Before the
FEDERAL TRADE COMMISSION
Washington, D.C.

In the Matter of	)	
	)	
Market Manipulation Rulemaking	)	Project No. PO82900
	)	

COMMENTS OF THE AMERICAN PETROLEUM INSTITUTE AND THE NATIONAL PETROCHEMICAL AND REFINERS ASSOCIATION IN RESPONSE TO REVISED NOTICE OF PROPOSED RULEMAKING

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The American Petroleum Institute ("API") and the National Petrochemical and Refiners Association ("NPRA") welcome this opportunity to submit comments on the Commission's Revised Notice of Proposed Rulemaking ("RNPRM").[1] API and NPRA appreciate the Commission's efforts to address concerns with the proposed rule identified in our prior comments[2] and those of other commenters. In particular, API and NPRA welcome the Commission's recognition that wholesale petroleum markets differ significantly from securities markets and the Commission's efforts to tailor the proposed rule to reflect those differences.[3]

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[1] API and NPRA are national trade associations representing the U.S. oil and natural gas industry. API's approximately 400 members cover all facets of the industry, including exploration, production, transportation, refining, and marketing. NPRA's more than 450 members own or operate virtually all U.S. petroleum refining capacity and include most of the nation's petrochemical manufacturers. API and NPRA offer an industry-wide perspective on the issues raised by the RNPRM that may be of assistance to the FTC.

[2] *See Comments of the American Petroleum Institute and the National Petrochemical and Refiners Association* (June 23, 2008) [hereinafter, *API/NPRA Comments*]; *Comments of the American Petroleum Institute* (Oct. 17, 2008) [hereinafter, *API Comments*]; *Comments of the National Petrochemical and Refiners Association* (Oct. 17, 2008) [hereinafter *NPRA Comments*].

[3] *See* Federal Trade Commission, *Revised Notice of Proposed Rulemaking: Request for Public Comment on Prohibitions on Market Manipulation in Subtitle B of Title VIII of The Energy Independence and Security Act of 2007* [hereinafter *RNPRM*] at 22 ("[T]he Commission believes that modifying the proscriptions of the initially proposed rule will better focus it on wholesale petroleum markets, which differ significantly from securities markets.").

We believe, however, that further improvements are possible and desirable, based on information that the Commission has gathered in the course of this proceeding.

EXECUTIVE SUMMARY

The submissions of API, NPRA and their member companies throughout this proceeding have emphasized a common theme. The FTC's numerous and extensive investigations of the petroleum industry have uncovered no evidence that market manipulation has distorted petroleum markets or harmed consumers. Consumers will be harmed, however, if the Commission adopts a rule that undermines the efficiency of these markets and makes it harder for participants to respond effectively to ever-changing conditions. Although we continue to believe that the balance of likely benefits and costs supports a decision not to promulgate any rule at this time, these comments will offer constructive suggestions for improvements to the proposed rule.

Specifically, we recommend that the Commission revise the proposed rule in three respects:

- ***Eliminate, Or Further Narrow And Clarify, The Scope of Liability for Omissions.*** Responsible market participants today disclose information that is valuable to customers and trading partners while refraining from disclosures that could undercut business opportunities or facilitate anticompetitive collusion. A market manipulation rule that imposes liability on omissions will disrupt this balance, thereby deterring market participants from releasing valuable information into the market and increasing costs for all market participants. It will also invite challenges to truthful but incomplete disclosures, which will further pressure market participants not to disclose information. Accordingly, the rule should be revised to eliminate liability for omissions. This objective can be accomplished by adopting the alternative rule language set out at page 88 of the RNPRM and confirming that this language covers affirmative fraudulent acts and statements but not omissions.

  If any final rule imposes liability for omissions, it should expressly state that silence, pure omissions, and "no comment" are not actionable. It should also expressly state that if conduct is subject to liability as an omission under Section 317.3(b), it shall not be subject to liability under Section 317.3(a). Furthermore, any final rule should expressly reflect the absence of any duty on market participants to update or correct information if circumstances change. Imposition of such a duty would be counterproductive, further discouraging market participants from disclosing information that they would otherwise disclose.

- ***Require Specific Intent For All Conduct.*** The RNPRM correctly recognizes the shortcomings of a knowledge / extreme recklessness standard as applied to omissions and proposes an intent standard for this category of conduct.[4] The rationale for applying a higher scienter standard to omissions also applies to affirmative statements, which provide an important means by which wholesale petroleum market participants disclose information that benefits consumers and contributes to market efficiency. Similarly, a lower scienter standard (knowledge) risks upsetting existing business practices when applied to conduct other than statements (*e.g.*, supply decisions, production decisions, etc.). The alternative rule language, which would apply an intent standard to all conduct, represents a significant improvement.

  A weakness in both the revised proposed rule and the alternative rule language is that the intent standard proposed by the Commission would allow the rule to reach misleading statements made in the context of bilateral market transactions, even though the speaker had no intention or expectation of distorting or otherwise affecting market conditions and even though wholly adequate remedies for such statements already exist under state law. API and NPRA continue to believe that specific intent—defined as an intent to deceive or defraud in order to manipulate a covered market—is necessary to limit the rule to the market-distorting conduct that Congress intended to address in Section 811. The unnecessarily broad scope of the proposed rule, combined with the severe penalties available under Section 811, risk triggering industry compliance regimes that sharply curtail efficiency-enhancing disclosures and other beneficial conduct in the context of bilateral transactions that have no potential to affect market conditions.

- ***Require Market Effects For All Conduct.*** Section 317.3(b) of the revised proposed rule limits liability for omissions to those that "distort[ ] or tend[ ] to distort market conditions." While this is an improvement over the previous version of the proposed rule, the rationale for a market distortion requirement applies with equal force to practices covered by Section 317.3(a). In enacting a "Prohibition on Market Manipulation," Congress focused its attention on deceptive or fraudulent conduct that manipulates a *market*. Nothing in the language or legislative history of Section 811 indicates that Congress intended to cover any practice that affects only the parties to a specific transaction and has no impact on the broader market. The alternative rule language, which applies the

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[4] *RNPRM*, at 68 (observing that a knowledge / extreme recklessness standard "would have imposed on wholesale market participants the obligation to know whether a person would likely be defrauded or deceived by the conduct at issue, which could be difficult.").

market distortion requirement to all covered conduct, is markedly better than the revised proposed rule in this regard. If the Commission retains the distinction between affirmative statements and omissions reflected in Sections 317.3(a) and (b) of the revised proposed rule, the final rule should be revised to apply the market distortion requirement to both of these provisions.

In addition, any final rule should clarify that the market distortion element requires proof that the challenged conduct either distorted a market or was likely to do so under the circumstances. As drafted, this requirement covers omissions that "tend to distort" market conditions. "Tendency" is an imprecise term, susceptible to widely different interpretations. The inclusion of this term in a final rule would risk an expansive interpretation, subjecting market participants to potential liability for conduct that presents no real risk of affecting any market or consumers.

I. AS WHOLESALE PETROLEUM MARKETS ALREADY FUNCTION WELL WITHOUT A MARKET MANIPULATION RULE, THE COMMISSION SHOULD PROCEED WITH GREAT CARE.

Most of these comments respond in detail to the Commission's questions, revised proposed rule, and the alternative rule language. Before engaging in that detailed analysis, however, we discuss the context in which this rulemaking arises. That context reveals a well-functioning industry, whose enormous benefits to the American economy would be reduced through the uncertainty of an ambiguous "market manipulation" regulation.

A. Wholesale Petroleum Markets Are Efficient And Competitive.

The U.S. petroleum industry is highly competitive. New entry and a decline in vertical integration between crude oil production and refining have increased competition in many segments of the petroleum industry, including refining.[5] Numerous firms populate each

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[5] *See* Michael A. Salinger, Director, Bureau of Economics, FTC, Prepared Statement of the Fed. Trade Comm'n. on Petroleum Industry Consolidation before the U.S. Congress Joint Econ. Comm. (May 2007), *available at*, http://www.ftc.gov/os/testimony/070523PetroleumIndustryConsolidation.pdf; Bureau of Economics, FTC, *The Petroleum Industry: Mergers, Structural Change, and Antitrust* (continued…)

level of the business—at the refinery level, for example, concentration remains well below the levels of many other competitive U.S. industries.[6]

Since 1973, the FTC has conducted well over 100 investigations examining every facet of the petroleum industry. The Commission has not found evidence of collusion or market manipulation. On the contrary, the FTC's studies of petroleum wholesale markets have confirmed the industry's competitiveness. The picture of the U.S. petroleum industry that emerges from the empirical data is one of a well-functioning and competitive market.

B. Wholesale Petroleum Markets Work Well Because Overly-Broad Regulation Is Not in Place to Deter Productive and Beneficial Activity.

The secondary effects of any market manipulation rule should be considered in the context of how wholesale petroleum markets currently work, both normally and in emergencies such as supply disruptions from hurricanes. At all levels of wholesale distribution, including decisions involving refineries and terminals, parties must decide how much to produce, from whom to purchase the input, to whom to sell the output, and at what prices or costs. These decisions currently take place without an FTC manipulation rule. Such production, supply, and distribution decisions in the petroleum industry are enormously complex. Wholesale petroleum markets contain sophisticated, well-informed buyers and sellers that understand the motivations of their counterparties. These parties often trade on the basis of proprietary information that shapes their expectations about future supply and demand. Such markets work best when

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Enforcement (Aug. 2004, *available at,* http://www.ftc.gov/os/2004/08/040813mergersinpetrolberpt.pdf).

