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Dissenting View Of CFTC Energy And Environmental Markets Advisory Committee Member Tyson Slocum, Energy Program Director, Public Citizen, Inc.

First, it is important that I recognize the work of Commissioner Giancarlo and the other eight members of the Energy and Environmental Markets Advisory Committee (EEMAC). While I vigorously disagree with the conclusions of the report to which the other Members have agreed to endorse, and to the manner in which it was produced, I appreciate their service, and look forward to constructive dialogue in the future.

Public Citizen is quite different from the other eight members of the Advisory Committee in terms of the constituents we represent, but we are far from alone among those impacted by CFTC-jurisdictional markets. Our members' ability to heat or cool their homes and afford transportation are profoundly impacted by the price formation of energy commodities in CFTC-jurisdictional markets. We believe that Congress clearly understood the need for the CFTC to impose position limits to protect consumers from excessive speculation, and that it should be the priority of the Commission to finalize the current position limits rule.

Our dissent addresses four key areas.

I. The EEMAC 2015 Report Was Not A Collaborative Product Of The EEMAC, Was Authored On The Independent Initiative Of Only Select EEMAC Members, And May Not Be A Valid Product Due To The Co-Authorship By An Individual Not On The Nine-Member Committee At The Time He Co-Authored The Report

According to the EEMAC Charter,¹ the “Objective and Scope” of the EEMAC is to “submit reports and recommendations to the Commission.” Section 751 of Public Law Public Law 111-203 states, in part, that “An Energy and Environmental Markets Advisory Committee is hereby established. The Committee shall have 9 members.”

But the creation, objective and scope of the report at issue here was not conceived as a result of a deliberative process that involved all nine of the EEMAC Members. The assignment of the creation of a report was discussed at neither of EEMAC’s previous two public meetings, nor in any other forum that involved the consultation of all nine Members. Rather, it appears as though the report at issue here was produced through the independent initiative of only two people, including one brand-new member to EEMAC, Dr. Craig Pirrong. In fact, Dr. Pirrong is so new to the EEMAC that I only learned he was a member when he was listed as a co-author of the report at issue here. Neither of the Report co-authors informed me that they were taking initiative to write a report to present later for my review. As

¹ www.cftc.gov/idc/groups/public/@newsroom/documents/file/charter021308.pdf

an EEMAC Member, I was never informed that a report was being written until after the report was already drafted.

This failure to produce a report in a process that actively collaborated with all nine Members of EEMAC results in questions as to whether or not the Report accurately reflects the input of all EEMAC Members.

A truly collaborative process would have resembled this:

- A. The nine Committee Members would meet to discuss forming a subcommittee to produce a report.
- B. The subcommittee would produce a draft to the Members for their review.
- C. Once the nine Members agreed on a draft, they would send it to the full Advisory Committee (including all Associate Members) and schedule a public meeting to discuss the report.
- D. After a public discussion with Associate Members, the nine Members would then vote on the report, or, after consultation with the Associate Members, revise the draft.
- E. The final report would then be submitted to the Commission.

Instead, two individuals, without any formal consultation or authorizations from the full nine Members, wrote a draft report. Instead of submitting that draft report to the nine Members, they submitted it to the office of Commissioner Giancarlo. Giancarlo's office then submitted the draft report to the nine Members, providing us two weeks to review the draft and cast a vote in approval or in dissent. Any dissent would be allowed to produce a minority report.

Furthermore, there is a discrepancy about whether or not one of the co-authors was one of the nine Members at the time he wrote the report. Dr. Pirrong is listed as a co-author of the report, and I first received a copy of his report on February 5, 2016. But the CFTC Order that approved Dr. Pirrong to serve on the nine-Member Committee was not dated until February 17, 2016. It therefore appears as though Dr. Pirrong co-authored a Committee report prior to his service on the Committee. At no time was I contacted about having a non-Committee member contribute to a report for my consideration. It therefore appears as though the Report cannot be considered a valid product of the Committee, as I believe only full Committee members can produce the report.

