yet to issue a proposed rulemaking about Swap data repositories. Until a Swap data repository is set up and running, it is difficult to see how it would be appropriate for the Commission to set position limits. Without additional information about trades in the OTC market, the Commission could neither have enough information to adequately determine the appropriate position limits, or have the information necessary to enforce position limits, assuming the appropriate formula could be determined without full access to OTC market information.

In conclusion, I would again caution that my remarks are based on hearsay and not on an actual proposed rule. It is hard to be critical of something that does not yet exist. I hope that Chairman Gensler in his testimony today will inform the Subcommittee that the Commission is aware of the challenges surrounding the current imposition of position limits, and that the Commission hearing tomorrow will not consider enacting position limits before adequate information is obtained.

I would also caution the Chairman and the other Commissioners, however, that if the Commission moves forward with a proposed position limit rule before information from the OTC markets are made available, they should be prepared for more hearings on this topic next year.

Mr. Chairman, that is a longer opening statement than my usual, which suggests I am leaving the House of Representatives for someplace else. But I am grateful for the opportunity to express my opinion today. I am delighted to be with you, and I thank you, Mr. Chairman, for recognizing me, and I look forward to our continued close working relationship.

[The prepared statement of Mr. Moran follows:]

PREPARED STATEMENT OF HON. JERRY MORAN, A REPRESENTATIVE IN CONGRESS FROM KANSAS

Thank you, Mr. Chairman. I believe Congressional oversight is a good thing. While I will not be here to chair this Subcommittee next year, I believe my successor, and the incoming full Committee Chairman, Mr. Lucas, will readily exercise the House Agriculture Committee's oversight authority over the Commodity Futures Trading Commission (CFTC).

In regard to the topic of position limits under the Dodd-Frank Act, however, I believe it is premature to hold an oversight hearing because the CFTC has yet to release a proposed rule. Thus, we are left to hold a hearing based on hearsay, a few exchanges between CFTC Commissioners during a hearing on another issue, and a speech and opinion editorial released to the press by Commissioner Chilton. Having said that, I am concerned about where the Commission's position limit discussion is going.

First, I would note that early on in the legislative process, both myself, Ranking Member Lucas, and other Members of the Agriculture Committee introduced amendments to place limits on the authority of the CFTC to impose position limits. During that debate, we were clear that the commodity futures markets needed greater transparency and we were in favor of creating mandatory reporting requirements. We were hesitant, however, to give CFTC broader powers to impose position limits until we had adequate information about the over-the-counter (OTC) markets. We felt the Congress needed to know who was trading in the OTC market, the size of the OTC market, and whether the OTC market was or was not having an adverse affect on exchange-traded markets before bestowing greater position limit authority on the Commission. Unfortunately, those amendments did not pass, and we now have a situation where a regulator may be contemplating imposing position limits without having access to the information necessary to determine the appropriate position limits or to enforce such position limits once they are set.

Despite what some believe is a mandate for the Commission to set position limits within a definite time period, the Dodd-Frank legislation actually qualifies CFTC's position limit authority. Section 737 of the Dodd-Frank Act amends the Commodity Exchange Act (CEA) so that Section 4a(a)(2)(A) states: "the Commission shall by rule . . . establish limits on the amount of positions, as appropriate . . . ." The Act then states in subparagraph (B): "For exempt commodities, the limits required under subparagraph (A) shall be established within 180 days after the date of the enactment of this paragraph." When subparagraphs (A) and (B) are read in conjunction, the Act states that when position limits are required under subparagraph (A), the Commission shall set the limits within 180 days under subparagraph (B). Subparagraph (A) says position limit rules should only be prescribed when "appropriate." Therefore, the 180-day timetable is only triggered if position limits are appropriate.

In regard to the word "appropriate," the Commission has three distinct problems. First, the Commission has never made an affirmative finding that position limits are appropriate to curtail excessive speculation. In fact, to date, the only reports issued by the Commission or its staff fail to identify a connection between market trends and excessive speculation. This is not to say that there is no connection, but it does say the Commission does not have enough information to draw an affirmative conclusion.

The second and third issues related to the appropriateness of position limits are related to adequacy of information about the OTC markets. On December 8, 2010, the Commission published a proposed rule on "Swap Data Recordkeeping and Reporting Requirements." This proposed rule is open for comment until February 7, 2011, and the rule is not expected to be final and effective until this coming summer at the earliest. Furthermore, the Commission has yet to issue a proposed rulemaking about swap data repositories. Until a swap data repository is up and running, it is difficult to see how it would be appropriate for the Commission to set position limits. Without additional information about trades in the OTC market, the Commission could neither have enough information to adequately determine the appropriation position limit or have the information necessary to enforce position limits, assuming an appropriate formula could be determined without full access to OTC market information.

To conclude, I would again caution that my remarks are based on hearsay and not an actual proposed rule. It is hard to be critical of something that does not yet exist. I hope that Chairman Gensler, in his testimony today, will inform the Subcommittee that the Commission is aware of the challenges surrounding the current imposition of position limits and at the Commission's hearing tomorrow, he will not consider enacting position limits before adequate information is known. I would caution the Chairman and other Commissioners, however, that if the Commission moves forward with a proposed position limit rule before information from the OTC markets are made available, they should be prepared for more hearings on this topic next year.

Again, thank you for recognizing me Mr. Chairman and I look forward to the testimony of today's witnesses.

The CHAIRMAN. Well, thank you very much. I appreciate that, and we do wish you well and we are happy to have you with us today.

At this time, I would like to recognize Mr. Peterson for any comments he might like to make.

OPENING STATEMENT OF HON. COLLIN C. PETERSON, A REPRESENTATIVE IN CONGRESS FROM MINNESOTA

Mr. PETERSON. Thank you, Mr. Chairman, Ranking Member, and good morning everybody. Thank you, for holding this hearing today. The Subcommittee and this Committee started looking into excessive speculation in the derivatives market more than 2 years ago before the evidence of the financial crisis actually started to appear.

We passed bipartisan legislation to bring greater transparency and accountability to the derivatives market, and many of the Committee-passed provisions were included in the Wall Street Reform and Consumer Protection Act which was signed into law this past summer.

There are many important provisions within this law, but the one we are addressing today is the speculative position limits. The law sets a deadline of January 17, 2011, for the CFTC to announce the proposed rule for this provision, but recently many have expressed concerns about the CFTC meeting this deadline.

While the CFTC has held seven open meetings to write rules for the law's many provisions, most recently on December 9th, speculative position limits have not yet been addressed, and this leaves little time for the Commission to address this issue. It is important that the CFTC remain on track and implement the Wall Street Reform and Consumer Protection Act in a timely manner and as Congress intended.

I understand that there is another meeting being held tomorrow and that the position limits will be addressed at this time. I think that is good news. But I question whether this could have happened earlier.

I want to welcome Chairman Gensler and Commissioner Chilton to the Committee today. We appreciate the good working relationship that we have had and look forward to working with you as we go forward. As I say, we have worked closely together and hope that we could help you in implementing this law. So I look forward to hearing your testimony, along with the rest of today's witnesses, and again thank the chair for his leadership on this issue.

[The prepared statement of Mr. Peterson follows:]

PREPARED STATEMENT OF HON. COLLIN C. PETERSON, A REPRESENTATIVE IN CONGRESS FROM MINNESOTA

Good morning, and thank you Mr. Boswell for holding today's hearing of the Subcommittee on General Farm Commodities and Risk Management.

This Committee started looking into excessive speculation in the derivatives market more than 2 years ago, before evidence of the financial crisis started to appear. We passed bipartisan legislation to bring greater transparency and accountability to the derivatives market and many of the Committee-passed provisions were included in the Wall Street Reform and Consumer Protection Act which was signed into law this past summer.

There are many important provisions within this law, but the one we are addressing today is speculative position limits. The law sets a deadline of January 17, 2011 for the CFTC to announce the proposed rule for this provision, but recently many have expressed concerns about the CFTC meeting this deadline.

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It is important that the CFTC remain on track and implement the Wall Street Reform and Consumer Protection Act in a timely manner and as Congress intended. I understand there is another meeting being held tomorrow and that speculative position limits will be addressed at this time. This is good news, but I question whether this could have happened earlier.

I want to welcome Chairman Gensler and Commissioner Chilton to the Committee today. We have worked closely over the last few years and I look forward to continuing this relationship as you move ahead with implementing this law. I look forward to hearing your testimony, along with the rest of today's witnesses and again thank the Chair for holding this hearing.

The CHAIRMAN. Thank you, Mr. Peterson.

I would like to recognize Mr. Lucas for any comments he would like to make.

OPENING STATEMENT OF HON. FRANK D. LUCAS, A REPRESENTATIVE IN CONGRESS FROM OKLAHOMA

Mr. LUCAS. Thank you, Mr. Chairman, for calling this hearing today. I am not sure that I should call this the last in a long series of hearings this Committee has had on the regulation of derivatives in this Congress, or, perhaps better described, as the first in a long series of intensive oversight hearings I promise this Committee will engage in through the next several months. One thing I am sure of, and I have to echo the comments of my colleague, our good friend from Kansas, who is going to the other side of the building—I didn't say to the other side of the world—he will be missed indeed in this body.

I can't use that other phrase, Jerry, I am sorry, I just can't say that word that some people now describe you within the public in the future, but your efforts on behalf of Kansas agriculture and this Committee have been and are much appreciated.

One of the many legislative battles that you and I fought was the integrity of our domestic futures markets. We have long been focused on making sure the markets provide our farmers, ranchers, and commercial end-users the ability to manage their risk and discover market-driven prices. Those efforts and the efforts of everyone on this Committee resulted in legislation that ultimately became Title VII of the Dodd-Frank Act.

Although there are so many issues and authorities contained in Title VII, the imposition of position limits probably received the most attention by this Committee. The imposition of position limits in various forms and fashions played huge parts in my and Mr. Peterson's legislative initiatives, and Mr. Goodlatte's before that. We have always known the balance between liquid vibrant markets and transparent price discovery markets were, and are, imperative.

In the end, the position limits regime in the Dodd-Frank isn't what I would have written, but it is a cautious approach that provides the Commission with the appropriate discretion to address what I believe is a political problem and not necessarily a problem driven by artificial volatility or distorted supply and demand.

The Dodd-Frank Act committed a new level of authority and discretion to use that authority to the Commodity Futures Trading Commission. I have heard from several of the regulated community, and have seen myself, how consumed the Commission and the staff is with implementation.

I do not envy you in the least. It is a huge task, perhaps too big to be done in the timelines provided. As this fragile economy attempts to get back on its feet, we ought not to be throwing regulatory hurdles in its way, costing even more jobs and higher prices. I fear that is what will happen if the most sweeping reform of the nation's derivative markets is done hastily and without all due deliberation. I am not pressing for a perfect rule, but we have to have a good rule. I stand willing to consider easing of statutory deadlines to ensure rules don't end up further distorting markets and costing American jobs.

I certainly look forward to hearing from our witnesses today, and I am prepared for that informed decision as they work their way through the implementation of position limits. And I would note, if the Chairman indulges me for one moment, this may well be the last hearing where my first Agriculture Committee Chairman continues to look down over our shoulder, Mr. de la Garza, in the way pictures are handled. I look forward to having Mr. Goodlatte looking over my shoulder, and having what will inevitably be the awesome portrait of Mr. Peterson to admire at the other end of the room. Such is the nature of the way these bodies move forward.

Again, Mr. Chairman, thank you for calling this hearing.

The CHAIRMAN. Thank you very much.

The CHAIRMAN. We would like to request that the other Members submit their opening statements for the record so the witnesses may begin their testimony and ensure there is ample time for questions.

I would like to welcome our first panel which, of course, is the Honorable Gary Gensler, Chairman of the Commodity Futures Trading Commission and the Honorable Bart Chilton, Commissioner of the Commodity Futures Trading Commission.

Chairman Gensler, welcome. Please begin when you are ready.

STATEMENT OF HON. GARY GENSLER, CHAIRMAN, COMMODITY FUTURES TRADING COMMISSION, WASHINGTON, D.C.

Mr. GENSLER. Good afternoon. Thank you, Chairman Boswell, Chairman Peterson, Ranking Member Moran, Ranking Member of the full Committee, Congressman Lucas. I thank you for inviting me here to testify on behalf of the CFTC and I am pleased to be testifying along with Commissioner Chilton. Commissioner Chilton has been a real advocate that the markets that CFTC oversees work for all Americans, and he has been a leader in ensuring that we reestablish position limits in the energy and metals market and that they be extended to the swaps markets.

Before I mention things on position limits, just let me update you on our work on implementing Dodd-Frank. We have been consulting extensively with fellow regulators and the public. I think the CFTC staff and I have met now—we keep a running count internally—over 300 times with fellow regulators. That would be 60 times a month with the SEC, the Federal Reserve and other regulators. We also are soliciting broad public input. We have had 7 days of public roundtables, usually with the SEC joining us. Additionally, many individuals of course want to come in and see us. We post these on our website to have transparency, and as of Monday there have been 460 such meetings from the public coming in to talk to us about these things.

Thus far the Commission has moved forward with 30 proposals, and including some final rules and interim final rules and advance notices, the total count is 37 that we have published.

We look forward to comments from the public. No doubt we will get tens of thousands of comments as we sort through this and we look forward to that.

We have our eighth public meeting tomorrow where we plan to have two additional meetings in January in other key areas.

With regard to position limits, the Dodd-Frank Act did expand the scope of the Commission's mandate to set position limits to include swaps, and I anticipate that we will consider staff recommendations tomorrow. These will include recommendations to include agricultural, energy and metals commodities.

I also anticipate the staff's recommendation will be for position limits both for the spot month—this is when contracts are moving into delivery—as well as single months and all-months-combined. That is what Congress had asked us to look at, all three. We have asked staff to try to do this within one rule.

The spot month limits are currently set are set in markets for energy, metals, and agriculture. We will be taking a look at 28 individual contracts. I think there are currently set in 26 of these contracts.

In terms of the single month and all-months-combined limits, we currently have contract limits for most agriculture, and the staff will have some recommendations with regard to energy and metals as well.

It is only with the implementation and passage of the Dodd-Frank Act, though, that the Commission has broad authority to collect information on the swaps market, as many Members have indicated. To this date we have really had very limited authority to collect data on the swaps market.

We approved a rule in October on position reporting for physical commodity swaps that would allow us for the first time to collect data, more detailed data, on the swaps market. The comment period for that closed early December. Staff is currently looking through all those comments before we can finalize a rule on swaps data collection. This is different than the swaps data repository we actually put out. You might be—sometimes people call it large trader reporting, but we did put that rule out, as I say.

Before I close, I just want to thank everybody here for your support on resources. I know that the House of Representatives did pass a continuing resolution. The Senate still is going to be taking up resources. The President's request of $261 million of resources for this fiscal year is very important. We think an estimate will be 300 to 400 new applicants, swap dealers, swap execution facilities, data repositories and the like that will be knocking on our doors, probably come next summer, for us to move forward. We estimate overall we will probably need about 400 more people. We are currently at about 680 people.

With that, I look forward to your questions. I also look forward to your oversight. I think it is a very important part of our American system. It is also a good way that we can get these rules done and look forward to your advice and counsel.

[The prepared statement of Mr. Gensler follows:]

PREPARED STATEMENT OF HON. GARY GENSLER, CHAIRMAN, COMMODITY FUTURES TRADING COMMISSION, WASHINGTON, D.C.

Good afternoon, Chairman Boswell, Ranking Member Moran and Members of the Subcommittee. I thank you for inviting me to today's hearing on behalf of the Commodity Futures Trading Commission (CFTC).[1] I am pleased to testify alongside my fellow Commissioner, Bart Chilton.

Implementing the Dodd-Frank Act

Before I discuss the CFTC's rule-writing process with regard to position limits, I will update the Subcommittee on the CFTC's implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act. The Dodd-Frank Act is very detailed, addressing all of the key policy issues regarding regulation of the swaps marketplace. This Subcommittee's work on the Act should be commended. The Act reduces risk while promoting transparency in the swaps markets.

To implement the Dodd-Frank Act, we have organized our effort around 31 teams who have been actively at work. Two principles are guiding us throughout the rule-writing process. First is the statute itself. We intend to comply with the statute's provisions and Congressional intent to lower risk and bring transparency to these markets.

Second, we are consulting extensively with both other regulators and the broader public. We are working very closely with the SEC, the Federal Reserve, other prudential regulators and international regulators. To date, we have had more than 304 meetings with other regulators at the staff or Chairman's level.

We also are soliciting broad public input into the rules. This began the day the President signed the Dodd-Frank Act when we listed the rule-writing teams and set up mailboxes for the public to submit their views directly.

We also have organized seven public roundtables to hear on particular subjects. Last week we held a joint roundtable with the SEC and prudential regulators on issues related to capital and margin requirements for swaps. Additionally, many individuals have asked for meetings with the CFTC to discuss swaps regulation. As of Monday morning, we have had more than 466 such meetings. Just as Congress brought transparency to the swaps markets, the CFTC has added additional transparency to our rule-writing efforts. We are now posting on our website a list of all of our meetings, as well as the participants, issues discussed and all materials given to us.

We are in the process of publishing proposed rules, using open Commission meetings for this purpose. So far, we have had seven public meetings. We have another meeting scheduled tomorrow during which the Commission will consider rules related to position limits, swap execution facilities, derivatives clearing organizations and business conduct standards.

Thus far the Commission has approved 30 proposed rules, one final rule, two interim final rules and four advanced notices of proposed rulemaking. That does not include the four proposed rulemakings that the Commission will consider tomorrow.

The Dodd-Frank Act requires the CFTC and the SEC to write rules generally within 360 days after the date of enactment. This means we have 213 days left for

[1] Commissioner Bart Chilton did not participate in the approval of this testimony.

the majority of the rulemakings. In the case of position limit mandates, Congress had directed a more ambitious schedule.

Position Limits Rulemaking

Legislative and Regulatory History

Since 1936, the Commodity Exchange Act has prescribed position limits to protect against the burdens of excessive speculation, including those caused by large concentrated positions. Between the CFTC and the futures exchanges, there are currently position limits in the spot month on physical delivery contracts in the agricultural, energy and metals markets. There also are position limits in a number of financial contracts. In addition to these spot month limits, between federally-set position limits and those set by exchanges, there also are a number of agricultural contracts that have single-month and all-months-combined position limits. The exchanges had set all-months-combined limits in energy markets until 2001 and in metals markets earlier, after which the limits were replaced with position accountability regimes.

The debate on the position limits provisions included in the Dodd-Frank Act began with actions taken by the House Agriculture Committee in the summer of 2008. According to the Committee report, the Agriculture Committee and this Subcommittee held six hearings with 44 witnesses on issues related to position limits. The House later passed H.R. 6604 in September 2008.

The CFTC itself held three public meetings in the summer of July 2009 to gather further input from the public and Members of Congress regarding position limits for energy markets. In January 2010, the Commission published a proposed rule to set position limits on four energy contracts. In response to the proposal, the CFTC received more than 8,200 comments from the public. The CFTC announced the withdrawal of that proposal in August with plans to re-propose pursuant to the Dodd-Frank requirements. To be properly informed during the current rule-writing process, the Commission and staff are reviewing the comments received in response to the January rulemaking. The CFTC is scheduled to consider a new position limits rulemaking tomorrow.

In March 2010, the Commission held an additional public meeting to consider the appropriateness of position limits in the metals markets. The public's views from that meeting and the comments that were later submitted also will be helpful as the Commission considers a proposed rulemaking on position limits in the metals markets.

The CFTC does not set or regulate prices. Rather, the Commission is directed to ensure that commodity markets are fair and orderly. The January position limits proposal was intended to meet Congress's mandate and to promote market integrity. The CFTC is directed by statute to act in this regard to protect the American public.

When the CFTC set position limits in the past, the agency sought to ensure that the markets were made up of a broad group of market participants with a diversity of views. At the core of our obligations is promoting market integrity, which the agency has historically interpreted to include ensuring markets do not become too concentrated.

Position limits help to protect the markets both in times of clear skies and when there is a storm on the horizon. In 1981, the Commission said that "the capacity of any contract market to absorb the establishment and liquidation of large speculative positions in an orderly manner is related to the relative size of such positions, *i.e.,* the capacity of the market is not unlimited."

Dodd-Frank Requirements

The Dodd-Frank Act requires the CFTC to set position limits for the following classes of contracts:

- futures;
- options on futures; and
- swaps that are economically equivalent to such futures or options.

The Dodd-Frank Act also directs the Commission to set aggregate position limits for the following:

- contracts listed for trading on designated contract markets,
- contracts traded on a foreign board of trade providing persons in the U.S. with direct access that settle against the price of one or more contracts traded on a futures exchange or swap execution facility; and
- any other swap contracts that perform or affect a significant price discovery function with respect to regulated entities.

The Act requires that the CFTC set the first set of position limits within 180 days of enactment for exempt commodities and within 270 days for agricultural commodities. The Commission has some additional flexibility with respect to the timing of the rulemaking for the aggregate limits.

The Commodity Exchange Act exempts positions that are held as *bona fide* hedges from position limits. The Dodd-Frank Act provided further detail on the types of positions that fall in that category. End users and other persons with physical holdings in the energy and metals markets will not be limited in the amount or size of their positions that are entered into to hedge their physical purchases, holdings or sales.

In establishing the limits for energy and agricultural commodities, the CFTC is required to set spot-month, single month and all-months-combined position limits to achieve the following goals:

1. diminish, eliminate or prevent excessive speculation;
2. deter and prevent market manipulation, squeezes and corners;
3. ensure sufficient market liquidity for *bona fide* hedgers; and
4. ensure that the price discovery function of the underlying market is not disrupted.

