U.S. COMMODITY FUTURES TRADING COMMISSION
ENSURING THE INTEGRITY OF THE FUTURES & OPTIONS MARKETS

SPEECHES & TESTIMONY

# Statement of Commissioner Mark Wetjen, Public Meeting of the Commodity Futures Trading Commission

**November 5, 2013**

Thank you, Chairman Gensler, and many thanks to the professional staff for their hard work on these important proposed rulemakings relating to position limits. Today's notice of proposed rulemaking takes an important step towards fulfilling a core mission of the CFTC: to ensure the integrity of the markets we oversee by combating excessive speculation that can cause price volatility. Position limits are the primary policy tools chosen by Congress to accomplish that mission.

## The Dodd-Frank Act Imposed a Mandate on the CFTC to Set Position Limits for Physical Commodity Contracts

Today's release respects that congressional directive and seeks to address a few open legal questions related to the intent and scope of the commission's new position-limits authority under the Dodd-Frank Act. The proposed legal and policy decisions in this rulemaking are not ones of first impression for Congress or this agency. In many cases, they were considered at length during the legislative process, and again during the commission's rulemaking process. Most recently, a federal district court considered whether the Dodd-Frank Act does, in fact, mandate a rule like the one we propose today.

The commission's newest proposal is intended to be responsive to that court's opinion and clear in at least one respect: It concludes that section 4a of the Commodity Exchange Act, considered as an integrated whole, may be reasonably construed to require the commission to impose, at appropriate thresholds, limits on the amount of positions in agricultural and exempt-commodity markets.

The commission reached the conclusions in the document before us only after due deliberation and consideration of its experience and expertise in overseeing the position-limits regime over many decades. I am confident, moreover, that the conclusions are consistent with a plain reading of the statute and the intent of the supporters and drafters of these provisions in the Dodd-Frank Act. It was largely for these reasons that I supported the decision to appeal the district-court ruling last year.

Indeed, there is a reasonable statutory basis for the view that Congress intended position limits to be mandatory with respect to those commodities that the commission has sufficient data on, or experience regulating. For example, the commission's pre-existing position-limits authority was substantially amended by the Dodd-Frank Act, which added multiple new subsections that focus specifically on physical commodities. This buttressed what before had been more generalized authority. In the paragraph providing this new authority, the words "shall" and "require" are repeatedly used, which generally are not the words of optionality but rather the words of mandates.

The placement, intent and meaning of certain modifiers to that language will no doubt be the subject of many comment letters and considered again by the commission before it issues its final position-limits rule. But to conclude that the Dodd-Frank Act's position-limits authority for these contracts is entirely discretionary, would suggest that the statute merely affirmed the commission's pre-existing authority.

I find it implausible that Congress would add many sections of new statutory text to simply affirm authority that the commission already has. Such a conclusion does not seem to comport with the obligatory language used in the statutory amendments, and it does not comport with my understanding of the statute's intent as informed by my experience working as a Senate aide during consideration of these provisions. That experience is affirmed by the amicus brief filed by 19 U.S. senators in support of the commission's appeal, including those senators primarily responsible for the relevant amendments to the Commodity Exchange Act.

I would note, too, that today's release refers to the multiple congressional investigations and findings made prior to the Dodd-Frank Act's passage regarding the impact of

speculative activity on physical-commodity prices. One need not agree or disagree with those findings in order to be persuaded that they informed Congress as it amended the Commodity Exchange Act to provide new authority to the commission.

The futures markets have a long history of embracing speculative position limits as a tool to enhance transparency and minimize manipulation. Today's release builds on that history and finds that position limits are necessary as a prophylactic measure – that is, to lessen the likelihood that a trader will accumulate excessively large speculative positions. Although today's release does not present a specific finding for each referenced contract, I fully expect that public comments pertaining to the selection of such contracts, as a phase-in measure, will be submitted as part of the administrative record and fully considered before finalization of the rules.

I am not convinced at this time that a finding is necessary, as a matter of law, for each referenced contract. In my view, the commission's determination to adopt thresholds for the proposed contracts in the final rule, with the benefit of public comment, could be viewed as an implicit finding by the commission that position limits are necessary in each case. Initially applying position limits to specific contracts as a matter of practicality does not in any way conflict with the commission's general finding that such limits are necessary as a prophylactic measure in the rest of the physical market.

**Bona-Fide Hedging**

I support today's release, but I do have some questions about certain technical aspects of the proposed rules before us.

Today's rule includes modifications to the definition of bona fide hedging based on certain changes in the statutory text. In response to those changes, the staff has recommended a narrower definition, as well as eliminating the present manner in which market participants may seek non-enumerated hedge exemptions.

