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The Honorable Mickey Edwards
U.S. House of Representatives
2434 Rayburn HOB
Washington, DC 20515

Dear Senator Edwards:

H.R. 2869 and S. 1729, reauthorizing the Commodity Futures Trading Commission, will soon be considered by a Conference Committee of the House and Senate. These two bills are intended to strengthen the regulatory structure for futures markets, to prevent potential abuses and to lead to greater public confidence that markets are operating fairly. In large measure, we believe these bills will accomplish these goals and the leadership on the House and Senate Agriculture Committees should be commended.

However, in haste to address need for stronger regulations, we believe these bills could unintentionally inflict real economic damage to an efficient futures marketplace, resulting in costs ultimately paid by producers in the form of lower prices. While the hearing and mark-up process in both houses provided no evidence that "insider trading" was an area of trading abuse, both bills contain provisions prohibiting such activity. In addition, H.R. 2869 would prohibit the disclosure of so-called "insider information".

To understand the potentially disastrous adverse consequences this legislation could have on commodity markets, the basic differences between commodity markets and stocks/securities markets need to be clarified. In stock markets, a pending takeover attempt, development of a new product or other potential "windfall" that is known only to a few "insiders" can translate into virtually assured profits for those in a position to abuse such information. Commodity markets, on the other hand, are more broadly traded by all participants and are affected by a much wider variety of factors -- crop reports, government programs, weather and transportation capacity, to name a few. In trying to anticipate movements in price, participants have to digest and analyze literally hundreds of factors. The result is that the singular impact on price of any anticipated, pending or completed trade in the marketplace is very uncertain. Thus, potential for abuse of any such "insider information" in commodities, unlike stocks, is muted by the very nature of the market.

In seeking the best available knowledge about the market and its direction, market information is traded and bartered like a commodity -- through millions

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of informal telephone calls, fax messages and other timely means. Country elevators, with their hand on the pulse of producers, are in the best position to assess and provide information on farmers' willingness to market grain and local crop prospects. Exporters and terminal operators are in the best position to determine how friendly large processors and importing nations are toward acquiring more grain. Such information is "traded" and exchanged freely in today's marketplace between large and small companies, and is a primary reason the markets react so instantaneously to changing conditions. It is also the reason that the markets are so efficient, allowing the grain handling and marketing industry to provide their services at the lowest possible cost. The ultimate beneficiary of this efficiency is clearly the U.S. farmer. If this efficiency is impeded, costs of marketing and handling will undoubtedly escalate and the average market price to farmers will decline.

H.R. 2869 would make it a felony, punishable by a monetary fine up to \$500,000 and a 5-year prison term, for any employee of a commercial grain company to disclose information related to a cash commodity trade of more than 500,000 bushels, if such disclosure is with the intent that the recipient of the information would trade on the basis of such information in a way that is not part of his legitimate business activity. On the surface, this provision appears sound. But considering the nature of information exchange in commodity markets, the impacts on efficient information flow in commodity markets could be highly adverse.

First, the level of reportable positions that would be subject to this provision are very low. A quantity of 500,000 bushels is the equivalent of 1 1/2 unit trains of grain, a position that is common for country elevators in the heart of the grain belt. There are probably more than a thousand country elevator unit train shippers nationwide. "Incidentally, this is hardly a trade of the level that would be expected to be "market moving" in a cash market where annual volume is 7.5 billion bushels for corn and 2.5 billion bushels for wheat and a futures market where there is a total trading volume of over 48 billion bushels for corn and over 25 billion bushels for wheat.)

