TESTIMONY OF GARY GENSLER
CHAIRMAN, COMMODITY FUTURES TRADING COMMISSION
BEFORE THE
U.S. HOUSE APPROPRIATIONS SUBCOMMITTEE ON
AGRICULTURE, RURAL DEVELOPMENT, FOOD AND DRUG ADMINISTRATION, AND RELATED AGENCIES
WASHINGTON, DC
April 12, 2013

Good morning Chairman Aderholt, Ranking Member Farr and members of the Subcommittee. Thank you for inviting me to today's hearing on the President's request for the Commodity Futures Trading Commission's (CFTC) fiscal year (FY) 2014 budget. I'm pleased to testify along with my fellow Commissioner Scott O'Malia.

This hearing is occurring at an historic time in the markets because under Congress' direction, the CFTC now oversees the derivatives marketplace: not only futures that we have overseen for decades, but also the swaps market. The agency has completed 80 percent of the swap market reform rules required under the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act). The public is benefiting from seeing the price and volume of each swap transaction. This information is available free of charge on a website, like a modern-day tickertape. For the first time, the public will benefit from the risk reduction and greater access to the market that comes from centralized clearing. And for the first time, the public is benefiting from the oversight of swap dealers. So far, 75 have registered and must adhere to sales practice and business conduct standards to help lower risk to the overall economy.

The marketplace is increasingly shifting to implementation of these common-sense rules of the road. Now it is all the more clear: the CFTC is not the right size for its new and expanded mission Congress has directed it to perform.

The CFTC's current funding is $207 million prior to sequestration. We recognize that the federal government is operating under a sequester and that budgets for agencies across government require additional scrutiny. Our mission, however, has expanded dramatically. We have a duty to help protect the economy and taxpayers from risks in the financial system. Thus, the President' FY 2014 budget requests an appropriation of $315 million and 1,015 FTEs.   The overall funding levels requested approximate the plan set forth in the President's 2013 Budget ($308 million and 1,015 FTE), but also take into account industry progress in implementing financial reform. Although 1,015 FTE resources requested in this budget are at the same level as for FY 2013, adjustments were made across our mission activities to reflect the transition from Dodd-Frank rulemaking to swaps market oversight in 2014. Primarily, the Commission shifted its requested resource allocation to support and maintain direct examinations – a critical component of customer protection.   Market events have highlighted that the Commission must do everything within our authorities and resources to strengthen oversight programs and the protection of customers and their funds.

The President's budget request for the Commission strikes a balance between important investments in technology and human capital, both of which are essential to carrying out the agency's mandate. This approximately 52 percent increase in funding includes a 62 percent increase in IT services, but only a 44 percent increase in staff.

The CFTC is dedicated to using taxpayer dollars efficiently – nearly a fourth of the overall budget request, $73 million, is for outside IT services. When the CFTC's dedicated IT staff is included, the request is $94.8 million for IT, or nearly a third of the overall budget. But it still takes human beings to watch for market manipulation and abuses that affect hedgers, farmers, ranchers, producers and commercial companies, as well as the public buying gas at the pump.

The CFTC is operating under a strategic plan for FY 2011-2015. This plan raises the bar on the agency's performance measures to more accurately evaluate our progress. But the agency's performance is affected by the challenges of limited resources. For the second year in a row, there are many goals that were not met, as are detailed in the agency's Annual Performance Report (APR). The CFTC is reviewing the results of the APR and will include the findings in this year's revision of the strategic plan and consider the results as the agency reevaluates the allocation of resources.

In my remaining testimony, I will review the five areas that make up over 90 percent of our requested budgeted staff increase: registrations, examinations, surveillance and data, enforcement, and economics and legal analysis.

Registration and Product Reviews

A significant task before us in FY 2014 will be the continuation of registration of effected entities, as well as reviews of new products for both the clearing mandate and the trading mandate.

We want to consider registration applications in a thoughtful and timely manner, be efficient in reviewing submissions, and be responsive to market participant inquiries –but this will require sufficient funding. For FY 2014, the President's request supports $38.9 million and 147 FTEs for these two mission areas, an increase of $22.6 million and 92 FTEs.

The estimated 200 clearinghouses, trading platforms, swap data repositories, swap dealers and major swap participants that are recently registered or may seek CFTC registration within the next year is a dramatic increase over any registration effort the agency has overseen in the past. The Commission needs staff to facilitate the registration of the following:

- **Clearinghouses –** Entities that lower risk to the public by guaranteeing the obligations of both parties in a transaction. We are working with five entities seeking to register as DCOs and have inquiries from others. These entities would join the 14 we currently oversee.

- **Designated contract markets (DCMs) –** U.S. trading platforms that list futures and options and likely will start listing swaps. The CFTC currently oversees 16 DCMs, and by 2014, staff expects another two to three to seek registration.

