Testimony of

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Regarding

Potential Excessive Speculation in Commodity Markets: The Impact of Proposed Legislation

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Introduction

My name is Michael Greenberger.

I want to thank the Committee for inviting me to testify on the important issue that is the subject of today's hearings.

After 25 years in private legal practice, I served as the Director of the Division of Trading and Markets ("T&M") at the Commodity Futures Trading Commission ("CFTC") from September 1997 to September 1999. In that capacity, I supervised approximately 135 CFTC personnel in CFTC offices in DC, New York, Chicago, and Minneapolis, including lawyers and accountants who were engaged in overseeing the Nation's futures exchanges. During my tenure at the CFTC, I worked extensively on, *inter alia*, regulatory issues concerning exchange traded energy derivatives, the legal status of over-the-counter ("OTC") energy derivatives, and the CFTC authorization of trading of foreign exchange derivative products on computer terminals in the United States.

While at the CFTC, I also served on the Steering Committee of the President's Working Group on Financial Markets ("PWG"). In that capacity, I drafted, or oversaw the drafting of, portions of the April 1999 PWG Report entitled "Hedge Funds, Leverage, and the Lessons of Long-Term Capital Management," which recommended to Congress regulatory actions to be taken in the wake of the near collapse of the Long Term Capital Management (LTCM) hedge fund, including Appendix C to that report which outlined the CFTC's role in responding to that near collapse. As a member of the International Organization of Securities Commissions' ("IOSCO") Hedge Fund Task Force, I also participated in the drafting of the November 1999 report of IOSCO's Technical Committee relating to the LTCM episode: "Hedge Funds and Other Highly Leveraged Institutions."

After a two year stint between 1999 and 2001 as the Principal Deputy Associate Attorney General in the U.S. Department of Justice, I began service as a Professor at the University of Maryland School of Law. At the law school, I have, *inter alia*, focused my attention on futures and OTC derivatives trading, including academic writing and speaking on these subjects. I currently teach a course that I designed entitled "Futures, Options, and Derivatives."

The question whether there has been excessive speculation of U.S. energy futures markets in general, and futures based on U.S. delivered crude oil contracts specifically, has been the subject of many hearings. I have previously testified at six of those hearings, the most recent held on June 24, 2008 before the United States Senate Committee on Homeland Security & Government Affairs. To put the issue of this Committee's hearings in context, I summarize and update the points I made at that hearing immediately below.

Summary and Update of Prior Testimony

One of the fundamental purposes of futures contracts is to provide price discovery in the "cash" or "spot" markets.[1] Those selling or buying commodities in the "spot" markets rely on futures prices

[1] The Economic Purpose of Futures Markets and How They Work, COMMODITY FUTURES TRADING COMMISSION, http://www.cftc.gov/educationcenter/economicpurpose.html (last visited July 8, 2008).

to judge amounts to charge or pay for the delivery of a commodity.[2] Since their creation in the agricultural context decades ago, it has been widely understood that, unless properly regulated, futures markets are easily subject to distorting the economic fundamentals of price discovery (*i.e.*, cause the paying of unnecessarily higher or lower prices) through excessive speculation, fraud, or manipulation.[3]

As the 1935 Report of this Committee stated: "The fundamental purpose of the measure [i.e., what was to become the Commodity Exchange Act of 1936 ("CEA")] is to insure fair practice and honest dealing on the commodity exchanges and to provide a measure of control over those forms of speculative activity which too often demoralize the markets to the injury of producers and consumers and the exchanges themselves."[4]

Indeed, President Roosevelt, when introducing what became the CEA said: "[I]t should be our national policy to restrict, as far as possible, the use of these exchanges for purely speculative operations."[5] In this regard, this Committee then stated: "This bill authorizes the Commission . . . to fix limitations upon purely speculative trades . . ."[6]

The CEA has long been judged to effectively prevent excessive speculation and manipulation. Accordingly, prior to the passage of the Commodity Futures Modernization Act of 2000 ("CFMA"), "all futures activity [was] confined by law (and eventually to criminal activity) to [CFTC regulated] exchanges alone."[7] At the behest of Enron, the CFMA authorized the "stunning"[8] change to the CEA to allow the option of trading energy commodities on deregulated trading platforms, *i.e.*, exchanges exempt from CFTC contract market registration requirements, thereby rejecting the contrary 1999 advice of the President's Working Group on Financial Markets, which included the Secretary of the Treasury, the Chairman of the Federal Reserve Board, and the Chairmen of the SEC and CFTC. [9] This exemption from contract market regulation is called the "Enron Loophole."

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[2] *See* Platts Oil Pricing and Market-on-Close Methodology Explained, Platts (July 2007) at 3, *available at* http://www.platts.com/Resources/whitepapers/index.xml.

[3] *See*, *e.g.*, Jonathan Ira Levy, *Contemplating Delivery: Futures Trading and the Problem of Commodity Exchange in the United States*, *1875-1905*, AMERICAN HISTORICAL REVIEW 307 (2006) ("'[T]he man who managed or sold or owned those immense wheat fields has not as much to say with the regard to the price of the wheat that some young fellow who stands howling around the Chicago wheat pit could actually sell in a day'"(quoting *Fictitious Dealings in Agricultural Products: House Comm. on Agric. Committee Hearing Reports* (1892)).

[4] Report No. 421, U.S. House of Representatives 74th Cong, Accompanying the Commodity Exchange Act, March 18, 1935.

[5] President Franklin D. Roosevelt, Message to Congress, February 9, 1934.

[6] Report No. 421, U.S. House of Representatives 74th Cong., Accompanying the Commodity Exchange Act, March 18, 1935.

[7] PHILIP MCBRIDE JOHNSON & THOMAS LEE HAZEN, DERIVATIVES REGULATION 28 (Cumm. Supp. 2008).

[8] *Id*. at § 1.17.

[9] *Id*. at 28; *see also* President's Working Group on Financial Markets, Over-the-Counter Derivatives Markets and the Commodity Exchange Act 16 (1999), *available at* http://www.ustreas.gov/press/releases/reports/otcact.pdf (last visited July 8, 2008) ("Due to the characteristics of markets for non-financial commodities with finite supplies, however, the Working Group is unanimously recommending that the exclusion [from regulation] not be extended to agreements involving such commodities.").

Two prominent and detailed bipartisan studies by the Permanent Subcommittee on Investigations' ("PSI")[10] staff concluded that large financial institutions and wealthy investors had needlessly driven up the price of energy commodities over what economic fundamentals dictate, adding, for example, what the PSI estimated to be @ $20-$25 per barrel to the price of a barrel of crude oil.[11] At the time of that estimate, the price of crude oil had reached a then record high of $77. The conclusion that excessive speculation has added a considerable premium to energy products has been corroborated by many experts on[12], and observers of, these markets.[13]

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[10] PERMANENT SUBCOMMITTEE ON INVESTIGATIONS OF THE COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS, THE ROLE OF MARKET SPECULATION IN RISING OIL AND GAS PRICES: A NEED TO PUT THE COP BACK ON THE BEAT (June 27, 2006) [hereinafter June 2006 Report]; PERMANENT SUBCOMMITTEE ON INVESTIGATIONS OF THE COMMITTEE ON HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS, EXCESSIVE SPECULATION IN THE NATURAL GAS MARKET (June 25, 2007) [hereinafter June 2007 Report].

[11] June 2006 Report, *supra* note 10, at 2, 23.

[12] *See*, *e.g.,* Edmund Conway, *George Soros: Rocketing Oil Price is a Bubble*, DAILY TELEGRAPH (May 27, 2008), *available at* http://www.telegraph.co.uk/money/main.jhtml?xml=/money/2008/05/26/cnsoros126.xml (last visited July 8, 2008) (quoting Mr. George Soros as stating "Speculation . . . is increasingly affecting the price"); Written Testimony of Michael Masters, *Hearing Before the Committee on Homeland Security and Governmental Affairs*, *U.S. Senate* 2 (May 20, 2008), *available at* http://hsgac.senate.gov/public/_files/052008Masters.pdf (last visited July 8, 2008) (quoting Michael W. Masters as stating "Are Institutional Investors contributing to food and energy price inflation? And my unequivocal answer is YES"); Oral Testimony of Edward Krapels, Hearing Before the Committee on Energy and Commerce Subcommittee on Oversight and Investigations, U.S. House of Representatives, (June 23, 2008) (quoting Mr. Edward Krapels as stating "I think the amount of speculation is really substantial [within the crude oil market.]"); Oral Testimony of Roger Diwan, Hearing Before the Committee on Energy and Commerce Subcommittee on Oversight and Investigations, U.S. House of Representatives, (June 23, 2008) (quoting Mr. Roger Diwan, responding to Rep. Whitfield's question: So you're saying if we adopt these regulatory changes, we could almost cut the retail price of gas in half in a relatively short period of time? "I don't know how quickly it takes to get prices down, but it's clear that prices will reflect closer the marginal cost of producing oil."); Alejandro Lazo, Energy *Stocks Haven't Caught Up With Oil Prices*, WASH. POST (Mar. 23, 2008), *available at* http://www.washingtonpost.com/wp-dyn/content/article/2008/03/21/AR2008032103825.html (last visited July 8, 2008) (quoting Mr. Fadel Gheit as stating "The largest speculators are the largest financial companies."); MICHELLE FOSS, UNITED STATES NATURAL GAS PRICES TO 2015, 34 (2007), *available at* http://www.oxfordenergy.org/pdfs/NG18.pdf (last visited July 8, 2008) (asserting "The role of speculation in oil markets has been widely debated but could add upwards of $20 to the price per barrel."); Tim Evans, Citi Futures Perspective: PM Energy News & Views, at 2 (July 3, 2008) (quoting "With the latest push to the upside, we see the crude oil market becoming even more completely divorced from any connection to fundamental factors and becoming even more obsessed with the simple question, How high can it go?"); Advantage Business Media, *Economist Blames Subsidies for Oil Price Hike*, CHEM.INFO (2008), *available at* http://www.chem.info/ShowPR.aspx?PUBCODE=075&ACCT=0000100&ISSUE=0609&ORIGRELTYPE=DM&RELTYPE=PR&PRODCODE=00000&PRODLETT=M&CommonCount=0 (last visited July 8, 2008) (quoting Dr. Michelle Foss as stating "We have an overpriced commodity, and this is going to be around for a while."); Kenneth N. Gilpin, *OPEC Agrees to Increase Output in July to Ease Oil Prices*, N.Y. TIMES (June 3, 2004) *available at* http://www.nytimes.com/2004/06/03/business/03CND-OIL.html?ex=1401681600&en=5dbd50c5b369795b&ei=5007&partner=USERLAND (last visited July 8, 2008) (quoting Mr. Kyle Cooper as stating "There is not a crude shortage, which is why OPEC was so reluctant to raise production."); Upstream, *Speculators 'not to blame' for Oil Prices*, UPSTREAMONLINE.COM, (April 4, 2008), available at http://www.upstreamonline.com/live/article151805.ece (last visited July 8, 2008) (quoting Mr. Sean Cota as stating "It has become apparent that excessive speculation on energy trading facilities is the fuel that is driving this runaway train in crude prices"); Mike Norman, *The Danger of Speculation*, FOXNEWS.COM (Aug. 19, 2005), *available at* http://www.foxnews.com/story/0,2933,166038,00.html (last visited July 8, 2008) (Mr. Norman stating "Oil prices are high because of speculation, pure and simple. That's not an assertion, that's a fact. Yet rather than attack the speculation and rid ourselves of the problem, we flail away at the symptoms.").

