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Session 6: "Regulating Energy Commodities"

Speakers:

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[Note: Recorders did not pick up introduction of panel (see biographies for details on the panelists) or introduction of session.]

Steve Harvey: Why don't we start kind taking our seats and give it just a...well, no looks like we're pretty close. It's a disadvantage, I guess being last on a beautiful day in Washington after a nasty winter. So, I'm glad that the *[inaudible]* brave folks are still here with us. This panel is on regulating energy commodities. My name is Steve Harvey. I'm the Director of the Office of Oil and Gas at EIA. I will not go into the details that Howard Greunspecht, our Deputy Director went into, but when Richard Newell, our Administrator, came in last year, one of the first things he announced was an effort to look at energy and financial markets. I think, in brief, the idea was we really thought that in the EIA, we needed to incorporate more dynamics into our explanation of what was going on in the price formation process and really strengthen our comprehension of the effects coming out of the market itself. And what that means is, we've got to pay some attention to market dynamics and the way that we really did not necessary pay as much attention in the past or in a way that we really want to as we go forward. One of the first and most immediate things when you think about market dynamics right now in energy commodities, though, is change.

There are a lot of issues on the table, and we would like to sort through the regulatory and policy issues that are on the table with the panel today. Now, my notion of being a moderator is that my hardest work is actually in picking the people that come up here and do the really hard work of telling the story, and my priorities in doing that are...first, really who are the people I'd like to hear tell about these issues, and then, secondarily, but very importantly, how do we sort of capture important perspectives in the marketplace. It is impossible to get any individual to represent other than particular organizations but represent sort of components of the marketplace, and so, what I'd like to do is not go through and to read the bylaws, but what I'd like to do is get through an order of our speakers, and why I'm happy that they're here, and that I'm looking forward to hearing this, and I hope that you will, too. And, in a little bit, the prospectives that I'm hoping to hear...they're the direction I'm hoping to hear from them as we hear them talk today. We'll be starting with Dan Berkovitz. Dan is the General Counsel at the US Commodities Futures Trading Commission. I'll just use CFTC from here on out. I got to know the enemies...his previous job was Counsel to the Senate's Permanent Committee on Investigations under Senator Carl Levin, and in that job, I know Dan did some very compelling, very interesting work on a lot of energy market dynamics. So, it is exciting to see him go to the CFTC, and I think it's going to be very valuable to us today to have the General Counsel of CFTC describe to us a little bit of their recent policymaking initiatives and hopefully even talk a little bit about, certainly not a CFTC perspective, but perhaps the Chairman, Greunspecht's perspective on some of the activities going on more broadly in policy. After Dan, we'll hear from Sean Cota. I don't know Sean particularly well, but I'm a fan of his. He's been very active in testifying in the last couple years on these sorts of issues. He is the President of Cota & Cota, one of the most successful fuel marketing businesses in Vermont and New Hampshire. He has represented the heating oil, gasoline, and diesel retailers in a lot of contacts but certainly and specifically in the markets advisory committee on NYMEX or at CFTC. I'll keep this straight. And again, he spoke and he has testified in the Senate. He has testified in the House and brings a strong perspective that we believe is important to put on the table, which is physical consumers or physical purchasers of the energy. Certainly, as a retailer much closer to that end of the energy chain and one that' very important to have confidence in the way that markets operate as we go forward. Third, is Skip Horvath. I've known Skip forever. Now, Skip is the President and CEO of the Natural Gas Supply Association. Before going to NGSA, he was at the Interstate Natural Gas Association, where he reached the level of Chief Operating Officer. He was just a senior analyst when I was junior analyst, in the early 80s at NGSA; and Skip is here really talk from the perspective of producer hedgers...from producers who are involved in the marketplace and their view of the market and how it functions. I should say as I'm saying, represents...it's again not that there is anyone particular perspective in any of these groups, but it's important I think to hear voices from those different areas. And finally, Deanna Newcomb. I don't know Deanna very well, but when I started talking to various folks about who could speak to the perspective of trading organizations to this policy issues, it was unanimous, and so, we invited Deanna who is Regulatory and Compliance Analyst at McDermott Will & Emery in Houston. She has many, many years of advising trading companies on compliance matters, government investigations, regulatory audits, and the like; and I'm hoping that she will share with us a little bit of the view of how trading operations look at these policy changes and how they operate and think their operations based on that. So, given that what I'm going to do...I did not encourage a lot of prior cooperation on my panel. I've asked them to limit their times so that we can stick to real time. Each tells their story in order from their perspective, and then during that, please send up questions. I think when we finish with Deanna, we're going in strict alphabetical order here that...what I'm going to do is encourage them to respond to one another for a little while, and then I'll begin filtering in the questions that you all sent up as well, and we will try to finish here at quarter after five or twenty after five, so that we can go on to the reception. So, with that I would like to turn over to Dan Berkovitz.

Dan Berkovitz: Thank you, Steve and Administrator Newell, who I just saw a minute ago who was here. I would like to thank you and EIA for providing the CFTC and me with an opportunity to participate in this conference and help explain where will I be headed in some of these issues. Steve mentioned...I've known Steve and many of the EIA folks for many years when I was up in the Senate looking at the energy markets. It was actually daily...I do mean this seriously...daily, I would look at the EIA website and look at weekly at This Week in Petroleum and look at the NYMEX prices, and that really was an invaluable source of information about what's going on in the market. And when we talked about transparency in the marketplace, it's through efforts like EIA and the information they produce. So, it's a real pleasure for me as a user of EIA, and I was a colleague in another Executive Branch. I have to give the standard Executive Branch disclaimer in that the views I'm giving and the words that I'm speaking don't really represent the views of anybody or the words of anybody. I'm not speaking on behalf of the Commission and thus the Commodity Futures Trading Commission does represent. The position of any individual commission is...but nonetheless I will try to useful information. Only discus several topics, last panel, for example addressed how we got to the current place we are in the market, what's going on in the market today. My focus is going to be a little more on where we might be headed in the future in terms of the regulatory structure. Taking what has happened in the past, the many causes, the multiple causes of what happened in 2008, not only in the commodity markets but more broadly speaking. In the financial markets, the near economic meltdown we have in the late 2008, and trying to take the lessons from that experience, transform it into constructive steps in the regulatory process to ensure that something similar doesn't happen in the future. In addition to the legislation, I'm going to touch on position limits rule, activities with significant price discovery contracts, and also briefly, our transparency initiatives which are designed to provide better data for the public and that analytical organizations such as EIA can use to really to try to understand our markets better. Let me start out with the legislation, where we are and where're going with that. I'll try to do it briefly, just hit some of the major concepts. Clearly, there are many causes for financial collapse in 2008, for the bubble, and some of the commodities in the housing market, and then the subsequent collapse of a number of major financial firms, and the necessity for federal bailout of those firms to protect further systemic collapse. One of the lessons from 2008 is for previous system...the system that we were currently under, where we really are relying totally on market forces to ensure that there is not excessive risk-taking — a philosophy that's really wasn't bad in the Commodity Futures Modernization that really didn't work very well. And we need a more robust system to ensure that there is not an excessive buildup of risks in the financial system. So, central to features of the legislation that the Administration proposed last summer, that's really in the House bill and in the Senate Banking Bill that has come out of the Senate Banking Committee, is regulation of the major financial institutions — the dealers, increased regulation of the dealers, increased use of clearing so that we have a neutralization of risk and additional transparency and regulated trading platforms. So, when we just say briefly, sort of where we are in the process. I have mentioned the Administration sent up a regulatory reform bill last summer, both the House and the Senate held hearings on it. The House Financial Services Committee and the House Agriculture Committee passed versions of the bill last fall. The two committees merged the bills and went to the floor of the House late last fall, last winter. And last December, the House of Representatives passed the Regulatory Reform Bill. The Senate has been on a different time frame. Just two weeks ago, the Senate Banking Committee reported out their bill. The Senate Agriculture Committee, which has jurisdiction over Commodity

