Resolution Addressing Excessive Speculation in Natural Gas Markets

WHEREAS, Efficient natural gas markets based upon market fundamentals such as supply and demand, price transparency, and liquidity are necessary to ensure that the price consumers pay for gas accurately reflects the underlying value of the natural gas commodity; and

WHEREAS, The price of natural gas in U.S. commodity futures and physical markets rose to unprecedented levels in the summer of 2008 and the price increase occurred without a significant disruption in supply and in the midst of the greatest economic slowdown since World War II; and

WHEREAS, Even though natural gas prices are relatively low at the present time, the price currently being paid by consumers for natural gas is elevated due to local gas utilities having to purchase gas at the sharply elevated prices of the summer of 2008 for storage for current winter use; and

WHEREAS, Recent studies by the International Monetary Fund and the Massachusetts Institute of Technology Center for Energy and Environmental Policy Research argue that excessive speculation in the commodity futures markets has lead to an increase in energy prices; and

WHEREAS, Natural gas is a major fuel for electricity generation and serves as an energy bridge to America’s energy future. As such, high natural gas prices have a detrimental effect on the cost of electricity and all sectors of the American economy; and

WHEREAS, Regulated utilities that provide natural gas to 70 million U.S. homes and businesses for the basic human needs of space and water heating, cooking, and clothes drying utilize commodity futures markets to hedge their natural gas procurement costs in order to reduce the impact of natural gas price volatility on consumers; and

WHEREAS, Unlike natural gas utilities who access commodity futures markets for the purpose of mitigating price volatility through hedging, during the past five years other market participants have significantly increased their speculation in natural gas markets, with more than 90 percent of trades coming from market participants who do not intend to take delivery of the commodity; and

WHEREAS, Large amounts of money from speculators have entered natural gas futures markets such that the dollar value of open interest in natural gas futures has almost doubled, from a level of $45 billion in 2006 to $87 billion in 2008; and

WHEREAS, The Permanent Subcommittee on Investigations of the United States Senate held hearings in June and July 2007 examining the relationship between excessive speculation and high natural gas prices resulting in a staff report on how excessive speculation can and has distorted natural gas pricing and caused consumers to pay more for the commodity than is justified by market fundamentals; and

WHEREAS, At the 2008 Summer Committee Meetings, NARUC adopted a resolution sponsored by the Gas and Consumer Affairs Committees that called for the formation of a Working Group of NARUC Commissioners for the purpose of studying how excessive
speculation affects the price consumers pay for natural gas and making recommendations on whether NARUC should endorse the recommendations issued in the Staff Report of The Permanent Subcommittee on Investigations of the United States Senate issued in June 2007; and

WHEREAS, The Commodities Futures Trading Commission (CFTC) has the jurisdiction to protect market users and the public from fraud, manipulation and abusive practices related to the sale of commodity and financial futures and options and to foster open, competitive and financially sound futures and option markets; and

WHEREAS, The Permanent Subcommittee on Investigations of the United States Senate found that the CFTC did not have sufficient authority to regulate U.S. energy commodity markets, because it could not regulate the Intercontinental Exchange (ICE) to the same extent that it oversees the New York Mercantile Exchange (NYMEX); and

WHEREAS, The Permanent Subcommittee on Investigations of the United States Senate found that a single large hedge fund, Amaranth Advisors, LLC, was able to distort prices, increase volatility and increase costs to natural gas consumers in 2006, in large part by avoiding regulation and public scrutiny by conducting clandestine trading operations on the ICE; and

WHEREAS, The “Enron Loophole” exempts energy commodities traded on electronic energy exchanges such as ICE from regulatory oversight and severely limits both the Federal Energy Regulatory Commission’s (FERC) and CFTC’s ability to identify and prevent excessive speculation in natural gas markets; and

WHEREAS, The Permanent Subcommittee on Investigations of the United States Senate recommended eliminating the Enron Loophole, CFTC monitoring of positions held by traders on both the NYMEX and ICE, expanding the scope of efforts to detect excessive speculation, and increasing funding for the CFTC; and

WHEREAS, Research presented at congressional hearings by Michael Masters and Adam White contends that excessive speculation by commodity index traders may inflate the price of natural gas to the detriment of consumers; and

WHEREAS, The staff of the CFTC issued a report on Commodity Swap Dealers and Index Traders in September 2008 that found that determining the impact of commodity index traders is difficult due to existing reporting requirements for large traders; and

WHEREAS, Congress increased CFTC funding and granted it rulemaking authority to address the Enron Loophole through passage of the Food, Conservation, and Energy Act of 2008; and

WHEREAS, Recent problems in financial markets and comments from the Obama Administration will likely lead to comprehensive reform that may improve the ability of regulatory agencies to protect the public in addressing excessive speculation, fraud, manipulation, and abusive practices; and

Regulatory System, that recommends changes in the way commodity futures and other financial derivative contracts often used in natural gas markets are regulated; and

WHEREAS, General reform of the financial regulatory system by Congress should include specific authority to address excessive speculation in natural gas markets; now, therefore be it

RESOLVED, That the Board of Directors of the National Association of Regulatory Utility Commissioners (NARUC), convened at its 2009 Winter Committee Meetings in Washington, D.C., encourages federal legislation adopting all of the recommendations presented in the June 2007 Staff Report of The Permanent Subcommittee on Investigations of the United States Senate; and be it further

RESOLVED, That NARUC supports the CFTC’s efforts through rulemaking to completely eliminate the Enron Loophole, in order to provide more transparency in futures trading, as described in the June 2007 Staff Report of The Permanent Subcommittee on Investigations of the United States Senate; and be it further

RESOLVED, That NARUC supports new federal legislation to address the flow of investment capital into financial markets in ways that produce commodity price movements that are harmful to consumers, businesses, and financial markets; and be it further

RESOLVED, That NARUC supports proposals such as increasing margin requirements for futures contracts on speculators who do not intend to take delivery on essential commodities like natural gas and requiring over the counter natural gas derivative contracts to be cleared by exchanges as simple steps to combat excessive speculation; and be it further

RESOLVED, That any federal legislation and regulatory action addressing futures markets should fully accommodate legitimate hedging activities by electric and natural gas utilities as a strategy to manage the risk of price volatility and mitigate the price impacts of such volatility on consumers; and be it further

RESOLVED, That the Working Group should develop recommendations to address natural gas index speculation and report back to the Gas and Consumer Affairs Committees; and be it further

RESOLVED, That NARUC supports actions of the FERC and CFTC to increase supply and availability of natural gas and vigorous enforcement action against fraud, manipulation, and abusive practices, which could help reduce the commodity price of natural gas.

Sponsored by the Committees on Consumer Affairs and Gas
Adopted by the NARUC Board of Directors February 18, 2009