The federal-position-limits regime, as now applicable to all physical-commodity contracts, reversed a long-standing policy of deferring to the expertise of the exchanges in establishing risk management and hedging exemptions. In recognition of that fact, though, Congress also specifically amended the Commodity Exchange Act to ensure that legitimate hedging activities are not inadvertently curtailed on account of the new approach.

With that in mind, the commission will need to carefully consider whether aspects of the rule adhere closely enough to congressional intent by recognizing appropriately-tailored hedging exemptions, including hedges that (1) represent "substitute[s] for transactions . . . to be made or positions . . . to be taken at a later time in a physical marketing channel" and (2) are put on to manage "potential change[s] in the value of assets that a person anticipates owning, producing, manufacturing, processing, or merchandizing."

The commission must weigh carefully against other public policy objectives the impact that a position-limits regime could have on liquidity in the markets and, in turn, on the commercial firms that rely on these markets to manage risk. Congress gave the agency broad authority to craft a position-limits rule that both protects against excessive speculation and is sensitive to these concerns.

For that reason, I am similarly interested in receiving public comment on the proposal to strike the § 1.47 process for seeking a non-enumerated hedge. It may not be possible, or appropriate, for the commission to determine in advance every conceivable hedging transaction entitled to an exemption. It may, in fact, be the case that certain transactions need to be analyzed and considered on a facts-and-circumstances basis.

Accordingly, I am hopeful that the commission will consider whether and how to best fashion a rule that provides appropriate flexibility as well as a timely response for market participants seeking an exemption. As of now, I am not convinced that requiring market participants to petition the agency to use its exemptive authority provides that desired flexibility and timeliness, especially given the resource constraints that the commission is likely to face in the foreseeable future.

**Aggregation**

Separately, the commission also is considering a new aggregation proposal, which would permit disaggregation for financial and non-financial entities if the commission finds that these entities comply with certain indicia of independence. Importantly, for majority-owned entities, the proposal sets forth a process for applying for potential disaggregation and demonstrating such independence and compliance with new conditions.

This process is largely responsive to comments made to the last aggregation proposal and I look forward to comments on all aspects of this rule.

I am especially interested in receiving comments on whether certain disaggregation filings should be self-executing and remain in effect until the commission notifies the entity that it can no longer reasonably rely upon the filing.

**Conclusion**

While I strongly believe that this commission has a legal mandate to impose a position-limits regime for physical-commodity contracts, I am disappointed in the manner in which that mandate has been pursued. Congress asked the commission to implement position limits before many of the other Dodd-Frank Act rules. Indeed, it directed the commission to act on an extremely ambitious timeline. For those who believe the commission should complete as expeditiously as possible the task Congress mandated, I worry that some of the tactics pursued might have had the opposite effect.

For instance, the commission was faced with the decision of whether to appeal the district court's ruling to vacate the commission's previously finalized rule. The Commission's experienced litigation team made strong legal arguments supporting a mandate, and consequently advised that the odds of winning the appeal were quite good. This is the same team that has enjoyed remarkable success before both district and appellate courts in defending commission rulemakings. For these reasons, and others, I concluded that pursuing an appeal was the right course, and supported the commission's decision to do so.

Since then, however, the commission either made decisions, or failed to make others, that eventually eroded the odds of success before an appellate panel. One of those decisions was to pursue the development of the proposal before us today. By doing so, however, the commission increased the odds that an appellate court would view the appeal as an inappropriate attempt to seek an advisory opinion. As a result, and in the face of insistence by some that a new rule proposal be pursued while the appeal was pending, the litigation team was forced to change course and later recommend that the commission abandon the appeal.

The legal arguments in support of a mandate have never changed – they remain strong and in my view reflect a reasonable reading of the obligations of this commission imposed by the Dodd-Frank Act. Instead, what changed were the tactics used to meet them.

I am disappointed that the commission's appeal had to be dropped, and considerable time and resources squandered as a consequence. I also regret losing the opportunity to defend the commission's interpretation of its own statute, which I believe is the best construction. And had the appellate court found otherwise, I believe it would have provided the commission with useful guidance on how best to implement a position-limits regime.

The consensus at the commission now commends pursuing the new position-limits proposal before us today, which I gladly support given that the appeal is no longer a viable option. Indeed, I believe the statute requires that we propose a new rulemaking in light of the decision to drop the appeal.

I look forward to reviewing the comments responding to the release, and I will devote an especially careful eye to those letters that address some of the specific questions I asked to be included in the document before us.

In closing, I would like to thank the rule-making team as well as the litigation team responsible for defending the commission. Both groups have put in long hours and provided the commissioners with valuable advice prior to this meeting.

So thanks again for your hard work. I look forward to supporting the staff's recommendations.

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