June 23, 2008

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Attention: Donald S. Clark, Secretary
Federal Trade Commission
Office of the Secretary
Room H-135 (Annex G)
600 Pennsylvania Avenue, NW
Washington, DC 20580

Re: Market Manipulation Rulemaking, P082900

Dear Mr. Clark:

This comment letter is being submitted jointly by Managed Funds Association ("MFA"), Futures Industry Association ("FIA"), New York Mercantile Exchange ("NYMEX") and CME Group Inc. ("CME") in response to the Advance Notice of Proposed Rulemaking issued by the Federal Trade Commission ("FTC" or "Commission") on the implementation of Section 811 of the Energy Independence and Security Act of 2007 ("EISA"). Section 811 makes it unlawful

> "for any person, directly or indirectly, to use or employ, in connection with the purchase or sale of crude oil[,] gasoline or petroleum distillates at wholesale, any manipulative or deceptive device or contrivance, in contravention of such rules and regulations as the Federal Trade Commission may prescribe as necessary or appropriate in the public interest or for the protection of United States citizens."

MFA, FIA, NYMEX and CME have a major interest generally in the deterrence and prevention of price manipulation in commodity markets. Price manipulation has a corrosive effect on the proper functioning of any market. We therefore commend the FTC for moving quickly to begin to develop rules prohibiting price manipulation in wholesale market transactions in crude oil, gasoline and petroleum distillates.[1]

I. Introduction

Crude oil, gasoline and some petroleum distillates[2] (e.g. heating oil) are the subject of futures trading on the NYMEX floor and through an electronic trading platform operated for NYMEX by CME and therefore are "commodities" under the Commodity Exchange Act ("CEA") (7 U.S.C. § 1a(4)), the federal statute administered by the Commodity Futures Trading Commission ("CFTC"), which regulates U.S. futures markets and trading. NYMEX and CME

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[1] MFA is the voice of the alternative investment industry. MFA members include professionals in hedge funds, funds of funds and managed futures funds. MFA members represent the vast majority of the largest hedge fund groups in the world who manage a substantial portion of the approximately $2 trillion invested in absolute return strategies.

FIA is a national trade association. Its regular membership consists of 35 of the Nation's largest futures brokerage firms, registered with the CFTC as futures commission merchants and its associate membership consists of approximately 150 firms involved in virtually all other segments of the industry. FIA regular members execute customer orders for, and provide the financial guarantees underwriting, approximately 90% of all transactions on U.S. futures markets.

NYMEX is a for-profit corporation organized under the laws of the State of Delaware. It is the chief operating subsidiary of NYMEX Holdings, Inc. As a designated contract market and a registered derivatives clearing organization regulated by the CFTC, NYMEX is the largest exchange in the world for the trading and clearing of futures and options contracts on energy and metals commodities, including crude oil, heating oil and gasoline futures contracts.

CME was formed by the merger of Chicago Mercantile Exchange Holdings Inc. and CBOT Holdings, Inc. in 2007. CME is the parent of Chicago Mercantile Exchange Inc. and Board of Trade of the City of Chicago, Inc., both CFTC regulated, designated contract markets as required under 7 U.S.C. § 7. CME also provides services to other exchanges; of interest here, it provides order routing and execution services to NYMEX. CME serves the global risk management needs of its direct customers and those who rely on the price discovery performed by means of its competitive markets. Under the CFTC's jurisdiction, CME offers a comprehensive selection of benchmark products in most major asset classes, including futures and options based on interest rates, equity indexes, foreign exchange, agricultural commodities, energy, and alternative investment products such as weather and real estate.

[2] The scope of the term "petroleum distillate" is uncertain. The FTC should consider including a definition of the term in its proposed rules for public comment.

are CFTC-approved self-regulatory organizations, called designated contract markets, which are charged by statute with a responsibility to prevent price manipulation on their exchanges. 7 U.S.C. § 7 (b)(2). Members of MFA and FIA are subject to regulation under the CEA, as market participants, registered intermediaries, or both, and therefore must comply with the many CEA provisions prohibiting different forms of manipulation of futures market prices as well as the price of any related commodity in interstate commerce. See 7 U.S.C. §§ 9, 13(a)(2) and 13(b). Collectively, NYMEX, CME, and members of MFA and FIA touch in one way or another virtually every futures contract traded in the United States. We therefore have a great stake in the proper administration of the CEA and its provisions, especially as they relate to price manipulation.

Congress found that U.S. futures markets serve three vital "national public interest[s]" by providing a means for 1) managing and assuming commodity price risks; 2) discovering commodity prices; and 3) disseminating those prices. 7 U.S.C. § 5(a). The congressionally-approved formula for achieving these public interests is "trading in liquid, fair and financially secure trading facilities." *Id*. The CEA further specifies that "to foster these public interests, it is … the purpose of this [Act] to deter and prevent price manipulation…." 7 U.S.C. § 5(b).

The linchpin of the CEA's statutory structure is its grant of "exclusive jurisdiction" to the CFTC, adopted in 1974 and reaffirmed by Congress as recently as last month: "The Commission shall have exclusive jurisdiction … with respect to accounts, agreements, … and transactions involving contracts of sale of a commodity for future delivery traded or executed on a contract market designated … pursuant to section 5 … of this Act." CEA § 2(a)(1)(A); 7 U.S.C.

§ 2(a)(1)(A). Congress enacted this provision to ensure that CFTC regulations and the CEA would be the sole legal standards applied to U.S. futures trading.

Congress designed CFTC exclusive jurisdiction to serve the public interest by avoiding the application of duplicative, or potentially conflicting, legal and regulatory standards to futures market participants, professionals and exchanges. In this way, CFTC exclusive jurisdiction promotes the very public interests Congress has found futures markets serve: price discovery and risk shifting. 7 U.S.C. § 5(a). Congress understood that price signals generated by futures markets would be used by participants in non-futures transactions and that other regulators of those transactions -- whether the Securities and Exchange Commission, Agriculture or Treasury Departments or the Bureau of Mines -- might otherwise have had a regulatory interest in the transactions that generated those prices. Congress enacted the CEA's exclusive jurisdiction provision to provide legal certainty to futures market participants and futures exchanges that the CFTC, and only the CFTC, had regulatory authority over futures trading in the U.S. In the words of Acting CFTC Chairman Walter Lukken, "Exclusive jurisdiction of futures trading ensures that the futures markets, where many commodities also have a separate cash market regulator, will not face inconsistent and redundant regulation and the uncertainty of differing legal standards." [3]

We believe the Commission should adopt appropriate rules prohibiting manipulation in the purchase and sale of crude oil, gasoline and petroleum distillates at wholesale under Section

[3] Statement of Acting CFTC Chairman Walter Lukken Before the Subcommittee on Oversight and Investigations of the House Committee on Energy and Commerce, December 12, 2007.

811 of EISA. But those rules should not implicitly or explicitly extend the Commission's jurisdiction in a manner that overlaps with the CFTC's exclusive jurisdiction over futures trading generally and futures market manipulation specifically. We therefore respectfully request that the Commission propose and adopt a safe harbor provision or other appropriate exception from its rules confirming that nothing in its Section 811 rules would govern or apply, in the words of the CEA, "with respect to accounts, agreements…and transactions involving" futures and options markets and other trading instruments which are subject to CFTC exclusive jurisdiction. 7 U.S.C. § 2(a)(1)(A). The operations of CFTC-regulated designated contract markets (like NYMEX and CME) and registered futures professionals (like the members of MFA and FIA) as well as the actual trading in futures markets should be subject to a single legal standard established under the CEA by the CFTC and the courts. This issue is of paramount importance to the competitive status of U.S. futures markets.

In addition, given our experience with market manipulation prevention and standards, we offer the following suggestions:

1) the FTC and the CFTC should work cooperatively without duplication of effort to police price manipulation in those wholesale, non-futures energy transactions over which each agency has anti-manipulation jurisdiction, as the Commission itself has recognized (73 Fed. Reg. at 25618 n.39);

2) the absence of a securities law disclosure foundation for wholesale energy transactions argues against adopting an SEC-style anti-manipulation formulation like SEC Rule

10b-5; the CFTC's anti-manipulation jurisprudence for commodities in interstate commerce is more relevant to the FTC's mission; and

3) the FTC's rules implementing Section 811 should include a specific intent to create an artificial price standard to ensure that legitimate commercial conduct is not mislabeled and punished as manipulation.

We will discuss these recommendations in more detail below.

II. The FTC's Proposed Rules Should Not Apply to Futures Market Activity Covered by CFTC Exclusive Jurisdiction.

Section 811 of EISA should not be interpreted to erode CFTC exclusive jurisdiction over futures market activity. The historical context, statutory text, case law and purposes of the exclusive jurisdiction provision compel this conclusion. It is also fully consistent with the provisions of EISA.

