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Book Review

The History of Commodity Futures Trading and Its Regulation

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Book Review

THE HISTORY OF COMMODITY FUTURES TRADING AND ITS REGULATION. By Jerry W. Markham.* New York: Praeger Publishers, 1987, pp. xv, 306.

Commodity futures trading in the United States has enjoyed a long and colorful regulatory history. Yet, the legal profession did not notice this small industry until recent years. The securities markets got all the attention. By 1974, however, commodity futures trading had grown to the extent that Congress concluded that the importance of futures trading to the general public and to the nation equaled the importance of the securities markets. In that year, Congress also created a new federal agency, the Commodity Futures Trading Commission, and gave it exclusive jurisdiction over futures trading. Since that time, futures trading has continued to grow. Indeed, the industry has virtually exploded into new areas, such as stock indexes and T-bonds; today, most financial institutions are directly or indirectly involved in the futures markets. Nevertheless, available literature has given little coverage to the history and background of the federal government's efforts to regulate these markets. Jerry W. Markham has now published a book that sheds some light on that past.

Mr. Markham's book, *The History of Commodity Futures Trading and Its Regulation*, is divided into three parts, each of which would stand on its own. The first part traces the history of commodity futures trading, the problems that have plagued the industry over the past hundred years, and the regulatory responses to those problems. The second part discusses the historical development of the Commodity Futures Trading Commission ("Commission" or "CFTC") as an organization and also discusses the roles individual Commissioners and staff members have played in that development. The third part reviews the instruments regulated by the CFTC: futures contracts, leverage

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contracts, and commodity options. It also discusses instruments which resemble futures, leverage contracts or commodity options and how the Commission and the courts have dealt with these "hybrid" instruments.

In Part One Markham focuses on some recurring problems in the markets and the legislative or regulatory attempts to solve them. For example, the early manipulations by such historic figures as Benjamin P. Hutchinson, credited with the first significant corner in the wheat pit, and Arthur Cutten, "perhaps the greatest grain speculator this country ever knew,"¹ were traced as background events in encouraging the legislature to prevent market manipulation. These early legislative attempts to deal with manipulation culminated in the Commodity Exchange Act of 1936. Similarly, concerns about options go back to 1865 when the Chicago Board of Trade "sought to prohibit 'privilege' trading, because it was widely thought that such trading was simply gambling."² In response to recurring options scandals a prohibition on options on all regulated commodities was included in the Commodity Exchange Act of 1936. Of course, concerns about manipulations and options did not cease with the passage of the 1936 Act. Regulatory constraints dealing with reporting requirements, speculative limits, and foreign traders are recurring issues which have grown in importance at various times over the past fifty years and which have their roots in concerns about manipulation. Further, Markham discusses "the great Russian Grain Robbery" and the infamous exploits of Harold Goldstein as preludes to the passage of the Commodity Futures Trading Commission Act of 1974.

The provisions of the 1974 CFTC Act and the significant amendments during the 1978 and 1982 reauthorizations are discussed. While the 1974 Act was certainly important, some of the most significant provisions of the Commodity Exchange Act were not created in 1974 but rather were developed to meet regulators' needs over the past half century. The basic concept that futures contracts may be traded only on "designated" exchanges and that these exchanges have self-regulatory responsibilities coupled with federal oversight has been embodied in

¹ J. MARKHAM, *THE HISTORY OF COMMODITY FUTURES TRADING AND ITS REGULATION* at 22 (1987).

² *Id.* at 8.

various pieces of legislation since the Grain Futures Act of 1922. While the CFTC was given injunctive authority in 1974, the Department of Agriculture originally sought this power in 1968. Restrictions on the Commission's authority included in 1974 have been eased by subsequent amendments. The book lays out the evolving nature of regulatory controls in a very comprehensible manner.

One of the provisions of the Act that was incorporated in 1974 without an evolutionary period was the Commission's jurisdiction over leverage transactions. While Congress granted jurisdiction in the 1974 Act with very little study and debate, these transactions have prompted a great deal of study and debate during the intervening 12 years in vast disproportion to their significance in the marketplace. The handling of leverage transactions points out a significant weakness of the book, and this weakness is a function of the presentation of the largest portion of the book as a history. To be sure, every history must stop at some point so that the book can go to press, but to cut off the story just prior to the enactment of the 1986 amendments seems to be poor timing on the part of the publisher. The 1986 leverage debate saw (1) the Commission propose, by a split vote, the elimination of leverage, (2) the Republican controlled Senate Agriculture Committee support the elimination of leverage, (3) the Republican administration support the expansion of leverage, (4) the Democratic controlled House Agriculture Committee support a limited expansion of precious metals leverage after heated debate, (5) the House of Representatives vote to reject its own Committee's recommendation and then reverse itself on the same day, and finally, (6) the Conference Committee and the Senate agree with the House provision of leverage. Leverage, which has been a thorny political issue for years, was the most heated issue during the 1986 reauthorization, an issue on which the largest exchanges and the Commission were on the same side and lost. Unfortunately the publisher was not able to wait long enough for Mr. Markham to finish the story.

While the book focuses on the history of commodity regulation and the historical development of the Commission, it generally does not devote a great deal of attention to individual cases or does not address large numbers of cases to assist the attorney looking for the right case to bolster a position. The

second part of the book dealing with the organization of the CFTC, however, does include substantial discussion of enforcement cases in various areas of law. The discussion of manipulation and the difficulty of proving manipulation charges is particularly interesting. While persons new to commodity law may find the historical treatment in Part One the most useful portion of the book, the private bar dealing with the CFTC may find Part Two especially useful. It is always helpful to have a guide when approaching an unknown bureaucracy. Those individuals representing respondents in enforcement matters may find this part particularly useful as they often will not have the opportunity to develop the working relationship that those with ongoing regulatory interests enjoy.

The third and final part of Mr. Markham's book is very timely. After discussing the characteristics of futures, options, and leverage contracts, the book examines the various criteria the Commission and the courts use in determining whether a given instrument should be traded on an exchange as a futures contract or banned as an illegal commodity option. Finally, Markham discusses the so-called hybrid instruments and other off-exchange transactions. This issue is the subject of current debate. Those participating in this debate will find Markham's treatment of the off-exchange issue a useful starting point.

While Chicago and New York City may be called home by most of the leading members of the commodities bar, one of the bar's most prolific writers, Jerry W. Markham, comes from Vine Grove, Kentucky. As you might guess, Markham grew up knowing more about hound dogs and squirrel hunting than futures and options. Nevertheless, he has overcome that advantage and has produced a very readable and informative volume on the history and regulation of the commodity futures markets.

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