Futures Trading Commission, many of the over-the-counter derivatives, is working on a bill, and we expect them to release a bill in the near future. The Senate...now that healthcare reform legislation has passed, the President has said and Majority Leader Reid in the Senate that regulatory reform is one of the top priorities. So we at the CFTC, have been very, very active. Much more active recently in the last several weeks providing technical assistance to Members of Congress and getting ready for the debate in the Senate on this legislation. As I mentioned the essential features...there are three essential features of the legislation, about the Administration Bill and the House Bill and what has come out of Senate Banking Committee so far. One, is the regulation of the dealers, the derivative dealers; two, is clearing of what we call standardized swaps; and three, increased trading and transparency...increased trading on regulated platforms and increased transparency for those trades. When we talk about regulated dealers, who are we talking about? When we're talking about what's commonly known as swap dealers, and these are the entities that make the market and swaps. These are generally, the very large financial institutions...Without going into too many names, one, I think of a JP Morgan Chase, the Morgan Stanley, and Goldman Sachs...generally built the large swap dealers. There is another category that would be regulated. These are other financial institutions or other institutions that may not necessarily be a swap dealer. They don't call themselves out to be a dealer, so they do a very, very large swap business, and the risks that they create post systemic risks to the system, and this is the category that legislation refers to as major swap participants. So, these two categories, the swap dealers and the major swap participants will come under increasing regulation. By increasing regulation, I mean, there will be capital requirements, there'll be marginal requirements for the individual trades. They will be subject to business conducts standards such as requiring to adapt and adhere to anti-fraud, anti-manipulations standards. There'll be record keeping and recording requirements. They'll be required to monitor the activities of the persons of those institutions doing the trading. There'll be really fully regulated market participants; today, they are not. They will also be required to clear their standardized trades. You may ask, in a big issue that has been debated throughout the consideration of this legislation, as what do you mean by standardized trades. Which trades are going to be subject to clearing? The Administration proposed a test for what's a standardized trade. We have a number of factors, so that if it means these various factors such as standard price terms that can be offset with better and similar instruments, the use as a price reference, things like that we would define in a standardized and if it's standardized, it needed to be cleared. The House took a slightly different approach and adapted a more market-oriented standard. So, if a clearinghouse will accept it, and the CFTC, after reviewing whether it's appropriate for the clearinghouse to accept that will be subject to the clearing requirements. So, in a House bill and in the Senate banking bill which follows that there is really a more market-oriented test of which swaps should be required to be cleared. The swap dealers and the major swap participants will be required to submit their standardized or clear book swaps for clearing; and a major issue in this legislated debate has been beyond the swap dealers and the major participants. This has been come to call the end users, and the typical end user example would be, for example, an oil gas exploration company that uses swaps to hedge forward, to protect their sales of oil or gas exploration against price volatility.; And the question is as typically, well, probably the situation in secured oil and gas producers...let's say you're a gas producer, you have a choice going for the NYMEX and hedging your forward sales with the futures contract on the NYMEX to lock in the price of which you're going to sell that natural gas, or, alternatively, you can go over-the-counter to a swap dealer and that you might have a relationship with the bank, one of the major banks, and as part of that credit relationship, they'll offer you a swap. The end user community has made a very strong case to the Congress that flexibility should be preserved and that in many instances, they would prefer to do a swap with the swap dealer where they don't have to pose collateral rather than go to the clearinghouse and buy a futures contract when they were actually required to post a collateral. Natural gas producer *[indiscernible]* like the case more persuasively that I can...has limited capital available to, say, get over to a clearinghouse; and every dollar that you take from the oil and gas exploration and production means one less BTU of gas produced, and potentially raising the cost to the consumer. And not only natural gas producers, oil exploration...the case has been made very strong at the energy producers as the coalition of energy producers would made this a case in the Congress, and there's a much broader coalition of Corporate America manufacturers, automobile companies, the electric utilities, agricultural companies.

Both the Administration's proposal, the House bill, and the Senate Banking Bill contain variations on what's called the end-user exception. The House bill had a defined end-user exception for companies hedging...commercial companies hedging, operating a balance risk...the Senate Banking Committee gave it within the discretion of the Commodity Futures Trading Commission to determine which entities would be exempt from the clearing requirement. This is a major issue that is going to be continued to be debated within the Congress and has particular importance for the energy industry. Beyond the clearing requirement, most of the proposals tie a clearing requirement to a trading requirement, that if a swap is required to be cleared, it should also be traded on a regulated platform and with element of price transparency to the broader market. Of course, all swaps, whether they're done on a regulated facility or not, the Bills preserve the ability of companies to do solely bilateral transactions. It doesn't force people onto an exchange, or in some instances doesn't even force the monitor regulated platform. Bilateral customized transactions are still permitted, and all the transactions no matter which type, or it's on the regulated trading facility or an exchange or a bilateral, will be reported to some type of facility that that CFTC or the Securities and Exchange Commission or FERC, whatever appropriate regulatory agency, would have access to, so we will have access to all the swap data, no matter how it's executed. But the transparency requirements and the trading requirements would apply to things that are traded on exchange or what we call swap execution facilities. And another issue of debate within the Congress and within the community that's interested in this is just exactly what type of trading facility should be regulated, what type of choice should persons have in terms of which facilities they trade on, and exactly what the transparency requirements should be for those trades. My boss, Chairman Greunspecht, is very pro-use of regulated trading facilities, trying to get as many trades as possible onto regulated facilities while preserving the ability of individual traders to be able to select their counterparts who can block in large trades so that you don't have to expose large trades to the market and also providing as much transparency to the public after the trade has been completed as possible so that the marketplace can see where the last trade is and in the long run that will reduce cost for Corporate America. Those are the broad outlines of the legislation. I'd like to mention just a couple of other things that we have going on right now. On January 14th, the CFTC issued a proposed rule to impose position limits in the Energy Futures Contract. Right now, we have position limits in the spot month, but we have what's called accountability levels for other months and for all months combined in Futures Contracts, for example, oil and natural gas commodities. On the proposed rule which came out on the 14th, the common period is open until April 26. We are proposing to impose position limits in addition to the spot month. You would have fixed position limits for any single month and for all months combined. We currently have this in the agricultural markets, where we have fixed position limits for any individual month or in the spot months and all months combined. But in the energy markets, since the early 2000s, we have position accountability. We're also in the proposed rule attempting to have uniform process and standards for hedge exemptions and for exemptions for swap dealers.

We are in the process now of reviewing except...and sometime in the near future, I can't say exactly when, the review of contracts traded on exempt commercial markets to determine whether they perform a significant price discovery function; and this is an outgrowth of the 2008 Farm Bill which imposed regulation on electronic trading facilities. If there is a contract on electronic trading facility that performs a significant price discovery function, then the Farm Bill requires that it be regulated as a futures contract essentially; and this really is the ICE facility in Atlanta that's trading natural gas and electricity. So, we've been reviewing those contracts to determine whether they perform a significant price discovery function.

One major contract traded on ICE which the largest contract traded on this ICE electronic platform and ICE natural gas swap has already been determined to perform a significant price discovery function; and so ICE with respect to that contract, is regulated very similarly to a futures contract which means position limits are very similar to the NYMEX position limits.