Data Requirements

The Commission is working to meet each of the deadlines included in the Dodd-Frank Act. Setting position limits in the swaps markets poses a unique challenge because of the market's opacity. Prior to the Dodd-Frank Act, the Commission had only limited authority to obtain data regarding the swaps market. The Dodd-Frank Act includes essential provisions to bring transparency in the markets to both regulators and the public. At this point, however, the Commission does not have the same comprehensive data for the swaps markets, including economically equivalent swaps, as it has for the futures markets. The Commission also currently has limited access to data on linked contracts traded on FBOTs through direct access by U.S. participants. The Commission has collected some data from swaps dealers since 2008, using special call authority to do so. However, additional data is required on the swaps markets to determine the size of the overall market in particular commodities, as well as the nature of the positions in this market. In particular, the Commission lacks data that would identify the extent to which positions are held for hedging or speculative purposes.

On October 19, the Commission approved a proposed rulemaking on large trader reporting for physical commodity swaps. The proposal would require position reports on economically equivalent swaps from clearing organizations, their members and swap dealers. This would enable the CFTC to receive such data until swap data repositories are in operation and capable of fulfilling the Commission's need for this information. The comment period on the proposed rulemaking closed on December 2.

In addition, large trader reporting will allow the Commission to gather data that could be used to determine appropriate position limits. The rule builds on the Commission's ongoing special call for data from swap dealers.

Options for Position Limits Rulemakings

CFTC staff is considering options to phase in implementation of the position limits rules as the agency obtains the necessary data regarding the swaps market. Staff is examining whether certain elements of the rule for which the Commission has substantial data can proceed on a more expedited timeframe, while leaving those aspects of the rule that depend upon additional data for later implementation. Staff is considering whether it would be possible to implement spot month limits sooner than the single-month or all-months-combined limits.

The Commission could consider proposing single-month and all-months-combined position limits based on the open interest for futures, options and economically equivalent swaps. This is similar to the approach taken in the rulemaking that the Commission proposed in January. Open interest is currently used to establish position limits in the futures markets. Staff is reviewing an option that use data regarding open interest in the swaps markets to set hard aggregate limits. This approach would allow the Commission to hear from the public on the appropriate methodology for setting position limits while also allowing the Commission to collect additional swaps data through the large trader reporting regime. The actual hard limits would be applied when sufficient data becomes available.

Currently, spot month limits for physically-settled futures contracts are generally set as some percentage of deliverable supply to prevent someone with a large position from cornering or squeezing the market as contracts move to expiration. In contrast, single-month and all-months-combined position limits have historically been set as a function of the overall size of the markets to guard against the burdens of excessive speculation.

Resources

Before I close, I will briefly address the resource needs of the CFTC. The futures marketplace that the CFTC oversees is approximately $40 trillion in notional amount. The swaps market that the Dodd-Frank Act tasks the CFTC with regulating has a far larger notional amount as well as more complexity. Based upon figures compiled by the Office of the Comptroller of the Currency, the largest 25 bank holding companies currently have $277 trillion notional amount of swaps.

The CFTC's current funding is far less than what is required to properly fulfill our significantly expanded role. The CFTC requires additional resources to enhance its surveillance program, prevent market disruptions similar to those experienced on May 6 and implement the Dodd-Frank Act.

The President requested $261 million for the CFTC in his Fiscal Year 2011 budget. This included $216 million and 745 full-time employees for pre-Dodd-Frank authorities and $45 million to provide ½ of the staff estimated at that time needed to implement Dodd-Frank. The House of Representatives matched the President's request in the continuing resolution it passed last week. We are currently operating under a continuing resolution that provides funding at an annualized level of $169 million. To fully implement the Dodd-Frank reforms, the Commission will require approximately 400 additional staff over the level needed to fulfill our pre-Dodd-Frank mission.

I again thank you for inviting me to testify today. I look forward to your questions.

The CHAIRMAN. Thank you very much.

We will go ahead and hear the comments from Commissioner Chilton, and then we will have questions.

STATEMENT OF HON. BART CHILTON, COMMISSIONER, COMMODITY FUTURES TRADING COMMISSION, WASHINGTON, D.C.

Mr. CHILTON. Thanks, Mr. Chairman and thanks also to——

The CHAIRMAN. Let me interrupt you just for a second. A little oversight. We have Mr. Neugebauer with us today. He is very welcome, but I am supposed to get unanimous consent that it is okay for him to be here. The chair thinks it is okay for him to be here. No objections?

Thank you for coming.

Mr. CHILTON. Thank you, Mr. Chairman. I can say I just want to thank and congratulate Senator-elect Moran. It has been a pleasure working with you over the years, sir, and I look forward to continuing that. I look forward to the scrutiny we will get from Chairman Lucas in the future.

I did want to say a special thanks to Chairman Peterson. You guys passed back in 2008 legislation dealing with speculation. You may have passed it twice in a bipartisan way. I know you brought it up on the floor twice in 2008. So I appreciate your foresight and your oversight of this agency over the years.

I also want to thank my friend, Chairman Gensler, for being so helpful. His expertise of the markets and of finance has really helped us. The other Commissioners are pretty much folks that came from here, came from the Hill and we have ag backgrounds and we have some other backgrounds, too, but having Chairman Gensler there has made us better Commissioners and a better Commission. So I thank him.

If you look back at just the last 10 years, the futures industry around the world has increased three-fold. Yet in the U.S. it increased five-fold.

So a lot was going on. Between 2005 and 2008, we saw roughly $200 billion of speculative money, index money, hedge funds, pension funds; $200 billion came into these markets. Now, that happened to coincide with this commodity bubble. Wheat is around $7½–$8 now. It was at $24 then. Gasoline is—crude is like $87, $90 now. It went up to $147.27 in June 2008. As we all know and your constituents told you, they had concerns because gasoline was over $4.

Whether or not that increase in the speculative interest, that $200 billion, caused that bubble is a point that obviously can be debated. Some people say, move along folks, nothing here. Some people say it drove the prices. I come out sort of in the middle and say that—agree with MIT and Oxford and Rice and Princeton and even Lincoln University in Missouri. They all say that it had some impact. So, how much you can debate.

The increase in speculative limits since that time, if it was a concern in 2008 with the amount of speculation in the market, if it was a concern when Congress passed the law in July, it is even more of a concern now.

Now, before I give you some new statistics, don't get me wrong: We don't have speculators, we don't have a market. They are critical. Full stop. We have to have them. But if you look at what is going on between June of 2008 and where we are today or where we were in October, we see more speculative positions in the futures markets than at any time in history, $149 billion. That is an increase in the energy complex of 47 percent since 2008, an increase in the metals complex of 20 percent, and an increase in the agriculture complex by 18 percent. So there has been this large influx.

Now, the Chairman talked about all the rules and a number of Members have talked about the rules. There has been a flurry of activity. We have been going gangbusters. And the staff at the CFTC has been real inspirational. We all sort of talk about it every time we meet.

At the same time, by and large, while these rules have been sort of trains that are on time, position limits have sort of derailed. And the reason is exactly what Congressman Moran alluded to, whether or not we have this data on swaps in order to meet the deadline of January. And there are a couple of points; first, I am not sure we do have the authority to delay.

And this *as appropriate language*, Congressman Moran, I appreciate your point but to say that *as appropriate* is expansive enough of a definition to render the provision moot and meaningless, I think begs the question a little bit. I think we are required to implement it. I see no authority for us to delay, no legal authority. I asked the attorneys why we would delay.

Second, I think it is needed now more than ever, because of those statistics I just cited to you. And third, there are ways that we can do this. There are things that we can do as Chairman-elect Lucas said in a deliberate fashion, not *ad hoc* and not hasty, sir, that we can do to start doing what Congress set as our goals in January.

It may not be the full Committee but there are things that we can do now. I agree we don't want something hasty. We don't want to mess up markets. There are ways to go about this.

So far what we have been talking about is how we just go ahead and wait, and we are talking about a delay, we are talking about not getting this data until next September or October. So I am just trying to do what Congress told us to do. You can have different interpretations. I have mine, and I am trying to do the best, I don't think we are—as I said, we are going to have a meeting tomorrow, we are not quite back on the track, but we can get there. Thank you Mr. Chairman.

[The prepared statement of Mr. Chilton follows:]

PREPARED STATEMENT OF HON. BART CHILTON, COMMISSIONER, COMMODITY FUTURES TRADING COMMISSION, WASHINGTON, D.C.

Mr. Chairman, Ranking Member Moran, Members of the Subcommittee, thank you for the opportunity to be with you today.

In the last decade, we saw the U.S. futures industry grow five-fold when the rest of the world grew three-fold. In several years we saw over $200 billion come into regulated U.S. futures markets. This new money was primarily from speculators, much of which was held by speculators I call "massive passives," those with a known, fairly price-insensitive trading strategy. Then, in 2008, we saw a huge commodity bubble. Wheat was at $24. Today it is around $8. Crude oil spiked to $147.27 and gas was at $4 per gallon. Then the economy and commodity prices all fell off a cliff. Did the new speculators, including the massive passives, contribute to that price volatility-volatility that had farmers and ranchers, small and large agribusinesses and other businesses alike all paying higher prices than they should?

Researchers at Oxford, MIT, Princeton and Rice all say speculative interests had an impact on prices. Some have said the speculators drove prices. In fairness, some on the other side of the issue say there was no impact whatsoever. My take is somewhere in the middle. Speculators didn't drive prices, but they tagged along and helped to push them to levels, high and then low, that we would not have seen without them.

Futures prices should, by and large, be based upon the fundamentals of supply and demand. We saw delinked commodity prices in 2008, and some of us are concerned that we see that taking place this year.

Congress passed the Wall Street Reform and Consumer Protection Act in July. With more than 40 rules to be promulgated by our agency, Congress gave us expedited implementation dates for only nine regulations. For example, speculative position limits for energy and metals are to be implemented within 180 days and for the agricultural complex within 270 days.

As someone who has been calling for these limits, and who appreciates the work of the Committee in this regard since 2008, the early implementation deadline is important. Large and small agribusinesses and other commercial businesses rely upon these markets to hedge their risks. They are having an increasingly difficult time doing so, in part I believe, because of large position concentrations of speculators. Don't get me wrong, without speculators there isn't a market. We need them. We want them. Too much concentration, however, can be problematic and has the possibility of contorting markets.

Now today, we see even larger speculative positions than in 2008. In total, there is $149 billion in speculative money in these markets, representing an increase since June of 2008 of 47% in the energy complex, where we have seen a single trader with positions as high as 20%. In the metals markets, we've witnessed an increase in speculative contracts of 20% and one silver trader with roughly 40% of the market earlier this year. In the agricultural complex, speculative interests grew by 18% since June of 2008. All of this makes the implementation of position limits as Congress mandated important.

Some have suggested, however, that we not implement the limits on time because we don't have all the swaps data we need. There is a point there. Congress didn't require that we promulgate the swaps data rule until next July, so how do we come up with a reasonable limit, particularly an aggregate limit, without that data? While this is a worthy point, there are ways to address it. I'd be pleased to explain several options.

Some, however, inside and outside the agency have suggested we simply find a way around the law's implementation deadline. They suggest, for example, that we "implement" the position limit rule, but not make it "effective" until sometime much later. First, we have no such legal authority to do so. Second, that is exactly the type of dancing on the head of a legal pin Washington-speak that folks in the country are all too tired of—and they should be.

We shouldn't be about getting around the law. We should be about working to do what we were instructed to do, to protect markets and help consumers. Congress passed the new law. We must implement it in a thoughtful manner. End of story in my book.

Thank you for the opportunity to be with you. I'd be pleased to try to answer any questions.

The CHAIRMAN. Well thank you.

I thank both of you. I think the main purpose of what we are doing here today is to get daylight on what the process is, how it is going, and for us to understand better as we talk to our constituents who are out there and trying to fulfill our obligation.

A couple of questions and we will right go right down the line. But first, Mr. Peterson, do you have any questions?

Mr. Lucas?

Mr. Gensler, what impact, since we are talking what you just said, would a delay in the January energy and metals position limit rule have on the agricultural commodities rule expected in April?

Mr. GENSLER. Mr. Chairman, I anticipate staff will make a recommendation tomorrow on all agricultural energy and metals position limits and anticipate that it would be both for the spot month, and for—if I can just call it the *all-months-combined* limits. And I am hopeful that we will have the support tomorrow to publish that rule, get comments, and then, consider those comments under the Administrative Procedures Act and put out a final rule as soon as we can sort through all these comments.

I note we received 8,200 comments on the proposal for energy limits—reestablishing energy position limits in January of this year. We put that proposed rule out for a 90 day public comment period at that time. I think staff tomorrow will be recommending a 60 day public comment period. But with 8,000 comments that came in on that topic earlier, this is a very important topic and the public is going to weigh in. And we look forward to that.

The CHAIRMAN. I understand. So are you saying that you kind of expect to be on schedule for the agricultural commodities in April?

Mr. GENSLER. We are going to do everything we can. It is certainly our goal. But I am being open here about the arithmetic. I think that there are parts of this, the spot limit proposal, that we will be able to implement earlier, but on the "all-months-combined" limit proposal that there is a very real data issue with it.

In January of this year, the proposal that we put out was a formula, and if we finalized, would have been applied to data in January 2011. And while we won't be proposing exactly the same thing tomorrow, it was staff's recommendation earlier this year, it will be staff's recommendation tomorrow, that any formula ultimately be applied to the overall size of the market. This is an important component. And as I said earlier, we have just closed the comment period on a rule on collecting data. We look to move expeditiously to finalize that data collection rule, but data is an important component to this.

The CHAIRMAN. Thank you. Commissioner Chilton do you have any comment?

Mr. CHILTON. No. Other than the Chairman is right. If you do the math under sort of what the thinking is, I can't talk about the specific proposals yet, but none of them allay my concern that we are going to do this, as instructed by Congress. It may be the best we can get a certain number of votes for the Commission. But again, Mr. Chairman, there are things we can do today like implement some things in January that won't cause any consternation—that may not be, let's say, the full Kahuna—that won't have problems like Congressman Moran suggested. I think we should do that.

I mean if Congress is concerned about excessive speculation, there are certainly ways that we could set a price point; that is, a level at which we have heightened regulatory oversight and do what we call a special call. Where we go out and ask for swaps data and then we see where the positions are netted. And if they are, if these traders are actually above the certain position point, and if they are, use all of our authorities, our emergency authorities, our trading authorities, and work with the exchanges, ICE, and CME to get them down. I am not saying necessarily get them off those exchanges; I am saying to get their net position down that may be in swaps, may be in options, may be in futures.

I think there are things we can do and we can do them on time. It may not be as expansive as we would like, but I hope we move forward on that.

The CHAIRMAN. Thank you very much. The chair recognizes Mr. Moran.

Mr. MORAN. Mr. Chairman, thank you.

Chairman Gensler, do you agree with Commissioner Chilton in regard to the lack of flexibility in these time constraints that he indicates are imposed by Congress? My understanding was that your General Counsel at a hearing, Commission hearing in October, indicated that you do have flexibility in regard to that 180 day limitation.

Mr. GENSLER. I think that you observe correctly that I had asked the General Counsel, Dan Berkovitz, as to the phased implementation schedule in essence with regard to position limits. Subsequently, he told me that the Administrative Procedures Act and case law specifically allow an agency reasonable leeway.

The Commodities Exchange Act clearly permits the Commission to adopt position limits in phases, such as proposing a formula now—and I note that is what we did this past January as well—a formula now and impose the actual numerical limits once we have more data. This would be on the all-months-combined. What he was asked specifically, because I asked him the question, was could we do that? Could we propose a formula and finalize that formula but then have the formula apply to data as it comes in, maybe a number of months later?

Mr. MORAN. A number of months later. Mr. Chairman, do you anticipate at what point in time you would have sufficient data to reach the conclusions that you are perhaps being asked to reach now?

Mr. GENSLER. Well, it is also dependent upon the good work of the staff and this Commission, the CFTC, in finalizing a rule on data collection which, fortunately, we already have out there. I think if we finalize that rule and are able to collect data, it is somewhere in the time frame that Commissioner Chilton talked about. We don't have any difference on that time frame.

Mr. MORAN. Has there yet been a—one of the conversations we have had in this Committee for a long time is about the connection between excessive speculation and price fluctuations. Is there—there is—make sure I understand this to be true—I'll ask it this way: Has the CFTC or its staff completed a report that found excessive speculation caused an unwarranted or unreasonable price fluctuation in commodity markets?

Mr. GENSLER. If I can broaden the question a little bit.

Mr. MORAN. You may. I have broadened questions for number two and three as well.

Mr. GENSLER. I am sure. I don't think that the Commodity Exchange Act or Congress has said that the CFTC is an agency to regulate prices. What we have as our mission is to ensure fair and orderly markets, that the price discovery function is transparent, and that there is an integrity of the markets, and that the position limit regime that has been in place since the 1930s is to ensure that there is a diversity of points of view. It doesn't limit hedgers, it limits the number of contracts a speculator can hold, and speculators and hedgers, importantly, must meet in a marketplace, but that there may be burdens that come from excessive speculation.

I will use an extreme case: If somebody had half a market, for instance, and then they were to liquidate that position it would be a burden on the market. Maybe if it is only ten percent of the market, to liquidate that market, it would be a burden. So, over the decades what we did is we put in place limits in the agricultural markets. There were limits through the exchanges in the metals and energy markets in the 1980s and 1990s. In fact energy markets had limits all the way through the summer of 2001, for these all-months-combined. And it was to prevent, prospectively as much as anything, the burdens that may come from large positions and the concentration of those positions in a marketplace.

Mr. MORAN. Let me broaden my question by asking a similar question but with a different conclusion. Has the CFTC or its staff completed a report that found excessive speculation positions in commodity futures markets were leading to market manipulation? Which I think is the direction you were telling me is more important; that you are there to regulate market manipulation.

Mr. GENSLER. There are two components in the Act. There is manipulation, or if I can broaden that a little bit, corners and squeezes. But, Congress also said, not only in the 1930s but I think also in the Dodd-Frank Act, has reconfirmed that we shall set position limits to do something that is not just limited to protect against manipulation; it is also to diminish or prevent any burdens that may come from excessive speculation.

So they are not identical. And any burdens that may come from excessive speculation may be actually far before somebody corners or squeezes or manipulates a market. Manipulation also includes intent. So I am just trying to highlight. And it is part of our challenge that they overlap, but they are somewhat distinct.

Mr. MORAN. I have run out of time, but my question was: Have you found, has the CFTC or its staff found evidence of either of these things happening?

Mr. GENSLER. There are certainly cases that we have brought on manipulation. We bring an active caseload of manipulation. So I could have answered your question *yes*, but I was trying to distinguish it because I was trying to be more fair to your question.

Mr. MORAN. I appreciate your fairness. And Commissioner Chilton, I had questions for you. I have run out of time. I do appreciate the way you testify. I understand what you are telling me. And I am very grateful for the words that you use. Thank you.

The CHAIRMAN. Thank you. Mr. Marshall.

Mr. MARSHALL. Thank you, Mr. Chairman.

I want to associate myself with the remarks of Mr. Moran to open the hearing. I found myself, largely, completely in agreement with him. And to me at least, the answer to the questions that Mr. Moran just posed, has staff concluded based upon what evidence staff has been able to gather that these, as Mr. Chilton refers to them, massive passives have skewed the market? I think the answer is *no*, staff has not done that. Certainly staff has not issued a report saying that massive passives have skewed the market.

All of our efforts thus far, for years now, for 2 or 3 years now, have been focused on these massive passives, the influence of index funds, and whether or not these index funds are skewing prices too high.

I think that from your testimony, Mr. Chairman, that it is quite clear the CFTC has gone the extra yard in so many different respects to try to comply with these deadlines. My conclusion is that the deadlines are simply too aggressive, that we simply weren't reasonable in trying to pick these periods of time. You all don't have daily reports of large traders in the swaps market. There is all kinds of information that you would like to have to further the analysis of the impact of the massive passives, since that seems to be a focus here on the market. Nobody wants to screw up these markets by prematurely taking positions or literally imposing position limits across the market and causing problems in any number of respects, diminishing liquidity, enhancing the problems, if there are such problems, caused by the massive passives, driving people overseas. I understand the Financial Services Authority hasn't indicated at all it is going to move forward with position limits that mirror ours. There are just lots of different things.

And I completely agree with Mr. Moran's observation that the *as appropriate* qualification that we intentionally stuck in there gives you the discretion to go ahead and wait until it is appropriate. It seems to me you wait until you are convinced that there is a problem, and then you have come up with a solution to that particular problem that isn't going to unnecessarily burden the rest of the market.

Mr. Chilton, with regard to massive passives, Dodd-Frank, after we wrestled with this an awful lot, gave additional discretion to the Commission to distinguish among classes of traders in imposing position limits, and also gave additional discretion to the Commission with regard to exemptions.

I kind of understand that you all are thinking about we are going to distinguish *bona fide* hedgers and then call everybody else speculators. But within that *everybody else* class of speculators, there are the massive passives and then there are a bunch of other people. There are traditional large market traders that take both sides. There are market makers, folks like that.

Have you given any thought, Mr. Chilton, to using your new authority to distinguish among classes of traders within that class of speculators to distinguish these different groups of traders and impose different position limits or exemptions from position limits on those different classes of traders?

Mr. GENSLER. You raise a very good point. And Congress did give us authority to distinguish between non-*bona fide* hedgers. I think what staff will be recommending tomorrow is a more general approach that doesn't point, necessarily, at distinguishing between *bona fide* hedgers.