[13] INTERNATIONAL MONETARY FUND, REGIONAL ECONOMIC OUTLOOK: MIDDLE EAST AND CENTRAL ASIA 27-28 (2008) ("Producers and many analysts say it is speculative activity that is pushing up oil prices now. Producers in

The PSI staff and others have identified the Intercontinental Exchange ("ICE") of Atlanta, Georgia, as an unregulated trading facility upon which a considerable amount of exempt U.S. energy futures trading is done.[14] For purposes of facilitating exempt natural gas futures, ICE is deemed a U.S. "exempt commercial market" under the Enron Loophole.[15] For purposes of its facilitating U.S. WTI crude oil futures on U.S. trading terminals, the CFTC, by informal staff action, considers ICE, because of its wholly owned subsidiary, ICE Futures Europe, to be a U.K. entity not subject to direct CFTC regulation even though ICE maintains U.S. headquarters and U.S. trading infrastructure (*i.e.*, terminals and servers), facilitating, *inter alia*, @ 30% of trades in U.S. WTI futures trades.[16]

The Dubai Mercantile Exchange, in affiliation with NYMEX, a U.S. exchange, has also been granted permission to trade the U.S. delivered WTI contract on U.S. terminals, but is, by virtue of a CFTC no action letter, to be regulated directly by the Dubai Financial Service Authority ("DFSA").[17] NYMEX describes itself as "a founder and has ownership share in [DME] and provides clearing services for that exchange." [18]

NYMEX itself, the U.S. premier regulated energy futures contract market capturing the overwhelming share, *e.g*., of the U.S. delivered WTI futures market, has announced that it has applied to the United Kingdom's Financial Services Authority to have a NYMEX London trading platform registered with the that British agency,[19] after which NYMEX will apply for the kind of foreign board of trade no action relief that has already been granted to ICE and DME. Providing NYMEX's London trading platform with this kind of no action relief might very well convert full U.S. regulation of the most important U.S. crude oil futures contracts to considerable U.K. oversight.[20] These staff informal action letters, effectuating the exemptions for "foreign" owned U.S. trading terminals, by their own terms make it clear that they may be instantly revoked by the CFTC.[21]

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particular argue that fundamentals would yield an oil price of about US $80 a barrel, with the rest being the result of speculative activity."); *see also* Neil King Jr., *Saudi Arabia's Leverage In Oil Market Is Sapped*, WALL STREET J. (June 16, 2008), *available at* http://online.wsj.com/article/SB121355902769475555.html?mod=googlenews_wsj (last visited July 8, 2008) (quoting Saudi Oil Minister Ali Naimi as saying skyrocketing oil prices were "unjustified by the fundamentals" of supply and demand).

[14] *See* June 2007 Report, *supra* note 10, at 27.

[15] *See id.*

[16] *See* Written Testimony of Professor Michael Greenberger, *Energy Market Manipulation and Federal Enforcement Regimes: Hearing before the S. Comm. on Commerce, Science, and Transportation*, 3 (2008), *available at* http://digitalcommons.law.umaryland.edu/cgi/viewcontent.cgi?article=1026&context=cong_test (last visited July 8, 2008).

[17] Dubai Mercantile Exchange Ltd., CFTC No-Action Letter, 2007 CFTC Ltr. LEXIS 6 (May 24, 2007).

[18] *See* Written Testimony of Jim Newsome, Hearing Before the Committee on Energy and Commerce Subcommittee on Oversight and Investigations, U.S. House of Representatives, at 6 (June 23, 2008) [hereinafter June 23, 2008 Testimony of Jim Newsome].

[19] *Id.*; Jeremy Grant, *Nymex's Long Road to the Electronic Age*, FINANCIAL TIMES (Feb. 17, 2006), at 39. ("Nymex has indicated that it might be forced to move its electronically traded WTI to London so that it can compete on a level playing field with ICE.").

[20] *See* June 23, 2008 Testimony of Jim Newsome, *supra* note 18.

[21] *See* Written Testimony of Professor Michael Greenberger, *Energy Speculation: Is Greater Regulation Necessary to Stop Price Manipulation?: Hearing Before the H. Subcomm. on Oversight and Investigations* 11-12 (2007) (providing a complete discussion of the no-action letter process including termination), *available at*

One final gap in the oversight of excessive speculation in the U.S. crude oil (and agricultural) markets has been illuminated by the testimony of Michael W. Masters, Managing Member of Masters Capital Management, LLC, at recent May 20 and June 24 hearings before the Senate Committee on Homeland Security and Government Affairs.[22] Mr. Masters demonstrated that large financial institutions, such as investment banks and hedge funds, which were "hedging" their off exchange futures transactions on energy and agricultural prices on U.S. regulated exchanges, were being treated by NYMEX, for example, and the CFTC as "commercial interests," rather than as the speculators they clearly are.[23] By lumping large financial institutions with traditional commercial oil dealers (or farmers)[24] even fully regulated U.S. exchanges are not applying traditional speculation limits to the transactions engaged in by these speculative interests.[25] Mr. Masters has demonstrated that a significant percentage of the trades in WTI futures, for example, were controlled by non-commercial interests.[26] These exemptions from speculation limits for large financial institutions hedging off-exchange "swaps" transactions emanate from a CFTC letter issued on October 8, 1991[27] and they have continued to present day.[28]

Again, while the principal focus to date has been on skyrocketing energy prices, Mr. Masters' testimony, aided by a widely discussed cover story in the March 31, 2008 issue of *Barron's*,[29] has made clear that the categorization of swaps dealers outside of speculative controls even on U.S. regulated contract markets has been a cause of great volatility in food prices, as well as in the energy markets.

Many parties are now urging this Congress to close the Enron, London/Dubai, and Swaps Dealers Loopholes. On June 18, 2008, the Food Conservation and Energy Act of 2008[30] (the "Farm Bill") was enacted into law by a Congressional override of President Bush's veto. Title XIII of the Farm Bill is the CFTC Reauthorization Act of 2008, which, in turn, includes a provision that was intended to close the Enron Loophole.[31] This provision, while a good start, did not return to the status quo prior to the passage of the Enron Loophole: i.e., it did not bring *all* energy futures contracts within the U.S. futures regulatory format. Rather, the Farm Bill amendment requires the

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http://digitalcommons.law.umaryland.edu/cgi/viewcontent.cgi?article=1011&context=cong_test (last visited July 8, 2008).

[22] Masters, *supra* note 12.

[23] *Id.* at 7-8.

[24] Gene Epstein, *Commodities: Who's Behind The Boom?*, BARRON'S 32 (March 31, 2008) ("The speculators, now so bullish, are mainly the index funds. . . . By using the [swaps dealers] as a conduit, the index funds get an exemption from position limits that are normally imposed on any other speculator, including the $1 in every $10 of index-fund money that does not go through the swaps dealers.").

[25] Masters, *supra* note 12, at 7.

[26] *Id*. at 8, 11.

[27] J. Aron & Co., CFTC Interpretive Letter, 1991 CFTC Ltr. LEXIS 18 (Oct. 8, 1991).

[28] *See* Written Testimony of Michael Masters, Hearing Before Committee on Energy and Commerce Subcommittee on Oversight and Investigations, U.S. House of Representatives, at 5 (June 23, 2008) *available at* http://energycommerce.house.gov/cmte_mtgs/110-oi-hrg.062308.Masters-testimony.pdf (quoting "assets allocated to commodity index trading strategies have risen from $13 billion at the end of 2003 to $260 billion as of March 2008, and the prices of the 25 commodities that compose these indices have risen by an average of 183% in those five years!").

[29] *See* Epstein, *supra* note 24.

[30] Food Conservation and Energy Act of 2008, Pub. L. No. 110-246, § 13201; 122 Stat. 1651 (2008).

[31] *Id*.

CFTC "at its discretion" to prove on a contract-by-contract basis through administrative proceedings governed by the notice and comment provisions of the Administrative Procedure Act[32] that an *individual* energy contract should be regulated if the CFTC can prove that the contract "serve[s] a significant price discovery function" in order to detect and prevent excessive speculation and manipulation.[33] The Farm Bill Amendment affords the CFTC 15 months after enactment to implement that re-regulation process specified therein.[34]

The CFTC has publicly stated that it intends to apply the new legislation to only one of ICE's many[35] unregulated ICE energy futures contract, *i.e.*, only ICE's Henry Hub natural gas futures contract would be removed from the Enron Loophole protection and become fully regulated.[36] Thus, by this CFTC pronouncement, it now seems that no crude oil, gasoline, and heating oil futures contracts will be covered by the new legislation—not even the multi-billion agricultural/commodity index futures funds premised upon the prices of U.S. energy and agricultural commodities about which, *inter alia*, Michael Masters has testified are destabilizing the economic fundamentals of the agriculture and energy markets.