And then, the other thing I would like to mention especially here to the EIA conference is our increased transparency initiative. We have been publishing, for several months now, increased granularity in the data on the composition of the markets. Previously, we just had our commitment of traders' reports divided into commercial and noncommercial; and now, we have a number of other categories, so you can see whether there are market participants or swap dealers or index traders, and hopefully, that additional granularity in the data which we are continuing to work on in these commodities as well as possibly others can help the analyst answer some of the questions, "What is the effect of index trading?" or "What is the effect of this category of trading on the market?". At least, that the hope is that the additional data will provide better analysis, and we'll see whether we can actually get to the bottom of some of those questions.

So, thank you.

Sean Cota: Well, if you're going on the 80-degree weather...if you got where I came from this morning, in Vermont, there's still snow in the hills, so you can enjoy that and think of heating which is something that I do. What Dan talked about really on the process, I get confused with a lot of the terms that you hear around, like what is a swap? What's a swap dealer? What's a futures contract, and all of those things. So, you all in this room are smarter than the average Congressman, so I'll go on a little bit more detailed, and keep it as simple. But swap is essentially the same thing as a futures contract with risky and custom money built into it. It's kind of like a car lease and a car loan. Car loan, you own the car, you get the commodity of the car. You get the...you go to your bank and your bank gives a loan that's all packed together. You book the car asset and you book the liability of the loan. You don't do that with the car lease and you don't do that with swaps; and that's part of the resistance in our moving forward of the investment community, a lot of the large corporations. These are ways of doing hedging without it making an impact on their balance sheets, and, in the case of Greece, with credit default swaps, they were able with the assistance of JP Morgan and Goldman Sachs to hide three-quarters of the national debt; and that all relates to leverage and different games. So, to say why things are real, you need to put a quantity on things. I'm going to go through this really quickly but we have extra copies if you want them and you can e-mail us. I like the title here — "Financial Energy Commodities Speculation" — this connected the fact on fundamental price discovery mechanism or fundamentally EIA fundamentals don't matter. It's all about money for us and that's what it is about. Historically, supply and demand up till about 2004...really made an impact on setting prices and there's a disconnect that really began to hit at least the petroleum segments of the commodity markets and some of the metals and food at that point as well. But 2004 is an important...and you'll see why. Here, the traditional methodologies, 87 through 2003. See you got a price correlation and volumetric correlations that really come in pretty nice, and you can make some investments and say, "Okay, I think I know how much, how cool it's going to be, and I know how many customers are going to buy what and so I'll buy some futures contracts on that price, on that basis and I won't get wiped out."

There's a first anomaly, was the First Persian Gulf War. Ironically, I love the First Persian Gulf War with the way that they handled speculation. At that point, the New York Mercantile Exchange still dominated the oil trading markets, and a little known fact is that the merchant requirement when we started the ground war went to 50% merchant-like acuities. It was a massive deleveraging. People that really wanted the oil stayed in it. People that didn't, got out. Massive sell off. So, it affects price; leverage affects price. Inventories in 2004, things started get a little screwy. It doesn't make with the same methodologies that it happened in the past; 2005, again the same thing; 2006, 2007, and then of course, whacky 2008, where up is down, left is right. For the folks in Baltimore, it's almost in that *[indiscernible]* moment where everything we see or have seen is but a dream within a dream and nothing made any sense in that period. And the last 11 months, in the last 11 months, is actually quite predictive of what happened in 2008. I'll show you some more here. Again, this is all about capital flows everyone's chasing. They're on tail. You don't hear in the news media right now very much about, you know, the financial media, about the downside of commodities. Well, nobody is talking down, that's when most worried, and nobody is talking down, and everyone's chasing these trades and they're highly leveraged, and there's huge amounts of money going on whether it be investment funds, index funds, ETFs. I think the ETFs and index funds are actually the most dangerous that are out there. The index funds are just big dome investors. They just bet long; some in the industry for financial farmer call them invesculators. They think they're investing, but they're really speculating. They just don't know it, and because they go with such a large volume of money, and they actually publish it on their websites...if you're dealing a spread, deal for what the contango change is going to be. It's easy money that you can't lose. The big banks love it; and in order that they get to borrow from the Fed at 0% which is kind of nice. So, there's a high correlation that we’ve seen with all trades. You know, you used to have the old days where the Dow Jones Industrial Average industrial companies can use this thing called “energy”; and when energy prices go up, their stocks don’t do so well. The last year, that has been completely the absolute. Here’s your volume of passive investments that have gone into the markets. Again, these are just huge index fund growths, this staggering number is. And there’s some more. Passive index investment...here’s another chart that shows the volumetric amounts. One other thing that happens again? What they’re doing is they’re buying longer, across all months and they shorten in years, months because they never to intend to take commodity; and that sends a lot of mixed signals to the producers and buyers in the market because you see this contango out there saying, “There’s no demand.” And there’s no demand right now, so you know, particularly in my industry, and it creates this false sense of future value, or people build inventories where there’s no consumption, so it’s a complete disconnect. It has never happened before; and because of the flows of money, they overwhelm the markets. Then, here’s the shot on the indices in the huge volumes that have increased. This is the first half of 2008 — the flows of oil indices. Second half, this is after the collapse. And here we go again...again, index funds are plowing in. Now, index funds...here’s one of the little things that nobody knows. If you take a look at an index fund return and investment chart, they don’t get the same investment as if you invest in the commodity. The contango chart is being charged to the index funds. So, whatever that contango fee is, whether it be done in paper contracts or whether it be done in other swap arrangements that are more highly leveraged and have a backend of a physical product that’s stored, all of those, whether you’re renting a super tank, all that stuff gets in charged in the index fund. So, the index fund is a bad investment, in my opinion. And I’m not a broker, so I can tell you whatever I want. That’s a price correlation with the WTI and I forgot that one. Okay, here’s where the paper market really takes off. So, if you take a look at the chart and the blue bars of the physical portions of the oil market, and you get into 2004, things start to change. That's when I really got interested in the topic because I said, the world that I have known no longer exists, and what's up with that; and I said, it's just the oil. Turns out...it's actually everything, derivatives, CDOs, CDSs. But the volumes have increased and they're still increasing, just huge amounts of paper flow. Now, these paper flows can change the dynamics in the market, which gets into part of the regulatory efforts that we're trying to do in financial form of aggregate position limits. When you're dealing with the fixed commodity, unlike a currency which is in theory infinite, you can overwhelm these markets. I worked...I read a report by this guy named Dan Berkowitz that did a study on this company called, God, what was that, who is the hedge fund *[indiscernible]*. Thank you, my block with that, Dan, I forgot. Anyway, Emery at that one point, when they did the investigative reporting, they found out that the February contract in natural gas, Emery's position was 80% of the total market. Well, what would that impact in...you know, spread on various markets; and what impact would that they make if, say another individual decided to buy an option to buy every single family house or 80% of the single family houses in the country; and didn't last 15 minutes in a month. Would that make a price impact? Of course, it will make a price impact. Was that good or bad? Well, it depends on whether you're a house builder or you're going to be renting that house. The difference is rather substantial, but those sorts of market limits used to work when it was a monopoly exchange in oil. When NYMEX had the monopoly, then the exchange was self-enforcing. It was swaps and over-the-counter markets and all of these things that no longer pertain, so there needs to be a new regulatory structure that, one, identifies the volume and stuff that's out there and then puts limits on in *[indiscernible]* so that in finite markets, again, I'm not talking all markets, just finite markets, that these markets don't become overwhelmed. I mean, disconnect with dollar and WTI, let's say I went back. Here's one, this is an inflation WTI; you'll see that it comes together during the market collapse and the shake out that it's directly together; and now we see this disconnect occurring again which is an indication of another bubble. Persisting contango, again, that's the result of the index funds, something has not happened until this period of time. Negative Euro, again, some more effects.

