

COMMODITY MARKETS OVERSIGHT COALITION

October 8, 2009

The Honorable Blanche Lincoln
Chairman, Committee on Agriculture, Nutrition & Forestry
United States Senate
328A Senate Russell Office Building
Washington, DC 20510

Dear Madam Chairman:

The undersigned members of the Commodity Market Oversight Coalition wish to congratulate you on assuming the chairmanship of the Senate Committee on Agriculture, Nutrition, and Forestry. You have been a leading voice on the many important issues under the jurisdiction of the Agriculture Committee, and we look forward to working with you on a matter of particular concern to our members – the adequate regulation and oversight of the commodity and derivative markets and the prevention of excessive speculation.

Our organizations represent interests from across the spectrum, including commodity producers and processors, distributors, retailers, shippers, and end-users, as well as consumer advocates, religious and humanitarian organizations, and others. Since 2007, our coalition has contended that the commodity and derivative markets are subject to insufficient oversight. Excessive speculative investment has resulted in price volatility and uncertainty and disconnected the markets from supply-and-demand fundamentals, diminishing the role of the futures markets as a tool for effectively managing price risks. Excessive speculation culminated in last year's oil price bubble, which drove crude oil prices to more than \$147 per barrel. This speculative bubble put our members and the entire economy at great risk, and galvanized our coalition's commitment to addressing this problem through comprehensive legislative and regulatory reforms.

The Commodity Futures Trading Commission (CFTC), under the leadership of Chairman Gary Gensler, has implemented and proposed measures to increase market transparency and to prevent fraud, manipulation and excessive speculation. But the CFTC's authority is limited. The Commodity Futures Modernization Act (CFMA) of 2000 stripped CFTC authority from over-the-counter trades, including commodity swaps and derivatives. Congress must act to return to the CFTC the authority it lost in 2000.

Without comprehensive reform, another speculative bubble in commodities could easily form. You need look no further than recent activity in the price of crude oil. In the past 20 months, the price of a barrel of oil has gone from \$57 dollars in March of 2008 to more than \$147 dollars in July 2008, and then back down to less than \$32 in December. Oil is now climbing again and is trading at near \$70 despite the fact that the world economy remains sluggish: unemployment continues to increase, demand is still weak, and available oil supplies are well above average and climbing, and the value of the dollar has been essentially flat over the past several months.

Clearly, market fundamentals cannot explain the destructive volatility and unexplained price shocks we've seen in oil and other commodity markets. This has resulted in a general lack of confidence in our commodities markets, their stability and their ability to determine a fair price for commodities based on core market indicators and fundamentals.

What were once markets established for commodity producers and consumers to hedge against risk and protect themselves from price volatility have essentially become financial markets for Wall Street investors and traders and a dangerous new "asset class." Exchange-traded funds (ETFs) have been using these markets in a way for which they were not designed; for buy and hold, "passive long" investment strategies that disrupt the price discovery and price risk management functions of these markets. It is time to return these markets to the *bona-fide* physical hedgers for which they were created.

The longer it takes to Congress to pass meaningful reform, the greater the risk posed by excessive speculation for our fledgling economic recovery and the trillions of federal dollars Congress has spent to stimulate the economy and rescue the financial system. Another speculative bubble in commodities would choke economic recovery, further injure struggling taxpayers and consumer confidence, and increase the burdens on energy-intensive, core industries like agriculture, manufacturing, and transportation.

Former Chairman Tom Harkin has been a leader on these issues and he is to be commended for introducing aggressive legislation early this session that sought to remedy some of the main shortcomings of the current regulatory framework. In recent months, the Obama Administration has introduced a framework for comprehensive reform and the CFTC has made additional recommendations to Congress, both of which we endorse.