The CFTC has also made it clear that the Farm Bill amendment will not cover any *U.S.* futures contracts relating to the price of *U.S.* delivered commodities traded on the *U.S.* terminals of foreign exchanges operating pursuant to CFTC staff "no action" letters. As mentioned above, the Intercontinental Exchange ("ICE") of Atlanta, Georgia, for purposes of facilitating U.S. delivered WTI crude oil futures, is considered by the CFTC, through an informal staff no action letter, to be a U.K. entity not subject to direct CFTC regulation even though ICE maintains U.S. headquarters and trading infrastructure, facilitating, *inter alia*, @ 30% of trades in U.S. WTI futures of its wholly owned the London subsidiary on which the no action permission is based. Moreover, the Dubai Mercantile Exchange ("DME"), in affiliation with NYMEX, a U.S. exchange, has also been granted permission to trade the U.S. delivered WTI contract on U.S. terminals, but is, by virtue of a CFTC no action letter, directly regulated by the Dubai Financial Service Authority ("DFSA"). Again, even though the plain language of the Farm Bill does not exempt contract markets engaged in the U.S. trading of futures premised upon U.S. delivered commodities, the CFTC will not use the Farm Bill amendment to close the "London/Dubai" Loophole.

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[32] *See* RICHARD J. PRINCE, JR., ADMINISTRATIVE LAW TREATISE 424-25, 441-43 (4TH ED. 2002).

[33] Food Conservation and Energy Act of 2008, Pub. L. No. 110-246, § 13201; 122 Stat. 1651 (2008).

[34] *Id*. at § 13204.

[35] *See* Written Testimony of Jeffrey C. Sprecher, To Examine Trading Regulated Exchanges and Exempt Commercial Markets: Hearing of the Commodity Futures Trading Commission, (September 18, 2007), *available at* http://files.shareholder.com/downloads/ICE/325023768x0x132117/53a6f61e-b72b-47ca-8f8e-f8282c21c12b/CFTC%20Testimony%20091807.pdf (last visited July 8, 2008).

[36] *See* Written Testimony of Acting Chair Walter Lukken, *Energy Speculation: Is Greater Regulation Necessary to Stop Price Manipulation?: Hearing Before the H. Subcomm. on Oversight and Investigations,* 4 (Dec. 12, 2007) *available at* http://www.cftc.gov/stellent/groups/public/@newsroom/documents/speechandtestimony/opalukken-32.pdf (emphasis added) (last visited July 8, 2008).

Congress Should Insist Upon Full Market Transparency to Ensure That Excessive Speculation Is Not Overwhelming Crude Oil Futures Trading

As the Committee knows, there is debate over whether the U.S. crude oil futures market is overrun by excessive speculation. As I have said, my own view is that those independent observers who understand those markets, by and large, concur that the markets have come unhinged from supply/demand fundamentals in a manner that makes them no longer useable by the physical hedgers who find prices to be "locked in" too volatile and distant from market fundamentals.[37]

I would argue, however, that even if this Committee has doubts about whether excessive speculation or more serious malpractices are occurring in these markets and thereby unnecessarily driving up the price of crude oil, then those very doubts argue for legislation that makes these markets fully transparent. If all of these markets (e.g., OTC, foreign board of trade U.S. trading terminals for futures dependent on U.S. commodities, and swaps dealers) were required to execute trades on U.S. designated contract markets or designated transaction execution facilities, the real time and constant reporting to both the CFTC and to the market's own self regulatory observers, would make it indisputably clear whether the markets are functioning solely on economic fundamentals; or whether excessive speculation is placing an unnecessary financial burden on them and the American energy consuming public.

As it is, those who reject transparency are those who ask the U.S. energy consumer to accept on blind faith (and I would argue in the face of substantial and reliable data pointing in the opposite direction) that these markets are functioning smoothly.

A Prompt Return to the Time Tested Futures Regulatory Format Predating the Enron Loophole Will Create Much Needed Crude Oil Market Transparency

Whatever form legislation takes to increase transparency in all U.S. traded energy futures, I would urge that the following principles be embedded therein to reassure the American energy consuming public that the price of crude oil is tied to market fundamentals rather than excessive speculation.

Completely Close the Enron Loophole. While the Farm Bill amendment was a good start, the radically rising price of crude oil even in the last few weeks now augurs for returning all U.S. energy futures trading to the safe harbor of fully transparent U.S. regulated contract markets. A simple amendment to existing law would redefine an "exempt commodity" as a commodity that does not include an agricultural or "*energy* commodity," thereby bringing all energy futures, including energy swaps based on the price of energy commodities, within the CEA's regulated contract market trading requirement. An energy commodity should include traditional energy products, *inter alia*, crude oil, gasoline, diesel fuel, heating oil, propane, electricity, and natural gas, as well as metals which have also seen a drastic run up in price. The result of this legislation would return U.S. energy futures trading to the same status as U.S. agricultural trading, which must be conducted on the U.S. registered contract market.

[37] See the many opinions from those experts in note 12 *supra*.

U. S. Based Energy Futures Contracts Traded on U.S. Terminals Should Be Traded on U.S. Regulated Exchanges. To address the concerns about the “London/Dubai” Loophole, any futures contract premised on the price of U.S. delivered energy futures and traded on U.S. trading terminals should be required to be traded on U. S. registered contract markets. This requirement would not affect the overwhelming number of foreign exchanges now trading within the U.S. who have continued to limit their trading to foreign futures contracts.

Grace Periods. Reasonable grace periods should be provided in this kind of legislation to accommodate conversion of energy futures trading not now under U.S. oversight. A grace period no longer than six months should accommodate this conversion.

Aggregated Speculation Limits for Non-Commercial Hedgers. Consideration should also be given to requiring the CFTC to establish uniform speculation limits for non-commercial futures transactions involving the U.S. trading of energy futures contracts premised upon the price of U.S. delivered energy commodities. This would require the CFTC to “fix limits on the aggregate number of positions which may be held by any person” for each month and in *all* markets under CFTC jurisdiction. Under the existing regulatory regime, speculation limits are only applied by each contract market, and “aggregate positions” are never imposed. These aggregated limits would prevent a trader from spreading speculation over a host of markets, thereby accumulating a disproportionately large share of an energy market while satisfying each exchange’s separate limits. The aggregated limits should not be applied to “bona fide hedging transactions” involving the trading of energy futures contracts by those having a true commercial interest in buying or selling the underlying commodity.

Legislation meeting most or all of the above listed criteria include H.R. 6341, introduced by Congressman Van Hollen and Congresswoman DeLauro, requiring all energy futures contracts executed in the U.S. to be traded on U.S. regulated contract markets, thereby building on the Farm Bill amendment’s closure of the Enron Loophole by returning *all* energy futures trading, including the energy swaps market, to where it was immediately prior to that provision’s passage, i.e., on regulated exchanges; and that legislation expressly requires the trading on U.S. terminals of futures contracts premised upon U.S. delivered energy commodities to be similarly subject to a U.S. regulated contract market. The latter provision would close the “London/Dubai” Loophole.

Congressman Stupak has introduced H.R. 6330, which mirrors in function the Van Hollen/DeLauro legislation, but, in what I refer to as a “belt and suspenders” approach, specifically brings energy swaps transactions into the regulated futures environment; nullifies after a grace period all foreign board of trade no action letters; imposes CTFC imposed aggregated speculation limits on non-commercial interests for energy futures trading; requires speculation limits to be imposed on all traders except those who are hedging commercial interests related to the underlying commodity (thereby eliminating the hedge exemption from speculation limits for swaps dealers); and provides strict Congressional oversight of any exemptions provided to energy futures trading from the contract market requirements of the legislation.

Senator Nelson of Florida, with Senator Obama as a co-sponsor, has introduced S. 3134, which is similar to that portion of H.R. 6341 requiring all energy futures contracts to be traded on regulated exchanges.[38] Senators Cantwell and Snowe have introduced S. 3122, which mirrors that portion of H.R. 6341 directed to closing the London/Dubai Loophole by requiring all trading of futures based on U.S. delivered energy commodity on U.S. platforms to be governed fully and directly by U.S. futures law.[39] S. 3205, introduced by Senator Cantwell, is the Senate version of Congressman Stupak's H.R. 6330.

Also worthy of consideration are Senators Lieberman and Collins legislative options designed to undercut excessive speculation in these markets through direct and aggregated controls on non-commercial futures traders. One of their proposals would require the CFTC to establish firm and aggregated speculation position limits on all U.S. speculative futures trading no matter where the platform on which the trading is geographically located.[40]

There Are No Legal Restraints to Barring the "Foreign" Impact of Manipulation on U.S. Markets

Arguments have been advanced that there are legal impediments to the CFTC applying U.S. regulatory protections on Foreign Boards of Trade which bring their trading terminals to the U.S. If that argument were correct, it would be an impediment to much of the legislation cited above requiring the CFTC to do just that. These arguments are premised upon Section 4 (b) of the Commodity Exchange Act (CEA). Section 4 (b) provides in part:

> No rule or regulation may be adopted by the Commission under this subsection that (1) requires Commission approval of any contract, rule, regulation, or action of any foreign board of trade, exchange, or market, or clearinghouse for such board of trade, exchange, or market, or (2) governs in any way any rule or contract term or action of any foreign board of trade, exchange, or market, or clearinghouse for such board of trade, exchange, or market. [41]

However, this clause has been construed only to mean that the CFTC does not have jurisdiction over transactions conducted by *foreign* persons in a *foreign* country on a *foreign* board of trade.[42] *Kleinberg v. Bear Stearns*,[43] dealt with a situation where London traders were committing acts of fraud on a London exchange.[44] In that case, the Court held that the CFTC did not have enforcement jurisdiction, but explained, "It has been consistently held, at least implicitly, that CFTC may regulate and prosecute those who practice fraud in the United States in connection with commodities trading on foreign exchanges."[45]

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[38] S. 3134, 110th Cong. (2008), *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_cong_bills&docid=f:s3134is.txt.pdf (last visited July 8, 2008).
[39] Policing United States Oil Commodities Markets Act of 2008, S. 3122, 110th Cong. (2008), *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_cong_bills&docid=f:s3122is.txt.pdf (last visited July 8, 2008).
[40] Discussion Draft to establish aggregate speculative position limits (2008), *available at* http://hsgac.senate.gov/public/_files/aggspeclimits.pdf (last visited July 8, 2008).
[41] 7 U.S.C. § 6(b) (2008).
[42] PHILIP MCBRIDE JOHNSON & THOMAS LEE HAZEN, DERIVATIVES REGULATION 988 (2004 ed.).
[43] 1985 WL 1625 (1985).
[44] *Id*. at 1.
[45] *Id*. at 2 (internal citations omitted).