Now, when you're talking to a politician, you get to say, well how much will this cost the average consumer? What's the cost? You're saying that this, the dumb investors pile in and the speculators, the investment banks...they're doing highly leveraged deals. Der Spiegel had article a week or two ago that the Goldman Sachs leverage or something, nominal leverage like 33,000 times, you know, just staggering numbers. So, when you add leverage in all of these other things that didn't exist in the markets prior to 2004, you take a look at what the price is so, we took...2003 was kind of our baseline. That was the year that had lower inventories than what we currently have now. It's kind of at the higher range or pricing; and they come out average over that 12-month period; about *[indiscernible]*. We said, you know, based upon fundamentals and I did...we converted, I converted this back to 2010 dollars, so this takes in account inflation currency effects. So, what is the price today? So, this is the price from 2007 through 2014. You see where we are. In the...I didn't overlay that graph perfectly and I apologize, but the speculative premium...you can see the speculative premium back at the peak. This is crude oil; diesel was $2.70 of speculative premium. Now, right now, it is a dollar. Now, NYMEX is trading it at about $2.30, so it's not quite half the cost but it's a buck a gallon. So, when you're quantifying what are the impacts of the consumer, what impact has this on the economy? These has huge impacts. And none of the stuff actually builds long term investments, so you're not going to build a powerplant or a biofuels plant or any sort of plant in the long term unless you know that there is predictability in these markets because they are going to want to know that you got a certain amount of commodity that you're going to be able to produce at a certain price that will pay off the bond for these banks and errant bonds for these factories. And so, without predictability, you don't get long term investment, and former Secretary

Summer, at lunchtime he alluded to that; and I think he's absolutely correct. You need to have predictability in your market; and so I think he comes at it from a different angle than I do, but you need to have predictability. That's the cost. So, what do we do? We got to get...there's some of the folks that helped get us and answer email if you need it.

I'm part of a coalition of probably 450 groups. It's a commodity market so we're *[indiscernible]* coalition in the derivatives. Derivatives Reform Alliance. Thank you. And we're working...joining a lot of these projects in the financial reform. There's a lot of that going on; and a lot of the things are in the nitty-gritty details but most people don't say it. So, one of the nitty-gritty details is what does a swap dealer — what's not a swap dealer, what's an exempt end user, what's not an exempt end user. Those are key elements, and we've got to get it right. You know, if you define...let me give you two examples of people in the oil market. The largest traditional holder of oil in the United States is Morgan Stanley now, it's not Exxon Mobil, and Morgan Stanley is an excellent provider of product. They will always have product there. They don't ration on the Soviet method, that's what some of the major oil companies do so...in a lot of ways, they're very good. But their primary purpose is not to supply product. The primary purpose is to make money on the trades. So, if they're exempted as an end user on all of their trades as a bona fide hedger, none of those regulatory efforts that we're going to do is going to make any impact. So, that's one example. Conversely, you've got Cargill. Cargill is another example of a commodity producer that's a farm producer but they make the vast...they function in most aspects more like a financial player investment bank. And so, to the extent that you're going to exempt these players for being in the physical market, which I think you do need to do, you need to confine it directly down to the amount that they're hedging for the physical players, and anything beyond that is going to just not have any impact on these *[indiscernible]* of matters. So, I could go on all day but I won't. Thanks.

Skip Horvath: IThank you, Sean. I'm going to be addressing most of my remarks to Dan's presentation, but I'll touch on Sean's as well because he kind of got into *[indiscernible]* regulating...that the problem we're all trying to solve, and I mean all of us. I mean, we agree at the CFTC that this systemic risk has to be stemmed so that we don't bring the country down. I mean that's a lot of a goal. Who can't get behind that? And just review the, you know, the records...systemic risk. For those of you who don't pay whole attention to this, systemic risk is something that you cannot take a countervailing position in the market to protect yourself against, alright. You can't take another...you can't buy another set of stocks or bonds or any instrument that protects you from this risk; that's a systemic risk. In the vernacular, it's a risk that can't...that has a draw on the Treasury. It's a risk that's too big to fail. We're trying to prevent that again. And so the question is, what net can we use? What CFTC is trying to do then, I think, actually doing a pretty good job of is how far do you cast that net to make sure you take care of those systemic risks. In our view, and Dan, articulated it quite well, the net is cast too widely; and actually incorporates people who don't pull the systemic risks. I'm going to make a case that the energy companies...not just what I represent, which is the large producers, but pretty much anybody with assets in the ground...do not pull systemic risk. I'm just going to, you know, it's not going to be an academic discussion. I'm just going to give you a real-life example: Enron. Enron collapsed in 2002. How many people were around in their jobs when Enron collapsed? And so, yeah most of the audience. Aren't there many folks that are that young that don't remember that...that's only eight years ago. When Enron collapsed, the price started plummeting from about $100 level; it hit $16, that's when I bought by the way. I thought, you know, I looked at the assets that can possibly go any lower. It went down to $8, and then down to penny stock, and then out of business in a matter of weeks. So, other than me losing money, what happened? Well, there was a blip in the market, for a couple to three weeks, in the natural gas market. There was a blip in the stock market for a couple of days, which happened very quickly. Management was out. New management, many of whom from the different parts of the energy sector. Natural gas sector moved in, took over; the operators kept pushing out gas, pushing out water —I think I did that, didn't I? — pushing out electricity, all the other commodities that they were in. And I can tell you, that for the natural gas industry, not a single customer lost natural gas service due to the Enron failure. Not a single one. All the *[indiscernible]* contracts helped. That was an amazing, amazing feat, and the reason is assets in the ground. That's the difference between the group of people who hedge and those who are the swap dealers, the large financial players that Dan named, without trying to name, Jess Dam, that whole group of folks. They don't have assets in the ground. They have assets, but they have liquid assets, not assets from the ground, and that's a key difference. In our view, the net that has been cast there, for example, in the dud version, out of the banking committee in the Senate is just cast too widely. We're looking forward to see what the Ag Committee does when it pulls out their version of how to regulate those of us with assets; and that's important because the agriculture community also has assets in the ground. They have also a lot of votes in this Senate; and we've been in talks with them, and they pretty much agree with us. So, I think we are hopeful that we'll find the exemption we need to make sure we can still hedge and have a service for those who...because we're big companies, a lot of *[indiscernible]* would like to hedge but don't have the wherewithal can use our services to...we pull all those folks to hedge as a group. So, asset-owning industries is the OTC and we actually use it to reduce commercial risk. So, I want to point is that the mandated clearing that cast that net too broadly in our view, what it does, it actually has three perverse effects that I want to...I think is important to bring out.

First, in our view it centralizes risk, because you're taking risk now that spread a whole...a bunch of hundreds, maybe a thousands of counterparties, alright, because it's not centralized; and puts on a handful, I mean really small handful of clearinghouses;

and those clearinghouses are by and large controlled by the very people that caused the problem in the first place. So, we're having a hard time figuring out how that helps us get away from systemic risk. *[indiscernible]* argue that, that it actually increases systemic risk to some extent.

Second thing is the disadvantages those with assets in the ground *[indiscernible]* us because the assets are not recognized when you have to put up collateral in a clearinghouse. It's the same amount for...regardless of the participant. So, our assets are recognized as zero value. We *[indiscernible]* so are the assets of the financial player. Yes, but they don't have any assets in the ground. So, there's this, appropriately recognized as zero. So, that puts us at a big disadvantage to them. Again, they're the ones that cause the problem, so it's hard for us to see why this is a good thing.