6 *See, e.g.*, Timothy J. Muris and Richard G. Parker, *A Dozen Facts You Should Know About Antitrust and the Oil Industry* (June 2007), *available at*, http://www.uschamber.com/NR/rdonlyres/ecw4z24weaarlxr4y4owljhspsc4melp4frhuazd5ppvlkte5zvy6ngoyaegioeds3fjoaxatl53gqz7s3v57gl3tte/070625oilreport.pdf.

participants have incentives to invest in the creation of such proprietary information and are free to decide whether and how much of it to disclose to counterparties or otherwise inject into the marketplace.

Refineries do not always operate at full capacity. Instead, "turnarounds" and partial shutdowns for maintenance are routine. When a planned outage or downtime would affect customers, refiners may discuss their plans with those customers. Truthful announcements of downtime or other statements about capacity utilization increase the efficiency of the market, helping participants react rationally to future conditions.

Many refining companies currently provide a substantial volume of additional real-time information to their refined product marketers and crude oil traders who actively participate in the market and who will, on occasion, share such information with other market participants. The goal of providing a steady flow of production information to these employees is to give them the best possible information about a company's current and expected future operations. At the same time, the information is shared with these employees in the expectation that perfection in the information is unnecessary. In contrast, market participants have very different procedures for providing information to government entities, given the potential legal consequences of even inadvertent incorrect disclosures. Typically, companies limit *who* is authorized to talk to the government, and they have rigid fact-checking requirements for each individual piece of information they disclose. Such procedures make sense for official disclosures in which the government demands precision and for which there is time for complete data analysis and fact-checking, but would be extremely burdensome for purposes of market interactions in which the timeliness of information is as important as precision in quickly identifying market trends and reacting to events in real time.

Supply disruptions occur periodically. A pipeline may break; a refinery may have unplanned outages; or a natural disaster may shut down facilities. These emergencies, by their very nature, require creativity, ingenuity, and spur-of-the-moment decisions to balance competing needs in the face of a reduction in output. In the aftermath of Hurricanes Katrina and Rita, for example, companies rapidly changed "normal" distribution patterns. Many refineries were disabled and available petroleum supply from the Gulf Coast decreased substantially. Following each hurricane, Midwest refineries (as well as operating Gulf Coast refineries) increased production, sometimes operating above long-term sustainable rates, temporarily delaying maintenance, or shifting to other fuels to achieve greater production. In some instances, products from Midwest refineries were shipped south to the Gulf Coast rather than the usual, and opposite, pattern. Less product was shipped from Gulf Coast refineries to the East, and imports from Europe were increased substantially to compensate. Firms obtained product specification waivers to enable greater gasoline production and use of more flexible supply in affected areas. These and other steps promoted the quick return of price levels to pre-hurricane levels.[7]

C. <u>The Threat Of Liability Will Induce Firms To Enact Rigid Compliance Policies That Chill The Dissemination Of Useful Information</u>.

Unlike other unfair or deceptive acts or practices, for which the penalty per violation under the FTC Act is $11,000, the maximum penalty here is nearly 100 times greater—$1 million—and it compounds each day until a violation is rectified. If there is *even a risk* of liability arising from "incomplete" disclosures or projections that later prove incorrect, or from supply or production decisions that are later deemed "manipulative," the magnitude of these

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[7] *See* Fed. Trade Comm'n, *Investigation of Gasoline Price Manipulation and Post-Katrina Gasoline Price Increases*, viii-ix (2006).

sanctions is a strong deterrent to engaging in any activity that could risk liability. Even without monetary sanctions, it is the expectation of the Commission that companies will comply with a market manipulation regulation at all times. To meet that expectation of absolute compliance with the revised proposed rule, firms would be driven to implement rigid, burdensome compliance procedures that would restrict substantially their ability to engage in efficient and pro-competitive activities.

Uncertainty regarding the risk of liability for actions that were considered reasonable at the time but later may be challenged as "manipulation" based on *post hoc* analysis will force market participants to adopt costly procedures similar to those currently undertaken for vetting disclosures to government and necessitate the presence of lawyers as "partners" in business decisions. As noted earlier, the result of this dynamic would be to raise costs, create uncertainties, and prevent market participants from reacting rapidly and effectively to changing market conditions. Because lawyers will not be present for each business decision, the business people will make decisions relating to the buying, selling, and making of products subject to legal guidance, and those decisions will be subject to scrutiny later for manipulation. To be effective, that guidance must be as clear and simple as possible. Complex balancing tests may make sense for regulatory decisions, but business people need clear rules that they can follow to ensure compliance with a regulation in all circumstances. Unclear or overly complex rules may chill the flow of information, and ultimately harm consumers.

These disadvantages are likely to be especially apparent in the event of an emergency situation that disrupts supply. An overly-broad market manipulation rule would make it harder for the market to self-correct efficiently and effectively because it would create a significant disincentive for market participants to disclose the types of information necessary for the market as a whole to respond to rapidly changing conditions.

The presence of reduced supply during an emergency means that inevitably prices will increase and some consumers will suspect that they have been the victims of wrongful behavior. Today, many responsible market participants provide their best estimates of supply conditions without worrying about potential liability under a market manipulation rule. Nevertheless, any prediction of the future during an emergency is likely to be made with great uncertainty. If the prediction involves a refinery, the uncertainty only increases. Refineries are extremely complex, involving many employees and working parts. Whether they are shut down completely or are only partially damaged, restoration to full capacity depends on many variables, some of which may be beyond the control of the refinery owner, including access to electricity, the usability of the transportation system, and the availability of specialized parts or employees. Predictions about the immediate future made during an emergency sometimes turn out to be wrong. Months later, during an investigation, the FTC may discover that some individuals in a company knew or should have known facts that could have led the company to make a different prediction about the refinery's future capability. Because this possibility is all too real, with an overly-broad market manipulation rule in place, the safest course often will be simply to say nothing. As a result, the marketplace will have less information than it has now, making it less efficient and less responsive to consumer needs.

It is important to remember that, in an investigation, the FTC will be second-guessing decisions that occurred in real time, before information had time to circulate fully. *Ex post*, the FTC will have access to complete information, and the time to digest it, in ways that simply were not possible when the decisions were made. The Commission also may have complaints from "aggrieved" parties who have an incentive to gain advantages in future dealings or to rewrite contracts that proved to be unfavorable. All of these problems are present even under normal conditions, but they are especially likely to complicate any investigation of information provided, or not provided, during an emergency. Moreover, aggrieved parties may attempt to bring private actions to enforce any market manipulation rule, *e.g.*, under state "little FTC Acts."

By reducing the amount of information in the marketplace, a market manipulation rule could have a serious and harmful impact on the efficiency of petroleum markets, risking supply fluctuations and a higher price at the pump for consumers. The risk is particularly acute when market conditions are volatile and firms may struggle to gain an accurate picture of their own operations and the broader market landscape. Yet, it is precisely at such times that more, not less, information is needed to facilitate the adjustments in supply required to restore equilibrium to the benefit of consumers.

D. Any Rule Should Be Designed To Minimize Costs.

Because of the need for quick decisions without continuous legal consultation, a Commission decision not to promulgate a rule would provide markets and consumers with the greatest security that existing petroleum development and delivery systems will function efficiently and effectively. Thus, the costs of additional regulation and enforcement and their negative impact on these competitive markets outweigh any potential benefits. If the Commission does promulgate a rule, however, the substantial costs that would result from regulatory errors in its administration indicate that any requirements imposed by the rule should be defined with as much clarity and certainty as possible to minimize those costs and the negative unintended consequences to the consumer.

To minimize regulatory mistakes, we continue to recommend strongly that any manipulation rule be limited to (i) affirmative statements or conduct, and should exclude omissions; (ii) conduct that affects a market; and (iii) parties that specifically intend to defraud or deceive in order to manipulate a market. A market manipulation rule should protect the market, not individual participants who might be adversely affected by a particular representation that has no market impact. Other laws, such as contract law and state unfair practices laws, are available to address disputes or grievances involving individual transactions.

Finally, any market manipulation rule should not confuse the correct regulatory standard with the evidentiary and legal presumptions necessary to prove violations of the standard. Such legal presumptions are best developed through experience, on a case by case basis. Thus, under the Sherman Act, “Rule of Reason” analysis has been supplemented, after decades of experience, by categories such as “abbreviated” or “quick look” analysis. It is easier to prove a case using abbreviated analysis, but that application of the Rule of Reason did not develop simply to benefit plaintiffs. Experience has revealed that certain practices are so inherently likely to be anticompetitive that they can be evaluated without resort to full Rule of Reason analysis. Nevertheless, the Rule of Reason, requiring an evaluation of the benefits and costs of challenged practices, remains the touchstone for antitrust analysis.

Parts II through IV of these comments address liability for omissions, the appropriate scienter standard, and the need for a market effects requirement, respectively. The Appendix to these comments addresses the questions set forth at pages 83-89 of the RNPRM.

II. ANY RULE SHOULD EITHER ELIMINATE LIABILITY FOR OMISSIONS OR NARROW AND CLARIFY THE SCOPE OF SUCH LIABILITY.

Section 317.3(b) of the revised proposed rule is designed to cover deceptive omissions. As drafted, this section is open to a range of interpretations respecting what facts must be disclosed and when. As the RNPRM acknowledges,

> The Commission recognizes that identifying statements that are unambiguously misleading by dint of a material omission may be difficult in wholesale petroleum markets and create uncertainty within the business community about the Rule's application.[8]

Many market participants may conclude that they cannot confidently comply with this section of the revised proposed rule without moving either to a policy of "100% complete" disclosure or to a policy of "no comment," neither of which is practical or desirable. Section 317.3(b) will chill procompetitive disclosures, disrupt the flow of valuable information into the market, and impose new costs on sources and interpreters of market information. Therefore, we recommend that the Commission eliminate liability for omissions. If liability for omissions is retained, we urge the Commission to clarify and narrow the scope of this liability.