- **Foreign boards of trade (FBOTs) –** Regulated trading platforms in other countries that are generally equivalent to DCMs. Since the FBOT rule became effective, 19 FBOTs have filed applications with the CFTC. By 2014, staff expects an additional couple of FBOTs to seek registration with the CFTC.

- **Swap data repositories (SDRs) –** Recordkeeping facilities created by Dodd-Frank to bring transparency to the swaps market. Three are provisionally registered with the CFTC, and by 2014, an additional SDR may seek registration.

- **Swap dealers and major swap participants–** Under the Dodd-Frank Act, the CFTC is working to comprehensively regulate swap dealers and major swap participants to lower their risk to the economy. As the result of completed CFTC rules, 75 swap dealers and two major swap participants are now provisionally registered. This initial group includes the largest domestic and international financial institutions dealing in swaps with U.S. persons. Commission staff currently estimates that over time, 25-50 additional swap dealers may request registration with the National Futures Association (NFA). We'll be overseeing their registration and related questions.

- **Swap execution facilities (SEFs) –** The new trading platform for swaps. Commission staff estimates that 15 entities may request to become SEFs.

While we will have a system for provisional registration in place, market participants will want the certainty of final registration.

The Commission approved the first clearing requirement last November. A key milestone was reached last week with the requirement that swap dealers and the largest hedge funds clear as of March 11. The vast majority of interest rate and credit default index swaps are being brought into central clearing. Compliance will continue to be phased in throughout this year. Other financial entities begin clearing June 10. Accounts managed by third party investment managers and ERISA pension plans have until September 9. The Commission continues in the resource intensive review for determinations of other swaps that will be subject to the clearing mandate.

Full funding for the agency means that we will be best prepared to review the dramatic increase in requested registrations and to review swaps for the clearing mandate. A partial increase in funding means market participants will see a backlog in registrations, responses to their inquiries, and product review because we won't have personnel sufficient to review their submissions in a timely and complete manner. Flat funding will mean market participants will wait even longer. There will be significant backlogs for participants seeking to register with the CFTC, as well as for review of swaps for mandatory clearing.

Examinations

Another critical mission for FY 2014 will be more regular and more in-depth examinations of the major market participants the CFTC oversees. Examinations are the CFTC's tool to check for compliance with laws that protect the public and to ensure the protection of customer funds. The President's request would provide $44.3 million and 185 FTEs for examinations, an increase of $25.6 million and 104 FTEs. The CFTC would more than double our current allocation for this mission because the number of entities we examine is expected to more than double.

This is an area where the agency has fallen short of our goals in performance reviews. The CFTC directly reviews clearinghouses and trading platforms and will review SDRs. But while the agency reviews them directly, we don't have the resources to have full-time staff on site, unlike other regulatory agencies that do have on-the-ground staff at the significant firms they oversee. The CFTC also doesn't do annual reviews. Clearinghouses, for instance, currently are examined on a three-year cycle. For intermediaries such as futures commission merchants

(FCMs) and swap dealers, the CFTC relies on what are known as self-regulatory organizations (SROs) to be the primary examiners. Given our lack of resources, we're only able to double check the SROs' work on a limited number of FCMs each year, and the agency can spend little time onsite at the firms.

On top of the current lack of staff for examinations, our responsibilities in 2014 will expand to include reviews of many new market participants. For instance, there are currently 117 FCMs, 75 swap dealers and two major swap participants have provisionally registered, and more are expected to do so as the year progresses. More frequent and in-depth examinations are necessary to assure the public that firms have adequate capital, as well as systems and procedures in place to protect customer money. Reviews are critical to ensuring the financial soundness of clearinghouses, and ensuring transparency and competition in the trading markets.

Fully funding the increase for examinations means the Commission can move toward annual reviews of all significant clearinghouses and trading platforms and adequate reviews of other market participants. A partial increase for examinations means cutting back our monitoring plans for new market participants and more in-depth risk reviews. Flat funding means we will continue lacking the ability to assure the public that the CFTC's registrants are financially sound and in compliance with regulatory protections.

Surveillance and Data

Effective market surveillance is dependent on the CFTC's ability to acquire and analyze extremely large volumes of data to identify trends and events that warrant further investigation. For FY 2014, the President's request would support $61.7 million and 174 FTEs for surveillance, data acquisition, and analytics, an increase of $18.3 million and 53 FTEs. Of the $61.7 million request, 55 percent would be directed toward IT.

The Dodd-Frank swaps market transparency rules mean a major increase in the amount of incoming data for the CFTC to aggregate and analyze. The agency is taking on the challenge of establishing connections with SDRs and aggregating the newly available swaps data with futures market data. This requires high performance hardware and software and the development of analytical alerts. But it also requires the corresponding personnel to manage this technology effectively for surveillance and enforcement.