Third, you'll take the *[indiscernible]* out because they won't have collateral. You'll reduce the number of players on hedge market. Anytime you reduce the number of players in the market, you're going to increase the price volatility; and we lose the liquidity. So, that's...you know, and people complain now about the price volatility of natural gas. That would just make it worse.

So, those are three quick reasons why we're opposed to casting that's too broad to include us.

Switching gears a little bit, let's look at the economy as a whole, and, you, say you did an analysis that is merely quick and dirty. We were estimating that...if these are forced on the entire country for asset holders, roughly 900 billion, almost a trillion dollars of capital that would otherwise be invested in assets in the ground industries would be set aside and used nonproductively with some advice because it is serving a function on the clearinghouse as posing as collateral. My point is, this is not being invested in an infrastructure; and in the case of natural gas, it means as Dan...and Dan, by the way you said it actually much better, but I've never said it, I would like to review what he said. If *[indiscernible]* of money aside for collateral, then we can invest it in the ground, that reduces supply, and give in constant demand or growing demand that increases prices. So, it actually increases the price of natural gas to American consumers, and probably to other commodities as well although all these speak for the natural gas industry.

So, in short, mandatory clearing would move 900 million dollars, almost a trillion dollars. I'll take it out of the protective part of the American market at the time when we need to recover.

So, I'm going to switch gears a little bit, and move from that to something that Sean brought up in the chart. I am not actually putting the chart back up, but just to recall his chart, one where he had the physical commodity markets, blue bars at the bottom of the chart and the big red bars represent the paper markets and went up as time went on really high, so they were like the red bars, like twice as high as the physical. Paper markets twice as high as the physical 15 years ago; and today, their order of magnitude are more bigger than the physical markets; and that should give everybody parts, alright. That's what people called, back in a couple of years ago, excessive speculation, you know, without thinking about whatever...what does that mean, excessive speculation. And the first got a reaction of many people in the market was, "Look, it's the market and it's not a bad market. It's good market, it's a liquid market. It's...maybe could be more transparent, but it's not a bad market. So, just let it work." Well, after its collapse, we decided to take a look at it. Okay, what do folks smarter than us think about this connection between those in the blue bars and the red bars, between the physical and the paper financial markets? So, we had Li Ken Shu who actually is a counterpart of, or a colleague, of Steve Harvey's at the FERC, is now down in Houston as an academic, and had him do a literature search on what academics...what economists have said of a study about the link between those two markets; and what he found surprised us because he found nothing — very thin literature. When I say nothing, he found arguments on both sides. He found economists and experts saying that there is a link, and they try to make case but they had no real data or facts to support it. And he found people that said there is no link, but, again, there were very few facts or data to support it. It is an unexplored academic area among economists. So we want to remain open to the notion that something is going on in that chart that Sean put up, that it might mean something…sort of caution anybody from saying what it means right now. We don't really know, and I think it's going to take us sometime and some effort...some research efforts among the academicians to figure it out and sort it out. As far as Sean's parting point regarding...you got to be careful to, how do you separate out those who are true hedgers from those who aren't...and the CC, you guys hedge and you guys don't hedge at all. You're just speculators...we're really the speculators and not the hedgers, but there are groups that fall in-between, I think. We're open for discussion on how one does that. It doesn't mean we shouldn't try because it can be difficult, but we've got to find a way to make sure we don't cast that net too wide and hurt the economy that is trying very hard to recover. And other *[indiscernible]* I am looking forward to other presentations and discussion afterwards.

Steve Harvey: While the end is heading up, I haven't got a lot of questions from the crowd. If there are any, I don't know that we've got anyone...we're collecting them back there. Please do send them on up, and when Deanna is done, we'll start going through them.

Deanna Newcomb: Everybody, I'm the last speaker before everybody leaves, so I'm going to make it real short and then we'll get a move on, so. I'm going to try to stand still. My disclaimer is I work for a law firm but I'm not a lawyer, okay. I'm a compliance officer. I've been in the energy industry for about 19 years, and I was recruited about six months ago to work for McDermott Will & Emery, and I personally want to thank Steve for inviting me to speak here. But I know the EIA because I used to be on trade floor and every Thursday when the numbers came out, there is mass screaming on the floor what the numbers were and everybody tries to get around it, so it's mass chaos, you know, and everybody wants to know what's going on. So, that's you know, EIA, when that first came out, that's what I recall; and literally I was in an energy briefing Thursday before Easter and all the information, all the charts, all the numbers, everything has a disclaimer of EIA at the bottom. So, we live it if you've been in this industry a long time. So, this is what we know. So, that was my disclaimer so that everybody will know that, so. I tell everybody that and they laugh.

Where do you begin? I'm going to talk about...everybody has talked about regulations. I'm a compliance officer. Where do you begin with all these stuff? How do you...where do you even start? There's a...you know, it's like, okay, here we go. How do you keep up with it at all? I mean, we've heard all day long that the policies we need—we have policies. We need more policies. Where are we going to go? We are going to need more policies. My statement is, "You have to eat the elephant one bite at a time." You have to take one step at a time. So, you have to go one step at a time. So, where are we going to start in all this? This is where we go, and compliance is the key. It's the key to success. If you're going to be successful in regulation, you're going to be successful in the environment, you're going to be successful in the economy, you're going to be successful in the supply and demand...for physical supply and demand, you're going to be successful in business. You've got to be in compliance. It has to be. And to do that, it all...I mean, I thought you're going to laugh, but my husband is, "I'm a compliance officer in the energy industry. I can be employed for as long as I want to be." I mean, seriously, anybody else, you want to tell your kids this is what you want to do because you can, I mean, talk to anybody, here we go. What are they going to do? They are going to put more policies, more regulations, more laws around compliance. In energy it does not matter; if it's solar, biofuel, crude, coal, guess what? Pick your choice, you'll be employed. Where do you want to live? It doesn't really matter. The good thing is if you're in compliance...the good thing about it, you're getting more and more support. For example, the FERC came out — I don't know if you know about this

— the FERC came out. It’s the statement of penalty guidelines. You’re getting benefits if you have an effective compliance program in your company. It’s actually a factor to the penalties — very similar to the federal sentencing guidelines now. Whatever your penalty is, it is a factor to reduce the cost of what is going to charge your company. I mean it is a number that you can go to your management and say, “Look, you have an effective compliance program. This is how much it is going to save us.” First, let’s not get in trouble in the first place, but if we do, this is what’s going to do. This is how it’s going to...when you have tangible, I mean, they’re actually putting it in legislation and in laws and regulations. If you have an effective compliance program, it’s never been that way before. I mean, this is like, it’s wonderful. It’s actually very successful. I mean, it makes sense. Okay, so what’s in a successful compliance program? I’m not going into this in great detail but mainly with support, you will not be successful if you don’t have management support. And I’m not talking about the highest and somebody is going to say, “Your chief officer — you know, the chief guy staying at very top — suggests you have to have it.” That’s important because they’re going to give you the money and the resources, but you got to have the second level because that’s where it’s actually is going not to become a policy or mission statement. It’s not going to be something sitting on the shelf. You got to have the next layer...next level as well. You got to have your written policies and procedures because that’s the proof. When the regulators walk into the office and say, “What’s going on?” You’ve got to actually be able to show them something, that’s the paper, that’s the proof. You’ve got to actually have that second place. You got to train your new people, and it doesn’t matter if it’s formal or informal. It doesn’t matter if it’s online, in person. It’s whatever. There’s not a...you know, it could be anything. But you got to train.