A. <u>A Rule Imposing Liability For Omissions Will Disrupt The Flow Of Valuable Information To The Market</u>.

As it considers the secondary effects of its rulemaking, the Commission should be careful not to disrupt the balance of information that is provided to the market. Today, responsible market participants disclose information that is valuable to customers and trading partners, while refraining from disclosures that could undercut other business opportunities or facilitate anticompetitive cooperation among competitors. Imposing liability for omissions would alter the balance of information provided to wholesale petroleum markets, most likely by

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[8] *RNPRM*, at 69.

deterring market participants from releasing valuable information on issues such as supply availability, impending refinery outages, and the like.

As a general rule, companies in wholesale petroleum markets avoid publishing details of their business plans outside the company. Enforcement actions brought by government and private plaintiffs and the counsel of company lawyers repeatedly remind them that sharing competitively sensitive information can be viewed as a practice that facilitates collusion and should be avoided.[9] The Commission has even suggested in this rulemaking that providing too much information on future plans, such as impending outages, may appropriately be restricted:

> Refiners engage in periodic scheduled maintenance and refinery downtime in order to prevent breakdowns or change equipment. On the one hand, such maintenance and scheduled downtime are necessary for the safe and efficient operation of petroleum refineries; on the other hand, public announcements of downtime may enable competitors to collude inappropriately. The Commission therefore seeks comments on both the costs and the benefits of a rule restricting public pre-announcements of such downtime.[10]

Furthermore, often there are procompetitive business reasons to limit disclosure of production decisions, output constraints, facility improvements, and the like. In general, a firm's ability to profit from its business plans may be undercut if those plans must be shared widely. In the case of a refinery outage, for instance, a refiner may not want to disclose the fact that production is curtailed or that it is making spot purchases. Traders that are aware of the

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[9] *E.g., Todd v. Exxon*, 126 F. Supp. 2d 321, 325 (S.D.N.Y.) (exchange of salary information could violate Section 1 of the Sherman Act), vacated by 275 F.3d 191 (2d Cir. 2001); *In re Coordinated Pretrial Proceedings in Petroleum Prod. Antitrust Litig.*, 906 F.2d 432, 449 (9th Cir. 1990) (publication of pricing and other competitive information supported inference of conspiracy).

[10] FTC, *Prohibitions On Market Manipulation and False Information in Subtitle B of The Energy Independence and Security Act of 2007*, at 30, 73 Fed. Reg. 25614 at 25621 (May 7, 2008) [hereinafter *ANPRM*].

outage might seek to take advantage of the refiner's need to make substantial spot purchases to cover its contractual obligations. This could increase the refiner's costs of stockpiling product.[11]

Given the fact that disclosure and nondisclosure already (and appropriately) are in tension, a rule that created additional legal uncertainty regarding disclosures and thereby led market participants to limit the flow of valuable information to the marketplace would be troublesome. To illustrate the difficulties of applying Section 317.3(b) in real-world situations, we offer here a hypothetical in which a refinery must determine whether and what to disclose about a planned refinery outage:

> RST Refinery is the largest refinery in its region. In advance of turnaround work on several refinery units, which RST anticipates will last four weeks and during which it will have diminished output, RST begins making spot purchases of various refined products, so it can supply customers during the turnaround. At the time it is preparing a communications plan for the turnaround, RST has not yet stockpiled enough supply to meet all anticipated customer demand, but its goal is to have sufficient product from a combination of refinery output and stockpiles at all times throughout the four-week turnaround.

This very ordinary situation highlights how difficult it would be for market participants to identify omissions that could be misleading under Section 317.3(b) and how they might respond to a rule imposing liability on omissions in ways that would leave the market with less valuable information.

1. Liability For Omissions Would Invite Challenges To "Incomplete" Disclosures And Discourage Release Of Valuable Information.

Asked to review the refinery's communications plan for the turnaround, RST counsel learns that "four weeks" is the refinery's best estimate of the length of the outage, but it

[11] In this situation today, some suppliers buy through third parties to avoid revealing their short situation.

could be shorter or longer. Further, although RST is planning to meet anticipated demand for its various products by carefully timing its outages and spot purchases, and it anticipates that it will have access to adequate supply options to do so, it is possible that RST will be short some products at some times, and it has several scenarios of what shortages might occur and when.

A company in RST's position today often will elect to make *some* public announcement in order to avoid speculation and uncertainty if news of the turnaround leaks out. For example, a company could announce that it anticipates an outage of four weeks and that adequate supply should be available during that time. If the Commission were to adopt the revised proposed rule, however, RST counsel would have to advise on whether that type of disclosure created the risk of violating Section 317.3(b). The difficulty will be to determine whether any information that is not disclosed could be characterized as a misleading omission under Section 317.3(b).

One option would be for RST to make a detailed disclosure – with cautionary disclaimers and caveats – reporting that the refinery is uncertain about the length of the outage, that it must make spot purchases to be able to meet demand, and that there is a possibility of some shortages. To more completely minimize the risk of liability, the refinery could try to make a "100%" disclosure, publishing its various scenarios on the possible length of the outage and what shortages there could be if the turnaround does not go as expected and detailing the precise quantities of each product that RST intends to purchase on the spot market and on what days.

For legitimate business reasons, RST will not want to make such disclosures. RST recognizes that some customers might respond to the more detailed information about the outage and possible shortages by making alternative purchases of their own, as retail gasoline consumers "top off" when a possible shortage is rumored. This effect will tend to cause local price spikes and make demand less predictable. In other words, a "100%" disclosure could undercut the effectiveness of the very forecasts RST has made regarding the supply of products that will be needed during the turnaround. Furthermore, speculators likely would seize on such disclosures as an opportunity to turn a quick profit, further increasing local market volatility. Spot traders will seek to charge RST higher prices if they know it is short. Competitors could use this information to charge higher prices to customers, knowing precisely when RST cannot respond.

Under Section 317.3(b) of the revised proposed rule, however, market participants will incur risk if they make any statement that falls short of "100%" disclosure. What RST fails to disclose could be characterized as a misleading omission, one which in certain circumstances might "tend to distort" market conditions. A complainant could allege that customers were not told of possible shortages or a longer outage, so they lost the chance to make contingency purchases. In the event of a shortage and consequent local price spikes, arguably the omissions might have caused or tended to cause market distortions. Moreover, traders could claim they were not told of RST's continuing spot market demand. In hindsight, RST's disclosure could be found to involve misleading omissions to the extent that RST failed to account fully for the opportunistic behavior of other market participants.

Given the risks and uncertainties, the safer course of conduct for a refiner in RST's position is to make no public announcement. Despite the desirability of giving customers some assurances about supply, counsel likely would advise the company simply to provide "no comment," thus depriving the market of useful, efficiency producing information.

2. Eliminating Liability For Omissions Would Better Balance The Costs And Benefits Of Any Market Manipulation Rule.

We believe that not subjecting omissions to liability under any final rule would better balance the costs and benefits of market manipulation regulation. Liability for omissions will lead to a different mix of information from market participants than they provide today, usually less and sometimes more. Where the risk of liability encourages less disclosure, market participants will be deprived of valuable information that lawfully facilitates transactions today. Markets benefit from transparency, up to the point at which insights into competitor plans facilitate tacit coordination. Today, many traders and other petroleum market participants daily share market intelligence, in public statements and bilateral negotiations, without any intent to mislead and without disclosing competitive information that might create antitrust problems. They do so in real time, making best efforts to provide clear and accurate information, without the necessity (or time) for input from counsel or high-level management. In emergency situations, they publish the best information they have, even if they are not able to verify its accuracy. A rule that imposes liability on an ill-defined set of omissions will lead market participants to adopt compliance policies that limit disclosures, denying markets the benefits of the information that is readily disclosed today.

Where market participants seek to comply with an omissions rule by disclosing more information, companies necessarily will need to exercise tremendous caution, to be sure no affirmative statement is pregnant with any omission that arguably is misleading. Releases of information will come more slowly, may be formalized to avoid any misstep, and will undoubtedly be accompanied by disclaimers and caveats that might significantly undercut their value to the marketplace. More detailed disclosures may also present antitrust concerns and undercut legitimate business motivations.[12]

In any event, costs will increase for all petroleum market participants, taxing the efficiency of this important economic sector without significantly benefiting the market or consumers to justify the costs. Suppliers will impose compliance programs and devote resources to avoid the risks of "unintended" violations. Market participants that today rely on this information to operate efficiently will be forced to spend more to find new sources of information and to interpret less-informative reports from cautious suppliers.

Emergency situations, such as the aftermath of a hurricane, provide an even starker example of circumstances in which quick disclosures should be encouraged rather than discouraged. Where there has been or may be a supply disruption, both markets and consumers benefit from having access to the best up-to-date information about the extent of shortages and the availability of supply. Suppliers should be encouraged to provide the best information they have, without concern that the incompleteness of that disclosure might later be challenged. Broad and ambiguous liability for omissions likely will make caution and delay in disclosure or "no comment" the new standard.[13]

Even in a smaller emergency, such as an unplanned outage, suppliers must safely be able to disclose information without fear of liability for a failure to disclose information that is

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[12] As the ANPRM observed, "public announcements of downtime may enable competitors to collude inappropriately." *ANPRM*, at 30.

[13] When a hurricane threatens to prevent adequate fuel distribution, API and NPRA and its members work with federal and state officials to avoid supply disruptions. Because a market manipulation rule would make these disclosures to government officials more risky, suppliers would be discouraged from participating in these discussions, which would undercut efforts to ameliorate supply problems.

later deemed material. When an unplanned outage occurs, it is desirable that a refinery be able to assure the public that there are "adequate supplies," while omitting the details that could lead to inefficient responses like customers "topping off" their storage tanks, which quickly would make supplies inadequate and prices rise. A no-disclosures policy forecloses the benefits of such balanced statements.