A. The Legislative Context Of The 1974 Enactment Of CFTC Exclusive Jurisdiction.

In 1974, Congress overhauled the structure of U.S. futures market regulation under the Commodity Exchange Act. Congress recognized that "the futures markets play a significant role in the economic well being of [the] country"[4] and "wanted to strengthen futures regulation, create a comprehensive regulatory structure for the esoteric futures trading complex, and avoid

[4] H.R. Rep. No. 93-975, at 60 (1974).

regulatory gaps."[5] To that end, Congress considered whether to replace as the futures market regulator a branch of the Department of Agriculture called the Commodity Exchange Authority with a new independent agency, similar to the FTC or SEC, "to be an expert in futures regulation, which requires highly specialized skills."[6]

Congress intended that preventing price manipulation would be central to the regulatory mission for the new agency which would be a neutral arbiter of futures prices, not inclined to seek higher or lower prices.[7] "The proper regulatory function of an agency which regulates futures trading is to assure the market is free of manipulation and other practices which prevent the market from being a true reflection of supply and demand." (S. Rep. No. 93-1131, at 21 (1974). Congress understood that U.S. futures markets were poised for great growth as innovative new forms of commodity futures trading had either begun or were imminent. This development would give other agencies with regulatory authority over the new underlying commodities reason to assert jurisdiction over the futures markets. S. Rep. No. 93-1131, at 23

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[5] H.R. Rep. No. 93-975, at 1 (1974); S. Rep. No. 93-1131, at 19; 120 Cong. Rec. 34736 (1974) (statement of H. Comm. Chairman Poage) ("It was the intent of the [Conference] Committee to fill all regulatory gaps -- to regulate trading in futures and in options relating to commodities or commodity futures, because such trading is now poorly regulated, if it is regulated at all.").

[6] H.R. Rep. No. 93-975, at 71 (1974), see also S. Rep. No. 1131, at 22 (1974 ("persons of demonstrated knowledge in futures trading").

[7] H.R. Rep. No. 93-975, at 60 (1974).

(1974). Congress also knew that futures and options trading had already been subjected to the vagaries of state blue sky laws and SEC enforcement actions prior to 1974.[8]

Against this backdrop, Congress adopted the Commodity Futures Trading Commission Act of 1974, which included three major structural reforms. First, Congress created the CFTC as the independent expert futures market regulator. Second, Congress greatly expanded the list of "commodities" that had been subject to the CEA by including all "goods[,]articles,… services, rights, and interests in which contracts for future delivery are presently or in the future dealt in." 7 U.S.C. § 1a(4). Third, Congress granted the CFTC "exclusive jurisdiction" and mandated that "the [CFTC's] jurisdiction over futures contract markets…is exclusive…and the [CFTC's] jurisdiction, where applicable, supersedes state as well as Federal agencies."[9] The 1974 Conference Committee further explained that "under the exclusive grant of jurisdiction to the [CFTC], the authority of the Commodity Exchange Act (and regulations issued by the [CFTC]) would preempt the field insofar as futures regulation is concerned."[10]

B. The Text Of The CEA Exclusive Jurisdiction Provision Demonstrates Its Breadth.

The CFTC's exclusive jurisdiction provision is unambiguous and broad. Section 2(a)(1)(A) of the CEA states:

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8 (H R. Rep. No. 93-975, at 48, 120 Cong. Rec. 34737 (1974) (statement of H. Chairman Poage), 120 Cong. Rec. 34997 (1974) (Statement of Sen. Comm. Chairman Talmadge).

9 H.R. Rep. No. 93-1383, at 35 (1974) (Conf. Rep.) and S. Rep. No. 93-1131, at 23 (1974) (same).

10 H.R. Rep. No. 93-1383, at 35 (1974) (Conf. Rep.).

> "The [CFTC] shall have exclusive jurisdiction, except to the extent provided in subparagraphs (C) and (D) of this paragraph and subsections (c) through (i) of this section, with respect to accounts, agreements…and transactions involving contracts of sale of a commodity for future delivery traded or executed on a contract market designated or derivatives transaction execution facility registered pursuant to section 7 or 7a of this title or any other board of trade, exchange, or market,… [and]…Except as hereinabove provided, nothing contained in this section shall (I) supersede or limit the jurisdiction at any time conferred on the Securities and Exchange Commission or other regulatory authorities under the laws of the United States or of any state, or (II) restrict the Securities and Exchange Commission and such other authorities from carrying out their duties and responsibilities in accordance with such laws."

This statutory language establishes three things: 1) CFTC jurisdiction "with respect to" "accounts, agreements and transactions" "involving" futures that are traded on "any market" is "exclusive;" 2) any exceptions to CFTC exclusive jurisdiction are set out in the provision itself; and 3) except for those matters committed to CFTC exclusive jurisdiction, the FTC and other federal agencies retain their full powers.

As relevant here, Congress has vested exclusive jurisdiction in the CFTC with respect to accounts, agreements and transactions involving crude oil futures, gasoline futures and petroleum distillate futures. No other federal agency may regulate or police activity or conduct covered by that grant of jurisdiction, including the operations of exchanges, like NYMEX and CME, and of CFTC-registered futures professionals, like the members of MFA and FIA. The breadth of this congressional grant of exclusive authority is demonstrated by the statutory text itself which makes the CFTC's exclusive jurisdiction applicable to, for example, not just transactions "in" futures, but also transactions "involving" futures, and not just futures trading accounts themselves, but also conduct "with respect to" those accounts. Even the word "transactions" in this statutory provision has considerable elasticity, courts having found that it is "most naturally read as encompassing…a set of arrangements directly related to the actual sale of commodities futures." *FTC v. Ken Roberts Co.*, 276 F.3d 583, 590 (D.C. Cir. 2001).

The first "except" clause in Section 2(a)(1)(A) can not be read to give any federal agency, including the FTC, jurisdiction over futures trading that is subject to CFTC regulatory authority. The clause cites three sources of exceptions from CFTC exclusive jurisdiction. The first is subparagraph (C) which originally was enacted as part of the 1982 Shad-Johnson Jurisdictional Accord. The 1982 Accord reassigned to the SEC jurisdiction over some products which became securities outside CFTC jurisdiction. Public Law 97-303, 96 STAT 1409, Secs. 1, 2 (1982); Public Law 97-444, 96 STAT 2294, Sec. 101 (1983). *See* 7 U.S.C. § 2(a)(1)(C). The second is subparagraph (D), enacted as part of the Commodity Futures Modernization Act, Public Law 106-544 (Appendix E) (2000), which created "security futures products" to be jointly regulated by CFTC and SEC, 7 U.S.C. § 2(a)(1)(D). The third set of exceptions applies to the various statutory exclusions and exemptions Congress also enacted in 2000 under 7 U.S.C. § 2(c)-(i). None of these exceptions would apply to futures trading on designated contract markets regulated by the CFTC in crude oil, gasoline or petroleum distillates.

The provisions of the 2008 Farm Bill further underscore that Congress intends the CFTC to exercise exclusive jurisdiction over the trading activity it regulates. In that legislation, Congress empowered the CFTC to determine that certain otherwise CEA-exempt energy transactions offered on what are called "exempt commercial markets," which trade electronically, are "significant price discovery contracts" if certain criteria are met. HR 6124, 110 Cong. § 13,201(b) (2008). Once instruments are found to be "significant price discovery contracts," they become subject to heightened CFTC regulation, including reporting, recordkeeping, position limits and self-policing by the electronic trading facility. *Id*. The Farm Bill also adds "significant price discovery contracts" to the list of instruments subject to exclusive CFTC jurisdiction (H.R. 6124 at § 13203(c)) thereby reconfirming Congress' continued endorsement of the rationale and need for CFTC exclusive jurisdiction over instruments subject to its regulatory scrutiny.

C. Courts Have Uniformly Found In Favor Of CFTC Exclusive Jurisdiction When Challenged By Other Agencies.

The federal courts have on several occasions interpreted the scope of CFTC exclusive jurisdiction. The two primary cases arose in the context of disputes involving the CFTC and the SEC where the SEC asserted a new product was a security and the CFTC argued the product was subject to CFTC exclusive jurisdiction. The CFTC won each of these cases.

In *Board of Trade of the City of Chicago v. SEC,* 677 F.2d 1137 (7th Cir. 1982), the United States Court of Appeals for the Seventh Circuit set aside an SEC order which would have allowed for securities exchange trading of options on Government National Mortgage Association (GNMA) pass through securities. Although the SEC contended these options on securities were "securities" within the SEC's jurisdiction under the Securities Exchange Act of 1934, the Seventh Circuit held that the options were instead commodity options, which fell within the exclusive jurisdiction of the CFTC. (GNMA securities were already the subject of a futures contract and therefore were "commodities" under the CEA.) In this decision, the Seventh Circuit addressed the second "except" clause in Section 2(a)(1)(A) of the CEA. It rejected the SEC's argument that the clause was a claw back of SEC jurisdiction from CFTC exclusive jurisdiction, finding that the phrase "except as hereinabove provided" referred to only one provision, the affirmative grant of exclusive jurisdiction to the CFTC, and that anything covered by that grant was not subject to the federal securities laws or SEC jurisdiction. 677 F.2d at 1145.