Another key thing is monitoring and surveillance. It’s kind of goes back to what they just talked about right now. You got to know. You got to look. Somebody’s standards are hard standards. I don’t know what’s in the biofuels earlier today; and they talked about some of these hard percentages that you've got to get to. What you got to know you have to look in, and you got to be able to try that kind of stuff—NERC…some of the FERC stuff. I mean, there's hardcore reliability standards to keep our electricity stuff going on. Those are some standards that you got to keep track of. There are some serious things; and then you have the other surveillance that we're keeping up with the trends. You know, talking about we're going to be required to do surveillance, you're actually managing what traders are doing. What are they monitoring, their transform and manipulation? That's surveillance. You got to know what your company is doing. You got to be able watch it.

And last but not the least, review and monitor, and review your program. You can't just do it and *[indiscernible]*. You got to keep up what's going on.

This overall theme, you're going to say, okay, this is a compliance culture and you're like, okay that's touchy feely, what's that? It's your environment. Its people doing the right thing, and if you're going to be asked, "How are you going to stop a road trader?" This is what everybody asks me, as a compliance officer, how are you going to stop a rogue trader, and I look anybody square in the eyes and say, "You're not going to." There's not...if you have a rogue trader, you're not going to stop him. A compliance program will not stop a rouge trader. A compliance program will have to say if he is in control and will minimize their activity and will stop them faster than you will be able to find it quickly; and it'll be able to...the monitoring will be able to tell them, the training will be able to let them know that what they're doing is wrong; and it'll be identified as minimizing the risk. But you'll not be able to stop a rogue trader if you have one on sight. Your hiring will be able to stop the rogue trader, not your compliance program.

Another key factor is knowledge. You got to know the business. You got to know what your business is. You got to know are you in physical or you're financial. What are you doing? You got to know if you're in OTC business, or you're in exchange. You got to know what products you're actually trading. A perfect example is somebody's reports of CFTC talking about transparency. I have talked to many of my clients. They're trying to say, "Okay, what are we? Are we a swap dealer?" You know, now that they're no longer...these are just two general categories, what are we actually doing? The FERC is EQR, which is electronic quarterly reporting, and it actually breaks out the way they do their power trades so they can have more transparency. You have a junior person that's filling out these forms. You have to educate. They have to know what goes into this information; and it's critical because this information is actually feeding what's going to make somebody's critical decisions. You have to know and you have to try to tell everybody what's going on. Read the headlines. Read what's going on in the newspapers. Read what's going on in the rags. Figure out what's going...understand. Who's getting in trouble for what? Is our company doing the same thing? Maybe that's a little bit higher risk than what we want to do. Is that some of the risks that you were talking about? Is that something I'm willing to understand? What are the regulators looking at? The last panel...the gentleman from the market oversight, he explained what everything that the FERC is looking at, the CFTC has the same, you know, division that they look at everything that they're looking at. What is the entire organization looking at? You got to make sure what the regulators are looking at. Keep up with what the regulators changes are. That is like drinking from a fire hydrant, man. Let me tell you, in exchanges, how do you do it? That's the next question, you're like looking at me. How in the world do you keep up with the proposed changes, the notice of changes, your comments of changes, you know, how does this impact me? Maybe it's a potential new business that's...you're coming into. How do you read and then there's, you know, comments of changes that you agree with, comments of changes you don't agree with. You know, you want to make...information overload, and then it's instantaneously; and you have 30 days to comment. Oh, it's crazy. And you're reading more than you want to read. I don't know what to tell you. We can help some...I mean, our firm actually has things that we offer out. We send emails or several other things that you can get on the internet and get briefed like our Cliff Notes versions, but I said that the other day to my son and he didn't know what I was talking about, so. There're ways to get snippets. There're ways to get on email distribution lists. The websites for the CFTC and the FERC are phenomenal in getting information links, to get email sent to you. The only way you can keep up today is to actually know what's going on. I mean that is the absolutely the only way to know what's going on is to read and to comment. If it impacts your business and it's important to you, comment. If it's through an association, support what they're commenting on. If it's important to you, if it's business independently, comment on your own. But comment. Do not wait till it's final, because when it's final, it's final and you have to live with it; and then we're going to be living with it for who knows how long, and that's going to impact our industry.

So, what's next? Then what? You got this wonderful program. We got these regulations that are just coming at us from who knows how long, and they're not final yet, by the way because we don't know what's going to be coming next; and they will change eventually along the way. You know, I'm trying to be successful and there's still more and more coming. It's not if, it's when. The audits, investigations, inquiries, and data requests will come. They'll come, and they'll be informal. They'll be formal. They'll be public and they'll be nonpublic; and they will come; and they want data; and they want lots of it; and they want emails; and they may not be the target. It's a cast; they want information. They're trying to make sure the markets are run well. That is truly what they're trying to do. They're trying to make sure...the bad guys are doing not any more bad. The good guys...unfortunately, you're in a business of some, potentially, people doing bad things and they need to understand what's going on; and you may have traded with the bad guy. So, they need your information, too. They get the data but it impacts your business. You will get data request. You will get an inquiry. You will get a routine audit. It will happen. It is when. It is very disruptive at times. But if you have a program in place, it actually makes a little bit easier.

The other thing is, you may not be a target, but they are watching you on how you respond. They are watching you to see how cooperative you are. All regulators are. And the regulators are talking. The CFTC talks to the FERC. I think there's a formal arrangement, correct me if I'm wrong. It's their formal arrangement to communicate. They talk, and that's a good thing; then not if you share information to one, they share it together, so it's a good thing. And don't think it's just in the United States. They talk to the FSA. I call it intergalactic, man. You think it's not…it is…it's not a bad thing. If you're doing everything right, it's not a bad thing. We're trying to make this. We want people...we want the success in this industry. We want the confidence of the industry back because, what happens, it goes back to what the Secretary said this morning, "We want people to believe in the industry, so they'll invest in it"...in this industry; and then we'll have the money back into it which will only...you know, it's only a snow ball effect. It's only positive, and the way you do that you should get the confidence back in the industry, so. But, they won't give you the benefit of the doubt and you got to prove it; and the only way you have your evidence is you prove it — you have your policies and procedures. You have your training. You have your senior management support. So, when they do walk in the door, you show that all stuff to them. You're cooperative. You hand them your information. You provide them what they need. It's normal course of business. It's kind of like paying taxes, man. It's just part of it. Welcome to the energy industry. You're going to be regulated. If you're shocked, I don't where you've been living because, welcome, you know, it is what we do. Okay. Here we go. So, take the step, man. Here is the road we're walking. It is where we are at, so take the next step, maybe a couple of bumps along the way, but here we go. So my conclusion is, think about what you need. Think about where you're at. Think about...if you need updated policies. You need to update your procedures, train employees, maybe you already did but you have no employees coming in, just try the new ones, existing employees. Where are your monitoring systems? This is a big one. You don't know what you got unless you look and a lot of people are scared to see. There's a lot of stuff off the shelf, lot of people are building...this is a new area which a lot of people are concerned about. This can be expensive but it can also be done. I've done a couple of them myself. There's not a one size fits all. This is a big question I get asked all the time. Some people do...one compliance officer and outsource a lot of stuff. Other people do everything in house. Some people do, you know, in-person training; other people do all training on-line. There's not one size fits all. But the program pretty much fits the same thing. You got to keep up with what's going on. In the regular, you got to know what your business is. You got to keep up with what's, you know, you have to...all those elements are all the same. You got to comment on things if you don't agree. You know, you just keep up for all that.