In sum, the costs of outlawing potentially misleading omissions greatly exceed the benefits. The benefits of an omissions rule are speculative at best, as there is no evidence of systemic or even significant misleading omissions that have distorted wholesale petroleum markets.[14] Thus, we urge the Commission not to impose liability on omissions.

3. <u>The Commission Should Adopt The Proposed Alternative Language And Clarify That It Covers Affirmative Fraud, But Not Omissions</u>.

The RNPRM suggests alternative language for Section 317.3:

> It shall be unlawful for any person, directly or indirectly, in connection with the purchase or sale of crude oil, gasoline, or petroleum distillates at wholesale, to engage in any act (including the making of any untrue statement), practice, or course of conduct with the intent to defraud or deceive, provided that such act, practice, or course of conduct distorts or tends to distort market conditions for any such product.[15]

The alternative rule language suggested in the RNPRM is a significant improvement on the revised proposed rule, in large part because a plain reading of the alternative language indicates that it covers affirmative fraudulent acts and statements, but not omissions. This plain reading is supported by a comparison of the alternative rule language to Section 317.3 of the revised proposed rule. Section 317.3(a) of the revised proposed rule makes it unlawful to

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[14] *See supra*, at 5.

[15] *RNPRM*, at 88 (note omitted).

"knowingly engage in any act, practice, or course of business – including the making of any untrue statement of material fact." The alternative rule language is similar to Section 317.3(a) in that it makes it unlawful "to engage in any act (including the making of any untrue statement), practice, or course of conduct," intending to deceive. Unlike Section 317.3(b), however, which explicitly prohibits intentional omissions,[16] the alternative rule language does not say anything about omissions.

Adopting the alternative rule language does not mean that omissions never could be challenged as market manipulation. A combination of false statements and omissions could be actionable under the alternative rule language, as it would be under Section 317.3(a) of the revised proposed rule.[17]

We believe the alternative rule language's approach to omissions ultimately is better for competition and consumers than that of the revised proposed rule. Assuming the Commission determines that the risk of some "market manipulation" justifies adopting new rules, the costs and benefits would be better balanced if the Commission did not impose an omissions rule at this time. This would also allow the Commission to test the need and efficacy of its market manipulation rules by imposing less than the full range of prohibitions that are possible and testing a more limited set of rules in the market. Moreover, individual transactions still are protected by contract, fraud, and other laws.

We urge the Commission to adopt the proposed alternative language and clarify that it covers affirmative statements, but not omissions. In addition, we propose some

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[16] *See RNPRM*, at 65-66.

[17] *See infra*, at 22-23.

adjustments in sections III and IV to the scienter standard and the market distortion test to clarify further the alternative rule language.

B. If The Commission Adopts A Version Of The Revised Proposed Rule, It Should Narrow And Clarify The Rule In Several Important Respects.

If the Commission determines it is necessary to adopt a rule addressing omissions, we believe that the significant uncertainties created by Section 317.3 of the revised proposed rule could be somewhat ameliorated with clarifications provided by the Commission.

1. A Statement Of "No Comment" Should Not Be Actionable.

We first urge the Commission to make it clear that silence and "no comment" do not violate any proposed rule.

The structure of Section 317.3 indicates silence or "no comment" is the only safe policy. Specifically, the structure of the revised proposed rule suggests that Section 317.3(a) is intended to prohibit only fraudulent affirmative acts and statements, while Section 317.3(b) would prohibit only omissions that make a true statement misleading. Neither section should provide a basis to challenge silence. As the RNPRM states clearly:

> Revised proposed Rule Section 317.3(b) would not…impose an affirmative duty to disclose information. Rather, the provision would apply if "a covered entity voluntarily provides information – or is compelled to provide information by statute, order, or regulation – but then fails to disclose a material fact, thereby making the information provided misleading."[18]

Suppose that RST Refinery has made no announcement of the turnaround and therefore has not disclosed that it must make spot purchases, intending that other traders remain unaware that RST is short. If they knew, they would seek to charge higher prices. Traders ask RST about its large purchases, "Are you having an outage?" RST responds, "No comment."

[18] *RNPRM*, at 66 (footnotes omitted).

The structure and plain language of Section 317.3 should foreclose a challenge to silence or a "no comment" response.

Similarly, for the reasons discussed earlier, the alternative language too should not allow a challenge to "no comment." The alternative language does not prohibit omissions in the absence of a false statement.[19]

We urge the Commission to make it clear in any final rule that silence, pure omissions, and "no comment" are not actionable.

2. <u>Statements That Are Misleading Because Of Omitted Information Are Covered By Section (b), Not Section (a)</u>.

Section 317.3(b) of the revised proposed rule deals explicitly and comprehensively with omissions. The RNPRM identifies only one situation in which omissions may be part of a Section 317.3(a) violation: "[A]ny omission that is part of a fraudulent or deceptive act, practice, or course of business would violate revised proposed Section 317.3(a)."[20]

We agree that, if Section 317.3(a) is made part of any final rule, a combination of knowing *false* statements and misleading omissions could violate that section. This appears to be the intent of the quoted language from the RNPRM note 188, after which the RNPRM cites precedents from securities regulation and common law fraud that condemned the combination of *false* or *misleading* statements and omissions.

Statements that are misleading because of omitted information could violate Section 317.3(b). However, it would be completely inappropriate to allow omissions alone to violate Section 317.3(a). It would be inconsistent with the structure of Section 317.3 and would

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[19] *See supra*, at 19-21.

[20] *RNPRM*, at 65 n.188.

allow Section (a) to swallow Section (b), thereby rendering Section (b) superfluous. It also would undercut the Commission's reasoning for revising the rule to adjust the scienter and market effects standards for omissions.[21] Furthermore, the RNPRM elsewhere clearly says that "Revised proposed Section 317.3(a) would not prohibit omissions of material facts."[22]

Any liability for omissions must satisfy Section 317.3(b). We urge the Commission to make this clear in the text of the rule itself, for example by stating that if an act, practice, or course of business falls within the scope of Section (b), then it shall not be subject to liability under Section (a).

3. <u>An Omissions Rule Should Not Require Corrections And Updates Of Disclosed Information</u>.

The RNPRM asks whether Section 317.3(b) should be "expanded to require that a person update or correct information if circumstances change?"[23] This requirement would increase the risk that an omission could be found to be a violation and would further motivate market participants not to disclose information that today they would disclose.

Wholesale petroleum market participants do not need corrections and updates. These sophisticated buyers and sellers understand that market conditions can change rapidly. If some time has passed since a communication from one participant, others generally do not expect that communication still to represent the state of the market, nor do they delay their own

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[21] *See RNPRM*, at 65-66.

[22] *See RNPRM*, at 24.

[23] *RNPRM* at 86, Question 2.j ("If the merits of Section 317.3(b) as currently proposed outweigh any flaws or dangers, should it be expanded to require that a person update or correct information if circumstances change? How, if at all, would such an expansion alter the cost/benefit calculus? Explain.").

activities pending further word. The absence of corrections and updates today does not hinder markets from functioning.

The proposed market manipulation rule creates some risk of mistaken enforcement. The greatest cost of imposing the proposed market manipulation rule is that, to avoid the risk of a perceived or unintended violation, market participants will reduce their disclosures to the point at which the risk is mitigated to an acceptable level. Every expansion of the rules increases that risk and therefore reduces disclosures, which in turn increases costs to consumers.

Expanding the scope of Section 317.3(b) to require corrections and updates will further chill disclosures. The problem noted in the RNPRM, that "identifying statements that are unambiguously misleading by dint of a material omission may be difficult,"[24] would be compounded by a correct-and-update requirement. If corrections and updates are required, companies that communicate with other market participants will have to:

- establish procedures to discover any new or corrected information,
- determine if the new or corrected information – whether it was published by the firm or provided by another source of market information – is related to information the firm in the past has communicated externally,
- determine whether the new or corrected information makes a fact reported in the prior statement misleading, including determining whether that fact is "material" in that "a reasonable market participant would consider [it] important in making a decision to transact because such information significantly alters the total mix of information available,"[25] given that some time has passed since the original communication and other information sources have contributed to the total mix of information, and
- predict whether the omission has a tendency to distort a market.

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[24] *RNPRM* at 69.

[25] *RNPRM* at 62-63.

This presents a daunting set of problems. The compliance program that best reduces the risk of a violation is one that would further limit affirmative disclosures, to avoid future omissions serving as the basis for a Section 317.3(b) challenge.

A correct-and-update requirement raises other questions particular to Section 317.3(b), such as the speed with which one is obliged to identify and then publish that new or corrected information and the extent to which the new or corrected information must be published to ensure that it is heard by every recipient of the original statement.

If Section 317.3(b) is adopted, we urge the Commission to make any omission unlawful only if it renders an affirmative statement deceptive or fraudulent at the time the statement is made.

4. Any Final Rule Should Impose Liability On Omissions Only If The Intent To Mislead Was The Motivation For The Omission.

Finally, the revised proposed rule would be improved if Section 317.3(b) were revised to make an omission actionable only if the "intent to mislead was the primary motivation for the omission." This would provide protection for an omission that was motivated by legitimate business reasons but incidentally left other market participants without information they might have desired. Similarly, the Commission could provide assurances that an omission would be challenged only if there were no legitimate business reason to explain it.

III. THERE SHOULD BE A SINGLE, CLEAR STANDARD FOR SCIENTER.

Unlike the proposed rule set forth in the NPRM, the Commission's revised proposed rule "explicitly sets forth a scienter standard for each of the two conduct provisions."[26] This is a welcome improvement. Further revisions to reduce the overbreadth of the proposed

[26] *RNPRM*, at 48.

rule are, however, desirable. Specifically, industry compliance with, and Commission enforcement of, any final rule will be more effective if conduct covered by the rule is subject to a single scienter standard—specific intent. Moreover, as discussed in Part II of these comments, any final rule will be improved by eliminating liability for omissions. The alternative rule language is preferable to the revised proposed rule both because it eliminates liability for omissions and because it establishes intent as the scienter standard for all conduct covered by the rule. We see no ground for applying a lesser scienter requirement (*i.e.*, the knowledge requirement of Section 317.3(a) of the revised proposed rule) to conduct that does not involve an omission. Moreover, any final rule should clarify that the scienter required for liability is a specific intent to deceive or defraud in order to manipulate a covered market.