Mr. MORAN. Mr. Chairman, I apologize for interrupting. We have 5 minutes here. Maybe there will be an extra round of questions. Again, if you all are going to start issuing additional proposals, one, I don't think you ought to be attempting to stick by these timelines when you don't have all the information you would like to have in order to give really, really good, narrowly focused solutions to or at least determine first whether there is a real problem here, and then the narrowly focused solution. I don't see how you can just generalize this and lump everybody in——

Mr. GENSLER. I was just—I am agreeing with you on timelines. I think that what we are contemplating, what I believe staff will be recommending is some formula to apply to data, as has been earlier discussed. I took your question as to be whether we would be proposing a specific lower limit or something on one class of party. So, when I said "more general," I meant there is not a lower limit on one group.

Mr. MARSHALL. Have you given some consideration to that?

Mr. GENSLER. I would say there has been a lot of discussion, and we look forward to public comment on whatever we put out, and also with regard to this question and other questions. I don't know if, Commissioner Chilton, you want to——

Mr. CHILTON. There shouldn't be any exemptions from commercial. People that have an underlying interest in the physical commodity, whether or not it is a Swift or Cargill or just a normal farmer or independent petroleum producer, they should have exemptions. Other than that, there shouldn't be exemptions. Whether or not there should be different levels, you might be right, sir. It may be more appropriate to have a little more granular view of it, because—and we can address this if you look at what their net position is. It is one thing if people have a large position, but the added benefit of what we are going to be doing in the future is we are going to be looking at this swaps data to find out where they really are.

So we can't just base things on whether or not they have a percentage on ICE or a percentage on CME, you have to look at where they are net, and we will be able to do that with this new rule, I think.

Mr. MARSHALL. I will wait until the second round to continue.

The CHAIRMAN. Thank you. Mr. Johnson, please. You are on.

Mr. JOHNSON. Back in the heartland, a lot of people believe, rightly or wrongly, that prices don't always reflect supply and demand. I think you have expressed that too.

I have a question and then kind of an unrelated comment.

In your judgment, either witness's judgment, do you think the level of prices that ag commodities are at today is a result of the supply and demand factors and/or speculation? And how would you allot each in terms of what impact you think those respective forces are having in our market prices?

Mr. CHILTON. Congressman, by and large they are a factor of the fundamentals, but I couldn't—and I am not an economist. Neil Cavuto tried to get me to say, well, how much is speculators and how much is price demand, and I wasn't going there. I am not an economist and it would be irresponsible.

But to go to this thing about we need to document, we need to do this before we impose. The purpose of the Commodity Exchange Act says that we are to prevent and deter fraud, abuse, and manipulation. So all of a sudden we have been given, for people who don't want the regulation, this new hurdle to say, well, you have to prove beyond a shadow of a doubt that this equals that. These are very complicated markets, and it is not always easy to put things together like that.

So to protect consumers, to ensure the folks in your districts are using these vehicles, like they want to, for adequate risk mitigation, that is why these limits are important to put in place thoughtfully.

I get letters every day, Congressman. I have one right here from Dunkin' Donuts we received last night. They are concerned about speculation. Swift says they are thinking about getting out of the market in part because of speculation. Delta Airlines wrote the other day. These are real concerns about people, the hedgers who are in these markets that are concerned they can't use them.

Look, nobody is talking about going crazy on this. We just want to—I just want to do what Congress intended and try to do it in a reasonable fashion; doesn't make anything crazy, just do what we are told.

Mr. JOHNSON. I guess my comment would be this. As we all know—and I'll try to say that knowledge is power, terminology in some ways is power. And I would only surmise that certainly the average Member of Congress, and probably the average Member of this Committee—I can only speak for myself—has maybe a general understanding but only a general understanding about first, terminology; and second, the mechanism by which all this works.

I think your being here today, Chairman, calling this hearing is important. But I also think it is important to have a mechanism, have a mechanism by which the public and the Members of Congress frankly can understand very, very complex and very difficult concepts. I don't have the answer. But, it is a legitimate question, and it is something that I think is real important.

I deal with constituents back home, and I am probably speaking for everybody in this room, we have constituents who come to us every day; almost all of us represent rural areas. "Speculators are doing this, and the Commission is inadequate," if they even know the Commission exists, and I think having an ability for those people to understand, the public to understand and us to understand is really important.

The CHAIRMAN. Thank you very much. Mr. Schrader.

Mr. SCHRADER. Thank you Mr. Chairman. Following up on the line of questions so far, it seems like we are getting hung up on terminology, terminology that has a pejorative context to it like *speculation*. I would assume that in the 20th century the Commission's primary rule is to root out actual fraud, fraudulent actors that were doing things on purpose.

I guess I have to ask the question given the 21st century where you have these hyper-computer trades and massive investments and things flowing unbeknownst, with no mal-intention necessarily intended but mal—bad results coming out of it. I think no one could, while we may disagree about whether or not they are actually speculators causing this problem in 2008, everybody agrees there was a huge distortion in the market. I guess the question for both of you from me would be: Is it the CFTC's responsibility to protect American consumers, American farmers, American industries, by dealing with any distortion of the market, regardless of whether it was intentional or not?

Mr. GENSLER. I think the answer is yes. Speculators and hedgers meet in the marketplace, and farmers and ranchers and producers need those speculators in the marketplace so that you can have an assured price at the end of the harvest, for instance. But at the same time, this Commission was set up and its predecessors were set up to make sure that everybody can see the market, that is what is called transparency, and that it is free of fraud and abuses. The Commission has to ensure that the market is orderly and everybody has equal access, for instance, in a place that everybody can see it, everybody can access it, and it is free of manipulation and these other things.

Mr. SCHRADER. Mr. Chilton.

Mr. CHILTON. Thanks Congressman. That is a great question. It is insightful.

First of all, I want to say what I said in my testimony. Speculators aren't bad. You need them. You don't have markets without them. The concern that some of us had is just the concentration of them, so much that they can influence prices one way or the other, and you don't get to what Mr. Johnson talked about: adequate price discovery. But on these fast trading—they call them high frequency traders—they played a role in the flash crash. They didn't instigate it, but they played a role because they were arbitraging between the futures market and the securities markets for a while.

These trades are—talk about being complicated, Congressman, these trades go on, they trade thousands of contracts in a nanosecond. And their whole idea, different from how these markets have been set up sort of when they were in the open pits, they are trying to scoop up market dollars, these little pennies, in nanoseconds. They are trying to skim off the top.

Now, they do provide some liquidity to the markets, but that liquidity may be liquidity with other traders. And I am just concerned that we don't want this to become a gambling venue. You want it for the original purpose of the markets, for these commercial ags and other businesses to be able to hedge their risks.

So I am very concerned about it, these high-frequency traders, Congressman. I think we should be doing some sort of due diligence, maybe putting their programs, their algorithmic programs, into one of the exchange's testing environments, make sure they are not going to go haywire.

I think we should also as part of disruptive trading practice authority, the Chairman and I worked on a lot, have some responsibility. If they help to cause another flash crash, they should be held accountable.

If you look at the law right now, we don't have enough teeth in it. We are doing that as a result of the Dodd-Frank law, and we are going to put some more meat on the bones, and that is one area that I think we need to do.

Mr. SCHRADER. Thank you. I guess last is just a request. I would appreciate information, for me and maybe the Committee, regarding areas in the swap arena that you do feel you have adequate data for and rulemaking timelines as well as the timeline for rulemaking with—that you may want to phase in, given the lack of data that you have referred to, in some of the other areas.

Mr. CHILTON. The Chairman probably wants to comment further, and I know you only have a little bit of time. While everybody says we to need to get all this data that Mr. Marshall and people talked about, "Let's get it all, let's not make a haphazard decision," I agree. The spot month we could do right now even in the swaps area. This is the currently unregulated area. This is the one that you have given us the authority to look at.

And the reason we can set that limit now is because you base the limit on the deliverable supply of whatever the commodity is. So you don't need to see all-months. You don't need to see the aggregate. We could do the spot month right now, which would in part get us to where Congress instructed us to go. The Chairman wanted to add?

Mr. GENSLER. I concur. I think we have more flexibility. We have asked staff to make a recommendation where we could phase in and do something in what is called the spot month. Again, we have these limits—this is just when somebody is about to deliver the corn or wheat or oil into a contract. We have these limits in energy, metals and agriculture. I shouldn't say we. The exchanges and we have them. I think those could be phased in sooner than the all-months limit.

The CHAIRMAN. Thank you. Mr. Conaway.

Mr. CONAWAY. Thank you, Mr. Chairman. Gentlemen, thanks for being here.

Not beating the lack of data dead horse to even further pulverize it, but if you go ahead and move forward without the data, as may be the indication that is here, how quickly will you know you have gotten it wrong? Are there things that you will watch for to say that we have driven speculators off that side of the deal and that burdens on hedgers have increased?

I am assuming by burdens, Mr. Gensler, that you mean increased costs of transactions and other things, that you might expound on a burden a little bit. But how quickly will you know that you have done some harm, rather than just trying to ease into this thing without disrupting it and creating—going crazy, as Mr. Chilton said? What are your matrix or your benchmarks to say this one was too far?

Mr. GENSLER. Well, it is my hope and, again, we haven't had the Commission meeting that we will have tomorrow yet, but it is my hope that we will propose something and hear from the public that would allow us some time to get the data on these all-months-combined. So I may be disclosing my bias here, but it is a challenge. There is a 180 day and 270 day statutory date. Commissioner Chilton and I read that the same way.

Mr. CONAWAY. Excuse me. With respect to that, do you feel you have any responsibility, due to your fiduciary job, to tell Congress that those dates aren't good, that those were set arbitrarily and capriciously by Congress, and that once we looked at the level of work and the number of lawyers and the level of commitment, that the five of you have actually to read it and go through it and understand what you are doing to the markets? Do you have any kind of responsibility to say those dates aren't good?

Mr. GENSLER. Well, I think I am saying here today—and I thank the Chairman for having this oversight hearing—is that we are going to take up a rule tomorrow. It is a staff recommendation. We will see where my fellow Commissioners are. I don't want to prejudge that.

But if we were to propose something tomorrow, it would have a healthy comment period from the public and that will, by its very nature, pass the January date. So I am telling Congress that, no, we will not finalize this by that statutory date.

Mr. CONAWAY. This may be a broader body of work. You have the full Dodd-Frank piece of legislation, not just these limits and what we were talking about this morning, but you have a broader body of work. Have you looked at that and laid out the timelines and just say, yes, we can get all this done responsibly in that time frame?

Mr. GENSLER. I think we have the goal to get it done and we can get it done. And I will say, I think that Congress laid out the 360 days. So by completing our work by July 15 of next year it will help lower regulatory uncertainty, and that is a very important thing. And, of course, we also had a crisis in 2008. And that was a very real crisis.

Mr. CONAWAY. Speaking of the crisis, I have a short amount of time. I take that that you are fine with these dates. Mr. Chilton, you mentioned that some time frame in the run-up to the bubble in 2008 that there was $200 billion in new money in the system. How much of that money has fled the system? What are the levels today *versus* then?

Mr. CHILTON. I can't give you that, sir.

Mr. CONAWAY. My question, I guess the idea would be that if that money stayed in the market, as I suspect it did, and prices have fluctuated, we are way off the $147 on oil, as an example. And so I guess I am hard-pressed to see that that was—that money did have somebody on other side, and if there wasn't anybody on the other side, it raised the price to get somebody else in on the other side. I get that. But I want to make sure that we are not fighting the last war, and that is necessary because there are other comments that you have not—staff has not documented where all these bad things have happened, except on some isolated instances. But if you could get that number to us at some point in time.

Mr. CHILTON. It is actually—we know that a lot of money went out. And it went—I mean, look, as the Chairman said, we are not price setters. We are supposed to be commodity blind, although I have a little bit of penchant for the ags, and price neutral. We are not price setters. And I also get concerned when oil is $150 but——

Mr. CONAWAY. It hadn't been $150 except for about an hour and a half.

Mr. CHILTON. About 1.727 days, but it stayed high for a lot of people, Congressman, in the countryside, a lot of businesses went out. So we lost a lot of that speculative money, though. You are absolutely correct. Some it left the market and prices went all the way down, I believe in December, to like $35 a barrel. So this can go up, up, and down.

To answer, by the way, one of your earlier questions, I continue to say we need to err on the high side at first so that we don't do any damage. Because I agree with you; we don't want to make any issues here that contort markets or do something bad. Some things are working well.

Mr. CONAWAY. Do you have triggers or matrixes that you will watch.

Mr. CHILTON. We are very good at watching these markets, at watching liquidity. We don't want to drive speculation away. We don't want to drive it until we get to regulate the OTC market. We don't went to send it there. We don't want to send it overseas. So we have to do this in a responsible fashion, and we can do it, sir.

Mr. CONAWAY. I yield back.

The CHAIRMAN. Thank you.

Mr. Kissell.

Mr. KISSELL. Thank you, Mr. Chairman, and I welcome our witnesses today.

If you would allow me a moment of reflection here, this is—I am finishing up my first term in Congress, and the first hearing that I came to in Agriculture was about derivatives and speculation, and the witnesses we had that day were split. Some of them pretty much making the case that nothing went wrong, that the market worked because investors didn't lose any money and there was no, figuratively, train wreck at the end of the process like we saw with the banking system, financial system there.

And when I finally got a chance to ask the question—it was more of a statement than a question. And I pointed out to them that while investors may have not lost money *per se,* that the effects upon the American public were quite substantive in terms of how we had to deal with individuals and businesses and farmers, ranchers, everybody, how we had to deal with to whatever degree speculation caused these increases in prices.

So I don't so much today have a question as I just want to remind the witnesses and appreciate their responsibility here of the very intricate task of trying to make sure this process which is so important moves forward, but also a reminder that, as Mr. Schrader said, that the American public in general so largely depends upon this process working without creating the speculation and artificial price increases, so forth and so on.

With that said, I am going to yield my time, Mr. Chairman, to Mr. Marshall.

Mr. MARSHALL. Thank you, Mr. Kissell.

Just sort of following up where I was when I stopped, you clearly have the statutory authority not to move forward unless it is appropriate to do so. That is why that language was stuck in there. And that if you move forward without understanding precisely what the problem is, then it seems to me that you are not moving forward appropriately. And if your staff hasn't identified what the problem is, then how do you actually come up with a regulation to solve that problem. You don't even know what it is. It is sort of too broad a brush.

But back to this classes of traders. We intentionally stuck that language in there to give you the discretion to distinguish among the speculators and, if you chose to do so, I don't know whether there is a massive passive problem here. I just don't have the expertise. And there are, as Mr. Kissell points out, people on both sides of that.

So I leave it to you and your staff and your economists and whatnot to figure it out. But if it is massive passive that is the problem, then the solution should focus specifically on that, and one-size-fits-all position limits don't do that. And you just use ratios.

Assume you have 20 traders in the market, five of them are passive. You put a position limit in that is designed to maintain their percentage at no more than 25 percent. And then let us say a whole bunch of additional passives show up. Let us say 20 additional passives show up. Now I have 40 traders in the market and 60 percent of it is passive money.

So you really do need to at least consider distinguishing among the classes of traders if you conclude that that is a problem.

I associate myself with the questioning of Mr. Conaway in many different respects, and he has observed there is a fiduciary duty here.

And I guess a final question. Let us assume that you impose position limits and that there is a large market demand out there that is now sort of stymied. It doesn't have an opportunity to just come into these markets because you are aggregate. You are across all of the markets. Where does that money go? How do people who want to take a position in commodities to do whatever, hedge or because they want that in their portfolio or whatnot and they can't do it in these vehicles, where do they go? Do they go to Europe? Do they start hoarding commodities? I mean, what do they do?

Mr. GENSLER. If I can address the last point, because this has been raised with us.

If somebody wants to come into the market and hedge, if they are a *bona fide* hedger these limits won't affect them. If they are coming into the market, they are not a hedger, and they are of normal size in these markets, these numbers won't affect them either. The numbers that we currently have in the markets or even that we proposed in January, would have only touched a handful of traders in the energy markets, the largest speculators.

So it is truly just a very small group of people who are very large in the marketplace.

To answer your question, traditionally, they went to the over-the-counter market, but Congress has said bring that in. But potentially that could move on to contracts that were similar but not identical, or they would possibly move overseas. And we are very conscious of that, and we are looking at that.

Mr. MARSHALL. If they go elsewhere using those two devices—they go overseas or they go into contracts that are similar but not identical—doesn't both of those things have the same effect on the market as far as pricing is concerned?

Mr. GENSLER. It may. It may.

So that is part of why this, whatever we put out, is going to be a proposal. We really want the public comment to weigh in. I think that is a good process and a constructive process. Congress has directed us certainly to look at this and expand what we currently have in agriculture products to the over-the-counter markets, and we are contemplating to also do it in the energy and metals.

Mr. MARSHALL. Thank you, Mr. Chairman.

The CHAIRMAN. Mr. Luetkemeyer.

Mr. LUETKEMEYER. Thank you, Mr. Chairman.

It was interesting, Mr. Chilton. I appreciated your remarks. You said that MIT and Princeton and even Lincoln University of Missouri were involved in discussing some of the pros and cons of this. And I happen to be an alumnus of Lincoln University. So it is nice to see my little *alma mater* in the same stature as MIT and Princeton and those guys. So I appreciate your comment.

I noticed yesterday in *The Wall Street Journal* an article with regards to our discussion this morning with regards to how we are proceeding and the speed we need to be proceeding at with regards to coming up with rules, and I think that is basically what this hearing is about today.

And one of the comments that was made in there is that there is enough data already accumulated, that you can go ahead and make some of these rulings and not have to continue to research or come up with more data or more surveying. And this morning it seems like the comments have been coming from both of you gentlemen with regards to we need more data, we need more time. Can you allay that concern of this article here? Are they out in left field? Or where are we at in this?

Mr. GENSLER. I think there are many roles that Congress has asked us to do, but position limits is a particular challenge because it really is related to the size of the market. If you are going to limit something, if Congress is saying to limit something, you can pick whatever the percent is, it relates to the size of the market.

Most of the other rules are about reporting, about how a trading facility will work, how transparency works. I think that we have enough knowledge to go forward to lower the risk of clearinghouses.

Many of the rules don't have this same challenge. I think the position limit rule, to be quite direct with you, has a unique set of challenges because it is about the size of the market, the size of the crowd, and the interaction between hedgers and speculators.

Mr. LUETKEMEYER. So what you are saying is you have a lot of data on most of the things you need to be working on, but some of the issues, especially with regards to position limits, you need some more results yet to be able to come up with anything.

Mr. GENSLER. I think that is true to part of the position limits. I agree with Commissioner Chilton. I think on the spot month limits related to deliverable supply and how we have traditionally done that and the exchanges have, we could possibly move in a more timely way.

Mr. LUETKEMEYER. What is the impact with the lack of a rule? If we keep putting this off or we delay, what is the impact on the markets? What is the impact that we can expect for our farmers and our commodity folks?

Mr. CHILTON. Even those who say that speculators aren't having an impact would like to have the rule in place to some extent because then it would take the argument away that they are having an impact, if you get me.

Mr. LUETKEMEYER. Certainty is always nice, and that is the key to any kind of market. In today's world, they are debating the extension of tax law right now, and a certain uncertainty is a big part of that rule.

I'm sorry. Go ahead.

Mr. CHILTON. Congressman, we have seen in the crude market and the natural gas marketplace 20 percent. We have seen concentration by one trader. We have seen what I consider excessive speculation. This would be on the short side in the silver market. There are issues that I think, as the Chairman said, are the largest of the large that we need to be concerned about. We can do that right now through this thing that I talked about earlier looking at a certain level which we say that deserves escalated scrutiny that we can do this thing called a special call.

That is, we say, Chairman Boswell, you are over, say, ten percent of ICE or NYMEX. And then I say I want to know your other positions. You provide them to me, your swaps positions that we don't have the aggregate data on yet. Once we get that information, I see if you are above that level still. Because even though you might be above this position point, your swaps may show that you are below. But you also could say your swaps say you are way high. And then we would use our authority, work with the exchange, ICE, or CME to get down to an appropriate level.

That would deal with the largest of the large traders, the folks that people, your constituents, write you about and the folks that we look at every week in our surveillance meetings and say these are a concern for us. We can do that today. We don't need additional data. It wouldn't be hasty. And, as the Chairman and I agree, we could do the spot month right now.

Mr. LUETKEMEYER. I see as my time runs out here I just want to make one comment. And, Mr. Chilton, you made this earlier, that the intent is to protect the markets for their original purpose. And I sincerely hope that you continue to use that as your guiding thought in all of your deliberations. Because, to me, that is why we are here today, is to protect these markets for the original intent of the farmers and original commodity folks to be able to use these things, to use them to enhance their businesses and their ability to do business. It is not a speculative forum that we are worried about here. It is the original folks who use these things to manage their businesses.

So that would be my only comment and my only concern and my wish to you.

Thank you. And, Mr. Chairman, I yield back.

Mr. GENSLER. If I might say, that does guide us. I really do think that does guide us.

The CHAIRMAN. Mr. Murphy has joined us. He is not a Member of the Subcommittee but, by unanimous consent, we will recognize him at this time.

Mr. MURPHY. No questions.

The CHAIRMAN. Mr. Neugebauer.

Mr. NEUGEBAUER. Thank you, Mr. Chairman. Thank you for holding this hearing.

I think that the part of the Dodd-Frank that called for a finding—the question is the Exchange really—you all really haven't done anything in the sense of coming up with a specific finding. And so when you send the rule out, you are going to send a rule out that says we just think there needs to be limits out there. We don't have any finding that those limits are needed.

Am I understanding that correctly?

Mr. CHILTON. Certainly Congress told us to put the limits in. We had the authority actually before this, but we didn't have support to do this. So we were instructed in the Dodd-Frank bill to put limits in.

