United States Senate

COMMITTEE ON
ENERGY AND NATURAL RESOURCES

WASHINGTON, DC 20510–6150

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May 27, 2008

The Honorable Walter Lukken
Acting Chairman
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Dear Acting Chairman Lukken:

As you know, American families, farmers and businesses are currently struggling under the weight of record-setting fuel prices. With primary jurisdiction over matters related to national energy policy and energy regulation pursuant to Rule XXV of the Standing Rules of the Senate, the Committee on Energy and Natural Resources has a keen interest in more fully exploring the dynamics underlying the current run-up in oil prices.

To date, the Committee has held two hearings during the 110th Congress related to the role of speculators in U.S. energy markets. In addition, we have held a number of staff-level meetings with the Commodity Futures Trading Commission (CFTC) and other market participants and observers, to better understand the factors contributing to oil prices that have recently exceeded $133 per barrel. I recognize that tight oil market fundamentals and geopolitics are important determinants of global oil prices. However, I take seriously the testimony of oil industry analysts who have suggested that supply and demand for physical barrels of oil simply cannot fully explain today's prevailing oil prices. Moreover, the lack of comprehensive oil trade data has hampered attempts to quantify the impacts of speculative investment on the prices now imposing hardships on American consumers.

In particular, I remain concerned that the Commission's assertions to date--discounting the potential role of speculation in driving up oil prices--have been based on a glaringly incomplete data set. Increasing trading activity in U.S. crude oil takes place on foreign boards of trade (FBOTs) and in over-the-counter (OTC) markets, for which the CFTC has limited data and oversight authority. Similarly, I am concerned that CFTC analyses classify so-called "swap dealers"—including large investment banks as "commercial" market participants, along side physical hedgers such as oil companies and airlines, rather than as "non-commercial" participants. The practice of including investment banks in the commercial participant category calls into question the CFTC's continued assertion that non-commercial participants, or speculators, follow rather than lead oil price movements.

Finally, I am troubled by the fact the same level of transparency requirements applicable to agricultural commodities are not currently applied to energy trading. Given that the CFTC itself has recently cited escalating diesel and related grain transportation costs as factors contributing to divergent agricultural pricing patterns[1], it would seem that the Commission should exhaust every remedy at its disposal to shed light on current energy market dynamics.

In order to further our inquiry into these matters, the Committee would benefit from a greater understanding of certain aspects of the CFTC's oversight of--and statistical analysis in relation to--energy commodity markets. As such, I would appreciate your response to the attached questions no later than June 10, 2008.

With questions, please contact Angela Becker-Dippmann or Tara Billingsley of the Energy Committee staff, at (202) 224-4971. Thank you for your attention to this request. I look forward to your timely reply.

Sincerely,

Jeff Bingaman
Chairman

cc: Commissioner Michael Dunn
Commissioner Jill E. Sommers
Commissioner Bart Chilton

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[1] Statement of Jeffrey Harris, CFTC Chief Economist, Hearing before the Committee on Homeland Security and Government Affairs, U.S. Senate, May 20, 2008.

Questions for the Commodity Futures Trading Commission

Off-Shore Oil Trading:

1.) I understand that the CFTC receives on a weekly basis position data from the British Financial Services Authority (FSA) related to the West Texas Intermediate (WTI) crude contract traded on the ICE Futures Europe market--except during the last week of trading for an expiring contract, when such data is received daily.

a. Are the data received from the British FSA relative to the ICE Futures Europe WTI contract incorporated into the CFTC's weekly Commitment of Traders reports for crude oil? If not, why not? Do any legal barriers exist to doing so?

b. The CFTC testified before the Committee last month that "there is no evidence that position changes by speculators precede price changes for crude oil futures contracts.[2]" Did the data underlying this analysis include position information from ICE Futures Europe WTI contract? If not, why not? If so, what is the break-down of "commercial" vs. "non-commercial" positions held in ICE Futures Europe WTI contracts from the period in which the contract was launched in 2006, to the present?

c. Please quantify the volume of intraday trading in the ICE Futures Europe WTI contract since its launch in 2006, with respect to commercial versus non-commercial market participants.

d. As detailed more fully below, I am concerned that CFTC analysis performed relative to the role of ***"commercial"*** participants in commodity markets includes the activities of swap dealers—large institutional investors that appear to be classified along side physical hedgers in these markets, such as oil companies and airlines. Please quantify the share of swap dealer positions held in the ICE Futures Europe WTI contract, relative to the total share of open interest in the contract, the share of open interest for other "commercial" and "non-commercial" positions.