Part A of this section analyzes the hypothetical contained in Question 2W(1) of the RNPRM under the scienter standards set forth in the revised proposed rule and the alternative rule language. Part B addresses important respects in which we believe the proposed scienter standards should be revised and clarified.

A. <u>Analysis of Hypothetical (1) Illuminates The Importance Of Adopting A Specific Intent Standard For All Conduct But Assumes Away Important Underlying Issues</u>.

Question 2W(1) requests comment on the following hypothetical:

> Company ABC reports a trade to the XYZ Price Service, a service that collects transactional data and uses the data to set a benchmark price that the industry uses to negotiate spot purchases of refined product. XYZ procedures, which are well known throughout the industry, require reporting companies to identify transactions below a specified volume to limit the impact of transactions with inconsequential volumes on the benchmark price. The volume of ABC's trade is below the specified volume, but:
>
> (a) ABC inadvertently omits that information.
>
> (b) ABC establishes procedures to ensure that persons reporting transactions know to identify transactions below

the specified amount but the individual reporting these transactions fails to follow those procedures.

(c) ABC intentionally omits the information identifying the trade.

The particular questions posed in connection with this hypothetical can be answered readily but, as will become apparent, the statement of the questions assumes away some underlying difficulties.

1. Scenario (a): ABC Inadvertently Omits Information.

In the scenario described in subsection (a), there clearly is no violation under the revised proposed rule. The hypothetical refers to an omission of information; accordingly, the Commission would apply the more rigorous intent test of Section 317.3(b) of the revised proposed rule.[27] In addition, for the purpose of the hypothetical, we assume that the fact of inadvertence is not in dispute. Thus, the information was omitted "inadvertently," not "intentionally," as required by that section.

ABC should not be liable even if it were subject to the recklessness standard articulated under Section 317.3(a) because, according to the RNPRM, the "revised proposed Rule, including Section 317.3(a) of the Rule, would not extend to inadvertent conduct or mere mistakes."[28] In the real world, however, some may attempt to blur the line between omissions and affirmative statements subject to Section 317.3(a) and claim that even an "inadvertent" omission could be reckless and thus covered by the subsection. Plaintiffs might argue, for example, that the employee's inadvertence resulted from his own reckless inattentiveness. This

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[27] As already discussed, we assume that omissions would not be subject to liability under Section 317.3(a) of the revised proposed rule. *See supra*, at 19-21.

[28] *RNPRM*, at 57.

argument would not be possible under the alternative rule language, which requires an actual "intent to defraud or deceive."

In sum, this omission most likely would not violate either section of the revised proposed rule, but that conclusion would be more certain and the process less burdensome under the alternative rule language.

2. Scenario (b): ABC Fails To Follow Its Own Procedures.

The answer for the scenario described in subsection (b) appears to be that there is no violation under either section of the revised proposed rule. The failure to identify the small trade again looks like an omission; thus Section 317.3(b) applies. If we assume there is no evidence to show that the individual's failure to report was intentional, the intent standard of that subsection would not be satisfied. Similarly, this omission would not violate the alternative rule language because ABC's procedures to ensure disclosure of small volume transactions provide evidence of intent to avoid deception when it discloses to the reporting service.

For the reasons already discussed, ABC's conduct should not violate Section 317.3(a) either. However, as in the prior scenario, some may attempt to argue that the omission is subject to this sub-section and the conduct was reckless despite the existence of company procedures.

3. Scenario (c): ABC Intentionally Omits Information.

Scenario (c) appears to describe a violation under both the revised proposed rule and under the alternative rule language. The scenario specifically refers to intentional conduct that would satisfy the scienter requirements in any of these options. But we do not know what particular facts support the conclusion that ABC "intentionally" omitted the critical information, or whether ABC's failure to report one small transaction could reasonably be held to "distort or tend to distort market conditions" as required in Section 317.3(b) of the revised proposed rule and the alternative rule language.[29] In other situations, there could be serious questions about whether ABC could be said to have acted "intentionally;" whether the conduct was likely to affect the market generally or merely an individual transaction; and whether market distortion was specifically intended. In these situations, it could make a difference whether the Commission's revised proposed rule, the alternative rule language, or a specific intent standard were applied.

The proper objective of any rule issued under Section 811 is to cover deceptive conduct undertaken with the intent to manipulate a covered wholesale petroleum market and to do so without chilling procompetitive, efficient interactions in markets that are generally acknowledged to function well. This objective can best be achieved by defining more precisely and narrowing the applicable scienter standard. Specifically, whichever version of the rule is ultimately adopted, it should cover fraudulent or deceptive conduct only if it is *intended to deceive or defraud in order to manipulate a covered market*. Intent so defined will make clear on the face of the rule that deceptive conduct that seeks to manipulate a covered market—which was the conduct that Congress targeted in enacting Section 811[30]—will incur liability. Simultaneously, it will avoid the costs of uncertainty for market participants that seek only to profit from superior market intelligence, acumen or skill, and it will avoid unnecessary

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[29] For purposes of this discussion, we assume that the transaction in question was material in the sense that, had it been disclosed, other market participants would have regarded that information as important. In addition, as we have stated in prior submissions, and discussed elsewhere in these comments, we do not believe that Section 811 covers "attempts" to manipulate and believe that market effects are a necessary predicate for a violation. *See API/NPRA Comments*, at 32; *infra*, at 35-38.

[30] *See infra*, at 34.

deployment of scarce enforcement resources on conduct that, even if possibly deceptive, was not intended to manipulate a covered market, is unlikely to have a market-wide effect, and is otherwise actionable under separate legal authority.

B. Any Final Rule Should Resolve Certain Fundamental Issues.

Responses to the first hypothetical question identify, but do not require resolution of, three fundamental issues:

(1) Whether there has been an "untrue statement" or an "omission." This distinction determines which subsection of Section 317.3 of the revised proposed rule will apply, and the significance of additional issues.

(2) The practical impact of the distinction between the "knowingly engage" standard of scienter in Section 317.3(a) and the "intentionally fail" standard of Section 317.3(b).

(3) The specific outcome an actor must intend for the conduct to be subject to liability under any final rule.

We discussed the distinction between untrue statements and omissions in Part II of these comments. We will discuss issues (2) and (3) separately below, but it will become apparent that (i) all of these issues are interrelated, and (ii) both prosecution and compliance would be much simpler, and equally effective, if specific intent—that is, an intent to deceive or defraud in order to manipulate a covered market—were the standard for all conduct covered under a final rule.

1. The Intent Standard Of Section 317.3(b) Is Preferable To The Knowledge Standard Of Section 317.3(a).

The revised proposed rule reaches "knowingly" made untrue statements (Section 317.3(a)) and omissions made "intentionally" (Section 317.3(b)). The RNPRM makes it clear that the Commission intends the word "knowingly" to include not only actual knowledge but also recklessness: "an extreme departure from standards of ordinary care," in which the violator "either knew or must have known that his or her conduct created a danger of misleading buyers or sellers."[31] It does not cover inadvertent conduct or mistakes.[32]

In contrast, the word "intentionally" does not reach reckless conduct. It requires a showing that "the actor in question intended to mislead" and "[t]his approach represents a different scienter standard than the showing of extreme recklessness."[33] Whatever final rule the Commission may adopt will have to be understood and applied by many people other than the sophisticated practitioners in the Commission itself. Since the rules will cover companies that operate in many jurisdictions, it is important to have consistent interpretation, to the extent possible. Those who will have to understand and apply the rules on a day-to-day basis include thousands of business people in the petroleum industry, who need straightforward guidance and a sufficient understanding to devise clear compliance rules.[34] The ultimate purpose of any final rule should be to clarify—not merely echo—the general commands of the statute.

We understand and appreciate that the revised proposed rule is not intended to cover simple negligence in the conduct of an individual employee or in the administration of a company's compliance program. A massive body of law attempts to draw reasoned distinctions between negligence and recklessness, and gradations in between. Nevertheless, a test that refers to recklessness or "extreme" negligence is inherently subjective and fuzzy. Experience with the application of tort law generally indicates that, despite careful instructions, jurors invariably tend to be influenced by hindsight and extraneous factors. Individual fact finders and business people

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[31] *RNPRM*, at 61

[32] *RNPRM*, at 56-57.

[33] *RNPRM*, at 67-68.

[34] *See Comments of Flint Hill Resources, LP* (Oct. 17, 2008), *passim.*

can better understand and apply a simple rule that says it is illegal for people to lie about things that they know—*i.e.*, to engage in conduct with the intent to defraud or deceive. If applied to the affirmative statements and conduct covered by Section 317.3(a) of the revised proposed rule, this common-sense scienter standard would considerably reduce the element of subjectivity and uncertainty that currently exists in that provision. The benefits of an intent standard as compared to a broader knowingly / extreme recklessness standard are acknowledged in Section 317.3(b) of the revised proposed rule as well as in the alternative rule language and are no less applicable to affirmative statements and conduct than they are to omissions.

But it is possible to achieve even greater objectivity, without compromising the fundamental objectives of the rule.

2. Any Final Rule Should Apply Only To Statements Or Conduct That Are Intended To Manipulate A Covered Market.

The comments submitted by API and NPRA in response to the NPRM emphasized that there are extensive, mutually-guarded conversations in the ordinary course of dealing between buyers and sellers in wholesale petroleum markets.[35] Unlike many customers in securities markets, these commodity buyers and sellers are sophisticated traders, and it is neither in their interest nor in the public interest for them to disclose everything they know.