Always review your program. Never let it get stagnant. Once a year, regulators are going to ask what are you doing. When they come in, let them know. You're not doing anything; you're not afraid of them. Let them know. Tell them. I call them all the time. I mean, some of the stuff, folks, I've been...I've actually...this is kind of crazy, but I've been...I was at the company that had a settlement with regulatory agency and then we got audited on the settlement; and since I've moved on, the same auditor I've been in touch with two or three other times. You just know. They're people doing their job, and we're just trying to...once again, we're all trying to succeed and we're all trying to succeed for, I think, for the right reasons. You're just looking at something in just different angles.

Steve Harvey: Thank you, Deanna. While she's sitting down, I really think...I shouldn't let a comment Dan made earlier go unthanked. But yes, thank you very much for access to data and in your transparency efforts, and we are, in fact, trying to make use of that. Now, with everybody seated, any responses? Anybody want to react to anything anyone else has said to get us kicked off.

Skip Horvath: Just one of the things I always forget to do is put things in their perspective. You know, why are these numbers important? Why do we need regulations? And my Chemistry high school professor was the former Nepalese explosives professor — always making a great interesting class — in Chemistry said, “Remember your levels of significance.” So, when you’re talking about what level of these unregulated markets are, which energy is being whipped sawed around? The unregulated market is approximately $600 trillion right now, unregulated dark markets. Of that, probably, 300 trillion is US. Then to put other things into perspective; well, how big is the other large investment markets? So, the bond market used to be the big gorilla -bond market, I believe is somewhere around a 175 trillion, I think, somewhere, maybe at 75, I forgot to look it up the other day. US GDP is 14 trillion, world GDP is 55 trillion, right now it’s 75 trillion; and these are average leverages of 35 times. Some leverages, you know, the Goldman Sachs one’s off the chart, but it’s not uncommon for currency derivatives to be at 400 times leverage, and as I go on to my bank, and my bank said, “Well, why are you going to DC all time to say to re-regulate the stuff.” So, well I’m pretty lucky; I’m going to Vegas. These derivatives are like going to Vegas. So I got a thousand bucks in my pocket, you want to upfront me 400 thousand. She said, “What?” Well, so that’s what we’re talking about. Leverage skills. So, leverage and volume skill and although we had the collapse. The collapse was one quadrillion dollars when we’ve done some cancelling of these nominal values of contracts. The amounts of money are staggering, and it really is a house of cards; and that is where you get into the systemic risk issue, that you don’t know if the other side is bad until they go bad and everything is interconnected. That’s why when you had the rogue trader in London that did — I think it’s 23 — it goes like $10 million worth of lending crude immediately worldwide because of the linkage and the swaps and the leverage involved, crude oil went up over the weekend $5 a barrel because of the way that everything’s going. So, that’s the point that I think everyone needs to remember. Thanks.

Deanna Newcomb: Can I add on that point? The comment was made about the physical, financial...there's not a lot of, you know, studies and research about the physical and financial, but the people trade physical and financial and some people trade that way, together they are linked to some capacity that way; and there's some interconnections when they trade a little bit more, I think, not more on the trading aspect than on the research side. I think the research is falling behind a little bit, but it will be very interesting to see what the outcome, but I think more research is needed, but there is some studies and some manipulation around that activity that is coming out from FERC and some CFTC has done…some manipulation around both physical, financial, and people are trying to use physical, financial, and the different markets against each other. I don't know if anybody who want to comment on that, but I've actually looked into that and to some manipulation around that. You've got to be just really careful.

Dan Berkovitz: I'd just like to comment further on the clearing question. Clearing...the products have been cleared in the futures exchanges through all the financial crises, through the ups and downs that we've had, the 2008, you go to long-term capital management; you go to 1987, market crash. You name any market crash, the futures markets and the cleared contracts have been absolutely sound...and those contracts have...the traders and the participants and the end user have been absolutely guaranteed of their trades throughout. So, clearing is a very, very...it's a well-proven way to guarantee the sounds of the trades, and that's still why we have futures markets online. Many traders prefer them, so the clearing model works very well. So, in order to reduce systemic risk, we're trying to get as many of these trades into the clearinghouse as possible. Now, for any particular end user, for any particular company, I say, look, there's a high cost for me to clear. Certainly whether I clear or not is not going to break the system. You got to have some manufacturing companies, if I clear or not. How am I creating systemic risk, but it's the entity on the other side of that...it'll be the large financial institution that essentially is aggregating these risks in itself. It is making many unclear trades, individual participants, so what might not be a killer market move to the counterparty, for example, the end user, if all that risk is aggregated in a large financial institution, it could trigger a collapse of financial institution, or not necessarily a collapse, but if it has to sell a bunch of its assets to meet, perhaps, some threshold trigger to actually post collateral to the counterparties, and it starts selling its assets, and there's a loss of confidence in that institution, and credit starts to become scarce. Basically, what happened in 2008 to some of the financial institutions. So, clearing by both sides, it's not only beneficial to the end user, but it helps reduce the risk in the swap dealers. The energy and commodity end user class is really...is not a large percentage of the over the counter swap market. I think, commodities, all the physical commodities is less than 10%. It's in the single digits and percentages of the over-the-counter swap market. So, far more to exclude the entire commodity swaps from the class of clearing, it wouldn't necessarily...you'd still get the large majority of swaps cleared. But here's the concern that, for example, my Chairman has articulated with that approach is it becomes very hard to draw the line as to what is, for example, you say, "We're an end user, we actually have a business. We produce machines. We use oil. We buy raw materials and we want to hedge our production cost. We want to hedge our output. Oh, and by the way, we sell overseas so we have currencies swaps, too." So, actually our use of currency swaps, we want hedge trimmer for those, too; and we have these long-term contracts where we supposed to have interest rates. So, it's not just actual physical commodities that we're using to hedge, it's the financial commodity. So, we want hedge exclusion for our financial commodities; and then, the pension funds will come along and say, "We're not really speculating; we're just hedging the cause for all the pensioners. We're just to trying to keep up for inflation, for all our pensioners, and we're buying an index fund, for example, and commodities just to try to keep with inflation." If you actually look at those people who are beyond a lot of you- the index investments, it's not individuals…necessarily wealthy individuals who consider themselves speculators, it's pension funds.

Steve Harvey: We'd be better off going to Vegas.

Dan Berkovitz: It's pension funds. It's the large institutional investors and these things. And if you ask them what they're doing, they're not saying we're speculating. They say, "We're really trying to keep up with inflation. We want to ensure that the people don't lose purchasing power, the price of oil goes up, etc. So, we're really hedging, too. We're not speculating, and we should get the same treatment for our interest rate swaps or our currency because we're really trying to just protect the investment." It becomes very hard to draw the line, let's just see who's really hedging and who's really speculating and what's a legitimate hedge for a commercial purpose or what's a speculative hedge for some speculative purpose; and we're really, really working hard with the Congress and with the end user communities *[indiscernible]*. If this is going to be an exclusion for the commodity end users where people actually are taking things out of the ground, that the hedge funds, that the languages tighten off, so the hedge funds and financial players who do have a capital, who do have cash around, who can't put up collateral and don't, you know, aren't taking the molecules of gas out of the ground. That they don't come in and essentially eviscerate the requirement through the exceptions, so we're trying to get if there's going to be an exception, we're working hard to try to keep it tight because clearing really is the safest way to make a trade for the institutions.