And the original purpose in the Commodity Exchange Act doesn't say that you have to jump some hurdle that proves beyond a shadow of a doubt in a court of law that speculators moved gas prices ten percent. The law says that we are to prevent and deter fraud, abuse, and manipulation; and so that is sort of the guiding onus that I look at, sir.

Mr. NEUGEBAUER. That is one of the things that we may have a disagreement on. I don't necessarily know whether Congress told you to impose limits.

Mr. CHILTON. Section 737.

Mr. NEUGEBAUER. If you look at it, it says, as the Commission finds as necessary to diminish, eliminate, or prevent such burden. In other words, in what you have told this Committee today you don't have data that says that there are abuses or excessive speculation going on. I think the intent of Dodd-Frank was, if you find it, address it certainly. I agree with the gentleman from Missouri. The job for government is transparency and integrity.

But what we haven't heard today—and several of the people on the panel have asked this question. We haven't heard you say we have identified where there is excessive speculation going on that could manipulate the pricing in the marketplace.

Mr. CHILTON. Congressman, perhaps Congress should have put a finding in before we did it, but they didn't.

Mr. NEUGEBAUER. I know the story, and I agree with that. But since we didn't, we kicked the ball to you and we said you should go out and address that issue and conduct an economic analysis and to look at that and make sure. And if you find that, then you should take action. And we would want you to take action.

I think what you hear today is everybody agrees that we want integrity and transparency in the marketplace. What we also don't want is you all setting prices. I have heard you say, Mr. Chilton, it wasn't your job to set prices, but I will tell you by manipulating or by changing some of these limits, you could be in fact affecting prices. You may have the undesired result.

The question is, what is oil worth? I don't know. It may be worth $300 a barrel. It may be worth $50 a barrel. But we need to let the markets decide that.

I want to go back to the spot month, because there is so much to cover here. Since price discovery, most people would agree, happens either in the cash months or the spot month, then what would be the need, then, for having position limits in the outer months.

Mr. CHILTON. Well, in the spot month, there already are position limits. But the outer months, it was the question that Mr. Marshall actually alluded to when he talked about the massive passives. They have a different trading strategy, Congressman, these massive passives. And what they do is they are not—they don't really care what the price of oil or wheat is in the next day or so—I mean, they care, but they are not in it for a day or week. They are in it for the long term. They are saying, for example, crude oil is going to be worth more in 2 years.

What happens when you get these large massive passives who have a trading strategy, it is markedly different than what they have been in these markets traditionally. They are fairly price insensitive because they've got a long view of it. So they just roll their positions when the contract expiration comes up, and every other trader knows they are going to do it. And these massive passives can have 30, 40, 50 percent of the market. I think Congressman Marshall's question about whether or not you should have a limit there is a great question. I haven't figured out how you do it, quite frankly, sir, but it is an important area to look at.

Mr. NEUGEBAUER. Last question here. So—Mr. Gensler, so if—one of the things in the bill it says that you can do as appropriate. I think that was, again, Congress trying to make sure that we weren't being too prescriptive.

So in many positions—I mean, could the finding—if we finally went out there and looked into and analyzed what was going on, could one of the findings be that or the appropriate limit is zero or unlimited? What is appropriate?

Mr. GENSLER. I supported proposing position limits in January of this year, and I will be supporting what I believe staff will be recommending tomorrow. I still have to see it. It is changing a little this afternoon.

Because I do think in all-months-combined, as we have done in the agricultural markets for decades, as we did with the exchanges in the energy and metal markets in the 1980s and 1990s, that it ensures that there is a diversity of speculators in the market. One can debate how many, and I think that is a very important debate. But, I think that the integrity of the market and the price, how people come together, you need to have a diversity of points of view in the marketplace, not one or two or three large traders on the speculators' side dominating the marketplace.

I wanted to try to answer both of your questions together.

The CHAIRMAN. Thank you.

Mr. Peterson.

Mr. PETERSON. Thank you, Mr. Chairman. I waited until the end here because I want to head in a little bit different direction and ask you a couple of questions you may not want to answer.

This story that was in the *New York Times* on Sunday, I assume you have read that?

Mr. GENSLER. Yes.

Mr. PETERSON. And this has been brought up to me by a number of Members. That has created a fair amount of interest on the Hill here. So I want to know what your view is on a couple of things.

This issue of the—trying to put these on the electronic market and thereby reducing the spreads. I think that is some of what you are trying to do through this whole process, that the more we can get this information out, the better the market will work and the end-users will have a more fair place in the marketplace. I think that is kind of where you are at.

Mr. GENSLER. I think it is where Congress was. I think transparency helps tens of thousands of end-users. Some of it is through real-time reporting after the transaction, but some of it also comes on the smaller trades, not the big blocks, even before the transactions.

Mr. PETERSON. So this issue about the Citadel that is trying to set up this electronic trading that would give you real time or before the transaction reporting, if that was implemented, would reduce the spreads.

Mr. GENSLER. I think it brings greater competition, and the American system works best when there is more competition.

Mr. PETERSON. So that gets to the issue of what actually went on here. Apparently getting to the governance of these clearinghouses, which became an issue somewhat in the conference committee and with the Lynch amendment and so forth.

So it appears to me that these big guys are trying to keep this very profitable part of their business to themselves. Am I wrong about that?

Mr. GENSLER. I think it is also part of the American way to try to maximize profits. And they have shareholders, and so, I respect that.

Mr. PETERSON. And so you don't disagree with some of the characterizations in this article—that night we made the deal the last night on the derivatives, that set off a flurry of lobbying that went on from like midnight to 5 o'clock in the morning trying to undo what we had done. So I mean, generally, you can figure out what is going on by following the money. Obviously, we hit a nerve because we created—there must have been 250 bank lobbyists running around there trying to undo things.

Mr. GENSLER. They are still visiting us.

Mr. PETERSON. So this is something you are looking into, I assume, in the process of this whole implementation of the Dodd-Frank Act?

Mr. GENSLER. We anticipate tomorrow taking up four proposed rules including this position limit rule. But there are two others that are very important.

With regard to clearing—again, these are proposals. But with regard to clearing, it will be our last set and that will include something called participant eligibility and ensuring that futures commission merchants could get in. That *New York Times* article highlighted that, currently, the clearinghouses are closed clubs. They are very exclusive, not inclusive. And they say it is because it is risk management.

We are also taking up these electronic facilities or, technically, they are called swap execution facilities.

Mr. PETERSON. Is there a significant difference between making this available in real time or right before the trade as opposed to making it available 30 seconds after the trade?

Mr. GENSLER. Here is what is so important. If a party wants to make a bid or an offer—this is absolutely bipartisan—if somebody wants to make a bid or an offer, they should be allowed to do it. And, right now, that is very difficult in this marketplace. You have to be invited in, basically.

I think what Congress said was swap execution facilities. The words you used was "multiple participants have to have the ability to execute or trade with multiple participants." And to do that then somebody should have the ability to make a bid and broadcast it. And that is a very important part of being a swap execution facility. That anybody who wants to make a bid on the market can make a make a bid on the market. Obviously, they have to have the resources to stand behind their trades.

Mr. PETERSON. So where is that in the—when will the final decision be made on that? Do you know? When will you actually get that finalized?

Mr. GENSLER. We are taking up that proposal tomorrow.

I think what Congress did was historic. It is very important. It will bring transparency and competition to the market so that end-users will benefit. I think it will narrow spreads over time. And then we will put that proposal out, if the Commission supports it tomorrow, usually, for 60 day comment.

Mr. PETERSON. And then it will go to final rule?

Mr. GENSLER. Based upon public comment, by next July and have certain implementation dates as well. Give us some time for implementation.

Mr. PETERSON. So it should happen this year sometime yet?

Mr. GENSLER. You are referring to the year just about to begin?

Mr. PETERSON. I mean next year.

Mr. GENSLER. Yes.

Mr. PETERSON. And that will get at some of the criticisms that were in this article if we get this done.

Mr. GENSLER. I think there were three main criticisms in that article, all interlaced: Governance. We have published the governance rule on October 1. It was put out for public comment. We received 150 good, solid comments. We are trying to finalize that early next year. It goes to clearinghouses and the eligibility for all valid futures commission merchants to be part of those clearinghouses. We are going to try to propose something on that tomorrow. And, I think, the article went to the openness and competition in trading venues; and we are going to try to do that proposal tomorrow.

I think that end-users and agricultural interests and energy interests will benefit greatly if more competition and more transparency are brought onto these markets. And I believe that markets work best when you have competition and transparency, and I think that is what Congress told us to do.

Mr. PETERSON. There is no question that is what most of us wanted.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

That completes our first round. I know that Mr. Marshall has another question. Anybody else have further questions?

Mr. Marshall.

Mr. MARSHALL. Mr. Chilton, you mentioned that one reason to go ahead and impose position limits now is that it would remove pressure, the silver lining in this cloud that is hanging over the industry. It is hard for me to believe that it relieves pressure if you impose position limits that just don't do anything, or do too much, and somehow screw the markets up. So, the pressure remains, particularly if all of this phenomena is being driven by underlying market forces.

Congress for a reason did not make findings that there must be position limits in all of these different contracts. It is because we intentionally wanted the CFTC to have the discretion to make that decision. It seems to me you all have not made that decision except in sort of a broad sense, and to suggest that you need to move forward and actually impose position limits because Congress has mandated that ignores the as appropriate language, the as necessary language and ignores what we actually intended.

We didn't know what to do. We don't have the expertise. We deferred to you to make the decision ultimately what sort of position limits should be imposed.

And a final thing just to clarify what I said about ratios. When I gave those numbers earlier I was talking about assuming that all of the *bona fide* hedgers as now defined are in there and in the market. If you just look at the balance of the speculators, the ratio between the speculators winds up being fairly critical if you have concluded that massive passive money is a problem. I don't know whether it is. It may be good, for all I know.

But if you conclude that, you are going to have to set different position limits; and that is why we stuck that language in the statute, to give you the discretion to do that within that class of speculators.

Thank you, Mr. Chairman, for your indulgence.

The CHAIRMAN. Anybody else have any further questions?

Seeing none, thank you very much for your time and sharing with us and put a little daylight on the process. We appreciate it.

Mr. GENSLER. Thank you. And happy holidays if I don't see you until after the first of the year.

The CHAIRMAN. Thank you and the same to you.

The first panel will be excused, and we will call the second panel to the table as soon as possible.

We would like to welcome our second panel to the table. Thank you for your patience for waiting, and we are happy to have you here.

We have with us today Mr. Jim Collura, Vice President for Government Affairs of the New England Fuel Institute; Mr. Terrence Duffy, Executive Chairman of the CME Group of Chicago; Mr. Joel Newman, President and Chief Executive Officer, American Feed Industry Association; Mr. Jeffrey Sprecher, Chairman and Chief Executive Officer of IntercontinentalExchange out of Atlanta; and Mr. Robert Jones, Senior Vice President, ANB AMRO Clearing Chicago LLC, on behalf of the National Grain and Feed Association.

Mr. Collura, please begin when you are ready.

STATEMENT OF JAMES M. COLLURA, VICE PRESIDENT FOR GOVERNMENT AFFAIRS, NEW ENGLAND FUEL INSTITUTE; FOUNDING MEMBER AND SPOKESMAN, COMMODITY MARKETS OVERSIGHT COALITION, WASHINGTON, D.C.

Mr. COLLURA. Chairman Boswell, Ranking Member Moran, and Members of the Committee, thank you for the opportunity to testify on the importance of speculative limits for commodity dependent businesses and consumers.

I currently serve as the Vice President of the New England Fuel Institute, which represents more than 1,200 mostly small, family owned and operated home heating companies.

In 2007, in response to what was perceived as unpredictable and volatile commodities futures markets, and out of concern over possible excessive speculation in these markets, we partnered with the Petroleum Marketers Association of America and other business and consumer groups to form the Commodity Markets Oversight Coalition, or CMOC. I am delivering testimony today on behalf of this coalition, and I have submitted a list of supporting groups for the record.

CMOC is comprised of an array of commodity dependent bushiness and industries, as well as faith-based organizations and groups representing average American consumers. We favor policies that promote stability and confidence in the commodity markets and that preserve the interests of *bona fide* hedgers and consumers. Our coalition endorsed title VII of the Dodd-Frank Act, which includes the most substantial reforms of the derivative markets in more than a decade.

Members of this Committee, under the leadership of Chairmen Peterson and Boswell, and Ranking Members Lucas and Moran are to be commended for their years of hard work that resulted in the passage and enactment of this monumental piece of legislation.

The Dodd-Frank Act includes various regulatory initiatives necessary for market transparency and to prevent fraud and manipulation and excessive speculation, including a requirement the CFTC establish speculative position limits for regulated and currently unregulated markets. The law requires that the CFTC establish position limits for energy commodities by January 17, 2011. However, we are disappointed that the Commission has recently come under pressure to delay the imposition of these limits by the deadline as required by law. Our coalition opposes any such delay.

Some argue that the CFTC has not had enough time to thoroughly vet and consider the potential effects of such limits. However, the Committee should note that the Dodd-Frank Act does not provide the CFTC with the authority to establish limits. It actually expands existing authority.

The Commodity Exchange Act of 1936 requires the CFTC to set position limits in order to prevent a single market participant from controlling price movements. The law sought to prevent undue burdens on interstate commerce resulting from excessive speculation and, as a consequence, cause sudden or unreasonable price fluctuations or unwarranted changes in the prices of commodities.

However, the U.S. exchanges have abandoned hard energy speculation limits in favor of softer accountability limits. Under the leadership of Chairman Gensler, the CFTC in 2009 acknowledged that accountability limits were insufficient to prevent traders from taking controlling positions. Many traders were violating them with little or no action by the exchange.

The CFTC held a round of hearings in the summer of 2009 and introduced a proposal in January. In the 4 months between January and April of 2010, the CFTC received well over 8,000 comments on the proposed rule, the vast majority urging strong and meaningful limits in speculation. During that time, some argued against the CFTC's proposed action out of fear that it would drive market activity from regulated exchanges under so-called dark markets; those that reported little or no data or were subject to little or no oversight. The CFTC should not act, they argued, until it was granted authority over the OTC and foreign markets and could implement limits across the board.

The CFTC under the Dodd-Frank Act enjoys this authority. Once fully implemented, the Act will bring dark OTC markets to light by requiring exchange trading or clearing. It requires that foreign boards of trade that seek U.S. access first prove that they are subject to comparable oversight and regulation, including the imposition of position limits.

In addition, many overseas regulators are drawing up their own plans to impose speculation limits. If the CFTC were to delay implementation of these limits here in the United States, the impetus for regulatory reform in other jurisdictions overseas could be jeopardized.

The CFTC must act. Excessive speculation is real and it hurts. When prices surge to unjustifiable levels, consumers are left with higher food, gasoline, and home heating costs. Vital U.S. businesses, including manufacturers, airlines, truckers, and other transporters are hurt as well. Even still, some continue to believe that speculation can never be a bad thing. Despite ample evidence that excessive speculation has been destructive to commodity markets, some continue to doubt, question, or outright deny that speculation was ever or could ever be excessive.

Make no mistake, we believe in open, transparent, and competitive markets and that new regulation must not excessively burden market participants or unnecessarily impede market liquidity. Speculators provide the market with this liquidity. But excessive speculation drives commodity prices to levels unjustified by market forces and results in price bubbles that harm commodity hedgers and users in the broader economy, as we saw in dramatic fashion with the commodity bubbles in 2007 and 2008.

Establishing and imposing timely and meaningful limits will send a signal of confidence and stability, and help create more transparent, orderly, and functional commodities markets.

Thank you again for the opportunity to testify. I look forward to any questions you might have.

[The prepared statement of Mr. Collura follows:]

PREPARED STATEMENT OF JAMES M. COLLURA, VICE PRESIDENT FOR GOVERNMENT AFFAIRS, NEW ENGLAND FUEL INSTITUTE; FOUNDING MEMBER AND SPOKESMAN, COMMODITY MARKETS OVERSIGHT COALITION, WASHINGTON, D.C.

Honorable Chairman Boswell, Ranking Member Moran and Members of the Committee; thank you for the opportunity to testify before you today on the importance of position limits for commodity dependent businesses and consumers, and the broader economy and market stability.

I currently serve as Vice President of New England Fuel Institute (or "NEFI"), a not-for-profit home energy trade association that represents more than 1,200 mostly small, family owned- and operated-businesses. In 2007, in response to what was perceived as increasingly unpredictable and volatile commodities futures markets, and out of concern over possible excessive speculation in these markets, NEFI partnered with the Petroleum Marketers Association of America (or "PMAA") to form the Commodity Markets Oversight Coalition.[1] I am delivering testimony today as a spokesman for this coalition.

The Commodity Markets Oversight Coalition (or "CMOC") is an informal coalition whose participating members represent an array of business interests, including commodity producers, processors, distributors, retailers, commercial and industrial end-users, as well as groups representing average American consumers. The CMOC advocates in favor of government policies that promote stability and confidence in the commodity markets and that preserve the interests of *bona fide* hedgers, consumers and the broader economy.[2]

On July 21, 2010, President Barack Obama signed into law the Dodd-Frank Wall Street Reform and Consumer Protection Act.[3] Title VII of the Dodd-Frank Act, which was endorsed by members of the CMOC, included the most substantial new regulations of the U.S. derivatives markets in more than a decade. Members of this Committee, under the leadership of Chairman Peterson, Chairman Boswell and Ranking Members Lucas and Moran, are to be commended for their years of hard work that resulted in the passage and enactment of this monumental piece of legislation.

Obtaining the consensus necessary to assemble and retain support for Title VII of the Dodd-Frank Act was certainly no easy task. Many proposed reforms of the U.S. derivatives markets were met with great skepticism, if not outright opposition, from various special interests. Many market participants and stakeholders, from small businesses, farmers and energy end-users to massive Wall Street banks and trading houses, got involved in the debate.

Despite efforts by opponents to misrepresent or create doubt about many of the derivatives reforms in the bill, Congress included various regulatory initiatives necessary for market transparency and accountability and to prevent fraud, manipulation and excessive speculation. But rather than taking a detailed and proscriptive approach to the most controversial provisions, the Congress ceded much discretion to financial regulators such as the Commodity Futures Trading Commission (or "CFTC"). One clear example of this delegation of Congressional authority is the

[1] The Petroleum Marketers Association of America is a national federation of 47 state and regional trade associations representing over 8,000 independent petroleum marketing companies, including convenience store/gas stations, gasoline and diesel fuel retailers and suppliers, and home heating oil dealers.

[2] The coalition, when formed in August of 2007, was referred to as the "Energy Markets Oversight Coalition," but was changed to the "Commodity Markets Oversight Coalition" to reflect its members' interests in reforming derivative trading in a broad range of commodities, including agricultural and energy commodities.

[3] Pub. L. 111–203.

law's directive to CFTC to establish speculative position limits for regulated and currently unregulated markets such as over-the-counter swaps markets.[4]

The Dodd-Frank Act requires that these limits be established "in the spot month, in each other month, and in the aggregate across all months" and provides the CFTC with discretion in defining exemptions for *bona fide* hedgers. The new law requires that the CFTC establish speculative position limits for what are defined by statute as currently "exempt commodities," such as energy and metals, within 180 days of enactment, and for agricultural commodities within 270 days of enactment.[5]

We commend CFTC Commissioner Gary Gensler and his fellow Commissioners for their commitment to timely enactment and enforcement of new regulatory initiatives under this Act and for engaging stakeholders in a thoughtful and transparent rulemaking process. Tomorrow, the CFTC will hold the eighth in a series of public meetings on the implementation of the Dodd-Frank Act. Tomorrow's meeting will include discussion and review of proposed rulemakings for position limits. Despite this transparent and inclusive process, the Commission has recently come under pressure to delay the formulation and imposition of position limits by the deadline required by law. Our coalition opposes any such delay.

1. Imposition of Position Limits Is Not a New Idea

The Dodd-Frank Act does not *provide* the CFTC with the authority to establish speculative position limits; it actually *expands* existing authority under the Commodity Exchange Act of 1936. Section 4(a) of that Act required the CFTC to set limits on market positions that traders can take in any commodity in order to prevent a single market participant from controlling price movements. The goal was to prevent an "undue burden on interstate commerce" that would result from excessive speculation and, as a consequence, cause "sudden or unreasonable fluctuations or unwarranted changes in the price" of commodities.

Like the Dodd-Frank Act, the 1936 statue was enacted following a time of crisis for the economy, a catastrophic upheaval in U.S. financial markets, volatility and uncertainty in commodity futures markets and a debate over prudent regulation to remedy these problems and their causes. Farmers, arguing that speculation can indeed become excessive and manipulative, and therefore distort fundamentals and the price discovery function of futures markets, fought hard for position limits authority and won the day.

In 1936, Federal regulators acted quickly to impose position limits on agricultural markets that resulted in sixty years of relatively reliable and orderly commodities futures markets for agricultural, and eventually, energy commodities. However, in the 1990s the commodity markets began to change dramatically as a result of digitalization, globalization and the Internet. Traditional open-outcry exchanges on LaSalle Street in Chicago and Wall Street in New York found themselves in competition with new electronic and off-shore trading platforms. In an effort to remain competitive in energy commodity futures, options and swaps, many exchanges abandoned hard speculation limits in favor of softer "accountability limits."