Buyers and sellers, almost by definition, are likely to have different views about market conditions today or in the future. These views are based on their own market intelligence, which often is expensive to collect and evaluate, and companies are unlikely to incur the expense of collecting and evaluating such information in the future if a rule mandates that they disclose it to others. The rationale for rejection of a disclosure obligation with this

[35] *See API Comments*, at 12-13; *NPRA Comments*, at 7-8.

perverse incentive effect is comparable to the rationale for the protection of other kinds of intellectual property.

Commentators have described the guarded disclosures that occur in the ordinary course of business, as sophisticated traders seek to elicit information about future supply and demand from each other while protecting their own information to the extent possible.[36] The Commission has given no indication that it intends to interfere with this procompetitive aspect of ordinary business practice. The Commission's appropriately circumscribed intention will be best realized if coverage of the final rule is limited to acts or practices that are intended to deceive or defraud in order to manipulate a covered market, not to conduct that may be deceptive but was not intended to have any effect on a market.[37]

There are other good reasons for this proposed limitation. There may be conflicting expressions of intent in the myriad internal communications of a large organization. If, however, particular conduct or statements would make sense only on the assumption that the actor intends to profit from future transactions <u>other than the one immediately affected</u>, it would provide an <u>objective</u> indication of an intent to manipulate the market generally. (This standard is analogous to tests that are increasingly applied in cases under Section 2 of the Sherman Act to distinguish vigorous competitive behavior from exclusionary or predatory intent.[38])

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[36] *See* Final Transcript, Market Manipulation Rulemaking Workshop, Nov. 6, 2008, at 93-95 (comments of Charles Mills, CFDR).

[37] Our recommendation that any final rule require specific intent to deceive or defraud in order to manipulate a covered market is distinct from our separate recommendation that liability should accrue only if challenged conduct is shown to have had a material effect on the market. *See infra*, at 34-38.

[38] Because Section 811 targets actual manipulation of markets, any rule the Commission promulgates under Section 811 should be limited to actual market manipulation and should not impose liability for attempted manipulation. *See API Comments*, at 32-33. To the extent the (continued…)

IV. LIABILITY SHOULD BE LIMITED TO CONDUCT THAT HAS A MATERIAL EFFECT ON THE MARKET.

Both the revised proposed language and the alternative rule language include a requirement, not present in the previous version of the proposed rule, that challenged conduct distort or tend to distort market conditions. The inclusion of this requirement is an improvement that goes some way toward focusing the rule on the sort of conduct Congress sought to address: acts and practices that manipulate a market. As with the scienter requirement, however, the revised proposed rule makes an unfounded distinction between affirmative statements and conduct on the one hand and omissions on the other, applying the market distortion requirement to the latter category of conduct only. The better solution to this shortcoming is that of the alternative rule language, which eliminates liability for omissions and applies a market distortion requirement to conduct that remains within the scope of liability. If a final rule retains liability for omissions, we believe it should apply the same market distortion requirement to both omissions and affirmative statements and conduct. We also suggest that the market distortion requirement be clarified so that only conduct that has a material effect on a covered market is subject to liability or, failing that, only conduct that distorts a covered market or is likely to do so under the circumstances.

Commission is considering a rule that imposes liability for conduct that does not actually manipulate markets, there is an even stronger case for requiring a specific intent to manipulate the market as a prerequisite for liability. By way of analogy, the offense of attempted monopolization under Section 2 of the Sherman Act requires, *inter alia*, proof of a specific intent to monopolize and a dangerous probability of achieving monopoly power. *Spectrum Sports, Inc. v. McQuillan*, 506 U.S. 447, 456 (1993). In the context of a rule prohibiting market manipulation, similar considerations should lead the Commission to limit liability to cases in which a specific intent to manipulate the market can be shown, as well as a dangerous probability of successful manipulation—that is, a showing that challenged conduct distorted or was likely to distort a market. *See infra*, at 37-38.

Part A of this section explains why, in our view, any final rule should be focused on conduct capable of manipulating a market and discusses how best to shape a market effects requirement to that end. Part B of this section describes how this conclusion is supported by an analysis of the hypothetical contained in Question 2w(2) of the RNPRM.

A. Section 811 Applies To Manipulation Of A Market, Not To Individual Transactions That Have No Effect On A Covered Market.

Hypothetical (2) in the RNPRM illuminates the importance of limiting any rule promulgated under Section 811 to conduct that has a material effect on a covered market. As already discussed, and as explained in greater detail in our prior comments, Congress intended Section 811 to apply to deceptive or fraudulent conduct that manipulates a covered market, not to conduct with effects that do not extend beyond the transaction at issue.[39] As currently drafted, the rule would depart from congressional intent by restricting conduct that has no impact on markets or consumers. Such conduct is, and properly should be, the province of anti-fraud and contract law. Without a requirement that challenged conduct materially affects market conditions, the rule will cover a broad range of private commercial disputes that Congress never intended the FTC to regulate under Section 811.[40]

The RNPRM states that the Commission did not include a market effects requirement in Section 317.3(a) of the revised proposed rule in part because "there is no economic justification for fraudulent or deceptive conduct in any market."[41] The scope of the

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[39] *See supra*, at 2-3; *see also API Comments*, at 32-36.

[40] Adding a market effects requirement will also help to ensure that any final rule does not cover attempts. As noted in our prior comments, the text of Section 811 is limited to actual market manipulation and does not extend to attempted market manipulation. *See API Comments*, at 33.

[41] *RNPRM*, at 72. While the text of Section 317.3(a) does not include any form of market effects requirement, the RNPRM could be understood to state that the Commission intends to read some (continued…)

rule, however, should not be determined on the basis of whether fraudulent or deceptive conduct is ever justified, but rather on whether the rule faithfully implements Congress's intent that any rule regulate only *market* manipulation, and on whether the costs of such a rule outweigh its potential benefits. Evaluated against these criteria, the revised proposed rule is overly broad. Because the rule would authorize the Commission to impose very large fines regardless of whether the challenged conduct had any effect on a covered market, most firms are likely to adopt compliance programs that substantially restrict the information they disclose to other market participants and impede their ability to respond quickly and efficiently to rapidly changing market conditions.

The RNPRM also states that the Commission did not require a showing of price effects because such a showing "—and imposing the concomitant additional evidentiary burden upon the Commission—would introduce an unnecessary risk that conduct detrimental to the integrity of the market would escape successful challenge."[42] As noted in our prior comments, however, the Commission has a wealth of experience collecting such evidence in the context of antitrust investigations.[43] The Commission also has gained experience analyzing market effects in petroleum markets in its many investigations of the petroleum industry.[44] Thus, it seems

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form of such a requirement into that section. *See, e.g.*, *id.* at 55 ("As revised, Section 317.3(a) would prohibit fraudulent or deceptive conduct that not only serves no legitimate purpose, *but could also impair the efficient functioning of wholesale petroleum markets*.") (emphasis added). If the Commission intends Section 317.3(a) to apply only to conduct that could affect the efficient functioning of wholesale petroleum markets, the Commission should add language to that effect to the text of the rule.

[42] *RNPRM*, at 72.

[43] *API Comments*, at 34.

[44] *See API/NPRA Comments*, at 8-14. As already noted, these investigations have consistently concluded that manipulation in these markets is not a problem that requires regulatory intervention. *See supra*, at 5.

unlikely that a stronger effects requirement would impose evidentiary burdens on the Commission that would meaningfully hamper its enforcement efforts.

Accordingly, any rule promulgated under Section 811 should cover only fraudulent or deceptive conduct that materially affects a covered market. If, however, the Commission decides not to require such a showing, and instead retains the "market distortion" framework currently set forth in Section 317.3(b) of the revised proposed rule, we urge the Commission to revise the final rule in two respects.

First, the Commission should revise the rule to apply the market distortion requirement to all conduct covered by the rule. As currently drafted, the revised proposed rule would apply the market distortion requirement only to omissions under Section 317.3(b) and not to "act[s], practice[s], or course[s] of business" under Section 317.3(a). Nothing in the statutory text or the legislative history of Section 811 supports such differential treatment. Furthermore, the RNPRM's reasons for applying the market distortion requirement to omissions—namely, to avoid "creat[ing] uncertainty within the business community about the Rule's application . . . hav[ing] an unintended chilling effect on normal business activity, . . . [or] unnecessarily rais[ing] the costs of carrying out normal business activity in order to avoid potential litigation risks"[45]—apply with equal force to affirmative statements and other conduct covered by Section 317.3(a). The alternative rule language, which applies the market distortion requirement to all covered conduct, is a significant improvement over the revised proposed rule in this regard.[46]

[45] *RNPRM*, at 69.

[46] If the Commission decides not to apply the market distortion requirement to conduct other than omissions, we would urge the Commission, in the final rule, to provide a safe harbor for private communications between market participants, at least absent concrete evidence that such statements or conduct were part of a broader scheme to manipulate the market. *See API Comments*, at 22-24.

Second, both the revised proposed rule and the alternative rule language should clarify that conduct must either have distorted a market or have been likely to do so under the circumstances in order to be subject to liability. Under the revised proposed rule, an omission may incur liability even if it only "tend[s] to distort" market conditions. "Tends to distort" is an imprecise term, subject to expansive interpretations imposing liability even on omissions that, in the circumstances, had no real chance of affecting a covered market or consumers. To avoid such a result, any final rule should revise the market distortion requirement to apply only to conduct that either distorts a market or was likely to do so under the circumstances.

