



Government may clamp down on banks, funds and others that don't actually use crude. But will new rules bring down prices?

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NEW YORK (CNNMoney.com) -- Last year Andrew Hall, the head of Citigroup's energy trading unit, made over \$100 million, making him one of the highest paid people on Wall Street.

Meanwhile, Corey Carter, resident of an Alabama county where consumers' gas price burden is greatest, spent more than 25% of his \$240 weekly pay on gas.

Some experts argue that the experiences of people like Hall and Carter are linked by the economics of oil trading. They say it's not a coincidence that Americans are paying more at the pump in an era when Wall Street has taken a greater interest in energy trading.

Even the government is reassessing its opinion of speculation's impact on oil prices. In what could be a significant reversal, the United States may tighten the rules on energy trading.

"Using an essential commodity as [an investment tool] is crazy," said Judy Dugan, research director at Consumer Watchdog. "If you want a double dip recession, let's just get \$100 oil again."

Dugan is part of a growing chorus of people calling for greater government oversight of the commodities markets, where oil contracts

are traded. The government agency that regulates those markets, the Commodity Futures Trading Commission, is starting to listen.

Last month, the agency held hearings about what it could do to restrict speculator activity. Possible measures include setting stricter limits on the amount of contracts people are allowed to trade, increasing the amount of money investors have to put up to buy contracts, or simply better reporting on who is buying what. More hearings on market regulation are set for Wednesday and Thursday.

The fact that the CFTC is even considering changing the rules is a big departure from its stance under the Bush administration. Last year the CFTC was adamant that speculators were not driving up the price of oil, with its then-director testifying as much before Congress several times. Now, under President Obama, the agency has a new head and that position may change.

It was reported last month that CFTC would soon reverse itself and say speculators were at least partially to blame for the \$147-a-barrel prices seen last summer. Then the agency said those reports were not true. Now they will only say they will be "putting out additional elements of information." A spokesman for CFTC did not say when.

Most analysts think additional restrictions will be placed on speculators, probably sometime this fall.

"Oil prices can't triple and then fall by 85% within two years without a political response," Kevin Book, managing director at the research firm ClearView Energy Partners, wrote in a recent research note.

Big users of oil -- as opposed to non-users like banks, hedge funds and others who are generally lumped into the "speculator" category -- welcome any moves that might limit speculator interest.

"One day [last year] oil prices went up by \$11 a barrel," said David Castelveter, a spokesman for Stop Oil Speculation Now, a lobby group

made up mostly of airlines and trucking companies. "That's not supply and demand."

Castelveter isn't sure if tightening rules on oil trading will result in lower prices and less volatility, but he thinks it's at least worth a shot.

The effect on prices

But what types of restrictions the government might enact and what that might do to prices is an open question.

Ken Medlock, an energy economist at the James A. Baker III Institute for Public Policy, thinks restrictions will bring down prices.

Medlock authored a recent paper looking at investment money influence on the oil market, and said it's hard to see how it's not pushing prices higher.

There's just too much of a correlation between stock prices, the dollar and oil prices to think big investment money - as opposed to supply and demand - is not driving the price.

Specifically, he notes how "non-commercial" players -- i.e., banks, pension funds and the like -- now hold 50% of the contracts on the U.S. oil futures market. That's up from 20% in 2002.

He blames a large part of investor interest in oil futures on a 2000 law now known as the "Enron loophole." That rule exempted banks, funds and other non-users of oil from reporting their positions on electronic markets. At the same time, proliferation of electronic exchanges took off, and is now where most oil trading takes place.

"That's when there appears to be a fundamental shift in the market," said Medlock. "The technology has moved faster than the policy."

The lack of information brought about by the reporting exemption is what makes it so hard to figure out if speculators are unduly

influencing oil prices.

Others have made projections.

Last week it was reported that Germany's Commerzbank thinks oil prices will fall 30% if regulations that rein in speculators are passed.

But there are plenty of people who feel speculators are not behind the runup in oil prices, starting with the Bush-era CFTC and their counterparts in London.

Plenty of people point to the razor-thin margins between what the world was using and what it could produce last year when prices hit \$147, and note that as soon as the economy collapsed, oil prices did too. They also say that OPEC and other big oil producers have a role in influencing prices.

The Citigroup energy trading unit did not return calls seeking comment. But others have said increasing market regulation in an attempt to lower prices may be futile.

Deutsche Bank, which engages in energy trading, noted in a recent report that during the recent commodity boom, items that increased most in price were mostly rare metals not traded on an exchange, and thus not subject to speculator influence. And even items like rice and steel, also not traded on an exchange, saw a big runup in prices.

The report noted how the U.S. government has been attempting to regulate speculators for that last 100 years in other commodities markets in an effort to bring down prices, often with little success.

"Alongside speculators we believe fundamental factors should not be forgotten in terms of the rapid rise in commodity prices," the report said, highlighting strong demand and OPEC influence. "Perversely focusing on regulation to curb speculative activity may possibly increase the pricing power of OPEC over time at a time when the U.S.

government is attempting to do the exact opposite." ■