U.S. Commodity Futures Trading Commission
Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581
www.cftc.gov

Bart Chilton
Commissioner

(202) 418-5060
(202) 418-5620 Facsimile

March 25, 2011

The Honorable Maria Cantwell
511 Dirksen Senate Office Building
Washington, DC 20510

Dear Senator Cantwell:

Thank you for writing to the CFTC regarding speculation. The agency considers most letters from Capitol Hill as "comment" letters on regulations being promulgated. I, however, wanted to take a moment to respond to your letter.

On Wednesday, oil prices reached nearly \$106 per barrel—up 29 percent this year. Not since 2008, when many of us raised concerns about excessive speculation, have prices been so high. This comes at a time when a fairly high supply of oil and stable demand exists. Obviously there are myriad factors impacting prices: the Middle East, Japan and crude transportation issues, to name a few. At the same time, however, we have speculators coming into energy markets at blistering pace. In fact, the latest data indicates that in the energy sector, speculative positions are at an all-time high—up 64 percent from June of 2008 when crude oil prices touched \$147.27 per barrel.

I'm not suggesting that speculation is bad. In fact we need speculation and there is ample evidence (in addition to common sense) that speculation can decrease volatility. On the other hand, speculation can become excessive. In these instances, as we may be seeing now and as I believe we saw in 2008 and even for some period in 2009, that excessive speculation can impact prices. I'm not suggesting that speculators are driving prices or that they are the cruise control on prices. I do think, however, that they tap the gas pedal at times.

I didn't come to this conclusion lightly and continue to cite many studies, paper and quotes that make this same connection between speculation and prices (not just in the energy complex, but also in agricultural commodities and metals).

As you know, Congress enhanced the CFTC's ability to address excessive speculation as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act. Specifically, the Act mandates that the agency implement speculative position limits in the energy sector within 180 days. Obviously, that deadline has long since passed, which is unfortunate to say the least. I had urged the agency to implement limits on time.

We heard three primary arguments against implementation within the required implementation time period, that is, by mid-January, 2011.

First, some have suggested that when the statute says the Commission shall implement "appropriate" speculative position limits, that the word "appropriate" could mean that no limits whatsoever could be "appropriate." As many Members have said, this provision of the statute should not be interpreted with such elasticity as to mean no limits whatsoever. The reason Congress gave us the expedited implementation date was precisely because Congress wanted the agency to implement speculative position limits.

The second argument against implementing limits on time was that if we were to do so, there would be market migration. In essence, the suggestion is that if the CFTC set very restrictive position limits, traders would simply trade in other venues. First, there is the suggestion that the trading will migrate to currently unregulated over-the-counter (OTC) markets. These markets will, however, within months not years, be regulated by the agency. The other suggestion is that the trading will migrate to foreign boards of trades. Both of these suggestions are based on the dubious premise that limits the agency establishes would be overly restrictive. There is nothing that requires us to set a certain position limit level, and, in fact, I have always said that we should err on the high side at first—precisely to avoid any negative consequences—and re-calibrate as we move forward and know more about the markets.

The third argument against implementing limits on time was that the agency doesn't have the data to set reasonable, or appropriate, position limits. This is the only argument of the three that has limited merit. We do not yet have, and will not have for a few more months (September at the earliest) some of the OTC trading data that would facilitate setting position limits. Those who don't support position implementation now use that argument to say no limits should be in place whatsoever. Congress required that we have several limits: spot month, all month and aggregate month limits for currently regulated exchanges. The law also requires that we have those same three limits for OTC trading (spot, all month and aggregate limits). Those who oppose limits now don't agree that we could have already imposed spot month limits on all contracts (including OTC trades) using the available physical supply of the commodity. We could have done those in January, we can do them now. Similarly, we could have, should have and can now implement limits for all months and aggregate limits for currently-regulated exchanges. Finally, if there was a desire, I believe we could have developed an appropriate formula to impose limits on OTC trading for the very largest traders who also use the currently-regulated exchanges. This limit would have also had to err on the high side.

In summary, the agency could have implemented a speculative position limits regime in January. We can still do them now. I will continue to urge that we do so.

With regard to margin levels, your letter raises important issues that we need to consider in development of our proposed rulemaking. As you know, a proposed rule has not yet been issued by the Commission, and we need to consider the significant concerns you raise in the context of this proposal to ensure that excessive speculation does not uneconomically affect commodity prices.

Thank you again for your letter. If I can ever be of assistance on this, or any other matter, please don't hesitate to contact me.

Sincerely,

Bart Chilton
Commissioner