In *Chicago Mercantile Exchange v. SEC,* 883 F.2d 537, 539 (7th Cir. 1989), the Seventh Circuit reaffirmed that CFTC exclusive jurisdiction over futures supersedes the authority of other agencies. In that case, the SEC approved trading in a new product called an Index Participation (IP). Even though the Seventh Circuit accepted the theory that an IP was a security, the court of appeals also found an IP to be a stock index futures contract subject to exclusive CFTC jurisdiction. As the court stated, "if an instrument is *both* a security and a futures contract, then the CFTC" is "the sole regulator..." The grant of exclusive jurisdiction to the CFTC could have "no other possible meaning." *Id* at 544.

D. The FTC Has Previously Accepted CFTC's Statutory Exclusive Jurisdiction.

Some years ago, the Commission initiated an investigation against the Ken Roberts Company, which was registered with the CFTC as a commodity trading advisor, relating to instructional materials on futures and securities trading. Roberts resisted the Commission's investigative demands on the grounds that the CFTC had exclusive jurisdiction over such activities. The FTC explained that Congress designed the CEA's exclusive jurisdiction provision "to create uniform rules for the operation of the futures market" and rejected Roberts' request because the FTC's investigation concerned advertising for "teaching materials," not actual trading on the futures markets, and therefore did not implicate CFTC exclusive jurisdiction.[11] The Commission also pointed out that it was investigating whether to proceed under its general "unfair or deceptive acts or practices" authority in Section 5 of the FTC Act, a statute of general applicability and therefore undisturbed by CFTC exclusive jurisdiction.[12]

Roberts sought judicial review of the Commission's decision and the D.C. Circuit agreed with the Commission's reasoning that CFTC exclusive jurisdiction encompassed actual transactions involving futures trading, not "instruction in commodities trading." *Roberts,* 276 F.3d at 589. Again the D.C. Circuit acknowledged that the "goal" of the CEA's exclusive jurisdiction provision "was to bring the futures markets 'under a uniform set of regulations' and that 'only in the context of market regulation does the need for uniformed legal rules apply.'" *Roberts,* at 591, quoting *Am. Agric. Movement, Inc. v. Bd of Trade of the City of Chicago,* 977 F.2d 1147, 1155-57 (7th Cir. 1992).

The Commission's Roberts precedent is perfectly consistent with the Seventh Circuit's exclusive jurisdiction precedent. The FTC is well within its rights to pursue deceptive practices that do not involve actual transactions on or the operation of the futures markets. But futures market manipulation claims do involve both actual futures transactions and the core price

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[11] February 25, 2000 FTC Letter to Ken Roberts Company, page 5.

[12] *Id*. Section 811 of EISA is not a statute of general applicability; it would apply only to purchases or sales of gasoline, crude oil and petroleum distillates at wholesale and it would prescribe various practices in connection with those specific transactions.

discovery operations of the futures markets and should be outside the limits of Section 811 due to the CEA's exclusive jurisdiction provision.

As the FTC mentions in its Federal Register notice, the Federal Energy Regulatory Commission ("FERC") and the CFTC are engaged in a dispute over CFTC exclusive jurisdiction in connection with the Amaranth case. Without repeating the arguments we have made in our *amicus curiae* court filings in that case (our brief is attached to this letter), the dispute highlights why we believe the FTC should make explicit that its manipulation rules will not apply to futures trading activities within the CFTC's exclusive jurisdiction. The allegations in Amaranth concern misconduct only in the futures markets and not conduct by the respondents in any FERC jurisdictional transactions. FERC's claim rests on an alleged manipulation of the futures market price. The CFTC's case against Amaranth is based on an attempted manipulation, not an actual manipulation. Determining whether or not a futures market price has been manipulated is a core CFTC function that fits squarely within the zone of the CFTC's exclusive jurisdiction. FERC's attempt to superimpose its judgment over that of the CFTC, however, has led to legal uncertainty in the markets about what legal standard for price manipulation applies to futures markets. At best, FERC's actions are duplicative. At worst, they will result in conflicting agency precedent relating to futures market manipulation. Either way, FERC's actions embody the specific ills Congress enacted CFTC exclusive jurisdiction to prevent. We strongly urge the FTC not to follow FERC's lead.

E. The Text of EISA Supports Respecting CFTC Exclusive Jurisdiction.

Nowhere in the text of EISA did Congress express any intention to override CFTC exclusive jurisdiction. The absence of any effort by Congress to do so is important because EISA expressly preserved the continued application of other statutes where EISA was silent. Section 3 of EISA reads: "Except to the extent expressly provided in this Act or an amendment made by this Act, nothing in this Act or an amendment made by this Act supersedes, limits the authority provided or responsibility conferred by, or authorizes any violation of any provision of law (including a regulation), including any energy or environmental law or regulation." Under this provision, EISA may not "supersede" or "limit" the CFTC's exclusive jurisdiction unless "expressly provided" for in EISA. Congress did not expressly provide that the FTC's new anti-manipulation powers should limit or supersede the CFTC's exclusive jurisdiction. In fact, Sections 811-815 of EISA do not mention the CEA or CFTC in any way. Thus, the FTC's recognition of CFTC exclusive jurisdiction would be perfectly consistent with EISA.[13]

The terms of Sections 811 and 814(a) of EISA confirm this result. Section 811 authorizes the FTC to prosecute those who use manipulative devices "in connection with the purchase or sale of crude oil, gasoline or petroleum at wholesale." As noted by the Commission, "Section 811 … arguably covers sales and purchases starting at the point at which crude oil, gasoline, or a petroleum distillate is sold by the producer or importer, and ending at the point at

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[13] Misinterpreting EISA to limit or supersede CFTC exclusive jurisdiction also would violate the statutory construction principle that implied repeals of statutory rights are not favored. See *Tennessee Valley Auth. v. Hill*, 437 U.S. 153, 190 (1978).

which it is purchased by a retailer." 73 Fed. Reg. at 25621. Section 814(a) focuses its primary penalty provision on "suppliers."

The Commission's description of Section 811's focus on wholesale sales and purchases illustrates that Congress did not intend those provisions to apply to futures market transactions by wholesalers. Section 814's emphasis on suppliers also indicates that Congress did not intend the FTC's new powers to apply to futures. Futures contracts are trading instruments, not wholesale purchases and sales, and suppliers are surely not the only, or even predominant, participants in futures markets. Far from "expressly provid[ing]" any limitation on CFTC exclusive jurisdiction, this statutory language actually confirms that Congress never intended to disturb the CFTC's role as the sole federal futures market regulator and enforcement authority, even in futures on crude oil, gasoline and applicable petroleum distillates.[14]

Section 811 does not "expressly provide" for the prosecution of activities in futures or derivative markets that have an impact on wholesale prices. Any supplier that engages in a futures price manipulation must therefore be investigated and prosecuted by the CFTC under the uniform futures market price manipulation standard provided in the CEA. In contrast, any supplier that uses a manipulative or deceptive device in relation to a wholesale purchase or sale

[14] The CEA provides for significant penalties for *any* party who manipulates or attempts to manipulate the price of a commodity in interstate commerce. EISA by contrast has a highly bifurcated penalty regime that demonstrates Congress' regulatory concern was with suppliers. Section 814(a) provides civil penalty authority of up to $1,000,000, which can be assessed against suppliers for each violation for each day. The FTC's authority to assess civil penalties against persons that are *not* suppliers (which includes, for example, hedge funds and other speculators that do not participate in the wholesale markets), by contrast, is restricted, under Section 813 of EISA, to $11,000 per violation.

of crude oil, gasoline or a petroleum distillate could be subject to prosecution by the Commission under Section 811 or the CFTC under the CEA, as we will discuss in the next section.

Last, as we explained earlier, Congress enacted CFTC exclusive jurisdiction to allow U.S. futures markets to serve the public interest. Section 811 permits the FTC to adopt anti-manipulation rules "as necessary or appropriate in the public interest." FTC rules that purport to overlap with CFTC exclusive jurisdiction would not serve the public interest.

If the Commission disagrees, we would encourage the FTC to advise the public of its position and rationale in the request for public comments accompanying the proposed rules on this subject. This will allow interested parties to consider and submit comments on the FTC's views before final action is taken.

III. The FTC and CFTC Should Work Together to Prevent and Police Manipulation in Wholesale Crude Oil, Gasoline and Petroleum Distillate Transactions.