Sean Cota: Yeah, I think I'm right. Okay, in response and, Dan, we agree. I mean, we're not trying to protect those who have caused low systemic risk, and what we want to do is look at you and try to find...it's hard to work. It's easier to say, "Let's cast a net wide and catch everybody," but that's going to hurt the economy, so we'd rather look at you and try to make that as narrow exemption as possible as to help those guys. I'm going to suggest an idea, rather than have it on...and I know the clearing mechanism works very well, and you guys can see a lot and it's fairly transparent, but another word of caution is, let's say...one of my guys...let's say a gas producer...hedges with a large financial institution, and that financial institution is forced to register that trade somewhere on a daily or weekly basis; and then we have to go in and verify. Yes, that's true. We have that deal and you can see it. Say, on the DTCC up in New York, or something like that. Those are the ideas that need to be explored a bit because they're not sensationalized in the clearing. It doesn't cost us anything. We're willing to work and do that and verify a trade that you can and see and you can collect it all because you recognize what the safety seal lacks is the ability to see all these trades and pull together and say, here's what's going on in the bigger picture, and we need to do that and we support that. So, I'm convinced as to the way of dealing without simply pulling everybody into sensationalized clearing and we will give you on that; and we recognize, too. You know, the problem of say, a large financial institution buying a small producer somewhere and say, "I'm a producer, too. I get the exemption." And we want to prevent that as much as you do, that's...you know, gaining the system is not the way out of this. We have to prevent systemic risk and I am convinced there are ways to do it.

Man 4: You know, I actually hedge with the options of futures contracts in 2008 when we had that collapse, both the run up and the collapse. The volatility of my market was moving faster in two days than what my margin was, so we bought a futures contracts and put options; and when the market collapsed and Bear's turns went bad, I had this cold feeling over me, did I...was the counterparty...NYMEX cleared like I thought it was or was it *[indiscernible]* turns and therefore worthless; and within a few a minutes I figured out it was a NYMEX exchange clear product so I was guaranteed, but it would made the difference between my best year ever and being out of business. So, even for a small guy, systemic risk was critical for me.

Steve Harvey: We're starting to run out of time. We have four...we have actually six excellent questions that really fall into four questions, and so what I'd like to do is kind of quick lightning round go through a few of these questions that I are think are of interest. First one is clarifying. It doesn't specify whether it's related to legislation or to the proposed rule. It could relate to either one of them, but what is Howard Trades treated between the end users to use swaps for hedging and major swap participants and swap dealers. Would they be exempted?

Man 3: The way the House Bill for example in the Administration Bill, if one of the parties is an end user then the trade would not have to be cleared...submitted for clearing. It's one party as an end user would qualify for the end user exception under the House Bill for example.

Steve Harvey: The next question, this is initiated and it has come up a lot and so everybody may want to jump in and *[indiscernible]* level on this and there are two questions but I'll read, I'll read one of the two, it gets to the same issue. In a global market, how does the U.S. regulate commodity markets effectively without simply pushing the risk taking outside the U.S.? Given the global nature of energy prices, can meaningful regulation be achieved?

Man 3: I've got a few comments on that. That's one of the arguments you will always have. There's nothing that ever kept you from doing trades in Moscow or any other place that you want to do. So, those markets exist, you can move to them now. There's the issue of kind of prudential money...a lot of the investments that occur in the United States are investments that are based on pension funds, retirement funds, long term investments, and *[indiscernible]* funds; and that, kind of prudential money is going to stay here; and at the same time, the Europeans are developing similar regulations that will probably, because they talk longer than we do. It'll probably take a little bit longer but they'll probably in many ways be more restrictive. I think the wild card is going to be the FSA in London, but if you capture just those markets, you're going to capture probably 80% of the total market; and right now just in crude oil...crude oil, the only visible portion of the market is the CME portion, and this is the best gas because we really don't know because these are dark markets, but only 15% of that market is visible and that's the biggest most liquid one that there is seen in oil.

Man 3: One remarkable thing I was privileged to attend a meeting in an international conference here in the U.S. on this and listened to a number of presentations from European regulators and it's absolutely astonishing that the issues virtually down to every single issues just about the same...just who's subject are clearing, should we encourage exchange trading. They're struggling with the exact same issues as we're struggling with and the opposite argument is being made on the other side of the Atlantic. But if we do this and the Americans don't, the tradings are all going to come to New York, so both sides are worried about it but a concrete example of this is, within the last month on the CDS Greece issue, there was a movement in Europe after this...I think Sean referred to the great situation that perhaps CDS short selling of credit *[indiscernible]* swaps in the debt of a Greek government was contributing to a loss of confidence in the Greek government and raising the cost of debt of Greece. And maybe the Europeans are considering prohibiting short sales of credit before swaps on sovereign debt, Greek debt for example; and the United States said, "No we wouldn't support that here" and the response there for Europe was, "Well if we ban it here in Europe, all the businesses are going to America", so the ban in Europe really didn't go anywhere because we had indicated we will not implement it. It works both ways, the issue of both sides of the Atlantic right now are virtually identical. I don't know if they're going to come out identically, but it's really remarkable it's a great issue.

Man 3: But isn't it the concern that, you know…I think you guys are working well with your counterparts over there, alright, so I'm convinced that whatever you come up with together, you'll prevent that from happening too much. My concern is what does it mean when markets go to a dark country, and I'm making that term up. What I mean by that is, that's not part of this deal...whether the regulation isn't strong...what it means to those who have to participate is you don't know what you're getting yourself into, so your risks are up, our cost is going to go up and so all of our costs are going to go up. So, it...you know, I don't have an answer for that but I worry that a country that you may not really trust very much for other reasons will suddenly become a center of...and can gravitate and pull toward it these trades that are being chased on both Europe and the U.S. and I think that's the concern people have.

Deanna Newcomb: You have to be careful because doing business in any of those countries...establishing business, there's other in just commerce laws to get the advantage trust and all the other basic laws that you have initial establishing business there in the first place, and you have to be overcome before you actually have to deal with some of these things that they're dealing with.

Man 4: Two final quick questions. We're about out of time. This next one we can probably answer with yeses...yes or a no; and then whoever asked it if they want to followup can follow-up unless there's something behind this, I don't know exactly. Is there a structural bias on the NYMEX that it *[indiscernible]* buyers and *[indiscernible]* sellers?

Man 3: I guess yes or no. It depends. How's that?

Deanna Newcomb: That's a lawyer answer.

Man 4: You can do more that if you want.

Man 3: I think it depends on what the contract is, what the delivery points are. I think a lot of people don't utilize the NYMEX, ClearPort functions. ClearPort gave you the ability to do hedging really out of whatever the differential markets are. I think that's something that enables both buyers and sellers to make better connections than some of the other torts or trades; and again it's exchanged clear so, it's guaranteed...you know, bilaterals are bilaterals. You can make any kind of bet you want with whatever you want, and now you can make a bet with a guy in Angola if you want to get crude oil delivered by, you know, who knows. I don't know much about Angola but the Chinese like their oil but those sorts of bilaterals. You can always do, but you have...you don't they exist, you don't know what the risks are. There's no guarantor. So, that's my side. Okay?

Man 4: And then, our final question which I know ahead of time that Dan will not answer, but maybe he can give us a little bit of contacts because it's an interesting question. There are very few dollars involved in standardized swaps in the electricity industry. The trades outside of organized markets regulated by FERC. Will CFTC attempt to clear nonstandard swaps such as tolling arrangements?

Dan: I'm unfamiliar with the tolling arrangements, so I can't answer that.

Steve Harvey: Very good. Well, thank you very much. Thank our panel and enjoy the reception immediately following.

END OF RECORDING