To similar effect is the recent case of *Mak v. Wocom Commodities*,[46] concerning a Hong Kong resident placing futures trades with the defendant commodity brokers, both of which are Hong Kong corporations (Wocom).[47] The claims were denied because they were not sufficiently particularized.[48] However, the court stated that jurisdiction would have been extended if it had been clearly shown that there was "particularized harm to our domestic markets."[49] With ICE we currently have trading by U.S. customers in U.S. denominated currency on U.S. terminals in the foremost benchmark U.S. crude oil futures contracts with substantial evidence demonstrating "particularized harm to our domestic markets."

Indeed these cases are consistent with a fundamental tenet of federal financial enforcement jurisprudence that federal financial regulatory jurisdiction extends even to wholly foreign transactions when domestic financial markets suffer "from the effects of [an] improper foreign transaction[.]"[50] The leading commentators on U.S. derivatives regulation have, accordingly stated: "[E]ven without substantial activity in the United States, jurisdiction will exist when conduct abroad has a substantial affect upon U.S. markets and U.S. investors."[51]

Confirmation of this broad sweep of U.S. jurisdiction to address overseas malpractices significantly impacting U.S. markets is evidenced most clearly by the *Sumitomo* case.[52] In that case, the CFTC's enforcement division reached a settlement agreement with a Japanese corporation upon determining that the Japanese head copper trader of the Sumitomo Corporation manipulated the price of U.S. copper almost exclusively through trading done in London on the London Metals Exchange.[53] The CFTC imposed $150 million in fines and restitution.[54] Only a small portion of the trading was done in the U.S. and the London Metals Exchange contact with the U.S. was limited to a U.S. warehouse.[55] Despite these limited U.S. contacts, "the penalty [assessed was then] *the largest ever levied by a U.S. Government agency*," and it was widely recognized that the settlement indicated that "manipulation of any commodity traded in the [U.S.] could be the subject of a C.F.T.C. action, *even if no acts were committed in this country.*"[56]

Clearly, then, trading done on trading platforms within the U.S. would be subject to full CFTC regulatory authority. The fact that ICE is headquartered in Atlanta with its trade matching engines in Chicago and it controls through its U.S. terminals over 30% of the lead U.S.-delivered petroleum contract only makes the jurisdictional question that much easier. The same is true of the Dubai exchange that partners with U.S.-based NYMEX to trade WTI contracts on U.S. terminals; and of the prospect of NYMEX opening a London trading platform for its energy

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[46] 112 F.3d 287 (7th Cir. 1997).
[47] *Id*. at 288.
[48] *Id*. at 290-91.
[49] *Id*. at 291.
[50] Des Brisay v. Goldfield Corp., 549 F.2d 133, 135 (9th Cir. 1977) (citing Schoenbaum v. Firstbrook, 405 F.2d 200, 206 (2d Cir. 1968), *modified in other respects*, 405 F.2d 215 (in banc), *cert. denied*, 395 U.S. 906, 89 S. Ct. 1747, 23 L. Ed. 2d 219 (1969)).
[51] JOHNSON & HAZEN, *supra* note 42, at 984.
[52] In the Matter of Sumitomo Corporation, 1998 CFTC LEXIS 96 (1998).
[53] *Id*. at 2-3.
[54] *Id*. at 24-25.
[55] *Id*. at 11-14.
[56] Floyd Norris, *The Markets; A Record Penalty of Sumitomo, a Lesson on Market Volatility*, N.Y. TIMES (May 12, 1998), at D13 (emphasis added).

futures products, but escaping U.S. regulation for that trading through a staff no action letter treating NYMEX as if it were a U.K. entity.

Even more important, *Sumitomo* and its progeny are an answer to those many threats levied by large U.S. financial institutions that assert, if their trading on "foreign" trading terminals located in the U.S. is regulated, they will simply move that trading abroad. To be clear, any trading done in the U.S. on foreign exchanges is *a fortiori* covered by the applicable U.S. commodity laws.[57] So when the threat is made that the U.S. institutions will trade abroad, it means that it will be done completely outside of the sovereign U.S. However, the *Sumitomo* line of cases make clear that the CFTC, and for that matter, United States Department of Justice for purposes of related criminal prosecution,[58] can enforce violations of U.S. laws abroad if U.S. markets are significantly impacted by the wrongdoing in foreign countries. In short, speculators cannot escape the reach of U.S. civil and criminal law if they cause price distortions in U.S. commodity markets.

Moreover, as I have testified elsewhere, no exchange, wherever located, can develop liquidity in and maximize profits from trading U.S. delivered futures products without having a substantial U.S. presence.[59] This is evidenced by the 18 CFTC staff no action letters issued to foreign exchanges from all over the world allowing the placement of trading terminals in the U.S. [60] In short, the threat that trading in U.S. delivered commodities will be done exclusively abroad is idle when confronted by both economic and legal realities.

The Intercontinental Exchange Cannot Fairly Be Deemed British for Purposes of Trading U.S. Petroleum Futures in U.S. Dollars on U.S. Trading Terminals with U.S. Trading Engines

Of course, all of the above jurisdictional analysis assumes that ICE (and DME) are "foreign" boards of trade. While ICE has a London wholly owned subsidiary, that office is controlled by ICE's headquarters in Atlanta; ICE's trading engines are in Chicago; it is trading over 30% of the U.S. premier crude oil futures contract in U.S. denominated currency. ICE's non-petroleum products, i.e., natural gas futures contracts, are clearly traded within U.S. jurisdiction and are subject to re-regulation under U.S. law by virtue of the Farm Bill's "End the Enron Loophole" provision.[61] ICE also owns a fully regulated U.S. exchange: formerly the New York Board of Trade (NYBOT); now ICE Futures U.S. It defies all logic that such an exchange

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[57] JOHNSON & HAZEN, *supra* note 42, at 984.

[58] *See* Press Release, Department of Justice, U.S. Charges 47 After Long-Term Undercover Investigation Involving Foreign Exchange Markets, (Nov. 19, 2003), *available at* http://www.fbi.gov/dojpressrel/pressrel03/wooden111903.htm (last visited July 8, 2008).

[59] Written Testimony of Professor Michael Greenberger, *Energy Market Manipulation and Federal Enforcement Regimes: Hearing Before the United States Senate Committee on Commerce, Science, and Transportation*, 12 (2008), *available at* http://digitalcommons.law.umaryland.edu/cgi/viewcontent.cgi?article=1026&context=cong_test (last visited July 8, 2008).

[60] U.S. Commodity Futures Trading Commission, Foreign Boards of Trade Receiving Staff No Action Letters Permitting Direct Access from the U.S., *available at* http://services.cftc.gov/sirt/sirt.aspx?Topic=ForeignTerminalRelief (last visited July 8, 2008).

[61] Food Conservation and Energy Act of 2008, Pub. L. No. 110-246, § 13201; 122 Stat. 1651 (2008); Jessica Marron, *House and Senate Lawmakers Move to Close 'Enron Loophole' with Amendment to Farm Bill*, PLATTS GLOBAL POWER REPORT, (May 1, 2008) (stating that the "initial target of the [the Farm's Bill End the Enron Loophole Provision] is ICE's financially settled Henry Hub swap contract").

can be called "foreign" based on the name given to its wholly owned subsidiary (ICE Futures Europe) and maintaining a London office that could as easily be operated out within the U.S.

The same is also true of the Dubai Mercantile Exchange. Its principal partner is the New York Mercantile Exchange (NYMEX), a U.S. regulated exchange and a U.S. entity. The President of NYMEX sits on DME's board. DME has authority to trade the U.S. delivered WTI contract on trading terminals in the U.S. Under these circumstances, DME is clearly a U.S. exchange

The illogic of the FBOT staff no action process is highlighted by NYMEX, a U.S. regulated exchange headquartered in the U.S., establishing a London futures trading platform under the United Kingdom's regulatory regime and then applying for an FBOT staff no action letter to allow trading within the U.S. on its NYMEX London platform. NYMEX will then have converted itself from a U.S. entity into a British entity for purposes of U.S. trades on the platform with the principal regulation of those trades in the hands of the United Kingdom.

And, why should NYMEX not do this? It is following precisely the ICE template. However, the proposal defies all good sense, and, even worse, it will add darkness to the trading markets that affect the price of crude oil, gasoline, and heating oil within the U.S.