The FTC and the CFTC share enforcement jurisdiction over price manipulation in connection with wholesale purchases and sales in crude oil, gasoline and those petroleum distillates which are the subject of futures trading. Section 811 of EISA empowers the FTC to adopt rules prohibiting the use of manipulative or deceptive devices in connection with those wholesale transactions. In addition to futures price manipulation, the CEA makes it a felony for any person to "manipulate the price of any commodity in interstate commerce," (7 U.S.C. § 13(a)(2)) and authorizes the CFTC itself to bring civil cases against persons who engaged in such manipulations. (7 U.S.C. §§ 9, 13a-1, and 13b). Congress has now amplified those CFTC powers in the Farm Bill of 2008, increasing the CFTC's fining authority to the greater of $1 million per price manipulation violation or triple the monetary gain of such violations.[15] To the extent crude oil, gasoline or a particular petroleum distillate is a “commodity,” Congress has now strengthened the CFTC’s enforcement powers in the context of both cases alleging futures price manipulation and related cash commodity price manipulation.

Conduct that constitutes price manipulation of wholesale crude oil, gasoline and petroleum distillate purchase or sale transactions is not, however, subject to CFTC exclusive jurisdiction. Instead, this is an area of concurrent FTC and CFTC jurisdiction. Whether framed as manipulation of purchases or sales of a petroleum commodity “at wholesale” or manipulating “the price of a commodity in interstate commerce,” each agency has authority to investigate and prosecute price manipulations of wholesale transactions to buy or sell crude oil, gasoline or petroleum distillates.

We believe this shared jurisdiction makes considerable sense. The CEA does not focus its comprehensive regulatory structure on wholesale cash market buy and sell transactions, which are not designed to be hedging or price discovery transactions. Congressional concerns about duplicative, conflicting regulation, which underlie the CEA's exclusive jurisdiction provision, are therefore not implicated by shared concurrent jurisdiction of those wholesale buy and sell transactions. Concurrent jurisdiction also makes sense because it would allow the FTC and CFTC to establish a framework for formal enhanced cooperation in their enforcement efforts. As part of that process, and as relevant to the proposed rules under Section 811, we would

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[15] H.R. 6124 § Sec. 13,103(a)(2).

recommend that the FTC delineate its understanding of the scope and contours of the statutory phrases "purchase or sales … at wholesale." Such clarification will not only allow buyers and sellers to understand better if they are subject to FTC rules, it will also suggest guidelines that could be helpful to the CFTC and the FTC in working cooperatively and in a complementary manner in exercising their concurrent authority.

The CFTC has been very active in recent years in the enforcement area relating to non-futures energy product transactions.[16] As CFTC Acting Chairman Lukken recently reported to Congress: "During the last five years ... [i]n the energy sector, [CFTC] Enforcement investigated and prosecuted Enron and BP, dozens of other energy companies, and hundreds of other traders and hedge funds."[17] These enforcement actions have no doubt provided the CFTC with valuable experience and insight that could be relevant to both the FTC's development and implementation of its Section 811 rules.

A. Securities Law Principles Should Not be Adopted by the FTC.

We understand that the provisions of Section 811 of EISA were modeled after Section 10(b) of the Securities Exchange Act. We are concerned, however, that a blanket application of federal securities laws adopted under that provision -- specifically SEC Rule 10b-5 -- would lead

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[16] "Contrary to the testimony of some commentators, the CFTC has vigilantly pursued and punished manipulative conduct in energy markets during the previous five years. See Report of Commodity Futures Trading Commission on Energy Markets Enforcement Results (March 17, 2008) available at **http://www.cftc.gov/stellent/groups/public/@newsroom/documents/file/enfenergyenforcementactions.pdf**

[17] Written testimony of Acting CFTC Chairman Walter Lukken Before the Subcommittee on Oversight and Investigations of the House Committee on Energy and Commerce, December 12, 2007.

to uncertainty about compliance and enforcement which would be problematic for wholesale buyers and sellers alike.

SEC Rule 10b-5 was designed to address the interactions of brokers and customers as well as corporate insiders and market participants generally. It imposes on insiders and others an affirmative duty to disclose material facts. And it arises in the general federal securities law context of protecting public investors through a regime of primarily issuer-based disclosure of material information to try to equalize the information to which all investors have ready access. In the absence of that federal securities law context, we do not believe the FTC should make it a manipulative or deceptive device for a wholesale buyer or seller to fail affirmatively to disclose to other buyers or sellers material market information.

Private, bi-lateral wholesale transactions in crude oil, gasoline and petroleum distillate markets arise in a very different legal context and have never been subjected to an affirmative duty to disclose all material information or to abstain from transacting unless all inside, private information is disclosed. Relationships between securities market participants and participants in wholesale petroleum markets are very different and the standards applicable to the former cannot be applied to the latter.[18] The Commission should take those differences into account when it fashions a rule to prohibit misrepresentations by wholesalers as deceptive devices in connection

[18] For example, unlike securities markets, by definition, retail consumers do not engage in wholesale petroleum transactions. The Commission's 1983 policy statement on deception, outlining the principles by which its enforcement authority will be utilized, focuses in significant detail on the areas in which retail consumers may require protection. See http://www.ftc.gov/bcp/policystmt/ad-decept.htm.

with buy or sell transactions. The Commission also may want to prohibit wholesalers from making a false statement or a false report that could mislead a counterparty to a wholesale purchase or sale transaction. But the Commission's Section 811 rules should not include any affirmative duty for wholesale buyers or sellers to report or provide material information to a counterparty or others.

B. CFTC Manipulation Standards Should be Adopted By The FTC.

The CEA's anti-manipulation provisions and jurisprudence offer a better alternative than the securities law model. In fact, the CFTC has already flexed its anti-manipulation muscles in recent years in connection with wholesale energy transactions and markets, including its enforcement of the statutory prohibition against making false reports to affect the price of an energy commodity in interstate commerce. Based on this track record, the CEA manipulation standards appear to be more relevant and appropriate for the Commission's consideration as it develops regulations to effectuate Section 811. For these reasons, we would recommend that the FTC embrace the principles of manipulation law developed by the CFTC and courts under the CEA, as cited in the FTC's Federal Register notice.

The CEA has a time-tested standard for market manipulation, the intentional creation of an artificial price. To prove a claim of market manipulation under the CEA, it must be proved that a) a party possessed the capability to create an artificial price; b) an artificial price was created; c) the artificial price was due to actions of the party; and d) the party had the specific intent to create the artificial price.[19] We urge the FTC to implement this standard through its Section 811 rules.

The development of consistent CEA and EISA manipulation standards for wholesale purchases or sales of crude oil, gasoline and petroleum distillates would promote legal certainty by avoiding conflicting government approaches to price manipulation of the same or similar transactions. These uniform standards would enable buyers and sellers to know what law governed their transactions and how that law would be applied.[20] It also could avoid duplicative agency efforts if the FTC and CFTC would develop a formal or informal arrangement to coordinate investigatory activities and even enforcement actions. With each agency's resources now stretched thin, we see no reason why the public interest would be disserved by that kind of team work by the CFTC and FTC in connection with these wholesale transactions in crude oil, gasoline and petroleum distillates. Promoting legal certainty and agency coordination will also improve the competitiveness of U.S. markets.[21]

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[19] *Frey v. Commodity Futures Trading Comm'n*, 931 F.2d 1171, 1775 (7th Cir. 1991).

[20] The FTC cited one possible definition of market manipulation: "Market manipulation shall mean knowingly using or employing, directly or indirectly, a manipulative or deceptive device or contrivance — in connection with the purchase or sale of crude oil, gasoline, or petroleum distillates at wholesale — for the purpose or with the effect of increasing the market price thereof relative to costs." 73 Fed. Reg. at 25620. This definition has some common elements with the CEA manipulation standard, but applies only to a long or "higher" manipulated price, not a short or "lower" manipulated price and may be read not to include a scienter standard. It might be appropriate for the Commission to discuss this approach with the CFTC to try to harmonize efforts in this area.

[21] The United States Treasury Department has increasingly addressed the issue of regulatory cooperation and efficiency in response to the findings of the Committee on Capital Markets Regulation citing an erosion in the competitiveness of US capital markets. See Remarks by Treasury Secretary Henry M. Paulson before the Economic Club of New York. New York, NY (Nov 20, 2006) available at http://www.ustreas.gov/press/releases/hp174.htm; Remarks by Under Secretary for Domestic Finance Robert K.