Shortly after his confirmation as CFTC Chairman, Gary Gensler acknowledged that accountability limits have time and time again proved insufficient in preventing traders from taking large positions in violation of these limits and with relative inaction by the exchange. In fact, the CFTC found that in the 12 months between July 2008 and June 2009, individual month accountability limits were exceeded for crude oil, gasoline, heating oil and natural gas by 69 different traders. Some traders even exceeded limits every day during the trading period.[6]

There are well documented cases in which individual traders violated accountability limits and their actions had major consequences for market hedgers and consumers. This includes the $6 billion collapse of Amaranth Advisors in 2006, one of the largest hedge fund collapses in U.S. history. A Senate Permanent Subcommittee on Investigations report in June 2007 found that "Amaranth controlled 40 percent of all outstanding contracts on NYMEX for natural gas in the winter season (October 2006 through March 2007), including as much as 75 percent of the outstanding contracts to deliver natural gas in November, 2006."[7]

[4] *Ibid*, § 737.

[5] The Commodity Futures Modernization Act of 2000 (Pub. L. 106–554) created a new classification for commodities to be exempt from many trading rules under the Commodity Exchange Act, called "exempt commodities," which includes any commodity other than an excluded or agricultural commodity.

[6] Statement by CFTC Chairman Gary Gensler, Public Meeting on Establishing Position Limits, CFTC Headquarters, Washington, D.C., January 14, 2010.

[7] *Excessive Speculation in the Natural Gas Market,* Senate Permanent Subcommittee for Investigations Staff Report, June 25, 2007.

Amaranth occasionally held five or more times the "accountability limit" for natural gas, and according to the report, the NYMEX failed to take immediate action and in many instances where traders violated limits, never took any action. When the NYMEX finally ordered Amaranth to draw down its position, they simply moved their holdings onto an off-shore exchange where the CFTC and the U.S. exchanges had access to little or no data. But the size of the Amaranth position relative to the market eventually came back to haunt it, when in September, 2006 its position collapsed.

The record surge in natural gas prices at the height of the Amaranth position and the subsequent collapse demonstrated that without hard position limits one trader alone can move these markets. This event led many industries to recognize the problems associated with exempting energy commodities from position limits and catalyzed the establishment of our coalition in August of 2007. It also proved that "too big to fail" exists in the commodities derivative markets and that commodity speculation can be at times excessive. It also exposed in dramatic fashion the inadequacies of so-called "accountability limits" and lack of oversight and transparency in the commodity markets. More frightening still was evidence that a growing majority of trading was now occurring on so-called "dark markets," or markets that reported little or no data and were subject to little or no oversight and regulation.

As policy makers deliberated on appropriate reforms, the market continued to deteriorate for end-users. The following year, energy prices surged to unjustified levels. In the summer of 2008, and despite declining demand and historically high inventories, crude oil topped $147 per barrel. Consumers faced unprecedented gasoline and home heating costs. Food prices similarly surged to record levels. As food became unaffordable and aide declined, riots broke out in at least 30 food important dependent countries. Manufactures, airlines, truckers and other transporters saw fuel prices surge, which caused inflation in the cost of goods and services for every American. But like almost every speculative bubble, this one eventually burst, leaving many farmers, manufacturers and other end-users stuck with unaffordable commodity pricing contracts.

Shortly after his confirmation as CFTC Chairman last year, Gary Gensler acknowledged the need for immediate action to restore confidence and stability. The Commission began drafting proposed rules to address trading loopholes and exemptions, and to establish position limits for energy and metals. The Commission held a round of hearings in the summer of 2009 to solicit input from commodity hedgers, speculators, consumers and academics. Several members of this coalition delivered testimony before the Commission at this time.[8]

In January 2010, the CFTC proposed a rule for the establishment of speculative position limits for energy contracts, modeled largely after existing position limits that existed for agricultural commodities.[9] During the comment period ending April 26, 2010, the CFTC received an unprecedented number of submissions, well more than 8,000 in all, the vast majority of which indicated support for strong and meaningful limits on speculation. Several CMOC member groups were among those comments, and many expressed reservations at the relatively "high bar" formulæ recommended by the Commission.

Understandably, several Commissioners expressed reservations about establishing limits that could be considered too aggressive in light of the Commissions lack of authority over certain trading environments. At least two Commissioners feared in April that position limits would drive trade to "dark" over-the-counter and off-shore environments. The CFTC repeatedly called on Congress to give it authority over these markets, so that broad and uniform limits could be placed on all speculative positions and in all markets. On July 21, 2010, the agency got its wish when the Dodd-Frank Act became law.

The CFTC has enjoyed 75 years of authority to establish speculation limits in commodity markets. After nearly 2 years of debate and passage of the most sweeping reforms in the history of the U.S. derivative markets, they now have the authority to establish said limits across the board to all traders and in all markets. We see little merit to the argument that the CFTC has not sufficiently considered the imposition of such limits. We are discouraged that, despite ample evidence of excessive speculation in commodities markets that some continue to doubt, question or outright deny that speculation was ever and could ever be excessive.

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[8] Held on July 28 and 29, and August 5, 2010. (*www.cftc.gov/PressRoom/Events/Events2009/index.htm*)

[9] Notice of Proposed Rulemaking for Federal Speculative Position Limits for Referenced Energy Contracts and Associated Regulations, Commodity Futures Trading Commission, 75 FR 4143, Washington, D.C., January 26, 2010.

2. Hard Speculation Limits Will Not Disrupt Markets

Many CMOC participating groups represent vital commodity-dependent industries that have a steadfast belief in open, transparent and competitive markets. We believe that any new rules and regulations must be well reasoned, justified and not excessively burden market participants, or unnecessarily impede market liquidity. Speculators provide the market with this liquidity, but excessive speculation drives commodity prices to levels not justified by the market forces of supply and demand, results in pricing bubbles that harm commodity hedgers, end-users and the broader economy.

We also believe that the commodity derivatives markets, when they were first established more than 150 years ago, did not have as their primary constituents Wall Street speculators and investors looking to make a fast buck, nor was the CFTC established by Congress to serve such constituents to the detriment of hedgers and consumers.

Commodity exchanges were established to provide legitimate commercial businesses and end-users with a means to hedge risks associated with commodity prices. When unrestrained speculation is allowed to dominate markets and their hedging and price discovery functions, as we have clearly seen, it violates the Commodity Exchange Act's prohibitions on such activity. The CMOC rejects the contention of some in the financial services industry that limits to prohibit excessive speculation could be more disruptive to our markets more than excessive speculation itself.

Last week, the IntercontinentalExchange (ICE), the Chicago Mercantile Exchange (CME) and the New York Mercantile Exchange (NYMEX) denied that timely imposition of limits would disrupt markets. Reuters reported on December 8th that the "top U.S. futures exchanges expressed confidence that a revised plan to clamp down on commodities market speculation will not unduly burden the market" if it uses the previous (January, 2010) proposed rule as a starting point.[10] We believe the earlier proposed rule was insufficient to address "the burdens of excessive speculation" due to its very high limits. However, it is a starting point and because the CFTC now has authority to apply limits to previously exempt markets and participants, our coalition would be supportive of lower limits.

Some argue that establishing limits expeditiously in order to meet what they consider to be negotiable or arbitrary deadlines under the Dodd-Frank Act will drive market activity off-shore to trading environments that are free from such limits (as we saw earlier with the Amaranth case). This argument is a red herring, as the Dodd-Frank Act anticipates this response and establishes new registration requirements for foreign boards of trade (FBOTs) that seek to allow access from within the U.S., provided they meet a list of comparable regulatory criteria, including the imposition of speculative position limits.[11] The stated intent of the Congress was to prevent limits imposed by the CFTC to "cause price discovery in the commodity to shift to trading on the foreign board of trade."

In addition, regulators in Europe and elsewhere are currently in the process of drawing up their own plans to impose speculative position limits in addition to the many other transparency requirements and other regulatory initiatives prescribed by the Dodd-Frank Act. If the CFTC were to fail to apply aggregate position limits to implement the Dodd-Frank Act, the impetus for regulatory reform in other jurisdictions could be jeopardized. As we learn of the extraordinary measures that he Federal Reserve Bank took to provide European banks with hundreds of billions of dollars of loans on extremely favorable terms,[12] we are reminded of the high cost of relying completely on financial industry self-regulation. Weak position limits or a return to position accountability would provide industry with *de facto* self-regulation.

On November 1, 2010, our coalition submitted preliminary comments regarding the implementation of various regulatory initiatives under the Dodd-Frank Act. We announced then our opposition to any delay in the formulation and imposition of speculative position limits. We also suggested that additional stability and restraint on speculation could be achieved were the CFTC to develop limits specifically for index funds and to distinguish them as separate and distinct from more traditional speculators.[13] These so-called "passive investors" and their rolling contracts in energy and food commodities places commodities in a perpetual state of contango,

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[10] Wallace, John and Steve Orlofsky, "ICE, CME More Optimistic on CFTC Position Limits," Reuters News Service, December 8, 2010.

[11] Pub. L. 111–203, § 738 and § 737(a)(4).

[12] Harding, Robin with Tom Braithwaite and Francesco Guerrera, "Europe's banks tapped Fed," *Financial Times,* December 2, 2010.

[13] *General Comments to the CFTC on the Implementation of Title VII of the Dodd-Frank Act,* Commodity Markets Oversight Coalition, November 1, 2010, p. 6.

where out-month futures prices are perpetually higher than spot prices. Such an investment strategy ignores market fundamentals and distorts the price discovery nature of the markets. These large funds have transformed commodities markets from a means to hedge fluctuating prices into a new asset class for pure financial accumulation.

We also agree with a recent suggestion by CFTC Commissioner Bart Chilton that separate limits might also be considered for high-frequency trading (HFT) or so-called "computer algorithm-based trading" or "algo-trading" in commodity markets. Today, HFT accounts for ⅓ of all trading activity in U.S. futures markets and it is growing fast. Futures regulators and the Congress need to address this trend, especially in light of the "flash crashes" that have been witnessed in the securities markets, for which HFT has been considered at least partly responsible (including the 1000 point plunge in the Dow on May 6, 2010). Such "flash crashes" in the commodity trading markets could have devastating consequences for U.S. businesses and consumers.

3. Limits Will Restore Confidence in Commodity Markets

Establishing and imposing timely and meaningful speculative position limits as required by the Dodd-Frank Act will send a signal of confidence and stability to all market participants that end-users will again be able to rely on transparent, orderly and functional commodity markets. Continued inaction is not an option. Our coalition and the businesses and consumers we represent rely upon the CFTC to do their best to protect against fraud, manipulation and excessive speculation and to ensure a fair, transparent and accountable marketplace. Decisive action will be a strong and long overdue step in the protection of market integrity and the stability of the broader economy.

As the 111th Congress comes to a close, we commend it—and especially the Chairs and Members of the Agriculture, Banking and Financial Services Committees—for the hard work, political courage and leadership that made derivatives reform possible. Generations of Americans will be forever grateful for what you've done. But now this legislative legacy is in the hands of regulators. We trust that they will implement and enforce new authority, and that the new Congress will continue to provide them with the political support and financial resources necessary to do so.

Thank you again for the opportunity to testify. We would be pleased to answer any questions that you might have.

ATTACHMENT

Groups Supporting Testimony

ActionAid USA
Air Transport Association
California Black Farmers and Agriculturalists Association
Colorado/Wyoming Petroleum Marketers Association
Columban Center for Advocacy & Outreach
Consumer Federation of America
Consumer Watchdog
Florida Petroleum Marketers Association
Food & Water Watch
Fuel Merchants Association of New Jersey
Gasoline & Automotive Service Dealers of America Inc.
Illinois Petroleum Marketers & Convenience Store Association
Independent Connecticut Petroleum Association
Louisiana Oil Marketers & Convenience Store Association
Massachusetts Oilheat Council
Maine Energy Marketers Association
Maryknoll Office for Global Concerns
Michigan Petroleum Association/Michigan Association of Convenience Stores
Montana Petroleum Marketers & Convenience Store Association
National Association of Oilheating Service Managers
National Association of Truckstop Operators
National Farmers Union
Nebraska Petroleum Marketers & Convenience Store Association
New England Fuel Institute
New Mexico Petroleum Marketers Association
New Rules for Global Finance
New York Oil Heating Association
North Dakota Petroleum Marketers Association

Oil Heat Institute of Long Island
Oil Heat Council of New Hampshire
Oil Heat Institute of Rhode Island
The Organization for Competitive Markets
Petroleum Marketers Association of America
Petroleum Marketers & Convenience Store Association Kansas
Petroleum Marketers & Convenience Stores of Iowa
Propane Gas Association of New England
Public Citizen
R–CALF—USA
South Dakota Petroleum & Propane Marketers Association
United Egg Producers
Utah Petroleum Marketers & Retailers Association
Vermont Fuel Dealers Association
West Virginia Oil Marketers and Grocers Association
Western Peanut Growers
Western Petroleum Marketers Association

The CHAIRMAN. Thank you.
Mr. Duffy.

STATEMENT OF TERRANCE A. DUFFY, EXECUTIVE CHAIRMAN, CME GROUP INC., CHICAGO, IL

Mr. DUFFY. Chairman Boswell, Ranking Member Moran, and Members of the Subcommittee, thank you for inviting us to testify regarding the implementation of Dodd-Frank's provisions relating to position limits.

I am going to focus on the requirements of Dodd-Frank and then briefly discuss this theory that speculators are distorting futures markets.

Dodd-Frank requires the Commission to make a finding that position limits are necessary to diminish, eliminate, or prevent burdensome excessive speculation before imposing such limits. The CFTC is not permitted to act on the basis of assumptions or political demands. Core principle 5, section 5 of the CEA also demonstrates that position limits are not required in every case since it permits exchanges to adopt accountability levels as an alternative to rigid position limits.

Dodd-Frank also requires that CFTC wait to impose limits on futures exchanges until it can simultaneously impose limits on economically equivalent swaps. The purpose of this provision is to prevent a flight of trading from regulated exchanges with no limits to unregulated markets with limits.

Given these requirements, it is clear that the CFTC lacks sufficient data to impose limits on swaps and therefore may not act against futures. The Commodity Exchange Act allows limits to be imposed only on excessive speculation, not speculation generally. This is a clear recognition that futures markets cannot operate without the participation of speculators.

Arbitrary position limits distort markets, increase cost to hedgers, and increase cost to consumers. Position limits are unnecessary unless burdensome excessive speculation is present or is likely.

Academic literature and all the studies produced by the CFTC's economists demonstrate that position limits in futures trading are not the means to deal with real supply-demand issues.

It is my firm belief that efforts to focus on position limits rather than the underlying issues are certain to divert attention from the real problems and do more harm than good. Worse yet, position limits in derivatives markets that preclude investors from seeking economic exposure to particular asset classes drive those investors to speculate in physical commodities. This, in turn, has a significant and often detrimental impact on the flow of commodities in commercial channels.

We have already seen the beginnings of such distortions in the metals and energy markets in anticipation of the imposition of limits on derivatives. This is not a development that any of us should favor but one that is an unfortunate result of position limits based on bad economics.

CME Group is not opposed to position limits and other similar measures if used correctly. For example, we employ limits on most of our physically delivered contracts. However, we use limits and accountability levels, as permitted by the Core Principles, to mitigate potential congestion during delivery periods and to help us respond in advance to any effort to manipulate our markets.

CME Group believes that the core purpose that should govern Federal and exchange-set position limits, to the extent such limits are necessary and appropriate, should be to reduce the threat of price manipulation and other disruptions to the integrity of prices. Such activity destroys public confidence in the integrity of our markets and harms the acknowledged public interest in legitimate price discovery.

CME Group appreciates the opportunity to offer the foregoing comments regarding the implementation of Dodd-Frank provisions for position limits on certain contracts involving exempt and agricultural commodities. We hope that the views expressed today are helpful, and we look forward to answering any questions the Committee will have.

[The prepared statement of Mr. Duffy follows:]

PREPARED STATEMENT OF TERRANCE A. DUFFY, EXECUTIVE CHAIRMAN, CME GROUP INC., CHICAGO, IL

I am Terrence A. Duffy, executive Chairman of CME Group Inc. Thank you, Chairman Boswell, and Ranking Member Moran for inviting us to testify today. You asked us to discuss the implementation of provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act relating to position limits.

CME Group is the world's largest and most diverse derivatives marketplace. We are the parent of four separate regulated exchanges, including Chicago Mercantile Exchange Inc. ("CME"), the Board of Trade of the City of Chicago, Inc. ("CBOT"), the New York Mercantile Exchange, Inc. ("NYMEX") and the Commodity Exchange, Inc. ("COMEX") (collectively, the "CME Group Exchanges"). The CME Group Exchanges offer the widest range of benchmark products available across all major asset classes, including futures and options on futures based on interest rates, equity indexes, foreign exchange, energy, metals, agricultural commodities, and alternative investment products.

CME Clearing, a division of CME, is one of the largest central counterparty clearing services in the world, which provides clearing and settlement services for exchange-traded contracts, as well as for over-the-counter derivatives contracts through CME ClearPort®. Using the CME ClearPort® service, eligible participants can execute an OTC swap transaction, which is transformed into a futures or options contract that is subject to the full range of Commodity Futures Trading Commission (the "Commission" or "CFTC") and exchange-based regulation and reporting. The CME ClearPort® service mitigates counterparty credit risks, provides transparency to OTC transactions and enables the use of the exchange's market surveillance monitoring tools.

The CME Group Exchanges serve the hedging, risk management and trading needs of our global customer base by facilitating transactions through the CME

Globex® electronic trading platform, our open outcry trading facilities in New York and Chicago, as well as through privately negotiated CME ClearPort® transactions.

The theory that speculators in futures markets cause unwarranted price volatility and excessively high and/or low prices is not new; Congress has dealt with that notion since the late 1800s. The Commodity Exchange Act ("CEA"), however, does not limit speculation, but only "excessive speculation." This is an implicit recognition that futures markets cannot operate without the participation of speculators.

The so-called "speculators," such as index funds and swap dealers, who are the focus of recent intense criticism, are not engaged in traditional speculative activity, *i.e.,* trying to beat the market. Rather, swap dealers use futures markets to facilitate the hedging of more complex and specific risks accepted in connection with swap transactions with commercial customers and others. Denying or limiting their access to the futures markets will simply impede hedging activity by commercial market participants. Index funds aggregate the buying and selling decisions of many thousands of investors, most of whom are doing what they have been taught for decades to do: diversifying their investment portfolios and hedging inflation risks to their investment returns in order to maximize their retirement savings and their individual wealth.

Position limits are not a costless palliative. Position limits, when improperly calibrated and administered, can easily distort markets, increase the costs to hedgers and effectively increase costs to consumers. Unfortunately, many demands for speculative limitations assume that severe limits on speculation will bring prices to some favored level. On the contrary, position limits on futures contracts will not and do not control cash market prices. There is a complete disconnect between the implied promise to drive prices down or up, whichever the most vocal constituency desires, and the ability of position limits to deliver on that promise.

Introduction

We disagree with those who contend, in contravention of the clear academic evidence and of the clear intent of Congress, as expressed in Dodd-Frank Wall Street Reform and Consumer Protection Act (P.L. 111–203, July 21,2010) ("DFA" or "Dodd-Frank"), that speculative positions must be limited in order to eliminate price volatility and/or high prices or low prices for essential commodities.

Some of the proponents for limits are well intentioned, but have no credible evidence to support their claims. Some contend for example that strict limits on silver futures will allow the price of silver to go up to levels that they think is appropriate. Other proponents of strict position limits contend that limits on oil positions will cause the price of gasoline to fall to levels that are "better" for the economy or their constituents. The *Wall Street Journal* reported on December 8, 2010, that:

> "[T]he latest data also show an increase in speculation doesn't necessarily bring with it an increase in prices. Natural gas, for example, is down 21% this year despite a surge in speculative bets. In opposite circumstances with sugar, prices rallied despite a withdrawal of speculative bets." The WALL STREET JOURNAL—*Investors Pile Into Commodities,* Carolyn Cui and Susan Pulliam.

All of the serious academic literature, including all of the studies produced by the CFTC's economists demonstrate that position limits in futures trading are not the means to deal with real supply and demand issues that are prevalent in markets for many physical commodities. It is my firm belief that efforts to focus on position limits rather than the underlying economic issues are certain to divert attention from the real supply and demand dynamics and do more harm than good. Worse yet, position limits in derivative markets that preclude investors from seeking economic exposure to particular asset classes drives those investors to speculate in physical commodities, which has a significant and often detrimental impact on the flow of commodities in commercial channels. We have already seen the beginnings of such distortions in metals and energy markets in anticipation of the imposition of limits on derivatives. This is not a development that anyone should favor, but one that is the logical result of even the threat of position limits based on bad economics.

CME group is not opposed to position limits and other similar measures in all circumstances; we employ limits in most of our physically delivered contracts. However, we use limits and accountability levels, as contemplated by the Congressionally-approved Core Principles for Designated Contract Markets, to mitigate potential congestion during delivery periods and to help us identify and respond in advance to any threat to manipulate our markets. CME Group believes that the core purpose that should govern Federal and exchange-set position limits, to the extent such limits are necessary and appropriate, should be to reduce the threat of price manipulation and other disruptions to the integrity of prices. Such activity destroys public confidence in the integrity of our markets and harms the acknowledged public interest in legitimate price discovery.

CME Group is therefore vigilant in seeking to deter and prevent price manipulation or other illegitimate distortions of market prices. Speculation, however, is not manipulation, nor is it an abusive practice. As CME Group observed in its response to the Commission's January 2010 energy position limits proposal, speculation is essential to the orderly functioning of futures markets—it provides market liquidity which promotes more effective commodity price discovery and allows for the efficient transfer of price risk. See CME Group Comments, 10–002 Comment CL–02714, at 2 (Apr. 26, 2010) ("CME Comments"). The Commission's responsibility and challenge is not to restrict speculation per se, but to act when necessary to prevent "excessive speculation" from burdening interstate commerce through what the Commodity Exchange Act ("CEA") calls "unreasonable" and "unwarranted" fluctuations in the price of a commodity. To this end, Congress has granted to the Commission the authority to impose speculative position limits under Section 4a of the CEA, as amended by DFA.