But more important than the fact that virtually any cash trade would be subject to this highly threatening provision is the absolutely chilling effect this law would have on the information exchange in the market. Commodity traders in large firms would, in all likelihood, be prohibited by their employers from talking in any way about trade prospects for fear of such discussions being labeled as referring to "anticipated sales" which constitutes a felony penalty subject to a fine of \$500,000 and 5-years imprisonment. After all, how can the purveyor of such information be absolutely sure that it will be used only in legitimate hedging activity for another firm? In all likelihood, the large firms, with multi-national connections, would refuse to discuss their view of anticipated market demand at all. (We have been told by several companies that this in fact will become explicit company policy if this provision is passed.) In turn, the firms closest to producers would withhold information on crop prospects and farmers' willingness to sell grain that they typically trade to larger firms for their candid perspective on market demand information. Country

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elevator operators desiring to place "anticipatory hedges" to cover grain purchases from farmers after futures markets close on any given day, may also feel threatened if they are forced to justify such hedges as "legitimate business activity." Some big losers in this dramatically altered market environment will be country elevators and smaller companies that can no longer anticipate significant surges or weakening in demand, because of their lost information contacts. The ultimate losers will be farmers as the cost of hedging purchases and sales will escalate.

We urge your opposition to this provision in H.R. 2869. While it is intended to protect the market from intentional abuse of information, the vagueness in its wording and application will create a dark threatening cloud around the market that will virtually halt information flow on cash sales.

The drafters of this legislation have said that this was not their intent that the flow of information dry up. The colloquy on the floor of the House was intended to make this clear and to establish that the amendment was aimed at people who would usurp material non-public information from the privileged vantage of their employment and convert or disclose it for their own personal gain unrelated to the legitimate commodity business of their employer.

While the colloquy is an important reassurance of intent, it does not, by itself, do the job. Courts are not obliged to, and often do not, look to legislative history when they consider the language of the statute to be plain enough on its face. Therefore, there is still nothing to prevent a U.S. attorney from destroying the reputation of and impoverishing a person by the allegation that he or she gave out information of his or her employer's present or anticipated business to someone to whom disclosure is unrelated to the legitimate business of the employer, with the intent that the recipient trade futures on the basis of that information. Again, the vague language "material non-public information" and "present or anticipated...transactions" combined with the criminal nature of any violation and the levels of punishment cannot help, notwithstanding any amount of colloquy, to make almost every employee extremely intimidated by the prospect of facing an aggressive, malevolent or politically motivated U.S. attorney. Information flow, if this language found its way into law, would indeed dry up substantially.

The other provision in H.R. 2869 would prohibit inside trading by private traders on the basis of private business of their employer. While not as troubling as the provision prohibiting the exchange of information, this provision, too, is cause for concern.

Many commercials, prohibit their employees from trading for their own account. For employees of such commercials this provision is no problem. For other kinds of firms, whose present and anticipated transactions commonly exceed the reporting level and whose employees commonly trade for their own account, this provision could be a problem because those employees would be under constant threat of felony indictments. The vagueness of the phrases "material, non-public information" and "present or anticipated transactions" would increase the concern

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of those traders to the point that many would probably consider leaving, depriving their employers of competent and essential people.

Finally, both bills S. 1729 and H.R. 2869 would make it a serious felony for any person on a functioning committee to disclose or use in trading any of the information obtained through participation on the committee. It is reasonable to make such actions illegal (as they already are), but the amount of penalties involved are so severe, we question whether companies in our industry will allow participation by their employees on self-regulatory committees at all, for fear of having to defend individuals from overly aggressive prosecutors. The self-regulatory process is dependent on the willingness of volunteer participation from qualified people. This provision could discourage such participation in a substantial way.

We urge you as a conferee to take a reasonable approach in this issue of "insider trading and insider information". While the Senate version would create some problems, it is much less onerous and threatening than the House language. We urge you to reject those provisions in H.R. 2869 that threaten information flow and the free enterprise system in our industry. While surely well-intended, the efforts are misguided and will likely result only in a drying up of legitimate market information. The loss in efficiency of our markets, which we believe will be significant, will be a terrible price to pay in the name of preventing potential market abuse.

Sincerely,


John C. Pearson
President