The Commission faced a similar issue when it adopted its Deception Policy Statement, which proscribes acts or practices that are "likely to mislead."[47] Prior to the Policy Statement, the test was whether an act or practice had a "tendency or capacity" to deceive. That test was widely criticized, in part because it enabled the Commission to pursue bizarre interpretations of otherwise truthful claims.[48] In practice, "likely to mislead" is less elastic and imprecise than the old "tendency or capacity" standard, and has not posed practical difficulties in litigation.

B. Hypothetical 2 Illustrates The Importance Of Limiting Any Rule To Conduct That Manipulates A Market.

Question 2w(2) of the RNPRM requests comment on the following hypothetical:

> Trader A receives a request from RST Refinery for crude oil of a particular grade, specifying that it prefers not to buy crude from the country of Cepo for political reasons. Trader A is unable to find the kind of crude RST requires except in Cepo. Trader A:

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[47] Federal Trade Commission Policy Statement on Deception (1983), *appended in Cliffdale Associates, Inc,*, 103 F.T.C. 110 (1984).

[48] Timothy J. Muris, *Defining Deception*, 42 Antitrust & Trade Reg. Rep. 699 (1982), *reprinted in* 19 J. Reprints for Antitrust L. & Econ. 335 (1989).

(a) Sells the crude from Cepo to RST without disclosing that it is from Cepo.

(b) Sells the crude to RST and represents that it is from the country of West Friendly, knowing that it is from Cepo.

(c) Does not know and does not ask where the crude is from and sells it to RST without representing its origin.

As with the first hypothetical in Question 2w, the RNPRM invites discussion of the differences, if any, in the outcome of an enforcement action under this second hypothetical when applying the revised proposed rule as compared to the alternative rule language set out in Question 2v.

API and NPRA firmly believe that any final rule promulgated under Section 811 should not apply to any of the three scenarios described in Hypothetical (2). In each scenario, Trader A's actions had no effect on market prices or other market conditions. As already discussed, the statutory language of the EISA demonstrates that Congress intended Section 811 to apply only to deceptive or fraudulent acts or practices that manipulate a covered market. Because Trader A's actions, in each of the scenarios in Hypothetical 2, did not have such effects, they should fall outside the scope of any rule. Adding a requirement that the challenged conduct distorted the market, or was likely to do so under the circumstances, would appropriately implement Congress's intent to regulate only market manipulation. Such a revision would also avoid potential divergence or conflict with existing anti-fraud and contract law and would avoid chilling procompetitive disclosures and conduct while protecting consumers and other market participants from the effects of market manipulation.

In the event the Commission rejects this approach and instead selects between the revised proposed rule and the alternative rule language, an analysis of Hypothetical 2 demonstrates the relative superiority of the alternative rule language. We analyze in turn each of the scenarios described in parts (a) through (c) of hypothetical (2).

1. Scenario (a): Trader Does Not Disclose Origin of Crude.

Part (a) of hypothetical (2) describes a scenario in which Trader A "[s]ells the crude from Cepo to RST without disclosing that it is from Cepo." Under the alternative rule language, this situation would not be covered both because Trader A's actions did not "distort[] or tend to distort market conditions" for the product at issue, and because the alternative rule language does not cover omissions.[49] For the reasons already discussed, this is the correct result.

It is less clear how the revised proposed rule would apply to this situation. The better interpretation is that Trader A's conduct should be analyzed under Section 317.3(b). Because Section 317.3(b) applies only if "such omission distorts or tends to distort market conditions," it would not apply to Trader A in this situation for the same reason that the alternative rule language does not apply.[50]

An alternative interpretation of the revised proposed rule is that Trader A's actions also are covered by Section 317.3(a) on the assumption that an omission can also be characterized as an "act, practice, or course of business" within the meaning of Section 317.3(a).

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[49] *See supra*, at 19-21.

[50] It is significant for refiners to know the source of the crude oil because product characteristics differ from country to country, but a preference not to purchase for political reasons, as posited in Hypothetical 2, would be highly unusual. Therefore, Section 317.3(b) also would not apply because the crude oil's origin was not a "material" fact. Although the revised proposed rule does not define "material," the RNPRM states that the Commission "anticipates using a materiality standard that focuses on a fact that a reasonable market participant would consider important in making a decision to transact." *RNPRM*, at 63. Because reasonable market participants do not consider the crude oil's origin to be important in their decisions to transact, Trader A's did not fail to state a "material" fact within the meaning of Section 317.3(b). Of course, the purchaser might well have private remedies in this situation.

For the reasons already discussed, we believe such an interpretation has no merit and that the Commission, were it to adopt a version of the revised proposed rule, should explicitly disavow such an interpretation.[51] If such an interpretation were applied here, however, Trader A arguably could be subject to liability under Section 317.3(a)—despite the fact that its actions had no effect on the market. Section 811 should not impose liability on Trader A in these circumstances.

2. Scenario (b): Trader Misrepresents Origin Of Crude, Without Effect.

Part (b) of Hypothetical 2 describes a scenario in which Trader A "[s]ells the crude to RST and represents that it is from the country of West Friendly, knowing that it is from Cepo." As was the case under part (a), this situation would not be covered by the alternative rule language because Trader A's actions did not "distort[] or tend to distort market conditions" for the crude oil in question. Here again, this is the correct result.[52]

Under the revised proposed rule, by contrast, Trader A's intentionally false statement to RST Refinery could conceivably give rise to liability under Section 317.3(a) because Trader A, "in connection with the purchase or sale of crude oil . . . knowingly engage[d] in [an] act . . . that operate[d] . . . as a fraud or deceit" upon RST Refinery.[53] As previously

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[51] *See supra*, at 22-23.

[52] We note that Trader A could be liable to RST Refinery for fraud or breach of contract, although it is unclear what legally-cognizable damages RST Refinery could recover if it suffered no economic harm from Trader A's deception.

[53] As indicated in footnote 50, *supra*, we think the better interpretation of Section 317.3(a) is that it would not apply to Trader A's statement because it was not material. Section 317.3(a) is, however, open to an interpretation that it applies even to non-material statements. While Section 317.3(a) states that its coverage "include[es] the making of any untrue statement of *material* fact," the use of the term "including" in this clause suggests that even untrue statements of *non-material* fact may give rise to liability under Section 317.3(a). Thus, Trader A could be subject to penalties of up to $1 million per day for conduct that had no effect whatsoever on *any* market participant—let alone on the market or on consumers. This absurd result underscores the overbreadth of Section 317.3(a).

discussed, a rule that creates liability for conduct with no potential to distort the market risks deterring procompetitive disclosures. To avoid this result, the Commission, in the event it decides to retain the bi-partite structure of the revised proposed rule, should amend Section 317.3(a) to include a market effects requirement.

3. Scenario (c): Trader Makes No Representation of Origin.

Part (c) of Hypothetical 2 describes a scenario in which Trader A "[d]oes not know and does not ask where the crude is from and sells it to RST without representing its origin." As was true with respect to part (a) of hypothetical (2), this situation would not be covered by the alternative rule language both because Trader A's actions did not "distort[] or tend to distort market conditions" and because the alternative rule language, as we read it, is not intended to cover omissions. A similar conclusion follows under Section 317.3(b) of the revised proposed rule because it includes the same "market distortion" requirement. Because Trader A "does not know" the origin of the crude oil, it cannot fairly be accused of having "intentionally" failed to state a material fact. For the reasons already discussed, these are the correct results.

We also believe that Trader A would not be subject to liability under the most logical reading of Section 317.3(a) of the revised proposed rule.[54] If, however, Section 317.3(a) were interpreted to apply to omissions (an interpretation that, as already discussed, lacks merit), then the question would be whether Trader A's failure to ask about the origin of the crude oil—knowing that RST "preferred" not to buy crude from Cepo—could be characterized as "reckless" under the standards adopted by the D.C. and Seventh Circuits in the context of SEC Rule 10b-

[54] *See supra*, at 22-23.

5.[55] While further information surrounding RST Refinery's representations and Trader A's conduct is needed in order to answer this question, the fact that Section 317.3(a) as currently drafted could conceivably give rise to liability in this situation illustrates the overbreadth of the revised proposed rule.

CONCLUSION

API and NPRA appreciate the opportunity to submit comments on the Commission's RNPRM. We would be pleased to continue to work with the Commission and its staff to address the issues raised by the proposed rule.

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[55] *See RNPRM*, at 56-62.

APPENDIX

1. General Questions for Comment

a. Does the revised proposed Rule strike an appropriate balance between protecting consumers from petroleum market manipulation and limiting attendant costs to industry such as the chilling of legitimate business conduct and compliance burdens?

In considering whether an appropriate balance is struck discuss:

(1) the merits or flaws with having a different standard of scienter for Section 317.3(a) from Section 317.3(b);

(2) the merits or flaws of eliminating Section 317.3(b) and consolidating the Rule into a single anti-fraud prohibition as set out by Section 317.3(a);

(3) the merits or flaws of eliminating Section 317.3(b) and consolidating the Rule to a single anti-fraud prohibition as set out by Section 317.3(a), but with a scienter requirement of "intentionally engage" rather than "knowingly engage;"

(4) the merits or flaws of eliminating Section 317.3(b) and consolidating the Rule to a single anti-fraud prohibition as set out by Section 317.3(a), but adding a proviso that the challenged act, practice, or course of business distort or tend to distort market conditions; discuss the consequences of adding this proviso under both scienter alternatives of "intentionally" and "knowingly."

Answer: Please see the main body of our comments.

b. Do the conduct provisions in revised proposed Rule Section 317.3 provide sufficient clarity and precision in articulating prohibited conduct? Why or why not? If not, how could the Rule be modified to achieve those goals? Would a rule limited to Section 317.3(a) improve clarity and precision without impairing the basis for issuing a rule or the goal of preventing market manipulation to the benefit of consumers? Explain.

Answer: Please see the main body of our comments.

c. Does revised proposed Rule Section 317.3 prohibit the injection of false information into market transactions? If not, how could the provision be revised to achieve that goal? Explain.