CME Group understands the extensive demands being made on the Commission's limited resources. However, the Commission must gather critical data regarding swap markets and individual traders' swap positions. Without a thorough understanding of such data, the Commission runs the risk of inappropriately setting position limits. CME Group appreciates the great challenge this presents to the Commission.

I. Statutorily Required Basis for Imposing Position Limits

Section 4a(a)(1) provides in pertinent part:

> "For the purpose of diminishing, eliminating, or preventing such burden [of unwarranted or unreasonable price fluctuations resulting from excessive speculation], the Commission shall . . . fix such limits on the amount of trading which may be done or positions which may be held . . . as the Commission finds are necessary to diminish, eliminate, or prevent such burden." (emphasis added)

By its terms, DFA requires the Commission to make a finding that position limits "are necessary to diminish, eliminate, or prevent" burdensome excessive speculation before imposing such limits. Dan Berkovitz, CFTC General Counsel, confirmed that Section 4a(a)(1) sets forth a conditional mandate during the CFTC's July 2009 hearings on energy position limits. In response to Chairman Gensler's question, "What does the word 'shall' mean in 4a?," Berkovitz replied, "If the Commission finds that position limits are necessary to prevent, diminish, or eliminate such burdens, then there is a directive that it shall establish position limits." Transcript of July 28, 2009 CFTC Hearing on Energy Position Limits at 35–36 (emphasis added). The above quoted language from Section 4a(a)(1) was not deleted or in any way altered by DFA. New CEA subsection (a)(2) ("Establishment of Limitations") even reaffirms that any position limits must be established "[i]n accordance with the standards set forth in paragraph 1 of this subsection," which include the requisite "necessary" finding. Core Principle 5, Section 5(d)(2)(5) of the CEA as amended by DFA, also recognizes that "accountability levels" are an alternative to rigid position limits:

> (5) POSITION LIMITATIONS OR ACCOUNTABILITY.—
>
> > (A) IN GENERAL.—To reduce the potential threat of market manipulation or congestion (especially during trading in the delivery month), the board of trade shall adopt for each contract of the board of trade, as is necessary and appropriate, position limitations ***or*** position accountability for speculators. (emphasis supplied)

Moreover, the Commission must publish the statutorily required finding and the information in support thereof in any notice of proposed rulemaking to comply with the Administrative Procedure Act ("APA"). The APA requires that the notice of a proposed rule include "sufficient detail on its content and basis in law and evidence to allow for meaningful and informed comment." See, *e.g., Am. Med. Ass'n* v. *Reno,* 57 F.3d 1129, 1132 (D.C. Cir. 1995). Absent a finding with supporting evidence that position limits are "necessary," this APA requirement cannot be met because the public will not know the Commission's specific reasoning for the essential finding that triggers its proposed rulemaking.

DFA indicates that such limits would be "unnecessary" where burdensome excessive speculation does not exist or is unlikely to occur in the future. CME Group's comment letter on the Commission's energy position limits proposal discussed at length the absence of any credible empirical evidence of the existence of burdensome excessive speculation or its likely future occurrence. See CME Comments at 17–24. The weight of empirically sound analysis and research demonstrates that movements in commodity prices are attributable to fundamental market conditions rather than speculative trading. CFTC studies, for example, have found that supply and demand factors were largely responsible for the 2008 rise in oil prices and that, far from harming the market, speculators serve as an important source of liquidity for other participants. See, *e.g., CFTC Interagency Task Force on Commodity Markets, Interim Report on Crude Oil* at 3–4 (July 22, 2008); Michael Haigh *et al., Market Growth, Trader Participation and Pricing in Energy Futures Markets* (Feb. 7, 2007), available at *http://web.uvic.ca/econ/research/seminars/robe.pdf.* Like CFTC staff, the Government Accountability Office ("GAO") has not identified a causal relationship between speculation in the futures market and changes in commodity prices. See GAO, GAO–09–285R, *Issues Involving the Use of the Futures Markets to Invest in Commodity Indexes* at 5 (Jan. 30, 2009). The conclusions of these governmental studies and reports are consistent with those of academic and private sector economists. See, *e.g.,* Paul Krugman, *The Oil Nonbubble,* N.Y. TIMES, May 12, 2008, *http://www.nytimes.com/2008/05/12/opinion/12krugman.html* ("[T]he rise in oil prices isn't the result of runaway speculation; it's the result of . . . the growing difficulty of finding oil and the rapid growth of emerging economies like China.").

To the extent there are any legitimate concerns with the potential for excessive speculation to cause unwarranted or unreasonable price fluctuations, CME Group believes that futures exchanges effectively address such concerns through their existing market surveillance programs. CME Group provided a detailed account of the futures exchanges' capabilities in its April 26, 2010 comments filed with the CFTC. See CME Comments at 8–12. Briefly stated, the exchanges independently have the ability to establish position limits as warranted by the characteristics of their traded contracts, and to employ position accountability provisions as appropriate given particular market constructs and market conditions. This flexible regulation is a much more appropriate and effective means of addressing potentially manipulative or disruptive positions than are blunt position limits that fail to account for variability in specific contract months, market conditions, and market participation. Insofar as the existing exchange programs are and have been proven to be effective, CME Group believes the Commission would lack the statutory basis for establishing new Federal position limits on certain contracts involving exempt and agricultural commodities.

II. Mechanics of Imposing Position Limits

Assuming the Commission is able to find that position limits "are necessary to diminish, eliminate, or prevent" burdensome excessive speculation, CME Group offers the following views on how to impose those limits:

A. The Imposition of Limits Should be Deferred Until the Commission Can Properly Determine and Ensure Compliance with Appropriate Limits

Dodd-Frank sets forth several seemingly inconsistent timing requirements for the exercise of the Commission's position limit authority. New CEA § 4a(a)(2)(B) directs the Commission to impose limits for certain contracts, within 180 days for exempt commodities and within 270 days for agricultural commodities, respectively, of Dodd-Frank's enactment. Meanwhile, new CEA § 4a(5)(A) requires that limits for swaps that are economically equivalent to futures and options be established simultaneously with the limits under Section 4a(a)(2)(B). The statute, however, also vests the Commission with discretion to establish limits "as appropriate," thereby indicating that the Commission is not bound by the aforementioned dates. CME Group believes that DFA requires the Commission to defer imposing limits until doing so would be "appropriate"—that is, when it has the data needed to accurately set and enforce those limits and when it is in a position to impose limits simultaneously on futures (and options on futures) and swaps.

B. Position Limits Should Be Set with Due Regard for Legislative Objectives and Considerations

Under Dodd-Frank, the Commission is required to take into account several factors when setting position limits. New CEA § 4a(a)(3) provides that, to the maximum extent practicable, the Commission should use its discretion to establish limits to: (i) diminish, eliminate, or prevent "excessive speculation"; (ii) deter and prevent market manipulation, squeezes, and corners; (iii) ensure sufficient market liquidity for *bona fide* hedgers; and (iv) ensure that the price discovery function of the underlying market is not disrupted. Additionally, new CEA § 4a(a)(2)(C) states that the Commission must act to avoid shifting the price discovery function to FBOTs in establishing limits. In mandating these considerations, Congress recognized that limiting trading positions has the potential to reduce liquidity and adversely affect the hedging and price discovery functions of U.S. commodity markets. The Commission is obliged to give due weight to each consideration in setting any position limits and may not focus solely on imposing limits to diminish, eliminate, or prevent "excessive speculation."

C. The Commission's Exemptive Authority Should Be Interpreted Broadly To Accommodate All Non-Speculative Positions

New CEA § 4a(a)(7) gives the Commission authority to exempt from any position limit rule, with or without conditions, "any person or class of persons, any swap or class of swaps, any contract of sale for future delivery or class of such contracts, any option or class of options, or any transaction or class of transactions." Under this provision, the Commission's statutory power to exempt any person or class of person from position limits is greater than it has ever been before.

CME Group believes that DFA authorizes the Commission to use its broad new exemption authority under § 4a(a)(7) to grant exemptions to market participants who use futures, options, or swaps when economically appropriate to the reduction of the risks they face in their enterprises. Although it is impossible to enumerate the breadth of exemptions that should be permitted in order to ensure that entities are able to effectively manage exposure that is highly correlated to fluctuations in the price of exempt and agricultural commodities, an application for exemption should be judged on its merits in terms of the specific risks to be hedged, the relevant price relationships, the proposed position sizes, and the operational procedures for establishing and lifting the hedge.

If the Commission were to narrowly construe its § 4a(a)(7) exemptive authority to exclude non-speculative trading activity, then market participants could be forced to either actually speculate on those price risks (*i.e.,* not establish any positions to mitigate the risk), and potentially increase costs to consumers, or hedge their risks through transactions that lie outside the CFTC's position limit authority. Either strategy would undermine the Commission's mission to promote liquidity and protect the price discovery function of its regulated markets. The Commission should thus broadly interpret its exemptive powers and grant exemptions to market participants who are not seeking to establish positions in the futures market for speculative purposes but rather to serve their legitimate commercial and financial hedging needs.

III. Conclusion

CME Group appreciates the opportunity to offer the foregoing comments respecting the implementation of DFA's provisions respecting position limits on certain contracts involving exempt and agricultural commodities. We hope that the views expressed herein prove to be helpful and we are available to answer any questions the Committee may have.

The CHAIRMAN. Thank you.

Mr. Newman.

STATEMENT OF JOEL G. NEWMAN, PRESIDENT AND CEO, AMERICAN FEED INDUSTRY ASSOCIATION, ARLINGTON, VA

Mr. NEWMAN. Chairman Boswell, Ranking Member Moran, and Members, thank you for the opportunity to testify before you today.

The American Feed Industry Association is the largest organization devoted exclusively to represent the business, legislative, and regulatory interests of the U.S. animal feed industry and its suppliers. AFIA applauds this Subcommittee, its Members, and the full Committee for calling today's hearing.

AFIA members manufacture more than 70 percent of the animal feed in the United States, which amounts to over 160 million tons annually. Feed also represents roughly 70 percent of the cost of producing meat, milk, and eggs. With the majority of our industry input supplies priced directly on, or in reference to, regulated commodity markets, we depend significantly on an efficient and well-functioning futures market for both price discovery and also risk management.

Agricultural commodity markets were established to provide an efficient price discovery mechanism and a hedging risk management tool for producers and end-users. While this system encourages and requires speculative participants to provide liquidity, the significant increase of financial investors, as well as the special exemptions from speculative position limits that have been granted over time to Wall Street banks and others who are not end-users, has distorted the function of these markets.

The agriculture commodity markets functioned effectively for over 60 years after the 1936 Commodity Exchange Act first implemented speculative position limits. However, this changed in 2000 when Congress codified earlier CFTC regulatory actions granting Wall Street banks and other financial institutions an exemption from speculative position limits for hedging over-the-counter swaps and index transactions. While there are several factors that have led to increased volatility and price swings in agricultural commodities, excess speculation by index funds is certainly one of these factors.

As you are aware, the size and influence of these large financial players was never contemplated during the development of the original Commodity Exchange Act. Most of the index speculators tend to hold their positions rather than sell. This allows them to create artificial demands through their long-only positions and in essence really are bets on higher prices.

The magnitude of this scenario is clear in the numbers. In 2003, index speculator investment in 25 physical commodities was $13 billion. In 2008, these investments jumped to $260 billion, an 1,800 percent increase in 5 years. In 2010, these investments remain at $265 billion, with three index funds representing 94 percent of that amount and one fund representing 52 percent of those investments.

Earlier this year, we applauded the work by Congress to include provisions in the Act that would authorize CFTC to set reportable position limits on commodity contracts, as well as for aggregate and exchange-specific position limits.

Within this process, AFIA members support the following items: First, speculative position limits that enhance market performance and the appropriate narrowing of cash and futures market values as they near contract delivery period; the retention and equal application of the existing speculative position limits for agricultural commodities; retaining the current *bona fide* hedge definition which is in place; the removal of speculative position limit exemptions for financial institutions and other nontraditional participants in agricultural commodity markets.

While CFTC now has this authority, without removing these exemptions the speculative position limits will have a much more limited effect when they are put in place.

Given the strong relationship between crude oil and corn futures markets brought on by the dramatic and rapid expansion of the ethanol industry, establishing and enforcing energy speculative position limits is also important to secure the reliability of the entire agricultural commodity complex.

We support effective speculative position limits that work for both the *bona fide* hedger and the speculator. However, there is rarely a perfect solution to complex issues and waiting for a perfect solution before setting speculative position limits or taking other actions will only delay that much-needed transparency and controls required in these commodity markets. Therefore, we support implementation of interim limits where data is available and which can also be adjusted by CFTC with further data to confirm and support those changes.

I would be remiss if I didn't express AFIA's appreciation to Chairman Gensler, Commissioner Chilton, and the other CFTC Commissioners for their extensive outreach during this entire process.

Thank you for inviting me to participate in today's hearing. AFIA and its members stand ready to assist you in these efforts. I look forward to any questions.

[The prepared statement of Mr. Newman follows:]

PREPARED STATEMENT OF JOEL G. NEWMAN, PRESIDENT AND CEO, AMERICAN FEED INDUSTRY ASSOCIATION, ARLINGTON, VA

Chairman Boswell, Ranking Member Moran and Members, thank you for the opportunity to testify before General Farm Commodities and Risk Management Subcommittee as you review implementation of provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 relating to speculation limits.

I am Joel Newman, President and Chief Executive Officer of the American Feed Industry Association (AFIA), based in Arlington, Virginia. AFIA is the world's largest organization devoted exclusively to representing the business, legislative and regulatory interests of the U.S. animal feed industry and its suppliers.

Founded in 1909, AFIA is also the recognized leader on international industry developments with more than 500 domestic and international members, as well as nearly 40 state, regional and national association members. Our members are livestock feed and pet food manufacturers, integrators, pharmaceutical companies, ingredient suppliers, equipment manufacturers and companies that provide support services to the industry.

AFIA members manufacture more than 70% of the animal feed in the U.S., which amounts to over 160 million tons annually. Because feed represents roughly 70% of the cost of producing meat, milk and eggs, AFIA members are major contributors to food safety, nutrition and the environment, playing a critical role in the production of healthy, wholesome meat, poultry, milk, fish, eggs and pets.

AFIA is a member of the Commodity Markets Oversight Coalition, which was formed in 2007, and is a broad coalition of organizations committed to protecting the interests of *bona fide* hedgers and derivatives end-users. We thank the Subcommittee for including Jim Collura in this hearing to speak on behalf of CMOC. His leadership has been invaluable to the Coalition.

Your review of implementation of the Dodd-Frank Act by the Commodity Futures Trading Commission (CFTC) is both timely and appreciated by the men and women of the feed industry. As I have stated, feed represents approximately 70% of the on-farm cost of raising livestock and poultry. With the majority of our industry's input supplies priced directly on or in reference to regulated commodity markets, we depend significantly on an efficient and well-functioning futures market for both price discovery and risk management.

Agriculture commodity markets were established to provide an efficient price discovery mechanism and a hedging/risk management tool for producers and end-users. While this system encourages and requires speculative participants to provide liquidity, the significant increase of financial investors, permitted by special exemption from speculative position limits, has distorted the function of these markets.

Speculators are an important part of the commodity markets—without them there is no market. The agriculture commodity markets functioned effectively for 64 years after the 1936 Commodity Exchange Act first implemented speculative position limits. With these limits in place, the process of physical commodity customers using the futures markets as a price discovery and risk mitigation tool were able to rely on traditional speculator participation to provide a clear buyer/seller relationship and market liquidity.

However, this changed in 2000, when Congress codified earlier CFTC regulatory actions granting Wall Street banks an exemption from speculative position limits for hedging over-the-counter swaps and index transactions. While there are several factors that have lead to increased volatility and price swings of agriculture commodities, excessive speculation by index funds is certainly one of these factors. As CFTC has recognized, speculator participation in these markets without position limits does have an impact on prices.

These banks, which represent institutional investors, used the guise of "hedging" their invested capital to take advantage of the exemption. But in fact, their initial investments were speculative and were not hedging future needs or commitments for the underlying commodities. AFIA strongly supported ending this exemption, and we were very pleased when Congress took steps to address our concerns.

Over the past few years, as the volatility and instability in the stock and financial markets exploded, speculative activity in the agricultural commodity futures markets grew substantially. In some crop contracts, there were times when the daily speculator trading volume was nearly equal to, or in the case of wheat, was more than the entire U.S. annual production volume of these same crops. This not only added to extreme price volatility as *bona fide* hedgers scrambled to mitigate their risks, but in many cases it pushed end-users out of the market. In at least one situation, this speculator activity pushed an organization into bankruptcy when the impact of margin calls caused by the extreme price run-ups drained the company's liquidity to unsustainable levels.

As you are aware, from the Committee's analysis, when considering reforms for the futures markets and products, the size and influence of these very large financial players was never contemplated during development of the original Commodity Exchange Act (CEA). The recent dramatic increases in nearly all physical commodities values actually increased speculator demand, with the net result of commodity prices reaching unrealistic levels relative to true demand. Most of the index speculators tended to hold their positions rather than sell, which exacerbated the situation by producing artificially high demand accompanied by higher prices that negatively impacted nearly all end-users of the physical commodities.

The magnitude of this scenario is clear in the numbers: In 2003, index speculator investment in 25 physical commodities was $13 billion; in 2008, these investments jumped to $260 billion—an 1,800% increase. In 2010, these investments remain at $180 billion, with three index funds representing 92% of these investments and one fund representing 61% of these investments. (*Illustration 2*)

As a result, the feed industry was forced to pay higher prices for grains and other inputs, which were passed along to livestock, dairy and poultry producers and feed costs soared. Farmers, although receiving substantially higher prices for their commodities, were also hit by soaring costs for fertilizer and fuel, as similar speculator activities artificially further drove up oil prices.

Simply put, agriculture, from farm to retail, had to deal with extreme price volatility on a number of fronts without the effective support of our primary risk mitigation tool—the futures markets—because those markets were severely compromised by Wall Street banks ability to avoid speculative position limits and invest substantial levels of monies in the physical commodity markets. This not only allowed them to avoid the volatility of the dust storm on Wall Street, it provided them a significant return on those speculative "hedges" because of their ability to influence the escalation of market prices by creating artificial demand.

Earlier this year, we applauded the work by Congress to include provisions in the Act that would authorize the CFTC to set position limits on commodity contracts, as well as for aggregate and exchange specific position limits. Also, when commenting on CFTC's proposed position limits for energy contracts in March of this year, AFIA encouraged the Commission to consider such actions for other hard commodities to similarly protect agricultural commodities from the very large financial speculators that were masquerading as hedgers, parking their resources in physical commodity markets to ride out the extreme volatility then present in the stock and financial markets.

By including clear authority for the CFTC to set a variety of reportable position limits, Congress took a solid and welcomed step toward our mutual goal of ensuring these commodity markets and products effectively serve their primary role of providing *bona fide* commercial hedgers reliable tools to manage their economic risks.

With the expanded authority in place relative to speculation limits, AFIA is anxiously waiting for the CFTC to finalize its regulations and to put speculative limits into effect. We know this will take time and are hopeful the combination of the various categories of speculation position limits, combined with full implementation of the Act's other provisions, such as enhanced transparency and expanded regulation of nearly all derivatives, will assure *bona fide* hedgers of the viability of their futures-based risk management strategies.

I would be remiss if I did not extend AFIA's appreciation to Chairman Gary Gensler and his fellow CFTC Commissioners for their openness and diligence in addressing our concerns, particularly during the time Congress was developing its package of reforms. Through frequent meetings, they provided frank and candid overviews of their established authorities. When Congress was deliberating its reform legislation, the CFTC team also provided regular updates on progress toward the reform goals we and others were supporting. Just as important, they helped us understand how certain provisions in the Act addressed our concerns while approaching them in a different manner than we had proposed. Importantly, the CFTC has been aggressive in its outreach over the past few months as it works to implement the Act.

Like most supporters of reform in the futures industry, particularly as it relates to the topic of this hearing, AFIA would very much like to have speculation position limits set and in place today, as well the additional regulatory and transparency provisions. But we need the CFTC to ensure that when it sets limits, they also are ready to monitor and report trading activity, and ready to ensure compliance with and enforcement of the new law. It is critical for all *bona fide* end-users to know we are on a level playing field with speculators and each other.

Modern production agriculture is complex. The linkages between producers, end-users and uses of physical commodities are constantly evolving. The feed industry, for example, is still adjusting to the dramatic and rapid expansion of ethanol and other bioenergy industries. The intersection of corn, soybeans and other oilseeds for feed, food and energy—not mention other industrial uses for these crops—is our new reality, one that poses additional competition and risk management challenges for each of our respective industry sectors. This has also had the effect of linking corn futures to crude oil futures, adding further volatility to the entire commodity complex.

We are confident the CFTC is prudently moving as efficiently as it can to implement the speculative limits and other provisions of the Dodd-Frank Act under its existing and new authorities while making sure it clearly and fully understands the complexities of the derivatives markets. While being patient with the rulemaking process does produce certain levels of stress, we remain confident in and appreciative of the CFTC's efforts to date, and hope to remain so.

This brings me back to the beginning of my testimony. AFIA again applauds the Subcommittee, its Members and the full Committee for calling today's hearing to check in on the CFTC's progress on speculation limits. Your individual and collective interest in making sure progress toward implementation is both steady and correct does a great deal to reduce stress levels among AFIA's members.