(Continued…)

For these reasons, we recommend that the FTC and the CFTC develop formal coordination mechanisms for investigating and prosecuting anti-manipulation claims in wholesale transactions in crude oil, gasoline and petroleum distillates over which they exercise concurrent jurisdiction. Such measures might include the sharing of market data and analysis, the development of a joint committee to monitor developments in crude oil and refined product markets, and the creation of a process by which the agencies will decide which, if either, agency will prosecute a manipulation claim involving wholesale transactions to buy or sell crude oil, gasoline or petroleum distillates.[22]

IV. Specific Intent Should Be An Element Of The FTC's Price Manipulation Prohibition.

In order to prove a claim of market manipulation or attempted manipulation under the CEA, it must be shown that a party had the specific intent to create an artificial price. This requirement, while representing a substantive protection for an accused party, serves an equally vital role in facilitating robust, healthy and legitimate market activity. The CFTC has long

Steel before the American Enterprise Institute. Washington D.C. (Nov. 13, 2007); available at http://www.ustreas.gov/press/releases/hp677.htm See also Michael R. Bloomberg and Charles E. Schumer, *Sustaining New York's and the U.S.' Global Financial Services Leadership,* at 80 (Jan. 2007), available at http://www.nyc.gov (noting that "an increasingly heavy regulatory burden and a complex, cumbersome regulatory structure with overlaps at the state and national levels is causing an increasing number of businesses to conduct more and more transactions outside the country.")

[22] The Commission and the Department of Justice have developed an efficient model of shared jurisdiction in the context of investigations of merger activities. See http://www.ftc.gov/opa/2002/04/clearanceoverview.shtm.

recognized this role stating "we are unable to discern any justification for a weakening of the manipulative intent standard which does not wreak havoc with the market place."[23]

Transactions in product markets have the inherent potential to affect market price. Purchases of a product absorb existing supply at a given price and therefore have a tendency to cause market prices to rise. Similarly, sales of a product fulfill existing demand at a given price and therefore have a tendency to cause market prices to fall. This is particularly true when the quantity transacted is substantial relative to the normal supply-demand dynamics of a particular market. The absence of a specific intent standard as part of an anti-manipulation rule would expose innocent market participants to potential manipulation claims on the basis of lawful market transactions which happened to have a significant effect on market prices. Market participants, self regulatory organizations, courts and even the agencies would have no clear principles by which to distinguish innocent conduct from manipulative conduct. Such a threat would chill legitimate market activity and distort the very market fundamental dynamics that anti-manipulation prohibitions seek to protect.

Wholesale transactions are particularly susceptible to this kind of "false positive." Unlike futures market trading, wholesale transactions in the cash market may be episodic and

23 *In re Indiana Farm Bureau Coop.*, CFTC No. 75-14, 1982 WL 30249, at *5 (CFTC 1982). The FTC also emphasized: "Thus, market participants have a right to trade in their own best interests without regard to the positions of others as long as their trading activity does not have as its purpose the creation of 'artificial' or 'distorted' prices. Indeed, it is this very motivation which gives lifeblood to the forces of supply and demand, [and] [sic] makes the price discovery function of the marketplace viable. Moreover, since the self-interest of every market participant plays a legitimate part in the price setting process, it is not enough to prove simply that the accused intended to influence price." *Id*.

non-standardized. Two transactions in the same product may occur simultaneously at different prices because the economic terms of each transaction (delivery location, credit terms etc.) give rise to different costs and risks to the counterparties. Further, these unique transactional terms create smaller sub-markets for a product at a given price, making it even more likely that large transactions will have a significant effect on observed prices. Indeed, the inferior liquidity and lack of standardization in wholesale transactions complicate in many circumstances the determination whether a particular market price is artificial.

Wholesale transactions in crude oil, gasoline and petroleum distillates would be hampered if innocent commercial activity could give rise to potential manipulation claims. The absence of such a standard would create a vicious circle. Buyers and sellers would refrain from market activity, draining liquidity and further increasing the possibility that legitimate business activity could cause large movements in prices which might be mistaken as artificial. In order to prevent such a scenario we urge the FTC to adopt the specific intent standard of the CEA as part of any manipulation rule adopted under Section 811.[24]

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[24] We also urge the FTC to confirm that no private right of action exists under Section 811 and any implementing rules the FTC adopts. In the absence of a statutory authorization to bring such actions, private party suits should not be allowed. In addition, we suggest that the FTC not rely on its deceptive or unfair trade practice jurisprudence under Section 811. The Commission has noted that “neither knowledge nor intent” is a required element of a violation under Section 5 of the FTC Act (73 Fed. Reg. at 25619 n.56). We therefore believe it would be inappropriate to follow that precedent under Section 811.

V. Conclusion

We appreciate the opportunity to comment on the Commission's preliminary discussion on the implementation of Section 811 of EISA. We look forward to reviewing the Commission's formal proposals in this area and its efforts to strengthen the anti-manipulation safeguards available for wholesale purchase and sale transactions in crude oil, gasoline and petroleum distillates.

Respectfully submitted,

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Attachment

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

U.S. COMMODITY FUTURES TRADING COMMISSION,	:	
Plaintiff,	:	07 Civ. 6682 (DC)
v.	:	
AMARANTH ADVISORS L.L.C., et al.,	:	
Defendants.	:	

MEMORANDUM OF LAW OF THE AMICI CURIAE FUTURES GROUP IN SUPPORT OF PLAINTIFF COMMODITY FUTURES TRADING COMMISSION'S EXCLUSIVE JURISDICTION AND DEFENDANT AMARANTH ADVISORS' STAY MOTION

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INTRODUCTION

On August 16, 2007, the Court summed up this case's posture succinctly: "two federal agencies [are] going after the same parties based on the same conduct seeking essentially the same relief." (Ct. Conf. Tr. 4, Aug. 16, 2007). In this action, the Commodity Futures Trading Commission alleges under its statute -- the Commodity Exchange Act -- an attempt to manipulate the natural gas futures market price. In an administrative proceeding, the Federal Energy Regulatory Commission alleges under its statute -- the Natural Gas Act -- an actual manipulation of the natural gas futures market price. To reduce the possibility of conflicting adjudications, defendant Amaranth Advisors has moved to stay the FERC proceeding. Granting this motion would not dismiss FERC's proceeding or affect any Court of Appeals jurisdiction. It would simply allow the CFTC action in this court to be decided first.

The *amici curiae* Futures Group is comprised of the Managed Funds Association, Inc. and International Swaps and Derivatives Association, Inc. (major futures market participants); the Futures Industry Association, Inc. (major futures market intermediaries); and the New York Mercantile Exchange, Inc. and Chicago Mercantile Exchange Group, Inc. (major futures exchanges). The bulk of all U.S. futures trading occurs on NYMEX and CME in a wide-range of commodities, including natural gas, crude oil, metals, currencies, corn, soybeans, U.S. Treasury Securities and stock indexes. The Futures Group expresses no view on Amaranth's guilt or innocence. We know well the dangers of futures price manipulation; no legitimate market participant, brokerage firm or exchange would tolerate misconduct designed to create an artificial price. The CEA imposes on CFTC-approved exchanges, like NYMEX and CME, a clear affirmative duty to deter or detect manipulation of futures prices on their markets. 7 U.S.C. § 7(d)(3) and (4). Their efforts combine with the CFTC's constant policing to make preventing and punishing price manipulation the core of the CEA and CFTC regulation.

The Futures Group has a substantial interest in addressing two of the factors the Court will consider in deciding the stay motion: likelihood of success on the merits and the public interest. On the former, the issue the Court posed on August 16 was: "whether FERC is precluded from pursuing this matter administratively because the CFTC has exclusive jurisdiction." (Ct. Conf. Tr. 11) The answer is "yes," based on the text of the CEA's exclusive jurisdiction provision, 7 U.S.C. § 2(a)(1)(A), as well as its history and an unbroken chain of judicial precedent. (See Section I.)

Exclusive jurisdiction is not a matter of agency turf: it was intended instead to make the CEA and CFTC regulations supreme as the body of law for futures markets and trading thereon. CEA exclusive jurisdiction is therefore central to the public interests served by, as well as the operation and competitiveness of, the U.S. futures markets. Allowing FERC to proceed now would undermine these public interests. For 32 years, the CEA and CFTC regulations have provided the single legal standard -- the intentional creation of an artificial price -- for deciding whether a futures market price was manipulated. Every day, the NYMEX, CME and other self-regulating futures exchanges apply that standard to discharge their statutory duties. Now FERC claims a different legal standard for manipulation should be applied to futures markets, and possibly not just natural gas futures markets.[1] Its claim has generated considerable uncertainty among self-regulatory bodies, like NYMEX and CME, as well as futures market participants.

Congress enacted CEA exclusive jurisdiction to avoid this type of legal uncertainty, by preventing both duplicative and conflicting regulation of futures trading. Congress knew "the futures markets play a significant role in the economic well being of our country," (H.R. Rep.

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[1] On September 26, 2007, Dow Jones cited the view of a FERC Commissioner that FERC's jurisdiction could extend to currency and metals futures markets as well. I. Talley, *UPDATE: Court May Settle CFTC, FERC Oversight Turf Battle,* Factiva®, Dow Jones International News, Sept. 26, 2007.