Answer: Please see the main body of our comments.

d. Does a prohibition on the injection of false information into market transactions protect the integrity of such markets? Why or why not?

Answer: Please see the main body of our comments.

e. Should a market manipulation rule reach fraudulent or deceptive conduct that does not distort or tend to distort market conditions? Why or why not? (Note: As explained in the discussion above respecting Section 317.3(b), the Commission does not intend that a requirement that the challenged conduct distort or tend to distort market conditions mean that a specific price or other market effect be an element to be demonstrated to prove a rule violation.)

Answer: Please see pages 34-43 of our comments.

f. Discuss the benefits and costs of alternatives to promulgating the revised proposed Rule, including the following: (i) declining to issue a final rule; (ii) promulgating a final rule that mirrors the initially proposed Rule; or (iii) promulgating a final rule that solely prohibits false statements.

Answer: Please see the main body of our comments.

2. Questions on Specific Provisions

a. As drafted, does Section 317.3(a) provide sufficient clarity and precision as to the contours of prohibited conduct? Explain.

Answer: Please see the main body of our comments.

b. Is it appropriate that the rule prohibit acts, practices, and courses of business that operate or would operate as a fraud or deceit on any person? Discuss the merit or lack of merit of prohibiting fraudulent or deceptive conduct. In so discussing, explain:

> (1) whether Section 811 of EISA authorizes the Commission to publish a rule that prohibits *all* acts, practices, or courses of conduct that operate or would operate as a fraud or deceit on any person, including, e.g., common law fraud in which injury may not extend beyond the individual parties or otherwise impair the integrity of wholesale petroleum markets at large;
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> (2) whether, as a policy matter, Section 317.3(a) should prohibit *all* acts, practices, or courses of conduct that operate or would operate as a fraud or deceit on any person, including, e.g., common law fraud in which injury may not extend beyond the individual parties or otherwise impair the integrity of wholesale petroleum markets at large; if not, discuss how the reach of the provision should

be bounded, including, e.g., the merits of a proviso that the challenged conduct distort or tend to distort market conditions.

Answer: Please see the main body of our comments.

c. Discuss the merits or flaws of the Section 317.3(a) scienter standard that the challenged person "knowingly" act. In the context of wholesale petroleum markets and in comparison to the tentative "knowingly engage" standard, how would an alternative "intentionally engage" standard affect the ability of the Commission to protect consumers from deleterious market manipulation? What differences, if any, are there between the two alternative standards respecting the ability of firms to comply with Section 317.3(a), including the costs of compliance?

Answer: Please see pages 25-33 of our comments.

d. As explained in the discussion of revised proposed Rule Section 317.3(b), the Commission proposes that the Rule prohibit omissions of material fact – specifically, omissions of material facts that are necessary to ensure that a previously made statement is not misleading, provided that the informative content of the misleading statement distorts or tends to distort market conditions for any such product. What are the costs and benefits of this provision?

Answer: Please see pages 12-25 of our comments.

e. Describe acts, practices, or courses of conduct, if any, that would threaten the integrity of wholesale petroleum markets that could not be reached by Section 317.3(a) but could be reached by Section 317.3(b). If such conduct exists, what is its incidence? In comparison to conduct injurious to the integrity of wholesale petroleum markets reached by Section 317.3(a), does the potential injury from conduct reached by Section 317.3(b) justify its likely enforcement and compliance costs? Explain.

Answer: Please see pages 12-25 of our comments.

f. Does the inclusion of the explicit scienter requirement in revised proposed Rule Section 317.3(b) adequately reduce any danger of a chilling effect on the flow of information essential to the functioning of, and transparency in, wholesale petroleum markets? Why or why not?

Answer: Please see pages 25-33 of our comments.

g. Does the inclusion of the explicit scienter requirement—*intentionally fail*—in revised proposed Rule Section 317.3(b) sufficiently reduce the danger of a chilling effect on benign or desirable business activity within wholesale petroleum markets? Why or why not?

Answer: Please see pages 25-33 of our comments.

h. What forms of information, if any, should market participants be required to disclose in order to promote the functioning and integrity of wholesale petroleum markets? Explain. Under what circumstances, if any, would the failure to provide such information render otherwise truthful statements misleading?

Answer: Please see pages 12-25 of our comments.

i. To what extent would any danger of a chilling effect on benign or desirable business activity depend upon the existence (or lack thereof) of mandatory disclosure obligations in the petroleum industry? Explain.

Answer: Please see pages 12-25 of our comments.

j. If the merits of Section 317.3(b) as currently proposed outweigh any flaws or dangers, should it be expanded to require that a person update or correct information if circumstances change? How, if at all, would such an expansion alter the cost/benefit calculus? Explain.

Answer: Please see pages 12-25 of our comments.

k. What, if any, danger arises if the scienter standard in revised proposed Rule Section 317.3(b) were changed to "knowingly fail"? Explain.

Answer: Please see pages 25-33 of our comments.

l. Is it clear that the "intentionally" scienter standard in revised proposed Rule Section 317.3(b) means that the Commission need only show that a violator intends to engage in fraudulent or deceptive conduct – without regard to the violator's intent to affect market conditions or knowledge of the probable consequences of such conduct? Why or why not? If not, how could the scienter language be revised to limit the evidentiary burden to requiring only a showing that the fraudulent or deceptive conduct was intentional?

Answer: Please see pages 25-33 of our comments.

m. What types of evidence might be sufficient to demonstrate the proposed scienter standard in revised proposed Rule Section 317.3(b)? Explain. What types of evidence might be sufficient to demonstrate the proposed scienter standard in revised proposed Rule Section 317.3(a)? Discuss with particular emphasis on how, if at all, the evidentiary requirements to prove scienter differ between Section 317.3(b) and Section 317.3(a).

Answer: Please see pages 25-33 of our comments.

n. Is it clear that the "intentionally fail" scienter standard in revised proposed Rule Section 317.3(b) is neither a recklessness standard nor a specific intent standard? If not, how could the scienter language be revised to make that clear? Explain.

Answer: Please see pages 25-33 of our comments.

o. As explained in the discussion of revised proposed Rule Section 317.3(b), the prohibitions language of Section 811 of EISA is nearly identical to Section 10(b) of the SEA from which Rule 10b-5 derives. Notwithstanding this similarity, does the statutory language in Section 811 – "as necessary or appropriate" – provide a sufficient basis for tailoring the scienter requirement of a FTC market manipulation rule to address wholesale petroleum markets? Explain.

Answer: Please see pages 1-12 and 25-33 of our comments; please also see *NPRA Comments* at pages 8-15.

p. Intent need not be demonstrated to prove that an act or practice is deceptive or unfair in violation of Section 5 of the FTC Act. Does the presence of explicit scienter requirements in revised proposed Rule Section 317.3 create risk of judicial confusion regarding the differing elements of proof for an FTC market manipulation rule and for Section 5 of the FTC Act respecting unfair or deceptive practices? Explain.

Answer: Please see the main body of our comments.

q. Does the Section 317.3(b) proviso that a misleading statement distort or tend to distort market conditions for any covered product sufficiently ensure that the Rule strikes an appropriate balance between protecting consumers from petroleum market manipulation and limiting the costs to industry attendant with achieving that protection? Would adding the proviso to Section 317.3(a) achieve a better balance between protecting consumers and attendant industry costs in the enforcement of that provision of the Rule? Explain.

Answer: Please see pages 34-43 of our comments.

r. Does the Section 317.3(b) proviso that a misleading statement distort or tend to distort market conditions for any covered product unduly limit the Commission's ability to prohibit misleading statements that threaten the integrity of wholesale petroleum markets? Why or why not? If not, how could the provision be revised to achieve that goal? Explain. Were the proviso added to Section 317.3(a), would the Commission's ability to protect the integrity of wholesale petroleum markets be impaired? Explain.

Answer: Please see pages 34-43 of our comments.

s. Is it clear that the Section 317.3(b) proviso that a misleading statement distort or tend to distort market conditions for any covered product is not intended to create a price or market effects element of proof? I.e., is it clear from the language of Section 317.3(b) that in order to establish a Rule violation, the Commission need not prove any specific price or market effect? If not, how can the Rule be revised to make that point clear? Discuss.

Answer: Please see pages 34-43 of our comments.

t. What types of evidence might be sufficient to demonstrate that a misleading statement distorts or tends to distort market conditions for any covered wholesale petroleum product? For example, should it be sufficient simply to show that the informative content of a misleading statement is of the type typically absorbed by the market and incorporated into market prices? Explain.

Answer: Please see pages 34-43 of our comments.

u. Is it clear that a violation of revised proposed Rule Section 317.3 does not require that the violator possess market power – and need not have reduced competition – in a relevant antitrust market, as these concepts are defined by antitrust legal precedent? Why or why not? If not, how could the language be revised to make clear that neither a showing of market power nor a reduction in competition is an element of proof?

Answer: Please see the main body of our comments.

3. Consider the following alternative rule language:

> It shall be unlawful for any person, directly or indirectly, in connection with the purchase or sale of crude oil, gasoline, or petroleum distillates at wholesale, to engage in any act (including the making of any untrue statement), practice, or course of conduct with the intent* to defraud or deceive, provided that such act, practice, or course of conduct distorts or tends to distort market conditions for any such product.
>
> > * The phrase "with the intent" shall mean that the alleged violator intended to mislead – regardless of whether he or she specifically intended to affect market prices (e.g., specific intent), or knew or must have known of the probable consequences of such conduct – and regardless of whether the conduct was likely to succeed in defrauding or deceiving the target.

Would this alternative language better achieve (or would it not better achieve) the goals of Section 811 of EISA than the revised proposed Rule discussed in this Notice. Explain. Discuss the merits or flaws, if any, of this alternative language?

Answer: Please see the main body of our comments.