Under the ICE, DME and London/NYMEX scenarios, each of these exchanges are clearly U.S. exchanges and their trading terminals should be regulated as U.S. regulated contract markets. Moreover, as U.S. contract markets, they and the traders on those exchanges (no matter whether they trade in the U.S. or abroad) are fully subject to both CFTC civil jurisdiction and United States federal criminal statutes.[62] For example, in *Tamari v. Bache*[63] the Seventh Circuit held there was federal jurisdiction to enforce the Commodity Exchange Act, even though the trader and the trader's broker accused of fraud were both situated in Lebanon,[64] by stating: "that Congress intended to proscribe fraudulent conduct associated with any commodity future transactions executed on a domestic exchange, regardless of the location of the agents that facilitate the trading" and thus there was jurisdiction.[65]

The CFTC Has Consistently Viewed Foreign Exchanges Trading on U.S. Terminals Subject to Full U.S. Regulation

It has been shown immediately above, that as a legal matter there is no bar either within the CEA as now drafted nor within the case law that prevents the CFTC from gaining full regulatory control, over any futures trading done in the U.S Even if one were to assume that ICE, for example, is truly a foreign board of trade, Section 4 (b) only bars regulation of trading done by foreign citizens in foreign countries trading foreign commodities on foreign exchanges when such trading does not cause substantial dysfunctions to U.S. markets. Below it is shown that this well established law has governed the CFTC's FBOT staff no action process since its inception.

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[62] JOHNSON & HAZEN, *supra* note 42, at 986 (citing In the Matter of Ralli Brothers Bankers, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23, 314 (1986)).
[63] 730 F.2d 1103 (7th Cir. 1984).
[64] *Id*. at 1104-05.
[65] *Id*. at 1108; JOHNSON & HAZEN, *supra* note 42, at 987.

The staff no action process initiated in 1999 was not developed under a view that, pursuant to Section 4 (b), the CFTC could not regulate foreign exchanges who wished to put trading terminals in the U.S. To the contrary, the history is clear that those foreign exchanges themselves recognized that, in the absence of an exemption under Section 4 (c) of the CEA,[66] they would have to fully register as a U.S. contract market. As their plain language made clear when they were first issued in 1999, the FBOT no action letters originated from a rulemaking proceeding that, by its very terms, indicated that permission to put terminals in the U.S. derived from Section 4 (c)'s exemption from full regulation and not from Section 4 (b)'s absolute bar against foreign regulation.[67] It must be remembered that Section 4 (b) does not countenance exceptions to its general restriction. The no action letters include a myriad of regulatory conditions on the foreign boards of trade that are completely inconsistent with the absolute bar within Section 4 (b).[68]

If there were any doubt about the above analysis, it was belied by the actions of the CFTC on June 17, 2008 and July 8, 2008, when it added four new conditions to the existing ICE Futures Europe and Dubai Mercantile Exchange no action letters.[69] While these additional conditions have only been applied to ICE and DME, Acting Chairman Lukken's related comments show that the CFTC has the authority to incorporate them in the now outstanding 14

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[66] Written Testimony of Professor Michael Greenberger, *Energy Speculation: Is Greater Regulation Necessary to Stop Price Manipulation?: Hearing Before the H. Subcomm. On Oversight and Investigations*, 14-15 (2007), *available at* http://digitalcommons.law.umaryland.edu/cgi/viewcontent.cgi?article=1011&context=cong_test (last visited July 8, 2008).

[67] *See, e.g.,* LIFFE Administration & Management, CFTC No-Action Letter, 1999 CFTC Ltr. LEXIS 38, 4-5 (July 23, 1999); Access to Automated Boards of Trade (proposed rules), 64 Fed. Reg. 14,159, 14,174 (Mar. 24, 1999). As the proposed rules explained,

> Section 4(c) of the Act provides the Commission with authority "by rule, regulation, or order" to exempt "any agreement, contract or transaction" from the requirements of Section 4(a) of the act if the Commission determines that the exemption would be consistent with the public interest, that the contracts would be entered into solely by appropriate persons and that the exemption would not have a material adverse effect on the ability of the Commission or any contract market to discharge its regulatory or self-regulatory duties under the Act. *Id*. (internal citations omitted).

[68] Among the conditions present in all of the no action letters are the following: the exchange will satisfy the appropriate designation in its home jurisdiction, the exchange must work to ensure fair markets that prohibit fraud and other abuses by providing adequate supervision, continued adherence to IOSCO Principles for Oversight of Screen-Based Trading Systems for Derivative Products, members and guaranteed customers will only receive direct access if a clearing member guarantees and assumes all financial liability, there are sufficient safeguards to prevent unauthorized access or trading, at the Commission's request recipients will provide market information including access to books and records, and will submit all contracts to be made available through the no-action process, the volume of said trades and a list of names and addresses of all those using these exchanges. *See, e.g.,* LIFFE Administration and Management, CFTC No-Action Letter, 1999 CFTC Ltr. LEXIS 38, 65-72 (July 23, 1999); IPE, CFTC No-Action Letter, 1999 CFTC Ltr. LEXIS 152, 58-66 (Nov. 12, 1999); Dubai Mercantile Exchange Ltd., CFTC No-Action Letter, 2007 CFTC Ltr. LEXIS 6, 87-96 (May 24, 2007).

[69] Amendment to No-Action Letter Issued to the International Petroleum Exchange of London (now ICE Futures Europe), CFTC No-Action Letter, (June 17, 2008), *available at* http://www.cftc.gov/stellent/groups/public/@lrlettergeneral/documents/letter/08-09.pdf (last visited July 8, 2008); Press Release, CFTC, CFTC Conditions Foreign Access on Adoption of Position Limits on London Crude Oil Contract (June 17, 2008) *available at* http://www.cftc.gov/newsroom/generalpressreleases/2008/pr5511-08.html (last visited July 8, 2008).

other FBOT staff no action letters affecting every foreign board of trade with U.S. terminals, as well as any FBOT that seeks an exemption from U.S. direct regulation in the future.[70]

If Section 4 (b)'s absolute prohibition were applicable to FBOTs with U.S. terminals, as some have argued as a predicate to limiting legislative or administrative action in this area, how could the CFTC add these new conditions to the outstanding no action letters? Those new conditions, *inter alia*, require large trader reporting and the imposition of speculation limits.[71] The failure of the FBOTs to comply could result in the revocation of the no action letters, thereby requiring each FBOT to register as a fully regulated U.S. contract market.[72]

Those who would attempt to limit Congressional and regulatory controls on ICE, DME, and NYMEX/London have also relied upon a November 2006 policy statement issued by the CFTC on the FBOT no action letter process.[73] Much is made about the fact that Section 4 (b) is cited and quoted therein. Whatever the purpose of that 4 (b) reference, the assertion that 4 (b) presents an absolute bar is belied by the following within that policy statement:

> [i]n the absence of no-action relief, a board of trade, exchange or market that permits direct access by U.S. persons might be subject to Commission action for violation of, among other provisions, section 4(a) of the CEA, if it were not found to qualify for the exclusion from the DCM designation or DTEF registration requirement.[74]

In short, the failure to gain no action relief would mean that, in the absence of registration as a fully regulated contract market, the FBOT would have to remove its U.S. terminals according to the CFTC's own analysis. As the CFTC expressly stated in its June17, 2008 letter to ICE imposing the new conditions on its no action status, if ICE satisfies the four new conditions, the CFTC "will not recommend that the Commission institute enforcement action against [ICE] based upon [ICE's] failure to seek contract market designation or registration as a DTEF under Sections 5 and 5a of the Act."

Again, the action of the CFTC adding further conditions to the ICE no action letter, including large trader reporting and speculation limits, upon pain of an enforcement proceeding based on the failure to register as a U.S. regulated contract market, clearly demonstrates that the CFTC meant what it said in the above quoted reference from its 2006 policy statement, it has

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[70] Press Release, CFTC, CFTC Conditions Foreign Access on Adoption of Position Limits on London Crude Oil Contract (June 17, 2008) *available at* http://www.cftc.gov/newsroom/generalpressreleases/2008/pr5511-08.html (last visited July 8, 2008). As Acting Chairman Lukken stated,

> These new conditions for foreign access will provide the CFTC with additional oversight tools to monitor linked contracts. This powerful combination of enhanced trading data and additional market controls will help the CFTC in its surveillance of regulated domestic exchanges, while preserving the important benefits of our international recognition program that has enabled proper global oversight during the last decade. This raises the bar for all future foreign access requests and will ensure uniform oversight of linked contracts. *Id*.

[71] Amendment to No-Action Letter Issued to the International Petroleum Exchange of London (now ICE Futures Europe), CFTC No-Action Letter, (June 17, 2008) *available at* http://www.cftc.gov/stellent/groups/public/@lrlettergeneral/documents/letter/08-09.pdf (last visited July 8, 2008).

[72] *See supra* notes 68-70 and accompanying text.

[73] Boards of Trade Located Outside of the United States and No-Action Relief from the Requirement to Become a Designated Contract Market or Derivatives Transaction Execution Facility, 71 Fed. Reg. 64,443 (Nov. 2, 2006).

[74] *Id*. at 64,445 n.23.

broad powers to require a "foreign" exchange to fully register in the U.S. or terminate its presence in this country.[75] Section 4 (b) provides no impediment to those powers.

Efforts Designed to Oversee and Improve the Foreign Regulation of U.S. Delivered Futures on U.S. Terminals May Not Effectively Close the "London/Dubai" Loophole

Congressman Etheridge of this Committee[76] and Senators Durbin and Levin in the Senate have introduced legislation which ratchets up the existing CFTC oversight of foreign boards of trade energy futures trading on U.S. trading terminals ("FBOTs"). That legislation, while a major improvement over the present regulatory environment, still leaves primary and direct enforcement and oversight in the hands of the foreign regulator, *e.g.*, the U.K.'s Financial Services Authority in the case of ICE; or the Dubai Financial Services Authority in the case of the DME.

It is my understanding the this legislation deferring to the primacy of foreign regulators to oversee U.S. terminals operated by FBOTs derives from a concern that section 4 (b) of the Act bars U.S. regulation of even those FBOTs in the U.S.[77] As has been shown above,[78] section 4 (b), whatever it means, is an absolute bar to any U.S. regulation,[79] whereas H. 6334 does ratchet up U.S. regulation of the foreign exchange. Moreover, as shown above,[80] section 4 (b)'s bar only applies to foreign trades on foreign exchanges of foreign commodities not having a significant impact on U.S. markets. Therefore, policy concerns about section 4 (b) should not govern the regulation of FBOT terminals in the U.S., especially when those terminals trade U.S. delivered futures contracts; and even more so when the FBOTs institutional ties are so closely affiliated with the U.S. and U.S. institutions that the FBOT loses all claim to foreign status.