No. 93-975, at 60 (1974)), and designed the CEA's exclusive jurisdiction provision "to bring the markets under a uniform set of regulations" found in the CEA, and subject to the CFTC's expert administration. *AAM v. CBOT*, 977 F.2d 1147 at 1156 (7th Cir. 1992). After 32 years under CEA exclusive jurisdiction, the U.S. futures markets have grown to $5 trillion in daily trading volume by escaping the uncertainty, confusion and cost of "varying and potentially conflicting legal standards" (*id.*), exactly as Congress intended.

In sum, Congress enacted CEA exclusive jurisdiction because it did "not believe the public interest would be served by duplicating in one or more additional agencies regulatory authority over futures markets that presently exists in the Commodity Futures Trading Commission." H.R. Rep. No. 95-1181, at 13 (1978). Neither does the Futures Group. Neither should this Court. (See Section II.)

ARGUMENT

I. Because the CEA's Exclusive Jurisdiction Provision Ousts FERC of Futures Market Price Manipulation Jurisdiction, Defendants Have a Strong Likelihood of Success.

The Commodity Exchange Act's exclusive jurisdiction provision means what it says: the CFTC "shall have exclusive jurisdiction . . . with respect to . . . transactions involving" natural gas futures contracts trading on a CFTC-designated contract market, like NYMEX. 7 U.S.C. § 2(a)(1)(A). Where, as here, a statute's terms are patently clear, that is the end of the inquiry. *Hughes Aircraft Co. v. Jacobson*, 525 U.S. 432 at 438, 119 S. Ct. 755 (1999). "This Court's review . . . begins with the statute's language. Where that language provides a clear answer, it ends there as well." (internal citations omitted)

Ironically, FERC responds with a different "exclusive jurisdiction" claim -- that appellate courts have "exclusive jurisdiction" on appeal from FERC orders. FERC Br. at 1, 18-21. Embedded in this argument is a telling, perhaps conclusive, admission. FERC concedes that if one party is granted by statute "exclusive jurisdiction," that statute must be read to preclude any other party from exercising its powers within the "exclusive" area. Otherwise the word "exclusive" is meaningless. FERC never explains, because it cannot explain, why the asserted appellate "exclusive jurisdiction" divests this Court of jurisdiction, but CFTC "exclusive jurisdiction" does not divest FERC of jurisdiction. As the CFTC's brief confirms, FERC should lose on the merits because Congress granted "exclusive jurisdiction" to the CFTC to preclude other agencies from acting as FERC has here.

A. The Statutory Text of the CEA's Grant of Exclusive Jurisdiction.

The text of the Commodity Exchange Act reveals why FERC has no jurisdiction to pursue a case for futures price manipulation. It says:

> The [CFTC] ***shall have exclusive jurisdiction****, except to the extent otherwise provided* in subparagraphs (C) and (D) of this paragraph and subsections (c) through (i) of this section, ***with respect to*** accounts, agreements (including any transaction which is of the character of, or is commonly known to the trade as, an "option", "privilege", "indemnity", "bid", "offer", "put", "call", "advance guaranty", or "decline guaranty"), and ***transactions involving contracts of sale of a commodity for future delivery, traded or executed on a contract market designated*** or derivatives transaction execution facility registered pursuant to section 7 or 7a of this title or any other board of trade, exchange, or market, and transactions subject to regulation by the Commission pursuant to section 23 of this title. *Except as hereinabove provided*, nothing contained in this section shall (I) supersede or limit the jurisdiction at any time conferred on the Securities and Exchange Commission or other regulatory authorities under the laws of the United States or of any State, or (II) restrict the Securities and Exchange Commission and such other authorities from carrying out their duties and responsibilities in accordance with such laws.

7 U.S.C. § 2(a)(1)(A) (emphasis supplied). This provision establishes three things: 1) CFTC jurisdiction over futures trading on an exchange like NYMEX is "exclusive;" 2) any exceptions to exclusive jurisdiction are set out in the provision itself; and 3) "except" for those matters committed to CFTC exclusive jurisdiction, FERC and other agencies retain their full powers.

The FERC alleges that Amaranth's futures trading misconduct manipulated the natural gas futures price on NYMEX. Those allegations fit comfortably within the statutory description of the statute's mandate: the CFTC "shall have exclusive jurisdiction . . . with respect to . . . transactions involving contracts of sale of a commodity for future delivery, traded or executed on a contract market." 7 U.S.C. § 2(a)(1)(A). Giving meaning to each statutory term in that provision, FERC has no valid jurisdictional claim.

Three parts of the exclusive jurisdiction grant have specific statutory definitions. Natural gas is a "commodity" under 7 U.S.C. § 1(a)(4) (any goods, articles, rights and interests in which futures are traded). NYMEX is a "designated contract market" under 7 U.S.C. § 7. Its futures contracts are what the statute calls "contracts of sale of a commodity for future delivery."

The issue here thus turns on whether the elastic phrase -- "jurisdiction . . . with respect to . . . transactions involving" NYMEX natural gas futures contracts -- encompasses a market participant's trading of such contracts. An order to buy or sell, as well as the buying and selling of a futures contract, are surely "transactions." See *FTC v. Roberts*, 276 F.3d 583, 590 (D.C. Cir. 2001) ("transactions" in the exclusive jurisdiction provision "seems most naturally read as encompassing . . . a set of arrangements directly related to the actual sale of commodities futures"). All trading conduct is easily covered by jurisdiction "with respect to" and "involving" orders to buy and sell futures contracts, including misconduct which constitutes futures price manipulation (7 U.S.C. § 9, 13b). FERC's claim that futures price manipulation is not captured by that phrase (FERC Br. 34-36) cannot be squared with the actual words Congress used: futures price manipulation is surely conduct "with respect to transactions involving futures contracts."

Now consider the statutory prelude, the "[CFTC] shall have exclusive jurisdiction." The Random House Dictionary (2d ed. 1967) defines "exclusive" to mean "shutting out all others from a part or share."[2] The plain meaning of 7 U.S.C. § 2(a)(1)(A) is that the CFTC's jurisdiction over Amaranth's trading in natural gas futures contracts shuts out FERC from sharing that jurisdiction. As the Seventh Circuit has ruled, the congressional grant of exclusive jurisdiction under the CEA could have "no other possible meaning." *Chicago Mercantile Exchange v. Securities and Exchange Commission*, 883 F.2d 537, 544 (7th Cir. 1989).

FERC argues Congress created an exception to CFTC exclusive jurisdiction in 2005. The text of 7 U.S.C. § 2(a)(1)(A) disproves that contention. When Congress wants to shave off part of exclusive jurisdiction, it enacts exemptions within 7 U.S.C. § 2(a)(1)(A) itself, as exemplified by the phrase "except to the extent otherwise provided in subparagraphs (C) and (D) of this paragraph and subsections (c) through (i) of this section." FERC is not relying on any of those exceptions for its jurisdictional claim. Nor could it. Those provisions cover amendments in 1982 and 2000 that were designed to a) reassign some CFTC jurisdiction to the Securities and Exchange Commission, b) identify new products over which CFTC and SEC share jurisdiction or c) describe areas where the CFTC had no jurisdiction, let alone exclusive jurisdiction.[3]

The second sentence in 7 U.S.C. § 2(a)(1)(A) also is of no help to FERC. It begins "except as hereinabove provided" and then recites that agencies other than the CFTC retain their

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2 The plain meaning of exclusive should be beyond dispute. The Supreme Court itself has construed its own "exclusive jurisdiction" to deny the jurisdiction of other federal courts to hear cases brought by one state against another. *California v. Arizona*, 440 U.S. 59 (1979).

3 Subparagraph (C) originally was enacted as part of the 1982 Shad-Johnson Jurisdictional Accord. The 1982 Accord reassigned jurisdiction over some products to the SEC. Public Law 97-303 Sec 1, 2 (1982); Public Law 97-444 Sec 101 (1983). *See* 7 U.S.C. § 2(a)(1)(C). In 2000, the Commodity Futures Modernization Act, Public Law 106-544 (Appendix E) (2000), created security futures products to be jointly regulated by CFTC and SEC 7 U.S.C. § 2(a)(1)(D) and granted various statutory exclusions and exemptions under 7 U.S.C. § 2(c)-(i).

own statutory powers under the statutes they administer. Through this phrase, Congress has reaffirmed that CFTC exclusive jurisdiction is a trump card. If actions or conduct are subject to CFTC authority with respect to transactions involving futures contracts, the CFTC's authority is exclusive. If not, and only if not, then other agencies may exercise their applicable statutory powers. As the Seventh Circuit noted long ago, what is provided "hereinabove" in 7 U.S.C. § 2(a)(1)(A) is CFTC exclusive jurisdiction. *Board of Trade of the City of Chicago v. SEC*, 677 F.2d 1137 at 1145 (7th Cir. 1982), *vacated as moot*, 459 U.S. 1026, 103 S.Ct. 434 (1982). Thus, if Amaranth's trading activities fit within CFTC exclusive jurisdiction, the savings clause does not revive FERC's jurisdictional claim.