II. The EEMAC Report Conclusions Appear To Be Partly A Consequence Of Inadequate Membership Diversity

EEMAC is a product of Section 751 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, which states, in part, that the CFTC "shall appoint members with a wide diversity of opinion and who represent a broad spectrum of interests, including hedgers and consumers." It is the view of Public Citizen that the nine members neither represent a "wide diversity of opinion" nor "a broad spectrum of interests." The members include:

- One public interest organization representing household consumers (Public Citizen).
- Two representatives of the oil and gas production industry (ConocoPhillips and the Natural Gas Supply Association).
- One trade association representing investor-owned electric utilities (Edison Electric Institute).
- Two for-profit exchanges and clearinghouses for commodity and financial markets (ICE and CME).

- Two proprietary traders (Vectra Capital and Morgan Stanley/Futures Industry Association).
- One academic affiliated with commodity trading interests.

We understand that no advisory committee membership can always be perfect, but it does appear as though the participation involved in approving the Report is duplicative, and weighted in favor of interests that may have a predisposition to opposing the concept of position limits. The oil and gas production sector, for-profit exchanges and proprietary traders have multiple representatives that could perhaps be swapped for alternate stakeholders speaking for those who find benefit from position limits.

III. The Majority Report’s Conclusion That Position Limits Are Unnecessary Relies On Selective Arguments While Ignoring Significant Research Previously Provided to the CFTC And To Congress

The Report’s sweeping conclusions that the Position Limits mandated by Congress are not “necessary” because of a lack of evidence of excessive speculation rely heavily upon a presentation and comments provided by Dr. Craig Pirrong, who also happens to be the Report’s co-author. The Report concludes: “There is little to no evidence that the CFTC’s Proposed Rule mandating new federal position limits is sufficiently ‘necessary’ to satisfy the explicit requirement under the Commodity Exchange Act. In the absence of evidence of necessity, it is unlikely that any final federal speculative position limit rule could pass a cost/benefit test.”²

Prior to Dr. Pirrong becoming a member of EEMAC, and prior to co-authoring the Report, he gave a presentation as a panelist during our first EEMAC meeting on February 26, 2015. The concern I have with relying so heavily on Dr. Pirrong for analysis on whether or not position limits are necessary to address excessive speculation is that Dr. Pirrong is not necessarily an unbiased, neutral source on this subject. As the *New York Times* revealed, Dr. Pirrong was paid by the International Swaps and Derivatives Association, one of the trade associations suing to block the original position limits rule.³ The *Times* continued that Dr. Pirrong has a long list of paid contracts with energy speculators. Dr. Pirrong did not disclose these financial relationships with financial speculators when he gave his presentation to EEMAC, and that failure calls into question his true independence as an academic researcher.

The EEMAC meetings also failed to provide equal time for academic or other presenters who have provided documentation that excessive speculation is a problem in energy commodity markets that can be successfully addressed by imposing position limits. A recent scholarly article compiled several academic and market participant studies and testimonies documenting excessive speculation in oil markets.⁴ Any of these authors listed in this article could have provided proper balance to a panel in order to present an alternative view. The CFTC also held at least three previous day-long hearings on excessive speculation and position limits that could have been useful for our EEMAC Members to revisit.⁵ Neither of our EEMAC meetings to date featured balanced panels where a variety of conflicting views were presented in an effort to generate discussion among the EEMAC Membership.

² At page 2.

³ David Kocieniewski, “Academics Who Defend Wall St. Reap Reward,” December 27, 2013, www.nytimes.com/2013/12/28/business/academics-who-defend-wall-st-reap-reward.html

⁴ Michael Greenberger, Closing Wall Street’s Commodity and Swaps Betting Parlors: Legal Remedies to Combat Needlessly Gambling Up the Price of Crude Oil Beyond What Market Fundamentals Dictate, 81 *George Washington Law Review* 707 (2013), http://digitalcommons.law.umaryland.edu/fac_pubs/1244/

⁵ See www.gpo.gov/fdsys/pkg/FR-2009-07-21/html/E9-17421.htm and www.cftc.gov/PressRoom/PressReleases/pr5716-09