Again, legislation such as that proposed by Congressman Etheridge, is a major improvement of what had been the CFTC's oversight of FBOTs' U.S. terminals.

This kind of legislation affords the CFTC the authority to enforce the prohibitions of section 9 of the Act, concerning criminal penalties, including anti-manipulation prohibitions therein, and "to limit, reduce, or liquidate any position" on the FBOT in aid of preventing, *inter alia*, manipulation and excessive speculation enforcement.[81] Imposition of restrictions on the FBOT, however, must be preceded by consultation with the FBOTs foreign regulator.[82]

The CFTC "may apply such recordkeeping requirements [to the FBOT] as the Commission determines are necessary,"[83] and before the CFTC exempts an FBOT from full U.S.

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[75] Amendment to No-Action Letter Issued to the International Petroleum Exchange of London (now ICE Futures Europe), CFTC No-Action Letter, (June 17, 2008) *available at* http://www.cftc.gov/stellent/groups/public/@lrlettergeneral/documents/letter/08-09.pdf (last visited July 8, 2008).
[76] H.R. 6334.
[77] *See supra* notes 41-42 and accompanying text.
[78] *See supra* notes 43-60 and accompanying text.
[79] *See supra* notes 43-60 and accompanying text.
[80] *See supra* note 42 and accompanying text.
[81] *See* S. 3130 § 7, 110th Cong. (2008), *available at* http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_cong_bills&docid=f:s3130is.txt.pdf (last visited July 8, 2008).
[82] *See id.*
[83] *Id.*

contract market regulatory requirements, it must ensure that the FBOT operating the U.S. terminals "appl[y] comparable principles" to those of the CFTC for "daily publication of trading information and position limits or accountability levels for speculators" and provides to the CFTC "the information that the [CFTC] determines necessary to publish a Commitment of Traders report" for U.S regulated contract markets.[84]

Legislation of the kind introduced by Congressman Etheridge also requires the CFTC to conduct a review of FBOT no action status for existing FBOTs between the first anniversary of the passage of S. 3130 and one and one half years thereafter to ensure FBOT compliance with the new statutory requirements imposed by this legislation.[85]

In any event, recent actions taken by the CFTC to increase regulation of ICE and DME may place the requirements of Congressman Etheridge's bill in a new context.

CFTC's New Regulatory Requirements for Foreign Boards of Trade with U.S. Terminals

For at least two years prior to May 20, 2008, the CFTC had repeatedly assured Congress and market participants that the dramatic rise in crude oil, natural gas, gasoline, and heating oil was caused exclusively by supply/demand market fundamentals.[86] The CFTC had based its conclusions on its "exhaustive" research of all relevant market data.[87]

Indeed, as recently as May 20, 2008, before the full Senate Homeland Security and Government Affairs Committee, the CFTC's Mr. Harris, testified: "[A]ll the data modeling and analysis we have done to date indicates there is little economic evidence to demonstrate that prices are being systematically driven by speculators in these [agriculture and energy] markets....

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[84] *Id.* at §6.
[85] *Id.* at §11.
[86] Walt Lukken, Acting Chairman, CFTC, Prepared Remarks: Compliance and Enforcement in Energy Markets--The CFTC Perspective (Jan. 18, 2008), *available at* http://www.cftc.gov/stellent/groups/public/@newsroom/documents/speechandtestimony/opalukken-34.pdf (last visited June 21, 2008) (quoting Mr. Walter Lukken "While speculators play a integral role in the futures markets, the report concludes that speculative buying, as a whole, does not appear to drive up price"); Tina Seeley, *Energy Market Not Manipulated, U.S. Regulator Says (Update1),* BLOOMBERG.COM (May 7, 2008), *available at* http://www.bloomberg.com/apps/news?pid=20601072&sid=aX0iaEd9bOMU&refer=energy (last visited June 21, 2008) (quoting Mr. Walter Lukken, "We have not seen that speculators are a major factor in driving these prices"); Ian Talley & Stephen Power, *Regulator Faults Energy-Futures Proposal*, WALL ST. J. (May 8, 2008) (stating that Mr. Walter Lukken commented that his agency hadn't seen evidence indicating that speculators are "a major factor" in driving up oil prices); Oral Testimony of Walter L. Lukken, Commissioner, CFTC, *Before the Committee on Agriculture, U.S. House of Representatives*, (April 27, 2006) (quoting Mr. Walter Lukken "[B]ased on our surveillance efforts to date, we believe that crude oil and gasoline futures markets have been accurately reflecting the underlying fundamentals of these markets"); Sharon Brown-Hruska, Chairman, CFTC, Address before the International Monetary Fund: Futures Markets in the Energy Sector (Jun. 15, 2006), *available a*t http://www.cftc.gov/newsroom/speechestestimony/opabrownhruska-46.html (last visited Jun. 21, 2008) (stating "To date, the staff' findings have shown that these large speculators as a group tend to inject liquidity into the markets rather than having an undue impact on price movements"); Sharon Brown-Hruska, Chairman, CFTC, Keynote Address at the Managed Funds Association Annual Forum (Jun. 25, 2005), *available at* http://www.cftc.gov/opa/speeches05/opabrownhruska34.htm (last visited June 21, 2008) (stating the CFTC's study of the role of managed funds in our markets, "[C]ontradicts with force the anecdotal observations and conventional wisdom regarding hedge funds and speculators, in general.").
[87] *See, e.g., supra* note 86 and accompanying text.

[O]ur *comprehensive* analysis of the *actual* position data of these traders fails to support [the] contention" that there is excessive speculation or manipulation.[88] Rather, he said "prices are being driven by powerful economic fundamental forces and the laws of supply demand."[89]

In a rather dramatic about face, the CFTC suddenly announced on May 29, 2008 (or just nine days after Mr. Harris testimony) that that agency is in the midst of an investigation into the crude oil energy markets[90] and it will now begin to collect substantial amounts of new data to determine what is undergirding high oil prices.[91] This reversal in course is almost certainly the product of intense pressure placed on the CFTC by Congress to ensure that excessive speculative activity is not being conducted on the principal market over which the CFTC has declined primary responsibility, i.e., trading done on ICE and on ICE's U.S. terminals.[92]

As crude oil and gas prices continued to spike even after the CFTC's May 29, 2008, announcement, the pressure on the CFTC did not let up. Thus, by June 17, 2008, the CFTC once again increased its pressure on ICE.

In a dramatic June 17, 2008 letter to ICE, the CFTC Director of Market Oversight referenced the fact that ICE had moved its trading platform from London "to the ICE Platform operated by [ICE] in Atlanta, Georgia," and that that U.S. platform was now trading three U.S. delivered energy futures products (WTI, heating oil, and gasoline) "each of which is cash-settled

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[88] Written Testimony of Jeffrey Harris, Chief Economist, CFTC, *Before the Senate Committee on Homeland Security and Governmental Affairs, United States Senate* 20 (2008), *available at* http://www.cftc.gov/stellent/groups/public/@newsroom/documents/speechandtestimony/oeajeffharristestimony052008.pdf (last visited June 21, 2008).

[89] *Id.*; *see, e.g.*, Richard Hill, *Lieberman Says He Will Consider Legislation to Address Commodity Prices*, 40 BUREAU OF NAT'L. AFF. 21 (May 26, 2008) (emphasis added), *available at* http://corplawcenter.bna.com/pic2/clb.nsf/id/BNAP-7EVTDG?OpenDocument (last visited June 21, 2008).

[90] CFTC Commissioner Bart Chilton has acknowledged that the public announcement within the May 29 release raises the specter that "some people [will] head for the paper shredder [.]" Tina Seeley, *CFTC Targets Shipping, Storage in Oil Investigation (Update2)*, BLOOMBERG.COM (May 30, 2008), *available at* http://www.bloomberg.com/apps/news?pid=20601087&sid=aGzRMmD_b9MA&refer=home (last visited June 21, 2008).

[91] Press Release, U.S. Commodity Futures Trading Commission, CFTC Announces Multiple Energy Market Initiatives (May 29, 2008), *available at* http://www.cftc.gov/newsroom/generalpressreleases/2008/pr5503-08.html (last visited June 21, 2008).