As the CFTC also receives ownership and control information for trading accounts, it will have data to better detect intraday position limit violations and analyze high frequency trading.

A full increase for surveillance means the CFTC will have the ability to analyze futures and swaps data to protect market participants and the public. A partial increase would limit the agency's investments in analysis-based surveillance tools. And flat funding will limit our capacity to effectively utilize and aggregate the new data we now are receiving.

Enforcement

The CFTC's enforcement arm protects market participants and other members of the public from fraud, manipulation and other abusive practices in the futures and swaps markets. Our efforts range from pursuing Ponzi schemers who defraud individuals across the country out of life savings; to abuses that threaten customer funds; to false reporting of prices; to schemes to manipulate prices, including of goods, such as oil, gas and agricultural products. The Commission has opened more than 800 investigations in the past two fiscal years. The President's FY 2014 request would provide $57.7 million and 213 FTEs for enforcement, an increase of $18.1 million and 51 FTEs.

In 2002, we had 154 people devoted to enforcement, and that number is nearly flat with our current staff of 158. This staff has been called upon to enforce laws and rules that are new to our arsenal. The Dodd-Frank mandate closed a significant gap in the agency's enforcement authorities by extending the enforcement reach to swaps and prohibiting the reckless use of manipulative or deceptive schemes. In addition, the CFTC will be overseeing a host of new market participants.

A full increase for enforcement means more investigations and cases that the agency can pursue to protect the public. A less than full increase means that the CFTC will be faced with difficult choices. We could maintain the current volume and types of cases, but we would have to shift resources from futures cases to swaps cases or not cover all of the swaps market. Flat funding means not only that the Commission's enforcement volume likely would shrink, but parts of the markets would be left with little enforcement oversight.

The Commission's engagement in targeted enforcement efforts in the public interest include its historic actions regarding the rigging of benchmark rates, such as the London Interbank Offered Rate (LIBOR), a reference rate for much of the U.S. futures and swaps markets. Barclays, UBS and RBS were fined approximately $2.5 billion for manipulative conduct by the CFTC, the UK Financial Services Authority (FSA) and the Justice Department. At each bank, the misconduct spanned many years, took place in offices in several cities around the globe, included numerous people, and involved multiple benchmark rates and currencies. In each case, there was evidence of collusion. In the UBS and RBS cases, one or more inter-dealer brokers painted false pictures to influence submissions of other banks, i.e., to spread the falsehoods more widely. Barclays and UBS also were reporting falsely low borrowing rates in an effort to protect their reputation. While the cases led to $2 billion in fines flowing to the U.S. Treasury, what this is about is ensuring for financial market integrity.

Economics and Legal Analysis

For FY 2014, the President's budget would support $24.6 million and 97 FTEs to invest in robust economic analysis teams and Commission-wide legal analysis, a decrease of $3.6 million and 20 FTEs from our estimate under the pre-sequester continuing resolution. The CFTC's economists support all of the Commission's divisions, including surveillance and complex enforcement cases. They have served on Dodd-Frank rule teams to carefully consider the costs and benefits of each rule.

The decision to make downward adjustments in the resources requested for this critical mission activity was not an easy one. However, given the increasing number of intermediaries the CFTC now oversees, examination teams needed to be bolstered.

In 2014, the CFTC's economists will be integral in developing tools to analyze automated surveillance data and continue to evaluate new products for clearing.

Flat funding means a strained ability to analyze the market and detect problems that could be negative for the economy. Flat funding also means the Commission's legal analysis team will be cut back even further to support front-line examinations, adding to the delays in responding to market participants and processing applications and straining the team's ability to support of enforcement efforts.

Conclusion

The CFTC's hardworking team is just 8 percent more in numbers than at our peak in the 1990s. Yet since that time, the futures market has grown five-fold, driven by rapid advances in technology. The swaps market is eight times larger than the futures market. Effective market implementation of swaps reforms by the CFTC requires additional resources. We are not asking for eight times the funding or staff. Investments in both technology and people, however, are needed for effective oversight of these markets by regulators.

Though data has started to be reported to the public and to regulators, we need the staff and technology to access, review and analyze the data. With 75 entities having registered as new swap dealers and major swap participants, we need people to answer their questions and work with the NFA on the necessary oversight to ensure market integrity. Furthermore, as market participants expand their technological sophistication, CFTC technology upgrades are critical for market surveillance and to enhance customer fund protection programs.

This is an incredibly strained budget environment. But without sufficient funding for the CFTC, the nation cannot be assured this agency can closely monitor for the protection of customer funds and utilize our enforcement arm to its fullest potential to go after bad actors in the futures and swaps markets. Without sufficient funding for the CFTC, the nation cannot be assured that this agency can effectively enforce essential rules that promote transparency and lower risk to the economy.

Thank you again for inviting me today, and I look forward to your questions.