Furthermore, the Report alleges that there are current liquidity problems in commodity markets, and that the position limits rule may exacerbate this liquidity crunch. One problem with this allegation is that recent data actually shows record volume, volatility and liquidity in crude oil markets: “The CBOE Crude Oil Volatility Index, which measures expectations of price swings, rose to the highest level since February 2009 on Thursday [February 11, 2016] as West Texas Intermediate slumped to a 12-year low. That was accompanied by the highest aggregate trading volumes on record and rising open interest, according to exchange data.”⁶

IV. The CFTC—And Not For-Profit Exchanges—Should Play The Central Role in Establishing Firm Position Limits And Evaluating And Processing Hedge Exemptions

So-called Position Accountability Regimes were in effect at the exchanges when Congress wrote the Dodd-Frank Act. Congress clearly and specifically rejected such “Accountability Regimes” when it directed that the CFTC “shall” establish Position Limits under Section 737 of Dodd-Frank.

Congress did not direct the CFTC to delegate such authorities to the for-profit exchanges. As I mentioned during our second EEMAC meeting, the exchanges are for-profit companies that earn money by charging fees based on trading volume; they collect, package and sell propriety data based on information gleaned from trading activity on their exchanges; and they peddle preferential trading access through co-location and similar services.⁷ Profiting off of these activities can directly interfere with the exchange’s functions as market monitors and enforcers. While the exchanges maintain that they feature strong internal firewalls, the integrity of those firewalls are verified internally, and not by outside parties. And recent enforcement cases brought against the exchanges have exposed problems with these internal firewalls. Unfortunate examples exist where the exchanges sacrifice market integrity in pursuit of higher profits for their own operations. The *Financial Times* reported that CME, in an effort to break into a North Sea oil contract dominated at the time by rival ICE, offered a bonus of as much as \$1 million per month to the largest traders in its new, competing Brent crude futures product.⁸ Such “volume bonuses” undermine efforts to maintain market integrity.

In March 2015, the CFTC forced ICE to pay a \$3 million civil penalty for repeated data reporting violations over a 20-month period. Part of the reason the CFTC demanded ICE pay the civil penalty was due to the company’s insubordination and lack of responsiveness to Commission requests: “ICE did not respond in a timely and satisfactory manner to inquiries from CFTC staff from multiple divisions about these data-reporting issues, including initial inquiries from the Division of Enforcement.”⁹ And the CFTC was forced to sue CME in federal court in 2013 for violating internal firewalls and selling confidential trading information to an outside broker.¹⁰ These transgressions inspire little confidence within the public interest community that for-profit exchanges can be responsible for enforcing critical components of Dodd-Frank.

⁶ Ben Sharples, “Oil Volatility Jumps With Record Trading Amid Price Rout,” *BloombergBusiness*, February 12, 2016, www.bloomberg.com/news/articles/2016-02-12/oil-volatility-surges-with-record-trading-amid-price-rout-chart

⁷ At page 76, www.cftc.gov/idc/groups/public/@aboutcftc/documents/file/emactranscript072915.pdf

⁸ Ajay Makan & Gregory Meyer, “CME under fire over cash for trades in Brent,” August 18, 2013.

⁹ www.cftc.gov/PressRoom/PressReleases/pr7136-15

¹⁰ Kara Scannell, “CFTC sues Nymex over information leaks,” *The Financial Times*, February 21, 2013, www.ft.com/intl/cms/s/0/11e8490e-7c5d-11e2-91d2-00144feabdc0.html

Conclusion

It does not appear as though the Majority Report is a valid product of the nine-Member Advisory Committee, because one of the co-authors does not appear to have been a full member at the time that he wrote it. Furthermore, the nine-Member Advisory Committee never collaborated to specifically authorize the commission of this report. The Report's claim that Position Limits are not necessary relies on selective presentations while ignoring other academic research showing that position limits are necessary. And the for-profit exchanges are inappropriate entities to establish or enforce position limits alternatives. For these reasons, I must respectfully dissent from the Report and issue this Dissent.

Respectfully submitted,

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