[92] *See* Letter from Twenty-Two Senators to Walter Lukken, Acting Chairman, CFTC (May 23, 2008), *available at* http://cantwell.senate.gov/news/record.cfm?id=298325 (last visited June 21, 2008) (insisting that CFTC require ICE to demonstrate why it should not be subject to the same regulation as other U.S.-based exchanges and warning, "[a]bsent expeditious Commission action, Congress may need to step in to protect consumers and ensure that all markets trading U.S. delivered energy futures are transparent and free of fraud, manipulation, and excessive speculation"); Letter from Senator Jeff Bingaman to Walter Lukken, Acting Chairman, CFTC (May 27, 2008), *available at* http://energy.senate.gov/public/index.cfm?FuseAction=PressReleases.Detail&PressRelease_id=0fdd0eb4-4b1d-49f0-a3a2-f89fd0e4b1d3&Month=5&Year=2008&Party=0 (last visited June 21, 2008) (expressing concern that 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" and demanding an explanation of many CFTC activities); *Energy Speculation: Is Greater Regulation Necessary to Stop Price Manipulation?: Hearing Before the House Subcomm. on Oversight & Investigations*, 110th Cong. (2007) (statement of Rep. Joe Barton, Member, House Subcomm. on Investigations) (informing Walter Lukken, Acting Chairman, CFTC, that Congressed had empowered FERC to provide additional regulation in some energy markets because they were displeased with the CFTC's efforts).

on the price of physically-settled contracts traded on NYMEX."[93] Most importantly, the June 17 letter to ICE then stated:

> A foreign board of trade listing for trading a contract which settles on the price of a contract traded on a CFTC-regulated exchange *raises very serious concerns* for the Commission. . . . In the absence of preventive measures at [ICE], this circumstance *could compromise the [CFTC's] ability to carry out its market surveillance responsibilities*, as well as the integrity of prices established on CFTC-regulated exchanges. . .[T]he division retains the authority to condition further, modify, suspend, terminate, or otherwise restrict the terms of the no-action relief provided herein, in its discretion.[94]

In order to address the CFTC's "very serious concerns" that it had "compromise[d] [its own] ability to carry out its market surveillance responsibilities, as well as the integrity of the prices established" thereon, the letter then outlined four new conditions that it imposed upon ICE: "position limits or position accountability levels (including related hedge exemption provisions) as adopted by" U.S. regulated contract markets; quarterly reports of any member exceeding those levels and limits; publication of daily trading information comparable to that required of U.S. contract markets; daily reporting of "large trader positions" as provided by U.S. regulated markets.[95]

ICE was given 120 days to come into compliance with the new CFTC conditions.[96] The CFTC acknowledged that the new ICE rules would have to be approved by the FSA.[97] The June 17 letter to ICE concludes by stating that only if ICE complies with the conditions outlined therein can ICE be assured that the CFTC will "not recommend that the Commission institute enforcement action against [ICE] or its members" based on ICE's failure to register as a U.S. regulated contract market.[98]

On June 17, 2008, the day that that letter to ICE was released, CFTC Acting Chairman Lukken is reported to have told the Senate oversight committee: "The CFTC will also require other foreign exchanges that seek such direct access to provide the CFTC with comparable large trader reports and to impose comparable position and accountability limits for any products linked with US regulated futures contracts[.]" [99] On July 7, 2008, an identical CFTC staff letter was written to the DME.

It would seem that much of what the CFTC has done implements the data collection requirements included in Congressman Etheridge's bill. Indeed, the CFTC's threat of enforcement authority against ICE in its June 17, 2008 letter, while limited for these purposes to failing to register as a U.S. regulated contract market, would seem to make it clear that that agency could enforce all civil and criminal penalties asserted throughout the CEA against ICE

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[93] Amendment to No-Action Letter Issued to the International Petroleum Exchange of London (now ICE Futures Europe), CFTC No-Action Letter 2 (June 17, 2008), *available at* http://www.cftc.gov/stellent/groups/public/@lrlettergeneral/documents/letter/08-09.pdf (last visited June 20, 2008).

[94] *Id.*

[95] *Id*. at 3.

[96] *Id*.

[97] *Id*.

[98] *Id*.

[99] Nick Snow, *US CFTC Unveils New Foreign Market Data Pact*, OIL & GAS J., (June 18, 2008), *available at* http://www.mapsearch.com/news/display.html?id=332086 (last visited June 21, 2008).

and its members if appropriate, thereby possibly even exceeding the grant of section 9 enforcement powers afforded the CFTC with regard to FBOTs in S. 3130.

As will be shown below, however, the present skyrocketing cost of crude oil and its derivative products, as well as the resulting destabilization of the U.S. economy, would seem to counsel the use of the full force of the CFTC's powers to bring ICE and similar "foreign" exchanges with trading terminals in the U.S. trading futures premised on U.S. delivered energy commodities under complete, direct, and real time U.S. regulatory control.

Deference to Foreign Regulators over U.S. Energy Futures Trading Deprives U.S. Energy Markets and U.S. Energy Consumers of the Full Weight of CEA Protections

The question arises whether the U.S. should continue to regulate FBOT trading of U.S. energy futures on U.S. terminals principally through foreign regulators while requiring more aggressive CFTC oversight of that process. Or, should trading of U.S. delivered energy products on U.S. terminals be deemed a sufficient nexus to the U.S. and the well being of its economy to require direct U.S. supervision. If Congress settles for the status quo as evidenced by the CFTC's most recent actions if forsakes a wealth of traditional regulatory tools that the CFTC has to ensure that U.S. energy markets and prices are rooted in economic fundamentals.

The Lack of Emergency Authority to Intervene in Market Distortions. The most substantial risk in following the CFTC policy of leaving ICE and other similarly situated "foreign" exchanges under the principal supervision of foreign regulators while those exchanges have U.S. terminals trading critically important U.S. delivered energy products is that the CFTC cannot exercise its broad emergency authority to intervene immediately when confronted with emergencies and dysfunctions on U.S. regulated contract markets.[100]

Described as the CEA's "most potent tool," section 8a (9) provides that "whenever [the CFTC] has *reason to believe* that an emergency exists," it may take such actions "including, but not limited to "the setting of temporary emergency margin levels on any futures contract [and] the fixing of limits that may apply to a market position."[101] An "emergency" is defined:

> "to mean, in addition to threatened or actual market manipulations and corners, any act the United states or a foreign government affecting a commodity or any other major market disturbance *which prevents the market from accurately reflecting the forces of supply demand for such commodity*."[102]

It should be born in mind that these emergency powers afford the CFTC the *immediate* right to alter on a real time basis margin requirements and speculation and position limits to deal with crises as they arise "*which prevent[] the market from accurately reflecting the forces of supply demand[.]*" While section 8a (9) affords direct judicial review of orders after they are issued in a federal court of appeals, it does not by its terms require emergency orders to be preceded by

[100] JOHNSON & HAZEN, *supra* note 42, at 1218.
[101] 7 U.S.C. § 12a(9) (2008) (emphasis added).
[102] *Id.* (emphasis added).

notice and an opportunity to be heard, thereby ensuring speedy restoration of normal market processes.[103]

When one reads this broad power afforded to the CFTC, one could reasonably ask why it has not been used on days such as Friday, June 6, 2008 when the WTI crude oil futures prices rose nearly $11 per barrel in a single day.[104] That is best explained by the fact that the only real time market data in the hands of the CFTC on that day was from NYMEX—the fully regulated U.S. exchange with speculation limits in place; perhaps if the CFTC had meaningful and real time ICE data on that day, thereby seeing the entirety of the WTI crude oil market, it might have seen a need to intervene under its emergency authority to impose temporary position limits and margin requirements to cool down what was widely viewed as breathtaking volatility.

Of course, even when it receives the ICE data within 120 days of its June 17, 2008 requirements, the CFTC will still not have the authority under the governing CFTC no action letter to use its emergency intervention powers on ICE even though over 60% of ICE U.S. delivered WTI futures trading is done within our own country. Rather than exercising real time emergency authority, the CFTC will have to once again "negotiate" with the FSA to have that U.K. regulator intervene to deal with, *inter alia*, ICE WTI trade matching systems located in Chicago, Illinois.

Moreover, relying upon the FSA to intervene on a real time basis for a "major market disturbance" on a U.S. delivered energy futures contract traded on U.S. terminals is as problematic as a matter of policy as it is as a matter of logistics. Unlike the robust emergency authority given by Congress to the CFTC under section 8a (9), the FSA emergency powers have been implemented in a quite lackluster fashion. While its governing statute affords intervention power[105], FSA makes clear on its web site that the U.K. has translated any such authority when "major operational disruptions" are detected on ICE, to a "Tripartite Standing Committee" that would convene the "Cross Market Business Continuity Group" (CMBCG) to:

> "provide[] a forum for establishing senior-level practitioner views . . . . Its role is advisory: decisions will be for the relevant official or market authorities or for firms themselves either individually or collectively through the agency of the CMBCG. The CMBCG may also have a role in pooling information to help facilitate private sector decisions and workarounds to alleviate pressures on the system."[106]

This U.K. guidance for sharing "views" and for "pooling information" in an "advisory" capacity to "help facilitate private sector" decisions in London is what the U.S. industrial consumers of crude oil and the U.S. gas consuming public are left to fall back upon when WTI crude oil soon skyrockets to $150 per barrel as has been predicted by Morgan Stanley, one of the

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[103] JOHNSON & HAZEN, supra note 42, at 1221-22.
[104] *See* Simon Webb, *OPEC hike unlikely at emergency oil talks*, REUTERSUK, (June 20, 2008), *available at* http://uk.reuters.com/article/oilRpt/idUKL2058919720080620 (last visited July 8, 2008).
[105] § 313(A), Financial Services and Markets Act 2000).
[106] *Developments in financial sector crisis management*, FSA Homepage, *available at* http://www.fsa.gov.uk/Pages/About/Teams/Stability/crisis/index.shtml (last visited July 8, 2008).

founders of ICE.[107] The CFTC's June 17 imposition of new conditions on ICE do not convert the U.K.'s lackluster emergency responses into the vigorous emergency responses called for by U.S. law.

Indeed, any effort by Congress to insist upon "comparability" on emergency powers is futile. As the *Financial Times* has so aptly commented on June 20, 2008, the U.K.'s futures regulator "operates a . . . system of 'credible deterrence' of wrongdoing by *engaging in a dialogue with market participants*. Since the FSA's creation in 1997, it has brought *no* civil or criminal cases in energy markets."[108] In stark contrast, as Acting Chairman Lukken recently proudly reported to Congress: "[s]ince December 2002 to the present time, the [CFTC] has filed a total of 39 enforcement actions charging a total of 64 defendants with violations involving the energy markets," having referred "35 criminal actions concerning energy market misconduct" to the Department of Justice.[109]

The contrast between FSA and CFTC enforcement activity in the energy futures markets under their control is quite remarkable, especially since ICE is responsible for nearly 50% of all crude oil futures contracts traded worldwide and since the CFTC has not had access to meaningful ICE data.[110]

The American gas consuming public's trust in the FSA might also be shaken by the U.K.'s response to the June 17, 2008 CFTC announcement of the imposition of new transparency requirements on ICE's use of U.S. terminals used as a critical part of ICE's control of over 30 % of the U.S. delivered WTI contract. Mr. Stuart Fraser, head of policy at the City of London Corporation, is reported in the *Financial Times* to have called the CFTC June 17 letter "American imperialism," and adding for measure "if a bunch of [S]enators want to get rude about the FSA, that's fine, but don't interfere in *our* market."[111]

Of course, the UK is wrong to think trading on U.S. terminals of the U.S. WTI contract is "their" market. ICE is U.S. owned, operated in Atlanta with trading terminals and engines in the

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[107] Tim Paradis, *Stocks decline in jobs data, surge in oil prices*, ASSOCIATED PRESS (June 6, 2008), available at http://ap.google.com/article/ALeqM5gHs5OM3gFG_DytQQZFbWfgPT08MAD914K0H80 (last visited July 8, 2008). Goldman Sachs, also one of the founders of ICE, has predicted that the price per barrel of crude oil will surpass $200 by October of this year. Neil King Jr. and Spencer Swartz, *U.S. News: Some See Oil at $150 This Year --- Range of Factors May Sustain Surge; $4.50-a-Gallon Gas*, WALL ST. J. (May 7, 2008) at A3; Greenberger, *supra* note 21, at 7.