I urge you to consider additional hearings on the Commission's progress toward implementing all provisions of the Act. Thank you for inviting me to participate in today's hearing. AFIA and its members stand ready to assist you in these efforts. I look forward to answering any questions you may have.

ATTACHMENT

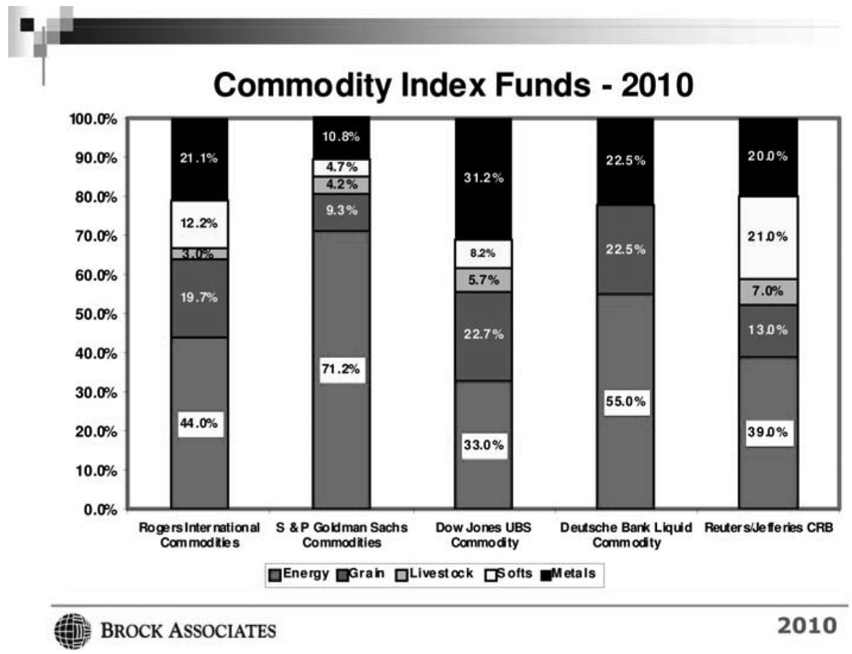

Illustration 1

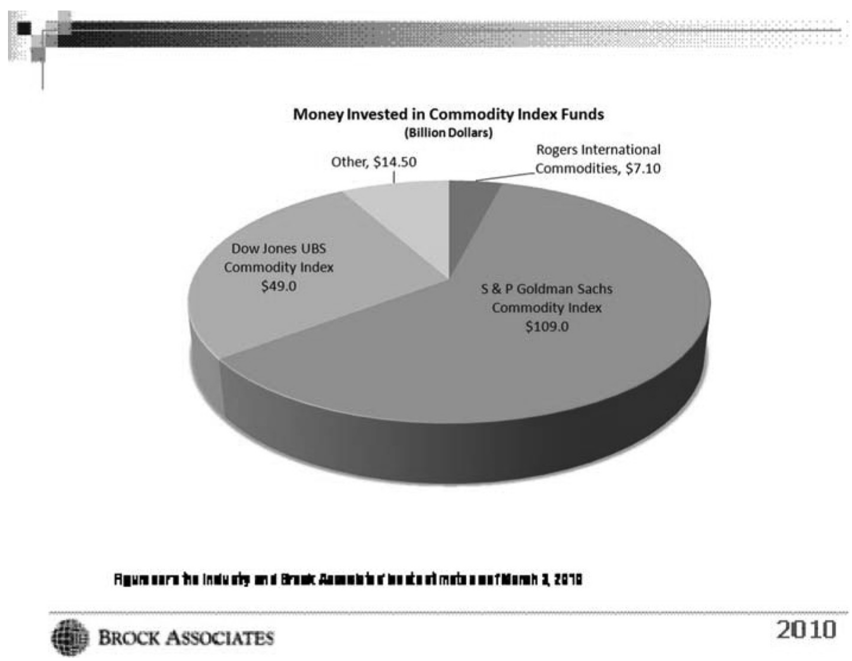

Illustration 2

Mr. MARSHALL [presiding.] Thank you, Mr. Newman.

Mr. Sprecher.

STATEMENT OF JEFFREY C. SPRECHER, CHAIRMAN AND CEO, INTERCONTINENTALEXCHANGE, INC., ATLANTA, GA

Mr. SPRECHER. Thank you, Chairman Boswell, Chairman Peterson, Ranking Member Moran.

I am Jeff Sprecher. I am the Chairman and Chief Executive Officer of IntercontinentalExchange, which is known in our industry as ICE; and I am grateful for the opportunity to provide comments on the position limit rulemaking that is pending before the Commodity Futures Trading Commission.

ICE has supported setting aggregate position limits across trading venues if administered in a fair and nondiscriminatory manner.

In summary, ICE's position on this subject has been very clear. We believe that the CFTC should set aggregate position limits in economically equivalent markets; to avoid negatively impacting liquidity that is relied upon by commercial end-users to hedge their risk, aggregate position limits should be set at levels taking into account the volumes of both the existing futures markets and the broader over-the-counter markets; and financially and physically settled contracts should be treated differently at their expiration in a revised position limit regime.

There have been exhaustive hearings by Congress and the Commission over the last several years, and they have concluded that economically equivalent contracts traded on separate exchanges operate as an aggregate market. Therefore, ICE agrees with Congress and believes that the Commission is the appropriate neutral authority to set and administer aggregate position limits for U.S. energy futures and for significant price discovery contracts. Only the Commission is in a position to view a market participant's positions across all venues and to administer aggregate position limits in an objective manner.

However, we also believe that the position limit rulemaking should focus on implementing the core requirements of Dodd-Frank, and that is namely setting aggregate position limits across markets, and they should avoid the consideration of experimental rules, such as rules that would set concentration limits for each and every exchange and every swap execution facility.

In setting aggregate limits, the Commission should take into account trading data from both futures markets and the broader over-the-counter swaps market. Failing to take into account accurate data from each of these markets risks setting aggregate position limits at levels that could negatively impact liquidity that is actually relied upon by the commercial users to effectively hedge their price risk. This would certainly be an unintended consequence, and it would be inconsistent with the goals of Dodd-Frank.

Finally, in setting position limits in the expiration or the spot month, the Commission should treat financially and physically settled contracts differently as market participants use financial and physical contracts differently for different purposes. The Commission already recognizes there is a distinction between financial and physically settled contracts. These rules promote contract convergence and they eliminate the need for significant numbers of hedge exemptions that exist in the energy futures markets today.

In conclusion, we are a strong proponent of open, competitive derivatives markets and of appropriate regulatory oversight; and, to that end, we are pleased to work with Congress to find solutions that promote the best marketplaces possible.

Mr. Chairman, I would like to thank you for the opportunity to share our views with you here today.

[The prepared statement of Mr. Sprecher follows:]

PREPARED STATEMENT OF JEFFREY C. SPRECHER, CHAIRMAN AND CEO, INTERCONTINENTALEXCHANGE, INC., ATLANTA, GA

Introduction

Chairman Boswell, Ranking Member Moran, I am Jeffrey C. Sprecher, Chairman and Chief Executive Officer of IntercontinentalExchange, Inc., or "ICE." We are grateful for the opportunity to provide comments on the position limit rulemaking pending before the Commodity Futures Trading Commission (Commission).

As background, ICE was established in 2000 as an over-the-counter (OTC) marketplace with the goal of providing transparency and a level playing field for the previously opaque, fragmented energy market. Since that time, ICE has grown significantly through organic growth fostered by product, technology and clearing innovation, and by acquisition of futures exchanges that have broadened its product offerings and risk management services. Today, ICE operates a leading global marketplace for futures and OTC derivatives across a variety of product classes, including agricultural and energy commodities, foreign exchange and equity indexes. Commercial market participants rely on our products to hedge and manage risk and investors in these markets provide necessary liquidity.

ICE believes proper regulation is essential for ensuring that market participants—as well as the broader public—have confidence in the price formation process that takes place in our markets. This assurance of integrity lies at the heart of the futures exchange model. The U.S. energy futures markets, governed by the Commission's comprehensive-but-flexible regulatory structure, have permitted commercial and professional market users to hedge future price risk in an efficient and cost-effective manner.

Position Limits

The Dodd-Frank Wall Street Reform and Consumer Protection Act gives the Commission new authority to set aggregate position limits on both energy futures and swaps and to have those position limits apply across competing exchanges and trading venues. This authority was granted by Congress because economically equivalent contracts may vary only where they are listed for trading, or in how they are settled, and have repeatedly been shown to trade as ***a single market*** up until the final days of trading.[1]

ICE supports aggregate position limits across trading venues if administered by the Commission in a fair, non-discriminatory manner. In summary, ICE's position on this subject is clear:

(1) Different sized position limits for different exchanges, or so-called "concentration limits", were considered and rejected by Congress, and should not form a part of the Commission's proposed rules because they are conceptually inconsistent with the "single market" theory and anti-competitively favor larger exchanges; and

(2) To avoid negatively impacting liquidity that is relied upon by commercial end-users to hedge their risk, aggregate position limits should be set at levels taking into account both existing futures volumes and the broader OTC markets.

The Dodd-Frank Act gives the Commission 180 days to implement the position limit provisions for energy. ICE believes that the position limit rulemaking would be easier and less costly to implement if the Commission focused its rulemaking on implementing the core requirements of Dodd-Frank, namely aggregate position lim-

[1] *Excessive Speculation in the Natural Gas Markets,* Staff Report, Senate Permanent Subcommittee on Investigations (June 2007), pgs. 36–38. *http://hsgac.senate.gov/public/_files/REPORTExcessiveSpeculationintheNaturalGasMarket.pdf.*

its across markets—and avoids consideration of experimental rules and such as single-exchange concentration limits that have already been rejected by Congress.

Concentration Limits for Single Exchanges Were Rejected by Congress and Are Redundant and Anti-Competitive

In the Commission's previous position limit rulemaking, which was withdrawn in anticipation of the passage of Dodd-Frank, the Commission proposed an aggregate position limit regime across markets, but with separate "concentration limits" for individual exchanges and trading venues. The concentration limit would be set at 30% of the given exchange or venue's open interest for all months, and 20% of open interest in any single month, with each percentage based on the exchange's open interest in the previous year. The Commission's rationale for the concentration limit was to prevent concentrated positions from causing abrupt price movements and distortions in a market, and to "fragment" the market to allow multiple traders to step in where a smaller number of traders may have existed previously. The theory rested upon the unproven assumption that large traders are crowding out smaller participants.

ICE disagrees with setting exchange specific concentration limits in any new rulemaking as they ignore the premise that economically equivalent contracts operate as a single aggregate market, were expressly rejected by Congress in drafting Dodd-Frank; and may have significant anti-competitive implications.[2] Exhaustive hearings by Congress and the Commission over the last several years have concluded that economically equivalent contracts traded on two separate exchanges operate as ***a single aggregate market.*** In testimony before this Subcommittee in September 2007, Dr. James Newsome, former Commission Chairman and then President of NYMEX, stated "the two competing trading venues [ICE and NYMEX] are now tightly linked and highly interactive and in essence are simply two components of a broader derivatives market."[3] This is because participants arbitrage between economically equivalent markets, causing prices to converge. As this Subcommittee is well aware, the one market concept was the impetus for provisions in the farm bill which mandate regulation of swaps determined to be Significant Price Discovery Contracts in an equivalent manner as futures. Thus, the idea of imposing concentration limits on an "individual exchange" basis is unnecessary given the aggregate limit, which will serve the same purpose.

Importantly, Congress expressly rejected a concentration limit in Dodd-Frank when it dropped language in the Section 738 of the Act in the House version of the legislation[4] requiring foreign boards of trade to set position limits based upon "relative" market size. In addition, having market specific concentration limits appears inconsistent with other parts of Dodd-Frank, which contemplates multiple competing Swap Execution Facilities with open access to central clearing houses where swap positions would be traded into on one SEF and out of on another SEF.[5] It is not apparent how this could be accomplished with SEF-specific concentration limits based upon open interest at an open-access clearinghouse used by multiple platforms.

Finally, a single exchange concentration limit is anti-competitive. The Commodity Exchange Act mandates that the Commission "regulate the futures markets by the least anti-competitive means available." By design, a concentration position limit will impose smaller, or stricter, concentration limits in smaller markets. A smaller market with fewer market participants has its open interest concentrated in these market participants. Thus, applying a concentration limit for an individual exchange will inhibit competition by impeding liquidity, given that smaller markets are concentrated. This would effectively lock in the market share of existing exchanges. A nascent exchange with such restrictions would likely face insurmountable odds in establishing a market and competing with incumbents. In addition, large market participants will effectively be prevented from leaving one market for another that offers a competitive advantage due to its inability to carry a similar sized position on the second market due to the "concentration limit." This would substantially curtail innovation and the choice that exists in today's markets. Slowly, over time, the dominant market will continue to gain market share, as liquidity attracts liquidity. In the end, concentration limits may create the opposite of what

[2] H.R. 4173, Section 3155.
[3] Testimony of Dr. James Newsome, Chief Executive Officer, New York Mercantile Exchange, before the Subcommittee on General Farm Commodities and Risk Management, United States House of Representatives (September 26, 2007).
[4] See, *supra* note 1.
[5] Dodd-Frank Wall Street Reform and Consumer Protection Act, Section 723(3).

the Commission intends: a diverse, highly competitive market for execution of derivatives.

Position Limits Across Futures and OTC Markets Should Be Set to Avoid Negatively Impacting Liquidity Available to Commercial Users of the Markets and Should Be Based Upon Data of Each Market

In setting aggregate position limits across futures and OTC markets, the Commission should act only after taking into account trading data from ***both*** the futures markets and the broader OTC swaps markets. Failing to take into account accurate data from each market risks setting aggregate position limits at artificially low levels that could negatively impact the liquidity relied upon by commercial users to efficiently hedge their price risk. Dodd-Frank requires the Commission for the first time to regulate previously un-regulated OTC markets that have themselves been used by segments of the commercial market to hedge risk. Should the Commission not take into account the size of this market in setting speculative position limits in the now-combined market, liquidity could be adversely impacted with commercial end-users paying wider spreads to hedge their price risk. This would certainly be an unintended consequence and inconsistent with Dodd-Frank's broader goals.

Conclusion

ICE is a strong proponent of open and competitive derivatives markets, and of appropriate regulatory oversight of those markets. As an operator of global futures and OTC markets, and as a publicly-held company, we understand the essential role of trust and confidence in our markets. To that end, we are pleased to work with Congress to address the challenges presented by derivatives markets, and we will continue to work cooperatively for solutions that promote the best marketplace possible.

Mr. Chairman, thank you for the opportunity to share our views with you. I am happy to answer any questions you may have.

The CHAIRMAN [presiding.] We thank you.

Mr. Jones.

STATEMENT OF ROBERT JONES, SENIOR VICE PRESIDENT, ABN AMRO CLEARING CHICAGO LLC; MEMBER, RISK MANAGEMENT COMMITTEE, NATIONAL GRAIN AND FEED ASSOCIATION, CHICAGO, IL

Mr. JONES. Good morning, Mr. Chairman, Members of the Subcommittee. I am Robert Jones, Senior Vice President of ABN AMRO Clearing in Chicago, a futures commission merchant. I serve on the Risk Management Committee of the National Grain and Feed Association, and I am here today to represent the views of the National Grain and Feed Association. We appreciate the opportunity to discuss position limits for enumerated agricultural commodities. Federal position limits are already in place for those commodities, and we believe they are at appropriate levels.

Generally, we have found that the Commission understands the impacts of its actions on commercial businesses and is responsive to our concerns. However, the deadlines that have been set in the law are very challenging.

For our industry, the price discovery occurs primarily in the futures market, so it's extremely important that we get these rules right. Given the choice, we would prefer to go a little slower and make sure we get it right, rather than rush rules through to meet a deadline and find out later about unforeseen consequences.

To provide some context for this, I would like you to think back to 2008. Agricultural futures prices escalated rapidly, resulting in a disconnect of cash and futures values, otherwise known as convergence. Basis levels for producers, essentially the difference between the cash and the futures, widened dramatically. The situation increased risk for grain purchasers and hedgers and caused extreme financial stress due to massive margining requirements.

At the same time, marketing opportunities for producers were limited. We believe that the expanded participation by nontraditional participants like index funds and pension funds played a role in the 2008 spike—not the only factor but a factor.

Today, conditions exist that could lead to a repeat of that situation. If another investment-fueled futures spike occurs, grain buyers may be forced to limit their purchases from U.S. agricultural producers as occurred in 2008. Certainly buyers would be forced to consider tighter limits on forward contract purchases, and at the very time many producers would like to take advantage of those favorable prices.

The NGFA believes that it would be imprudent for the CFTC to change current speculative position limits for the enumerated agricultural commodities.

In particular, we have a strong reservation about an approach that would create a combined position limit for over-the-counter instruments and futures based on open interest levels.

The majority of the risk management activity for the enumerated ag commodities involves futures traded on exchanges. The practical impact of a combined OTC and futures position limit likely would mean limits ratcheting steeply upward for futures. We fear the result would be a sort of perpetual motion machine leading to investment in enumerated ag commodities in ever-greater amounts and even wider basis swings occurring.

In addition, the commodity exchanges, notably the Chicago Board of Trade and the Kansas City Board of Trade, have worked diligently to reestablish convergence in their wheat contracts. Getting it wrong on position limits could undo progress that the exchanges are making toward enhancing the performance of their contracts.

Proper functioning of futures markets for traditional commercial users and producers should be the CFTC's overriding consideration in establishing position limits. A reliable relationship between cash and futures must be maintained.

Convergence matters, not just sometimes, but consistently and predictably. The National Grain and Feed Association does not favor excluding investment capital from agricultural futures markets, as we believe it does provide liquidity to our markets. However, we believe that the CFTC must establish reasonable limits on an investment in the enumerated ag commodities so these relatively small markets are not overwhelmed by investment demand.

Ignoring the unique characteristics of these markets could have highly undesirable consequences for agricultural producers and their traditional hedgers who use these markets for price discovery and risk management.

Thank you, Mr. Chairman, for the opportunity to present NGFA's views today. And we will be happy to respond to any questions.

[The prepared statement of Mr. Jones follows:]

PREPARED STATEMENT OF ROBERT JONES, SENIOR VICE PRESIDENT, ABN AMRO CLEARING CHICAGO LLC; MEMBER, RISK MANAGEMENT COMMITTEE, NATIONAL GRAIN AND FEED ASSOCIATION, CHICAGO, IL

Good morning, Mr. Chairman and Members of the Subcommittee. I am Robert Jones, Senior Vice President of ABN AMRO Clearing Chicago LLC, a futures commission brokerage in Chicago. I serve on the Risk Management Committee of the

National Grain and Feed Association (NGFA) and I am here today to represent the views of the NGFA.

The National Grain and Feed Association is the national nonprofit trade association that represents more than 1,000 companies that operate an estimated 7,000 facilities nationwide in the grain, feed and processing industry. Member firms range from quite small to very large, both privately owned and cooperative, and handle or process in excess of 70% of all U.S. grains and oilseeds annually. Companies include grain elevators, feed mills, flour mills, oilseed processors, biofuels producers/co-product merchandisers, futures commission merchants and brokers, and related commercial businesses.

A common thread for NGFA-member firms is that they rely heavily on efficient futures markets to provide price discovery and risk management for their commercial businesses. In particular, consistent and predictable convergence of cash and futures values is of primary importance to the NGFA. Establishing appropriate speculative position limits for the futures contracts utilized by these traditional commercial hedgers is critically important to maintaining the viability of futures contracts for risk management purposes. It also is essential in enabling our member companies to make forward contracting and other risk management tools available to farmer-customers.

We are especially glad for the opportunity this morning to discuss position limits for the enumerated agricultural commodities—that is, wheat, corn, soybeans, livestock and cotton. As you know, Federal position limits already are in place for those commodities. We believe those limits are at appropriate levels and that the process for establishing those limits has worked well. However, the Dodd-Frank Act requires that the CFTC now establish speculative position limits for all commodities, including agricultural commodities.

In the past, the NGFA generally had been supportive of occasional requests by futures exchanges to increase speculative position limits. However, futures price volatility in recent years and vastly increased participation by nontraditional participants has altered the situation and, at times, threatened the viability of exchange-traded futures for commercial grain hedgers. The rapid escalation of agricultural futures prices during 2008, and a resulting disconnect of cash and futures values, dramatically increased risks for grain purchasers/hedgers and caused extreme financial stress due to massive margining requirements. We believe that dramatically expanded participation in agricultural futures by nontraditional participants like index funds and pension funds played a role in the 2008 spike—not the only factor, but a significant one.

Today, conditions exist that could lead to a repeat of those conditions. With investment capital now seeking enhanced returns and many advisers recommending commodities as an investment vehicle, it appears the stage could be set for another investment-fueled spike in futures prices—an increase we fear will be largely unrelated to market fundamentals and could again result in extreme financial stress. If this happens, grain buyers may be forced to limit their purchases from U.S. agricultural producers, as occurred in 2008. Certainly, buyers would be forced to consider tighter limits on forward contract purchases, at the very time that many producers would like to take advantage of favorable prices.

Many Members of Congress have heard from producers about wider basis levels in recent years—that is, the difference between cash bids and futures values on-exchange. We believe strongly that artificially inflated futures values, due in part to participation of nontraditional investors, have led to a disconnect between cash and futures. The commodity exchanges, notably the Chicago Board of Trade and the Kansas City Board of Trade, have worked diligently to address the disconnect and to re-establish convergence in their wheat contracts. Getting it wrong on position limits could undo progress the exchanges are making toward enhancing performance of their contracts.