The statute's terms offer strong support for Defendant's likely success on the jurisdictional merits. Its history and relevant case law further strengthen that support.

B. <u>The 1974 Legislative History Affirms the Scope of Exclusive Jurisdiction.</u>

Congress enacted exclusive jurisdiction in the Commodity Futures Trading Commission Act of 1974. Before 1974, the Commodity Exchange Act applied to futures trading in only the commodities listed in 7 U.S.C. § 1(a)(4) and was enforced by an agency within the U.S. Department of Agriculture. In the CFTC Act, Congress expanded the reach of the CEA so that it applied to futures trading in anything but onions (*see Board of Trade of the City of Chicago,* 677 F.2d at 1142, n. 9), and created the CFTC as an independent regulatory agency charged with administering the provisions of the CEA.

The key feature of the 1974 legislative history was the role of the Conference Committee in reconciling the differing House and Senate versions of the pending bills' exclusive jurisdiction provisions. The Conference Committee decided the House version was ambiguous, so the Committee adopted the Senate's provision to make sure "the Commission's jurisdiction over futures contract markets ...is exclusive ... and *the Commission's jurisdiction, where applicable,* *supersedes* State as well as *Federal agencies*."[4] The Conference Committee further explained: "Under the exclusive grant of jurisdiction to the Commission, the authority of the Commodity Exchange Act (and regulations issued by the Commission) would preempt the field insofar as futures regulation is concerned." H.R. Rep. No. 93-1383, at 35 (1974) (Conf. Rep.).

The context in which Congress acted in 1974 adds further support to the expansive and crucial nature of exclusive jurisdiction. A number of themes run throughout this history.

- Congress recognized "the futures markets play a significant role in the economic well being of our country." H.R. Rep. No. 93-975, at 60 (1974).

- Congress wanted to strengthen futures regulation, create a comprehensive regulatory structure for the esoteric futures trading complex, and avoid regulatory gaps. H.R. Rep. No. 93-975, at 1 (1974); S. Rep. No. 93-1131, at 19; 120 Cong. Rec. 34736 (1974) (statement of H. Comm. Chairman Poage) ("It was the intent of the [Conference] Committee to fill all regulatory gaps -- to regulate trading in futures and in options relating to commodities or commodity futures, because such trading is now poorly regulated, if it is regulated at all.").

- Congress wanted to create an independent agency for futures, modeled after the SEC, but recognized securities regulation principles would be a poor fit for futures. S. Rep. No. 93-1131, at 19 (1974; H.R. Rep. No. 93-975, at 70-72 (1974).

- Congress wanted the new agency to be an expert in futures regulation which "requires highly specialized skills;" H.R. Rep. No. 93-975, at 71 (1974), see also S. Rep. No. 1131, at 22 (1974 ("persons of demonstrated knowledge in futures trading").

- Congress wanted the CFTC to be a neutral arbiter of futures prices, without the conflict of interest (not inclined to seek higher or lower prices) other agencies, including USDA, would have, H.R. Rep. No. 93-975, at 60 (1974). "The proper regulatory function of an agency which regulates futures trading is to assure the market is free of manipulation and other practices which prevent the market from being a true reflection of supply and demand." (S. Rep. No. 93-1131, at 21 (1974.)

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4 H.R. Rep. 93-1383, at 35 (1974) (Conf. Rep.) (*emphasis supplied)*; S. Rep. No. 93-1131, at 23 (1974) (same). It is surprising in light of this clear statement twice from Committees of Congress -- CFTC regulatory authority over futures where applicable supersedes other federal agencies -- for the D.C. Circuit to have called it "specious" to contend that what the CFTC regulates it regulates exclusively. *FTC v. Roberts*, 276 F.3d at 591. Perhaps the difference is that the FTC investigation at issue in Roberts did not focus on regulation of futures trading.

- Congress appreciated that as futures trading and regulation expanded to new commodities other agencies could try to regulate or otherwise exercise jurisdiction over futures markets. (S. Rep. No. 93-1131, at 23 (1974.)

- Congress knew that futures and options trading had been subjected to the vagaries of state blue sky laws and SEC enforcement actions prior to 1974. (H R. Rep. No. 93-975, at 48, 120 Cong. Rec. 34737 (1974) (statement of H. Chairman Poage), 120 Cong. Rec. 34997 (1974) (Statement of Sen. Comm. Chairman Talmadge).

This last point is critical in the context of FERC's jurisdictional assertions. Congress enacted CFTC exclusive jurisdiction to close down efforts by the SEC and state regulators to enforce their laws against those engaged in futures and options activities. This broad reach of CFTC exclusive jurisdiction was so well understood in 1974 that Congress added Section 412 to the CFTC Act to make sure that other agencies knew they could continue to investigate pre-1974 cases under their existing regulatory statutes. However, no regulatory agencies would be able to investigate or prosecute cases relating to futures misconduct arising after CFTC exclusive jurisdiction took effect, as the case law the CFTC's brief cites makes clear.

C. Courts Uniformly Hold CEA Exclusive Jurisdiction Bars Other Agencies From Futures Regulation.

The CFTC's brief describes well the history of judicial acceptance of CFTC exclusive jurisdiction largely in two contexts. The first group of decisions arose when state or federal regulators have sought to enforce their regulatory statutes against persons engaging in alleged misconduct with respect to transactions within the CFTC's exclusive jurisdiction. A universal theme running through these decisions is that, because Congress had established exclusive authority in the CFTC over activities in the futures markets, other regulatory agencies could not "exercise concomitant or supplemental regulatory authority over the identical activity." *International Trading v. Bell*, 556 S.W. 2d 420 at 425 (Ark S.C. 1977). One court, in discussing the SEC's attempt to patrol commodity options trading, was particularly blunt stating "whatever authority the Securities and Exchange Commission previously exercised . . . [it] has been unequivocally ended by Congress." *Bartels v. International Commodities Corporation*, 435 F. Supp. 865 at 869 (1977).[5]

A second class of cases illustrates further the reach of CFTC exclusive jurisdiction. Even where the SEC approved and stood ready to regulate securities exchange trading of new products that were, as a matter of economic substance, a commodity option or a stock index futures contract, the U.S. Court of Appeals for the Seventh Circuit nullified the SEC's approval, holding the CFTC's authority over the trading of such products to be exclusive. *Board of Trade of the City of Chicago*, 677 F.2d at 1138; *Chicago Mercantile Exchange*, 883 F.2d at 549-550.

The one case FERC relies upon where an exclusive jurisdiction claim was not upheld actually read 7 U.S.C. § 2(a)(1)(A) to include "business deals that involve the buying and selling of futures, which comports with Congress' goal of conferring the CFTC with sole regulatory authority over 'futures contract markets . . .'" *FTC v. Roberts*, 276 F.3d at 590. If the *Roberts* reading of CFTC exclusive jurisdiction is applied here, FERC plainly has no jurisdiction. In *Roberts* the Court concluded that CFTC exclusive jurisdiction did not preclude the Federal Trade Commission from investigating (rather than prosecuting) a firm that instructed people in how to trade futures, activity the D.C. Circuit was not at all sure was subject to any CFTC regulatory jurisdiction, let alone exclusive jurisdiction. 276 F.3d at 589. In contrast, as the CFTC's brief shows, it is patently clear that the Defendants' futures trading here falls well within the CEA's exclusive jurisdiction provision.

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5 The FERC's brief asserts that its new manipulation powers, modeled after SEC Rule 10b-5, overcome the word "exclusive" in the CEA's exclusive jurisdiction provision. FERC Br. at 10, 30-36. In 32 years, no court has ever held that the SEC itself could bring an enforcement action under Rule 10b-5 against futures traders solely for futures market manipulation. The SEC has never filed such a case.

D. The 2005 Energy Act Did Not Repeal CEA Exclusive Jurisdiction.

The CFTC's brief also correctly analyzes the 2005 Energy Act. As FERC's brief explains, its jurisdiction, like that of the CFTC, is transaction-based (FERC Br. at 4). ("NGA grants FERC jurisdiction over 'the sale of natural gas for re-sale.'") In 2005, Congress did not expand the scope of natural gas sales subject to FERC's jurisdiction in any way. The best evidence again is found in the statute itself: FERC's new manipulation authority is expressly limited to misconduct in connection with natural gas sales that already are "subject to the jurisdiction of the Commission." Energy Policy Act of 2005, Pub. L. No. 109-58, § 315 (2005). The absence of any stated change to FERC's transaction-based jurisdiction dispels any possible notion its new authority silently repealed CEA exclusive jurisdiction.