[108] Jeremy Grant, *ICE restrictions cold comfort for FSA*, FINANCIAL TIMES (June 20, 2008) (emphasis added), *available at* http://www.ft.com/cms/s/0/2ba33a0e-3e35-11dd-b16d-0000779fd2ac.html (last visited July 8, 2008).

[109] Written testimony of Acting Chairman Walter Lukken, *Hearing Before the Senate Appropriations Subcommittee on Financial Services and General Government And The Senate Committee on Agriculture, Nutrition and Forestry* 4 (2008), *available at* http://www.cftc.gov/stellent/groups/public/@newsroom/documents/speechandtestimony/opalukken-41.pdf (last visited July 8, 2008).

[110] Intercontinental Exchange, Inc., Annual Report Form (10-K) at 63 (Dec. 31, 2007) *available at* http://www.secinfo.com/dsVsf.tU7.htm (last visited July 8, 2008) (showing that ICE's total crude oil futures market share is 47.8%).

[111] Jeremy Grant, *Storm over push for regulatory reform on positions at ICE*, FINANCIAL TIMES (June 20, 2008) (emphasis added), *available at* http://www.ft.com/cms/s/0/a00c6a00-3e62-11dd-b16d-0000779fd2ac.html (last visited July 8, 2008).

U.S. and trading over 30% of U.S. delivered crude oil futures market in U.S. dollar denominated currency.

However, one could easily see how those officials in the U.K. might mistakenly view WTI trading on U.S. terminals as "their" market when the CFTC and ICE continue to refer to this self evidently "U.S." market as being conducted on a "foreign" exchange. If the CFTC were to flatly state the obvious (*i.e.*, ICE Futures Europe is wholly owned by a U.S. concern, having brought the corpus of the old British International Petroleum Exchange, for all intents and purposes, to the U.S.). the UK might grasp the reality of the situation, rather than the ICE perpetuated "London" myth.

Deferring to Foreign Regulators Undercuts the Self Regulatory and Surveillance Requirements of U.S. Law.

Next to the inability to exercise the extraordinary emergency powers afforded the CFTC to oversee its markets by deferring to the foreign regulators to supervise U.S. energy futures products on U.S. trading terminals, the most serious problem with further CFTC or Congressional deference to FSA is the foregoing of the substantial self regulation and surveillance provided by U.S. regulated contract markets to assist U.S. regulators in policing futures markets.

The "core principles" within the CEA that must be followed by an approved U.S. regulated contract market emphasize the importance having those markets serve as the first line of defense for the CFTC in detecting fraud, manipulation, excessive speculation, and other unlawful trading malpractices.[112] Without aggressive self-policing of the entirety of the regulated U.S. futures markets, the CFTC simply cannot do its job.

The seriousness with which U.S. regulated markets take their statutorily mandated self-policing and surveillance role is evidenced by NYMEX's "standards and safeguards" concerning trade and market surveillance. For example, NYMEX makes clear:

> Market surveillance is required under CFTC regulations. Each day, the compliance staff compiles a profile of participants, identifying members and their customers holding reportable positions. In addition, daily surveillance is performed to ensure that Exchange prices reflect cash market price movements, that the futures market converges with the cash market at contract expiration, and *that there are no price distortions and no market manipulation*. . . .[113]

As to trade surveillance, NYMEX provides:

> Compliance department analysts are trained to spot instances of misconduct, including "front running" or trading ahead of a customer; wash or accommodation trading

[112] 7 U.S.C. § 7(d)(2)-(6) (2008); (2) (compliance with rules); (3) (contracts not readily subject to manipulation); (4) (monitoring of trading); (5) (position limits); (6) (emergency authority); 7 U.S.C. § 7a(d)(2)-(3) (2008); (2) (compliance with rules); (3) (monitoring of trading).
[113] NYMEX, Enforcement of Exchange Rules, *available at* http://www.nymex.com/ss_main.aspx?pg=6 (last visited July 8, 2008) (emphasis added).

(transactions creating the appearance of trading activity, but which have no real economic effect); prohibited cross trading (trading directly or indirectly with a customer except under very limited circumstances, or matching two customer orders without offering them competitively); prearranged trading; and non-competitive trading.[114]

NYMEX reports that is has @ $6.5 million budget for oversight market surveillance with an enforcement staff of @ 40 personnel.

No detailed analysis of ICE's self-regulatory and surveillance system is required. Suffice it to say, that for all of ICE's worldwide markets which are accessible by the U.S. trading terminals, including the U.S. WTI contract, reports are that ICE employs no more than ten individuals on its surveillance staff, i.e., a staff that is one quarter the size of NYMEX. This staff monitors trading of a host of ICE contracts, including those contracts which control over 47% of the world crude oil futures.[115] Of course, for those energy futures trades ICE executes under the Enron Loophole (because those trades do not derive from the old-IPE), such as the critical Henry Hub U.S. delivered natural gas futures contract, ICE, as of now, has *no* self-regulation or surveillance system.

Moreover, leaving ICE's paltry surveillance resources to the side, the principal regulator to which the CFTC is deferring to oversee directly over 30% of U.S. delivered WTI contracts, the U.K.'s FSA, has only "two full time supervisors," monitoring all of the ICE contracts under their jurisdiction.[116] Again, this includes 47% of world's energy futures contracts.

In sum, even though the CFTC has ratcheted up ICE's regulatory obligations by adding large trader reporting and speculation limits to the WTI trading, it defers to the FSA for the remainder of the oversight of ICE. In effect, this deference to the U.K. for U.S. trading of the critically important WTI contracts surrenders emergency authority to intervene when there are market dysfunctions to impose temporary margin requirements and position limits; and it sacrifices the real "eyes and ears" policing these markets (i.e., the regulated exchanges themselves) by depending upon ICE's meager surveillance systems.

In a time of economic distress for American industry and the American consumer caused by skyrocketing energy prices, this country cannot afford to outsource authority to the UK to oversee trading on 30% of our own U.S. delivered crude oil futures contracts, much of which is consummated on U.S. based trading terminals and all of which is trade matched in Chicago, Illinois.

Finally, it bears repeating that during last summer's subprime mortgage crisis, Northern Rock PLC, one of the U.K.'s largest banks, was required to borrow billions of dollars from the U.K.'s central bank.[117] After news of the bailout was released to the public, thousands of customers wary of losing their savings stood in long lines for several days outside of Northern

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[114] *Id.*

[115] *See supra* note 109 and accompanying text.

[116] Grant, *supra* note 108.

[117] *See Rock Expects £30bn Loan this Year*, BBC NEWS (Nov. 7, 2007), *available at* http://news.bbc.co.uk/1/hi/business/7073556.stm (last visited July 8, 2008).

Rock's branches to withdraw deposits.[118] With Northern Rock on the brink of collapse, the FSA provided over $100 billion in loans to the bank and in February 2008, the British government finally was required to nationalize it.[119] In March 2008, FSA published an internal report stating that its regulation of Northern Rock "was not carried out to a standard that is acceptable," and highlighted its own failure to provide adequate supervision, oversight, and resources.[120] In addition to FSA's self-criticism, in April 2008, the European Union opened a formal investigation into FSA's restructuring of Northern Rock.[121]

This episode, maybe more than any other, reveals that Congress cannot afford to leave direct oversight of trading on U.S. terminals of the most important futures contract in determining the price of oil, gasoline, and heating oil. As demonstrated above,[122] Congress has the full authority to pass legislation placing those U.S. terminals under U.S. regulatory control.

Threats that the U.S. reassertion of regulatory control over trading within the U.S. will drive trading overseas are undercut by the reality of every major futures foreign exchange having set up shop in the U.S.; and by the well documented law described above that even a foreign trader in a foreign country who illegally disrupts U.S. markets is subject to the full force and effect of that law.

Finally, contrary to the assertion of the City of London Corporation, this is not a "British" market; it is a U.S. market principally being traded in the U.S. by a trading entity controlled by a U.S. corporation. The economic distress now being suffered by Americans over high energy products cannot be placed in the hands of foreign governments when those products are traded here and have such a huge impact on our economy.

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[118] *See Crisis Deepens for Northern Rock*, REUTERS (Sep. 17, 2007), *available at* http://www.iht.com/articles/2007/09/17/asia/17northern.php (last visited July 8, 2008).

[119] *See* Stephen Castle, *EU to Investigate Northern Rock Nationalization in Britain*, INTERNATIONAL HERALD TRIBUNE (April 2, 2008), *available at* http://www.iht.com/articles/2008/04/02/business/rock.php (last visited July 8, 2008).

[120] *See British Regulator Admits Failings in Oversight of Northern Rock, Announces New Procedures*, ASSOCIATED PRESS (March 26), 2008, *available at* http://www1.wsvn.com/news/articles/world/MI81198/ (last visited July 8, 2008).

[121] *See* Castle, *supra* note 119.

[122] *See supra* notes 41-60 and accompanying text.