Statement of Senator Susan M. Collins

"Ending Excessive Speculation in Commodity Markets: Legislative Options"

Committee on Homeland Security and Governmental Affairs
May 24, 2008

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High energy costs are having a devastating impact on our economy and our people – especially people in large, cold, rural states like Maine. Truck drivers, small business owners, fishermen, farmers, and countless others are struggling with the high cost of oil and gasoline. In Maine, where 80 percent of our homes are heated with oil, many families do not know how they are going to cope with the record high cost of heating oil this coming winter.

The high cost of energy is also taking a toll on businesses throughout our nation. For example, the paper mill in Millinocket, Maine, recently announced

it would be closing down because it is no longer profitable due to the cost of oil. If this occurs, the community will be devastated by the loss of more than 200 good jobs.

What is troubling is that the harmful spike in energy costs does not appear to be caused solely by supply and demand factors. Compelling evidence gathered by this Committee suggests that excessive speculation in futures markets is also a significant factor pushing up oil prices.

The increased cost of energy certainly reflects fundamentals, including increased demand from China and India and depreciation of the dollar. But massive new holdings of oil-futures contracts by pension funds, university endowments, and other institutional investors, who neither produce nor take

delivery of oil, also appear to be driving up prices. Their intentions may be simply to provide good returns and investment diversification, but many experts believe their activities are distorting commodity markets and pushing prices upward.

I am pleased to be working with Chairman Lieberman once again to write legislation that will help our nation – this time by preventing excessive speculation in energy and agricultural commodity markets.

I do have serious concerns about a major provision in the draft legislation, and that is the proposed ban on institutional investors trading in the commodity futures markets. While I believe that the influx of money from pension funds, university endowments, and other institutional investors has

had an impact on prices, prohibiting their investment altogether risks harming current and future retirees. After all, pension fund managers are investing in commodities as a way to diversify their holdings, hedge against inflation, and improve returns – all in keeping with their fiduciary obligations.

In my judgment, an outright ban would have unintended consequences for retirees relying on these pension funds. That does not, however, mean that I don't believe that reforms are needed – I do.

Senator Lieberman has proposed other policy options to address the effects of excessive speculation that make a great deal of sense to me. These proposals would limit the percentage of total contract holdings that non-commercial investors

could maintain in any one commodity market, and close the "swaps loophole" that currently allows financial institutions to evade position limits intended to prevent an investor from cornering a market.

As we identify and evaluate these and other policy options, we must also take care not to cripple the usefulness of futures markets for the producers, handlers, and purchasers of commodities who need to lock in prices, hedge risks, and see clues for price trends.

Two other issues are of critical concern to me: "dark markets" and resources for the Commodity Futures Trading Commission (CFTC).

There are still gaps in publicly available data to track the effect of speculation on prices. Price manipulation can go undetected on certain markets because they lack regulation or because trades are not adequately disclosed to regulators. This is why I have called for increased regulation and transparency in futures markets to guard against excessive speculation and price manipulation. And that is why I supported closing the "Enron Loophole" for electronic exchanges – a corrective measure that is now law.

A related concern is ensuring that the CFTC has the resources it needs to collect and analyze market data, monitor trading, and police markets. CFTC Chairman Walter Lukken testified recently that the trading volume of commodity futures contracts and options has soared from 37 million contracts in 1976, to more than 3 *billion* contracts last year. Yet, there are fewer employees at the CFTC today than in

1976, leaving much more work for fewer staff.

With Senator Lieberman's support, I hope to include provisions in our comprehensive bill that would allow the CFTC to make critical technology improvements, add a hundred staff, and support more robust monitoring and enforcement.

Besides lacking sufficient resources, the CFTC has been less than aggressive in using its existing authorities. To be fair, the Commission deserves credit for its recent investigations in market activity, its stronger data-sharing agreement with British authorities, and its withdrawal of proposed rules to raise speculative position limits on agricultural commodities. But these actions and others would have been more admirable if they had been pursued earlier and energetically, without prodding from

lawmakers and public opinion.

As usual, we must perform a careful balancing act – not simply for the abstract goal of market efficiency, but for the concrete goal of easing hardship for real people who are struggling with inflated food and energy costs.

I welcome our panel of witnesses, and thank them for helping us evaluate our policy options. Working together, I am hopeful that we can develop effective measures to curb excessive speculation, guard against price manipulation, and protect consumers who are suffering from high food and energy prices.

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