FERC itself is on record agreeing with that statement. At Congress' direction in the 2005 Energy Act, the FERC and CFTC entered into a Memorandum of Understanding (MOU). FERC explicitly recognized "the CFTC has exclusive jurisdiction with respect to . . . transactions involving" natural gas futures contracts, while CFTC recognized FERC's natural gas physical market jurisdiction was "exclusive." FERC and CFTC MOU, Oct. 12, 2005. This agreement shows that contemporaneous with the passage of its new anti-manipulation powers in 2005, FERC did not challenge the scope of CFTC exclusive jurisdiction in any way or suggest that it had been implicitly, partially repealed by Congress.

FERC claims the words "in connection with" in its new manipulation authority excuse it from the CEA's exclusive jurisdiction provision because natural gas physical sales may rely derivatively on futures prices and may result from that small percentage of futures contracts that are not offset, but held to delivery. (FERC Br. at 7-9) FERC cites, however, no evidence that Congress understood those words to override the CEA's provisions. Moreover, if FERC's theory is accepted, it would end CFTC exclusive jurisdiction because other agencies, including the SEC, Treasury Department and Agriculture Department, would have similar claims on futures market jurisdiction. Congress surely never intended that.

II. A Stay Would Serve The Public Interests Underlying CFTC Exclusive Jurisdiction.

If a stay is denied and FERC proceeds with its administrative action, it would imperil the public interests served by the CEA's exclusive jurisdiction provision. Congress designed exclusive jurisdiction to prevent uncertain and conflicting legal standards, as well as regulatory duplication, from interfering with the smooth functioning of U.S. futures markets in order to allow those markets to serve the public interests in hedging and price dissemination. 7 U.S.C. § 5(a). FERC's proceeding endangers that congressional objective.

In 1974, Senator Herman Talmadge emphasized: "In establishing this Commission, it is the Committee's intent to give it exclusive jurisdiction over those areas delineated in the act. This will ensure that the affected entities -- exchanges, traders, customers, et cetera -- will not be subject to conflicting agency rulings."[6] The FERC itself has read this same history and found that Congress intended the CEA's exclusive jurisdiction provision "to give a single expert agency the responsibility for developing a coherent regulatory program for the commodities industry and to prevent the costs and confusion associated with multiple regulators."[7] Yet

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6 120 Cong. Rec. 30459 (1974) (Sen. Comm. Chairman Talmadge). *See also* 120 Cong. Rec. 34736 (1974) (House Committee Chairman Poage explained the Conference Committee adopted the Senate exclusive jurisdiction formulation "in an attempt to avoid unnecessary overlapping and duplicative regulation.") In 1978, the Senate Committee on Agriculture, Nutrition and Forestry again reported, "The vesting of jurisdiction to regulate commodity futures trading in more than one agency would only lead to costly duplication and possible conflict of regulation or over-regulation." S. Rep. No. 95-850 at 23 (1978).

7 New York Mercantile Exchange, No. EL 95-81-000, 74 FERC ¶ 61311 (1996). Just last week, the leadership of the House Committee on Agriculture echoed FERC's understanding of this history. *See* Sept. 27, 200[7] Letter to CFTC Acting Chairman Walt Lukken from U.S. Reps. Peterson, Goodlatte, Etheridge and Moran. ("Congress made this unusual grant of exclusive jurisdiction to end the confusion caused by two separate federal regulators. This wisdom continues to prove itself.")

FERC's proceeding will lead to just the sort of "costs and confusion" it acknowledged Congress sought to prevent.

The CEA has a well-known, time-tested legal standard for futures price manipulation -- intentional creation of an artificial price. In FERC's proceeding, it will apply a different standard for futures price manipulation, one modeled after SEC Rule 10b-5. Congress long ago realized, however, that securities law concepts should not be exported to futures regulation, concluding it was "erroneous" to view futures and securities regulation as "twins." H.R. Rep. No. 93-975, at 71 (1974). Thus, a futures manipulation standard grounded in securities regulation cannot be further from the result Congress envisioned in 1974.

FERC's manipulation standard would be problematic even if it was not securities law-based as it will result in legal uncertainty or conflict, the worst of the ills for which exclusive jurisdiction was to be the antidote.[8] Neither futures market participants nor self-regulating futures exchanges will know what price manipulation standard applies to their trading or market surveillance. Just that uncertainty alone may cause large and reputable market participants to find other markets or methods by which to manage natural gas price risks. But if FERC adopts, as its brief suggests, a definition of manipulation that would punish unintentional, yet reckless, conduct, the impact on futures trading could be potentially devastating.

In futures markets, even the most innocent futures trader or commonplace trading strategies may have a price impact, depending upon market liquidity and other circumstances. Logically, that would be more true when market participants take larger futures positions, as

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8 Merely duplicative futures regulation will inevitably lead to increased costs for market participants, firms and exchanges. This would be enough to tilt the public interest scales in favor of a stay. Higher trading costs make it more costly to hedge or provide necessary market liquidity. They could also lead to a serious competitive disadvantage for U.S. futures markets.

many businesses do that use futures markets to hedge, for example, the risk of a future change in natural gas prices. If FERC applies an unintentional price manipulation standard to this futures trading (including its now undefined "reckless disregard" standard), legitimate traders engaging in common trading practices may eschew U.S. futures markets for fear of becoming ensnared in an after-the-fact dragnet by FERC, which lacks the CFTC's experience and expertise in futures markets and trading. FERC might even miscite such a trader's positions and conduct as reckless and the cause of a FERC-perceived manipulative price movement in natural gas futures.

The point is that FERC's enforcement of a new futures market manipulation standard will, at best, breed uncertainty, and more likely, legal conflict, into this important economic activity. That uncertainty or conflict may trigger a loss in market liquidity and related hedging opportunities, with dire consequences for U.S. futures markets. 7 U.S.C. § 5(a) (Congress finds national public interest served by liquid, fair and financially secure futures markets).

The problems for self-regulating exchanges are just as profound. NYMEX conducts constant market surveillance to prevent price manipulation of its natural gas futures markets under the CEA. 7 U.S.C. § 7(d)(4). In fact, Congress found that "effective self-regulation" by NYMEX and other exchanges under the CEA "serve[s] the public interests." 7 U.S.C. § 5(b). Technically, NYMEX would be expected to discharge its statutory duty to prevent manipulation under the legal standard defined in the CEA. Are NYMEX and other exchanges also supposed to apply the FERC manipulation standard? The CFTC's brief would say "no," because the CFTC's jurisdiction is exclusive and it is NYMEX's regulator. But FERC's brief and its proceeding cast a cloud on the CFTC's position.

The FERC might answer that NYMEX is supposed to enforce one set of anti-manipulation rules under the CEA, while FERC waits in the wings with admittedly very different standards. It is hard to think of a more confused or uncertain law enforcement scenario where one set of cops on the beat (NYMEX and CFTC) are enforcing one set of traffic laws at the "Futures Square Intersection," while another officer (FERC) enforces a different, yet unknown, set of traffic laws at the same Intersection. Any reasonable driver would avoid that intersection.

The stay motion urges this Court to provide for an orderly, sequential adjudication of these price manipulation cases. Logically, that would avoid the conundrum this Court could face if FERC proceeds first and finds Amaranth not to have intended to manipulate the futures price and not to have recklessly done so either. How could this Court then find that Amaranth intended to attempt to manipulate the futures price? Similarly, if this Court finds that Amaranth *did not* intend to attempt to manipulate the futures price under the CEA, and FERC finds that Amaranth *did* intend to manipulate the futures price, how will that conflict be resolved? And what market impact would be triggered by such legal uncertainty about the law of manipulation?

Granting the stay would allow the CFTC's case against Amaranth to move forward expeditiously. In the interim, FERC could concentrate its resources on other matters. It would also allow the CFTC and FERC to discuss ways to ensure the two agencies do not find themselves again in the situation where the CFTC believes FERC has no jurisdiction, but cannot convince FERC to stand down, even temporarily. This Court's eventual resolution of the merits of this case also could make it unnecessary or impractical for FERC itself to proceed. Thus, an orderly approach may conserve government resources.

The CFTC's posture in this Court is understandably conflicted. On the merits of exclusive jurisdiction, the CFTC knows FERC is wrong. But the CFTC does not want to appear to support a defendant whom it believes engaged in serious misconduct. What the CFTC's brief discounts, however, is that Congress enacted the CEA's grant of exclusive jurisdiction to serve identified public interests, not to protect any agency's territory. Exclusive jurisdiction was designed expressly to allow those, like the Futures Group, who compete in this specialized and complex area of commerce to conduct their legitimate and important business operations with the certainty that they must meet one set of legal standards, established by one regulatory body with experience and expertise in futures trading and markets. Granting the stay would promote that public interest. Denying the stay would not.

CONCLUSION

For the above stated reasons, the *amici curiae* Futures Group urges this Court to find that defendant Amaranth has a strong likelihood of success on the merits of its argument based on the exclusive jurisdiction provision in 7 U.S.C. § 2(a)(1)(A) and that the public interest would be well served by granting the requested stay.

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