Specifically, it is important that new legislation provide the CFTC authority to:

1. **Regulate over-the-counter swaps and derivatives**, except securities under the jurisdiction of the SEC. Congress should require that all standardized contracts be traded on CFTC-regulated exchanges where possible, or at least on a CFTC-regulated clearing corporation.
2. **Impose aggregate speculative position limits** to prevent excessive speculation and return our futures markets to their traditional role as a tool for the hedging and risk management of *bona-fide* physical players. This system worked well for decades until so many exemptions were granted that financial speculators have come to dominate the markets, undermining commercial market participants and eroding public confidence. It is absolutely essential that the CFTC be able to **set and enforce aggregate position limits across all markets and for all months**. We recommend that Advisory Groups, rather than public hearings, counsel the CFTC periodically on what percentage of open interest should be set as the per commodity limits.
3. **Prove a manipulation case under the same "reckless conduct" standard that the SEC, FERC, and FTC employ**, in contrast to its current difficult-to-prove "specific

intent” standard. This would make clear that market manipulations resulting from “reckless conduct” will be illegal.

4. **Deny “no-action letters” to foreign boards of trade unless the board in question is subject to a foreign regulator with comparable oversight and regulation** as is required of boards of trade within the United States.
5. **Ban “High Frequency” trading in the Commodity markets.** This trading practice employs tactics such as close-proximity electronic trading, super-computers and complex software to give a select few market participants an anti-competitive advantage. The SEC is considering a ban on such trading tactics but currently, the CFTC lacks explicit authority to do so. If the SEC bans this activity and the CFTC lacks the authority to follow suit, we fear “High Frequency” trading could become more prevalent in the commodities markets.

We encourage you to act swiftly and bring legislation before your committee that builds upon the above proposals. We stand ready to work with you to craft and consider legislation in the coming weeks that will provide meaningful reform to ensure a fair and efficient functioning of these markets in the years to come.

Finally, we commend you for hiring Robert Holifield as your staff director. He is a recognized expert on these issues and will provide you with invaluable counsel as you consider your policy options regarding the future of the futures markets.

Sincerely,

Agricultural Retailers Association
Air Transport Association
American Cotton Shippers Association
American Cotton Exporters Association
Atlantic Cotton Association
Arkansas Oil Marketers Association
American Feed Industry Association
Colorado/Wyoming Petroleum Marketers Association
Food & Water Watch
Florida Petroleum Marketers & Convenience Store Association
Friends of the Earth
Fuel Merchants Association of New Jersey
Gasoline & Automotive Service Dealers of America
Grassroots International
Institute for Agriculture and Trade Policy
Louisiana Oil Marketers & Convenience Stores Association
Maryknoll Office for Global Concerns
Massachusetts Oilheat Council
Mid-Atlantic Petroleum Distributors Association
(More)

National Association of Oil Heat Services Managers
National Association of Truck Stop Operators
National Farmers Union
National Grange
New England Fuel Institute
New Jersey Citizen Action Oil Group
New York Oil Heating Association
North Dakota Petroleum Marketers Association
North Dakota Propane Gas Association
Oil Heat Council of New Hampshire
Oil Heat Institute of Rhode Island
Petroleum Marketers Association of America
Petroleum Marketers & Convenience Store of Iowa
Propane Gas Association of New England
Public Citizen
Ranchers-Cattlemen Action Legal Fund USA
South Dakota Petroleum and Propane Marketers Association
Southern Cotton Association
Texas Cotton Association
United Egg Producers
Vermont Fuel Dealers Association
Western Cotton Shippers Association
Western Peanut Growers Association
World Cotton Exporters Association

Cc: The Hon. Saxby Chambliss, Ranking Member,
Senate Committee on Agriculture, Nutrition & Forestry
The Hon. Collin Peterson, Chairman and Hon. Frank Lucas, Ranking Member,
U.S. House of Representatives Committee on Agriculture
The Hon. Gary Gensler, Chairman, U.S. Commodity Futures Trading Commission
The Hon. Michael Dunn, Commissioner, U.S. Commodity Futures Trading Commission
The Hon. Jill Sommers, Commissioner, U.S. Commodity Futures Trading Commission
The Hon. Bart Chilton, Commissioner, U.S. Commodity Futures Trading Commission