For these reasons, the NGFA believes it would be imprudent for the CFTC to change current speculative position limits for the enumerated agricultural commodities. In particular, we have strong reservations about an approach that would create a combined position limit for over-the-counter instruments and futures based on open interest levels. The logic for not linking speculative position limits to open interest levels is as follows.

The majority of risk management activity involving the enumerated ag commodities utilizes futures traded on-exchange. The practical impact of a combined OTC and futures position limit likely would mean limits effectively ratcheting steeply upward for futures—attracting greater investment and boosting open interest levels—which would trigger increased position limits—leading to yet greater participation levels and increased open interest—and triggering even higher position limits—and so on. We fear the result would be a sort of perpetual motion machine leading speculative investment capital to invest in enumerated ag commodities in ever-greater amounts, exacerbating artificially inflated futures values and leading us back to even wider basis swings.

Instead, the NGFA strongly urges the CFTC to use proper functioning of futures markets for traditional commercial users and producers as the overriding consideration in establishing position limits. That means that a reliable relationship between cash and futures must be maintained. **Convergence Matters!** Not just sometimes, but consistently and predictably.

We also urge the CFTC to be vigilant in reviewing corporate linkage issues through which investment firms or other nontraditional participants may technically comply with position limits through separate entities, while coordinating positions that would circumvent the intent of the rule. This would seem to us consistent with the Commission's intentions to monitor account ownership and control to help ensure compliance.

Mr. Chairman, all these points lead back to one very important message: enumerated agricultural futures contracts must function effectively for traditional commercial hedgers and their farmer-customers. The NGFA does not favor excluding investment capital from agricultural futures markets. In fact, we believe that a desire to invest in our industry is a good thing. It forecasts growth and economic opportunity for U.S. agriculture and agribusiness.

However, we believe Congress and the CFTC must act prudently to establish reasonable limits on investment in the enumerated ag commodities and help ensure that those relatively small markets are not overwhelmed by investment demand. Ignoring the unique characteristics of the enumerated agricultural commodities when setting position limits could have highly undesirable consequences for U.S. agricultural producers and the traditional hedgers who use these markets for price discovery and risk management.

Thank you, Mr. Chairman, for the opportunity to present the NGFA's views. I would be happy to respond to any questions.

The CHAIRMAN. Thank you.

I thank the whole panel. We have votes coming up in about 15 or so minutes, we are told. We are not going to limit the discussion to take place here, let's, just to expedite a little bit, I will go right to Mr. Johnson.

Mr. JOHNSON. Thank you, Mr. Chairman. Just a quick question. I'm obviously particularly proud to have two of my fellow Illinoisans here, Mr. Jones and Mr. Duffy. I would ask you, it seems as though at least the Commission is of a mind that if we hurry to regulate our domestic exchanges, our European counterparts will follow.

It is my judgment, and I may be wrong and I am inquiring as to you specifically, as to whether you think that is the correct process; or whether you think, in fact, that that course would put our markets, CME and otherwise, at a competitive disadvantage. And do you think if we do put the cart before the horse, in my judgment, that the Europeans will impose similar position limits, or do you think they will simply lag back and take advantage of our premature action?

Mr. DUFFY. Well, I thank Congressman Johnson for the question because it is very interesting. I met with the gentleman from France. His name escapes me, but he is the head of the European Commission on this. And I asked him, when he told me along with Chairman Gensler when he came to visit us at the exchange, that they were in lockstep with the United States. I asked him when they passed Dodd-Frank in the U.K., and they said they did not pass Dodd-Frank. I asked them when they had other provisions put in place such as in the United States, and they had no such provisions, not even anything on the table.

They are making a lot of rhetoric, in my opinion. As it relates to regulatory reforming with the U.S., I do not see that to be the reality. The U.K., especially in London, is very dominated by the financial services industry. I think they will say many things to get a competitive advantage over the United States, and it would be a shame if that was allowed to happen. I am not talking my own book here, I am talking the United States' book here. We want to keep this business in the U.S. We want to be the central place to discover price. And I assure you that our friends over in Europe would love to have the business that the United States has today.

So I personally don't believe that they are going to follow suit with the United States in laws. They may do certain things, but not to the extent that we have done in this country.

Mr. JOHNSON. I appreciate it. To my fellow Members that remain on the panel and everybody here, Merry Christmas and Happy Holidays to all of you.

Mr. DUFFY. Merry Christmas, sir.

The CHAIRMAN. Thank you. Mr. Peterson.

Mr. PETERSON. Thank you, Mr. Chairman.

Mr. Duffy, this article that I referenced earlier, as I understand it, I guess you didn't respond, or I don't know if they called you or not about this article.

Mr. DUFFY. No, they did not.

Mr. PETERSON. But you were offering the Citadel service. And is it true that you couldn't get—they couldn't get people to sign up?

Mr. DUFFY. We had an offering with Citadel Investment Company roughly a year, year and a half ago, to bring to the market trading of credit default swaps initiative, and we did not receive any traction on that initiative with Citadel Investment firm for a whole host of reasons. We have had a lot of businesses that we invest in and we try, some work some don't, no different from our products. We test products, hundreds of them, and maybe one can be successful out of hundreds or thousands, so this is another venture that did not succeed.

Mr. PETERSON. You agree with the characterization that the reason it didn't is that these so-called secret committee of nine bankers froze it out?

Mr. DUFFY. I don't know of any facts to support that, sir, to be honest with you. I would not know that. But I would suggest that the clearinghouse at the CME Group is an open clearinghouse. I think Chairman Gensler referred to some of the barriers to entry to the clearinghouses in the United States. We don't have the barriers to entry into our clearinghouse that he was referring to. So there is not a multi-billion-dollar commitment into clearing at CME Group's products today. So there are risk-management issues in these OTC products. I am not saying that is not important. But in today's business that CME Group does, we don't have the barriers to entry that Chairman Gensler might have characterized incorrectly.

Mr. PETERSON. Did the risk committee change? Do you have a risk committee?

Mr. DUFFY. We do have a risk committee, sir.

Mr. PETERSON. Has the makeup of that changed?

Mr. DUFFY. The makeup of our risk committee can change throughout time. Obviously, we have certain members that come and go, but we have a composition of people that have interest in the marketplace that is reflective of the marketplace, and we think that is the best thing for all the users.

Mr. PETERSON. You would not agree that this risk committee is dominated by these so-called secret committee——

Mr. DUFFY. I didn't give that much credit, to be honest with you, sir. I don't believe that. I think the markets are much bigger than that. I don't think there is any collusion going along. Risk committees, there is way to much at stake for that to be going on, whether it is not a CME Group or any other institution.

Mr. PETERSON. Mr. Sprecher, you have a risk committee, too. Is it made up of big guys or more broad than that?

Mr. SPRECHER. Yes. We own five regulated clearinghouses, but one of them is specific for credit default swaps. The members of that clearinghouse are the 14 largest global banks. And each of those banks has a representative on the risk committee. That risk committee is overseen by an independent Chairman, and the issues that are discussed in our committee are risk issues, so I can't speak to these. What the article suggested were Wednesday meetings downtown or other things.

Mr. PETERSON. You are not aware of those?

Mr. SPRECHER. I am not aware of those.

Mr. PETERSON. Thank you. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you.

Mr. Conaway.

Mr. CONAWAY. Thank you Mr. Chairman. Gentlemen, welcome. Given that the state of play is at the CFTC, and not in Congress right now, what are you coming to Congress here to ask us? Are you coming to ask us to do anything with respect to the rulemaking that is going on, that the Congress actually needs to act, or are you wanting us to continue to watch what is happening at the CFTC? Anybody ask you to do something specific?

Mr. NEWMAN. I think as we identified in the positions for the American Feed Industry Association, we appreciate your continued oversight and watching the process, and ensuring that it does go forward and gets the results that everyone intended.

Right now we see our role as working more directly with CFTC in the comment process to make sure that our interests and so forth are taken into account in that process.

Mr. CONAWAY. Speaking of that question, have all of your organizations and your individual members had the appropriate level of access to the rulemaking process?

Mr. SPRECHER. Yes, we have.

Mr. NEWMAN. We have had very good cooperation and outreach to not only clarify what is being considered, but also to be able to have the input into the process.

Mr. CONAWAY. Mr. Collura, are you guys being considered?

Mr. COLLURA. Yes. We have had adequate access to the Commission, the rulemaking process; and actually as a coalition, we submitted comments, preliminary comments to CFTC on November 1.

Some of those suggestions we have made regarding the position of its rulemaking were actually kind of thrown around a little bit in discussion in a previous panel. One of those points made, Congressman Marshall, was very well taken about the importance for a lot of energy and agricultural groups in our coalition that are concerned about index speculation. I think that, I hope that tomorrow the proposed rulemaking will attempt to address that situation and, maybe like Commissioner Chilton said, find a way to somewhat segregate the various forms of speculation that occurred in the markets and address them as appropriate. And if not, we will be certain to——

Mr. CONAWAY. Help me with that. What type of various forms of speculation? You said various forms of speculation. What—help me understand what a form of speculation is.

Mr. COLLURA. I am speaking of traditional speculation such as hedges and futures investors——

Mr. CONAWAY. So it is not the form of speculating——

Mr. COLLURA. Right, *versus* the index funds which have a different investment strategy when it comes to commodity investments.

Mr. CONAWAY. You used a phrase which I thought was interesting. You said that basically the speculation—and you said it as a pejorative—are bets on higher prices. Is there a different reason to speculate than higher prices?

Is that the side of the deal that is buy low, sell high?

Mr. COLLURA. I am sorry, I am not sure I understand the question.

Mr. CONAWAY. You used a phrase as a pejorative that the speculators were betting on higher prices. And I was struck by that as to—I am not aware of a speculator——

Mr. COLLURA. My comment was in respect to the earlier comments that Congressman Marshall had raised about index speculation. These folks take passive rolling positions in commodities and can create almost a perpetual situation of entangling a market, where outside of spot months——

Mr. CONAWAY. Are there speculators that you would agree should be in the market?

Mr. COLLURA. I agree speculators, in general, should be in the market. Speculation, in general, is a good and healthy thing. It provides liquidity and provides risk management and, as was being discussed, risk management and risk mitigation.

Mr. CONAWAY. The comments about, you, your members, are they willing to accept higher prices for transaction costs as a result of limiting the number of speculators in a market? Is that a—does that have any—I will ask Mr. Duffy and Mr. Sprecher. You both mentioned higher transaction costs.

Are those—is that one of the burdens that we talk about if we mess this market up? And can you measure those higher transaction costs?

Mr. DUFFY. I think you can, sir. Prior to going into management at CME in 2002, I spent 25 years of my career actually trading these products and providing liquidity for all different types of products. And I know when there are fewer participants in a marketplace the bid offer widens significantly. And I don't care if you are trading government securities or you are trading pork bellies. It will widen significantly with less participants.

So the answer to your question is absolutely yes, and I have seen it for many, many years, firsthand, whether it is electronically or in the pit form.

And if I could just clarify one other point, sir, while I have the microphone, on these index funds. These index funds, just so we are all clear on this, they do not come to expiration of the market. We have all decided, or we have had a lot of discussion, that the price discovery function happens during delivery period of the marketplace. Index funds have long gone from the delivery period of any marketplace and have gone to the next month. So they are not affecting the price discovery of any one particular product.

And also when you look at who takes or makes delivery of these products, there are less than several hundred contracts on a delivery period every cycle when millions of contracts are being traded. So it is a very small percentage of delivery that is being done, and the index funds have long moved out of the marketplace.

I apologize for answering two questions at once.

Mr. CONAWAY. That is okay. I yield back, Mr. Chairman.

The CHAIRMAN. Mr. Marshall.

Mr. MARSHALL. Thank you, Mr. Chairman. I guess it is the influx of the index fund money that some say would push prices higher, and then that you would reach some sort of stable state where they are getting out and they are not affecting price the way you describe.

Mr. Duffy?

Mr. DUFFY. They would actually be selling the nearby contract, sir. So they would be putting pressure on the price discovery contract month, if they are index funds that are long. There are also index funds that are short, too.

Mr. MARSHALL. Right; once you get to that stable state.

Mr. DUFFY. Correct.

Mr. MARSHALL. And it may, again, I don't know, I just don't think that we here in this Committee or in Congress are competent to judge this. That is why we defer to the CFTC and specifically told the CFTC, "Don't do it if it is not appropriate to do it. Figure out whether or not you have a problem and then tailor the solution to that specific problem."

But we did hear this testimony that maybe the influx of commodities money into the market could pull—force prices to go up for a period of time and then there would be a stable state that you have described where they are just rolling and they are not really affecting price.

Mr. DUFFY. I assure you, anytime there is an influx of money into any particular product, whether it is a security of IBM stock, CME stock, or ICE stock, or a barrel of crude oil, you could have a short-term impact on price all the time. You can do that at the grocery store, you can do it at the gas pump, you can do it anywhere. But normally the market will come back into fundamentals right away.

Our point is these people are not affecting the price when it comes into what is the delivery period.

Mr. MARSHALL. The CFTC used its special call authority to gather large trader data, and it has been gathering large trader data, since late 2007; first, quarterly, and now it is doing it more frequently, maybe monthly. Eventually the objective here is to get it daily, and I guess that is going to occur late in 2011.

Are any of you aware of any studies—we have already talked about the CFTC itself looking at the large trader data to determine whether or not it has had an impact upon price—whether or not the trading by these massive passive index funds, what have you, whether they have had an impact on price? Are any of you aware of a study done by anybody—Lincoln, Princeton, you name it, doesn't matter who it is—taking that data, which is probably the best thing to be looking at, trying to figure out whether or not index fund trading has had an inappropriate impact? Anybody looking at that data who has come up with, yes, here is the problem and specifically here is what happened? Anybody?

Mr. DUFFY. We have looked at the data and we have seen no evidence to support that index funds are doing what you suggested. So we have looked at all the academic data and others coming out, and even CFTC's economist, and their data, their reports, and have seen nothing to support that speculators are influencing the price of products.

Mr. COLLURA. I believe that we might have some data and some information, which I can't cite offhand but I can certainly get the Committee in the future.

Mr. MARSHALL. That would be great, and share it with the CFTC as well. If the Committee has heard one message here, and it is fairly consistent on both sides of the aisle, is that we don't think the CFTC needs to move forward. They are not mandated to move forward by Congress to impose position limits if they don't know there is a problem.

So if you can help them identify the problem, because internally they are really struggling with this. You have some Commissioners who say, "Oh, yes, there is a problem." But they are not able to describe it. And the staff is saying, "We can't figure out what that problem is so we don't know what solution to suggest."

Mr. Jones, you said that your group was really troubled by imposing position limits across all markets, so not just in the exchanges but in the OTC market swaps world generally. And because it was good, and I have your language here: The practical impact of a combined OTC and futures position limit likely would mean limits effectively ratcheting steeply upward for futures.

When you say the limits would ratchet up, what you mean by that is your members would have position limits that were gradually pushed down so that they really weren't able to take as much advantage of the exchange as in the past?

Mr. JONES. I would say all or at least most of our members would fall into the qualified hedger category. What we are referring to there is, as I said early on, the majority of and particularly in the enumerated commodities of corn, soybeans, wheat, the majority of the trading that goes on, the price discovery occurs on the exchange and most of it is hedged. And so, unlike the energy markets, which I am no expert in, but there is a much larger OTC portion of that that occurs. So if we were combined with the OTC, it actually would create a much larger position limit that specs could have if they combined the two than what exists right now, if it were to flow into the futures market.

Mr. MARSHALL. The trouble I am having is seeing what effect that has on your ability to actually hedge.

Mr. JONES. Well, then that would follow what we said before if you were to get into this investment-fueled higher-price scenario, like we had in 2008, because you had this excessive amount of investment money that had come into the market.

Mr. MARSHALL. You are suggesting that the imposition of aggregate position limits would encourage additional investment market——

Mr. JONES. I would say would allow it, not encourage it.

Mr. MARSHALL. It is currently allowed without limit.

Mr. JONES. Not in the enumerated ags like corn, soybeans, our markets.

Mr. MARSHALL. You don't have an OTC, comparable contracts OTC with regard to those?

Mr. JONES. The exchange just recently—and I refer to Mr. Duffy from the CME—but it is not as mature, not the developed market that the futures, at this point in time——

Mr. MARSHALL. So you are worried that doing this would encourage that kind of phenomena?

Mr. JONES. At this point in time. We are not saying it shouldn't happen. We are just saying we shouldn't rush to do that without the CFTC. We have had ongoing discussion with CFTC and found them responsive to our needs. But we just don't think that they have to rush to make those things in our contract at this time.

Mr. MARSHALL. Thank you for your indulgence, Mr. Chairman. I appreciate all of your testimony.

The CHAIRMAN. Thank you.

Mr. Murphy.

Mr. MURPHY. I wanted to return to something the Chairman was asking about, and ask Mr. Duffy and Mr. Sprecher if they would comment a little more. When we went through the Dodd-Frank process, we were very worried about making sure we found the right balance, that our clearinghouses were out there allowing things to be cleared that could be, but that we didn't put regulatory pressure on you to take products that you couldn't price and therefore we would create additional risk.

This *New York Times* article was a little troubling because it was talking about secrets in a way that I think is a little theatrical, but there is a fundamental underlying issue that I am curious about how you guys approach this? You need people that are clearinghouse members to be solid enough that if there is a problem they can help solve that with capital calls and other things; but at the same time, it seems like there is a possibility that people could set those limits so high that only a handful of people can participate, and you do create an anti-competitive marketplace, how do you guys approach finding that balance?

Mr. Duffy, you talked about being open, but I don't know what that means. And that balance seems like it is a critical one to find, that we get the competition we are looking for without creating additional risk.

Mr. DUFFY. I am happy to refer to Mr. Sprecher to begin with, since he was mentioned in the article and we weren't. So I am happy to——

Mr. MURPHY. It is an issue for both of you.

Mr. SPRECHER. Let me steal the microphone away from Mr. Duffy.

I think specifically with credit default swaps, as you may know, we stepped forward at a moment in time when the market had collapsed and people were calling to remove the toxic assets off the books of the banks and built a clearinghouse to do that. And that is why we have 14 large bank members. And the only solution that we could come up with on how to deal with a failed bank is to force the other 13 members to accept a forced allocation of the failed positions amongst them that my company would administer.

We want to open that clearinghouse up, but we have to recognize that, particularly in the case of some of these complicated derivatives, the new members coming in have to be in a position to be able to accept an allocation of these derivatives, and then they have to be able to do something with them in a marketplace. And we do intend to open that up and we are working on regimes to get there. And certainly Dodd-Frank is an impetus to speed up that implementation.

I think the *New York Times* article was unfair in that it took the construction of that clearinghouse out of the context in which it was built.

Mr. MURPHY. Do you have the same kind of issues with the other regulated clearinghouses?

Mr. SPRECHER. Not necessarily. As the products get more liquid and more transparent and more exchange traded, it is much easier for a member to come in and accept the defaulting position and then liquidate it in a transparent market.

As you specifically know because of your expertise, the credit default swap market is an incredibly illiquid and complicated market, and there aren't many people that have the domain knowledge to do that right now.

Mr. DUFFY. If I could just support what Mr. Sprecher said, on our list of products, obviously we don't have the requirements that we would potentially have if we were to go in and do the OTC clearing because it is a different product. It is not illiquid, but it doesn't have the liquidity in participation of a list of derivatives market has today.

So in order to risk manage that properly so we don't have the system implode, you need to have capital requirements that make sense. You need to set margin requirements that are different than listed traditional futures. So we have to do different types of risk management as it relates to over-the-counter swaps-type clearing. So I would concur with my colleague, Mr. Sprecher.

Mr. MURPHY. Let me just comment. I think from my discussions with our colleagues, there was wide support for trying to open up these markets to the degree possible. What you are hearing from us, and you will continue to hear from us over the years, is that desire for you to, in a prudent fashion, because clearinghouses obviously need to be prudent, but to continue to try to make them open and accessible so we have more competition and more transparency. I think that is really a big underlying piece of what we were all working on through the course of Dodd-Frank, and so I will leave you with that as something to keep in mind.

The CHAIRMAN. Gentlemen, thank you very much for your spending this time with us. We appreciate it. And in recognition of the fact, we are looking forward for his good work, Mr. Conaway will be calling the next meeting of this Subcommittee, whenever that is going to be, so I would like to offer him any closing remarks he would like to make.

Mr. CONAWAY. Thank you, Mr. Chairman. I hope it is not speculating on something that has not actually happened yet. Chairman-elect Lucas will make that final decision. I hope to be, I have expressed an interest in chairing this Subcommittee.

I was heartened today when we had all five of you at least nod your heads that the CFTC's processes are open to you, that you get input into them as you are trying to on both sides of the issue, get your positions in front of the Commission. And if the baseball analogy works, if the umpire is getting screamed at by both benches, then there must be something okay going on behind home plate.

So I was heartened that you both said that CFTC's processes are working, that you have access to as they move along in that. So with that, Mr. Chairman, I yield back.

The CHAIRMAN. Thank you very much. And we do appreciate your coming. Our purpose today was to try to shed a little daylight on what is going on at this moment, the importance it is to our economy and all that goes on in the different markets.

I think it has been a good day. We have learned and got the insight of the Chairman and all the Commissioners and some of the needs that you have. And we want to invite you to continue to be in contact with us, and I am sure you will. So with that, I thank you again. I wish you a great holiday and we look forward to seeing you, if not before, at least next year. Thank you so much.

Under the rules of the Committee, the record of today's hearing will remain open for 10 calendar days to receive additional materials and supplementary written response from a witness to any questions posed by a Member.

The hearing of the Subcommittee on General Farm Commodities and Risk Management is adjourned.

[Whereupon, at 12:20 p.m., the Subcommittee was adjourned.]

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