Public Statements & Remarks

Opening Statement of Chairman Heath P. Tarbert in Support of Final Rule on Position Limits

October 15, 2020

I am very proud to bring to a final vote the Commission's rule on speculative position limits. Like my fellow Commissioners and so many who have held these seats before us, I promised during my confirmation hearing that I would work to finalize this rule. So to the Senate Committee on Agriculture, Nutrition, and Forestry, to the market participants who rely on futures markets, and to the American people, I am pleased to say—promise made, promise kept.

Today, we are removing a cloud that has hung over both the CFTC and the derivatives markets for a decade. Market participants, particularly Americans who need these markets to hedge the risks inherent in their businesses, will finally have regulatory certainty.

Long Journey of Position Limits

Ralph Waldo Emerson is quoted as saying "Life is a journey, not a destination." Lucky for him, his journey did not involve position limits. This rule has been one of the most difficult undertakings in CFTC history.

The Commission has issued five position limits proposals over the past 10 years. The first was adopted in 2011, but vacated by the U.S. District Court for the District of Columbia before it took effect. One proposal issued in 2013, and two more in 2016, were never finalized. All told, those four proposals received thousands of comments from the public—the vast majority of which objected to the proposals for good reason. Much ink was spilled, and many trees were felled over those proposals.

Finally, the Commission issued its fifth position limits proposal in January of this year. Today we will finalize that rule. But it is important to note we are not completely rejecting prior attempts. Instead, we build on the good from previous proposals while recognizing and fixing their shortcomings.

Any position limits rule involves a balancing act. To paraphrase a famous saying – *You can please some of the people all the time, and all the people some of the time, but*—as is certainly the case with position limits—*you can't please all the people all the time*.

That is especially true given the three things the Commission is tasked with balancing for position limits:

1. whether position limits on a particular contract are more helpful than harmful;
2. which positions should be subject to the limits and which should not; and
3. at what levels position limits should be set to allow for liquid markets but not excessive speculation.

Recognizing Dead Ends

Prior position limits proposals ultimately failed because they were unable to strike the correct balance on these three points.

First, prior proposals were based on a plausible, but ultimately unsupportable, interpretation—"the mandate." The mandate would mean there is no balancing test; instead, all futures would be subject to federal limits. Given the wide range of futures in our markets, this approach would require the CFTC to evaluate thousands of contracts. It also would necessitate limits on everything—regardless of the benefits those limits would bring or the burdens they would impose.

Second, prior proposals failed to recognize all the ways that participants use futures markets to hedge price risks. Agricultural, energy, and metal futures markets are vital to American businesses, which is why Congress explicitly excluded bona fide hedging positions from position limits. Reading the term bona fide hedging too broadly risks inviting the wolf of speculative activity into the market wearing sheep's clothing. Reading it too narrowly creates the possibility of locking out the businesses that need these markets to manage their risks. And taking away that ability to manage risk jeopardizes economic growth.

As a result, the Commission's prior proposals were too restrictive on what constitutes bona fide hedging. They threw up too many roadblocks for businesses to access futures markets. Ultimately, an overly rigid interpretation of bona fide hedging stood in the way of finalizing a position limits rule.

Finally, prior proposals set limits that were both too low and too rigid. Those limits did not balance the need for liquidity and price discovery against the risks of excessive speculation, which is the real mandate of Congress. The proposed limits were frozen in time, not budging from limits last updated as far back as 1999.

Getting Back on the Right Path

Recognizing the missteps of the past yields a path to success. Unlike prior position limits proposals that garnered a library of negative comment letters, this proposal is overwhelmingly supported by businesses and trade groups across many facets of our real economy.

There are several differences that will let today's rule succeed where others failed.

First, the rule recognizes the limits of limits. Position limits are *one* method to combat corners and squeezes, but that does not mean they are the singular tool that should always be deployed. Position limits are like a medicine that can help cure a disease, but also carries potential side effects. That is why Congress told us to use them only when "necessary." The necessity finding is like a doctor's prescription—someone needs to evaluate the risks of the disease against the side effects.

In addition, the rule takes into account market participants' needs. As I have always said, position limits is the rare case where the exception is as important as the rule. Today's rule lays out a robust set of enumerated bona fide hedge exemptions to ensure that participants in the physical commodity markets can access the futures markets. Building on the proposal, we have added clarity around unfixed price transactions and storage.

The rule also acknowledges the different ways people access the markets. We have streamlined the process for pass-through swap exemptions, making it easier for dealers to provide liquidity to commercial users in the swaps market. And the rule clarifies that someone can take a position during the Commission's 10-day review period of an exchange-granted, non-enumerated exemption. In short, we have built a robust set of enumerated exemptions and a workable non-enumerated exemption process.

The rule also strikes a balance with respect to the limits themselves. The January proposal included significant increases to spot and non-spot limits for the legacy agricultural products. Many commenters were concerned about these increases, particularly for non-spot limits.

The level of the non-spot limits in the final rule are a function of the significant growth in the market and the long delay in making adjustments. Open interest in many of the legacy grains contracts has doubled or tripled since we last updated position limits, reflecting the usefulness of these contracts as a benchmark for cash market transactions and faith in CFTC-regulated markets. The non-spot limits we are adopting are the same percentage of today's open interest as the 2011 limits were compared to open interest back then. Our markets have grown tremendously, and we cannot expect them to be subject to the same limits they were 10 years ago.

It is important to remember that federal position limits are a ceiling, not a floor. Exchanges have their own limits, which can be no higher than what we specify. And exchanges can calibrate those limits quickly to account for issues with deliverable supply or other cash market issues. As we have seen play out over the past decade, the CFTC has a difficult time adjusting position limits. Therefore, exchange-set limits are a way to fine tune position limits on a particular market within the outer bounds of the federal limits. Similar to the process for granting non-enumerated exemptions, we are leveraging the knowledge of the exchanges as well as their ability to act more nimbly to respond to market needs.

Arriving at the Destination

Some of my colleagues may see these features of the final rule as a flaw. While there are significant departures from prior proposals, after four *failed* attempts, that departure is exactly what we need. The flexibility in the necessity finding, the exemption process, and the adjusted limits are what make this rule workable. Otherwise, we are just repeating past mistakes and hoping for a different result—the very definition of insanity.

So let me conclude by saying that we have come a long way. Today we have reached the end of an arduous journey. We have learned from our mistakes and adjusted our approach. We have balanced the interests of all the participants in these markets—some of which are in diametric opposition to one another. Most importantly, we have crafted a workable and flexible system. The rule sets hard limits, but leverages the flexibility of exchanges to adjust for a particular market. The rule recognizes the variety of ways that businesses use these markets to hedge their risks, while recognizing how vital it is to have a method to address the unknown unknowns. And the rule acknowledges that position limits are not always necessary and sets out a solid methodology for determining when they are.

I again want to thank the CFTC staff and my fellow Commissioners for their tireless commitment to finishing this journey. I look forward to voting in favor of this final rule.

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