e. Please quantify the volume of intraday trading in the ICE Futures Europe WTI contract attributable to swap dealers, since the contract's launch in 2006.

f. Is the position-related data the CFTC receives from the FSA sufficient to assess crude-related positions of any sovereign wealth funds participating in the ICE Futures Europe market? Please quantify this investment and describe any notable trends.

g. Please provide the Committee with an account of any cross-border investigation and enforcement efforts that have spanned energy trading activities on both domestic markets and Foreign Boards of Trade. To the extent that such

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[2] Statement of Jeffrey Harris, CFTC Chief Economist, Hearing before the Committee on Energy and Natural Resources, U.S. Senate, April 3, 2008.

information might be governed by existing confidentiality requirements, rest assured the Committee will make arrangements to ensure this information remains private and confidential.

The Swap Dealer Loophole:

1.) The Commission has repeatedly testified before Congress that the role of "non-commercial" participants in crude oil markets has not significantly changed during the current period of prolonged run-up in prices. As previously mentioned, this assertion obscures the fact that swap dealers are, for purposes of CFTC analysis, classified along side physical hedgers as "commercial" participants in these markets. I found notable the CFTC's acknowledgement in testimony before the Committee that "swap dealers now hold significantly larger positions in crude oil," and that "this development has altered the traditional role of commercial traders" in the oil markets[3].

   a. Please explain the policy rationale for classifying swap dealers as "commercial" market participants, along side entities that participate in these markets as physical hedgers. Is there any current legal barrier to classifying these entities as "non-commercial" market participants for reporting purposes?

   b. The CFTC has testified before the Committee that "the non-commercial share of total open interest has increased marginally from 31 percent to 37 percent over the past three years[4]"—a figure that excludes the trading activities of swap dealers. How has swap dealers' share of total open interest grown over the past three years? How has the share of total open interest grown over the past three years when swap dealers are included in the "non-commercial" category?

   c. Please explain the rules related to "hedging exemptions," which may allow market participants to exceed position limits for trading crude oil. To what extent are swap dealers eligible for such exemptions, and how often have such exemptions been granted in crude oil since 2006? Similarly, please quantify the extent to which market participants granted hedging exemptions for trading the WTI contract on the New York Mercantile Exchange (NYMEX) hold additional positions in the ICE Futures Europe WTI contract. (While I understand a single corporate entity may have different subsidiaries or affiliates active in each market, please provide this analysis in a manner that aggregates such positions.)

   d. Please quantify the volume of intraday trading in NYMEX WTI crude contract since 2006, with respect to commercial versus non-commercial market participants, and swap dealers.

Transparency Requirements and Conflicts of Interest:

1.) Since January 2007, the CFTC has published a supplemental, weekly "Commitment of Traders" report detailing positions of index traders with respect to 12 agricultural commodities. In announcing the reporting initiative, the CFTC noted that the new report

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[3] ibid

[4] ibid

would incorporate "…positions of managed funds, pension funds and other institutional investors that generally seek exposure to commodity prices as an asset class in an unleveraged and passively-managed manner," along with the "positions of entities whose trading predominantly reflects hedging of over-the-counter (OTC) transactions involving commodity indices—for example, swap dealers holding long futures positions to hedge short OTC commodity index exposure opposite institutional traders such as pension funds."[5]

a. Why has the CFTC failed to take similar steps to increase transparency with respect to energy commodities through publication of a supplemental Commitment of Traders report—particularly with respect to crude oil?

b. Please describe any technical or legal barriers to including in any such supplemental Commitment of Traders report data relative to positions in the ICE Futures Europe WTI contract.

2.) Testimony and various press accounts[6] have recently noted the acquisition of petroleum storage capacity on the part of institutional investors active in energy commodity trading markets. Such trends lead to concerns regarding potential market manipulation strategies. We note that current CFTC regulations (17 CFR Part 19) require that, with respect to certain agricultural commodity markets, entities that exceed speculative position limits must file reports with the Commission outlining their underlying cash positions. Do any such similar reporting requirements apply with respect to energy commodities? If not, why not?

3.) Do any conflict-of-interest or insider trading-related regulations apply specifically to commodity market analysts or firms, analogous to those put in place with respect to securities as a result of the Sarbanes-Oxley Act of 2002 (P.L. 107-204)? If so, please describe such regulations—particularly as they apply to commodity market analysts and/or traders employed by investment banks with active proprietary trading operations.

[5] CFTC News Release, December 5, 2006; http://www.cftc.gov/newsroom/generalpressreleases/2006/pr5262-06.html

[6] Davis, A.; *Where Has All the Oil Gone?,* Wall Street Journal, October 7, 2007.