



Consumer Federation of America

May 1, 2013

The Honorable Debbie Stabenow
Chairman
Committee on Agriculture, Nutrition
and Forestry
U.S. Senate
Washington, D.C. 20510

The Honorable Thad Cochran
Ranking Member
Committee on Agriculture, Nutrition
and Forestry
U.S. Senate
Washington, D.C. 20510

Dear Chairman Stabenow and Ranking Member Cochran:

Thank you for the invitation to submit suggestions regarding issues to be addressed in the upcoming reauthorization of the Commodity Futures Trading Commission. We congratulate you for establishing an open and bipartisan process and for seeking input from a broad range of interested parties. We hope that the end result of that process will be a bipartisan bill that puts the agency on a sound financial footing, strengthens its authority in key areas, and shores up the crucially important derivatives market reforms adopted in the Wall Street Reform and Consumer Protection Act.

CFA is an active participant in both Americans for Financial Reform and the Commodity Markets Oversight Coalition, both of which are writing separately to suggest a broader range of issues to be addressed. For the purpose of this letter, however, we will highlight two issues where CFA has taken a more active role: CFTC self-funding and cross-border application of derivatives regulations. Both increased funding for the agency and a strong cross-border policy are crucial to delivering the financial market reforms promised by Congress when it passed the Wall Street Reform legislation

I. Put the CFTC on the Same Self-Funding Footing as Federal Banking Regulators

As your letter correctly notes, this year's reauthorization comes at an important but challenging time. Unlike other better funded federal financial regulators, the CFTC is nearing completion of the rule-writing phase of Wall Street reform and has begun actual implementation of rules designed to reduce risk, promote market integrity, and bring transparency to the over-the-counter swaps market. This is a remarkable achievement for a tiny agency operating on a shoe-string budget and facing resistance from well-funded and powerful Wall Street firms intent on maintaining the excessive profits they have long been able to extract from an opaque and unregulated market.

As the agency transitions from a primary focus on rule-writing to implementation, its ability to fulfill its regulatory mandate is seriously imperiled by a funding level that doesn't begin to match the scope of its responsibilities. Starving the agency of resources during this crucial implementation phase puts us all at risk: at risk that irresponsible Wall Street practices will go unchecked, threatening the stability of the global economy; at risk that unrestrained speculation in commodity markets will impede the ability of farmers and Main Street businesses to hedge their risks; at risk that municipalities, endowments, pension funds and other less sophisticated participants in the swaps markets will once again become victims of predatory practices. The ultimate victims will be the average Americans who pay for this abusive conduct in higher prices at the grocery store and the gas pump and who will be forced to bear the burden if a financial system run amok once again requires a rescue.

Many members of this Committee recognize the importance of the CFTC and have led the fight for increased funding to match the agency's increased workload. We greatly appreciate those efforts. As you know all too well, the agency had seen its funding severely eroded in the years leading up to the financial crisis. Its budget in 2007 provided a staffing level 23 percent below what it had been in 1999, a period during which the size of the markets it was responsible for overseeing grew five-fold. While some progress was made in the immediate aftermath of the crisis to restore prior staffing levels, the agency has never received the increased funding levels promised in the Wall Street reform legislation. The sad fact is that while the Senate has consistently supported funding increases, some in the House who opposed Wall Street reform have attempted to weaken and stall its implementation by denying adequate funding to the CFTC. The sequestration, with its indiscriminate funding cuts, only makes the problem worse.

The resulting underfunding will inevitably undermine implementation of the Wall Street reform law. It will make the CFTC slower to process registration applications and industry requests for guidance. It will undercut the agency's ability to spot and respond quickly to emerging threats. And it will weaken enforcement efforts just as recent examples – the “London whale,” Libor manipulation, and the MF Global bankruptcy to name just a few – have shown how rife with abuse these markets have become and how crucial a strong enforcement program and effective regulatory oversight are to market integrity and investor confidence.

For all these reasons, we believe the only answer is to finally put the CFTC on the same sound financial footing that virtually all other federal financial regulators enjoy through their ability to collect fees and set their budgets outside the congressional appropriations process. Two arguments are typically made against this proposal. Neither is convincing, in our view, particularly when weighed against the persistent under-funding which this agency has suffered.

- Wall Street typically argues that authorizing the CFTC to impose user fees would drive up costs that would be passed on to consumers and businesses. But major Wall Street firms have been known to charge fees that greatly exceed the agency's entire annual budget to a single customer to unwind a single deal, as J.P. Morgan proposed to do in the deal that drove Jefferson County into bankruptcy. In fact, given the size of the markets the CFTC oversees – a roughly \$30 trillion commodity market and \$300 trillion swaps market – any such user fees would be so tiny as to be all but undetectable.

- Congressional appropriators have sometimes argued that self-funding would seriously diminish Congress's ability to provide necessary oversight of the agency. Those who make this argument do not explain why a system that seems to function perfectly adequately for oversight of self-funded federal banking regulators or the newly created Consumer Financial Protection Bureau could not work similarly well for the CFTC. Moreover, as you well know, the House and Senate agriculture committees would retain both unimpeded ability to conduct congressional oversight and the tools necessary to ensure that the agency is using its resources wisely and effectively. The reauthorization process is one such tool.

Given a history of chronic underfunding, and in light of the crucial role the CFTC plays in safeguarding our nation's financial security, we believe the benefits of self-funding greatly outweigh any such questionable concerns. We urge you to include self-funding legislation in the reauthorization bill.

II. Ensure Strong Cross-border Application of Derivatives Regulations

Efforts led by this Committee to reduce the risks, increase the transparency, rein in excessive speculation, and promote effective oversight of over-the-counter swaps markets will be for naught if swaps dealers can evade regulations simply by conducting their transactions overseas. Today's financial markets are global in scope. It is an inescapable fact that modern technology enables large, multi-national swaps dealers to shift the "location" of transactions among hundreds, even thousands, of international affiliates in a matter of seconds. While the transactions (and financial services jobs) may migrate to foreign jurisdictions absent a strong cross-border policy, the risks will still come home to haunt us, as the U.S.-based parent company will still be on the hook for any resulting losses. Congress recognized that threat when it included a requirement in the Wall Street reform bill that these regulations must apply not just within our borders, but also to any activities outside the United States that have "a direct and significant connection with activities in, or effect on, commerce" of the United States.

In attempting to adopt an approach to cross-border application of U.S. rules that is consistent with this congressional mandate, CFTC Chairman Gary Gensler has met with stiff resistance not just from Wall Street but also from some foreign regulators, who argue that the United States should simply rely on them to regulate within their borders. But this would be a recipe for disaster. Despite their protestations, most foreign regulators are well behind the United States in finalizing those regulations. To delay implementation of our cross-border policy in order to defer to them would be to delay protections for U.S. investors and businesses that rely on these markets, perhaps for years or until the next financial crisis creates a new urgency for action. Moreover, it is not yet clear whether even the leading market regulators (in Europe and the United Kingdom, for example) will impose safeguards as rigorous as those required under U.S. law. Indeed, it is inevitable that some markets will seek to carve out a niche by offering businesses a haven from rigorous regulation, irresponsibly threatening the integrity and stability of global financial markets.

The good news here is that the statute already applies an appropriately comprehensive standard for cross-border application of U.S. rules. Our request to the Committee in this instance is first to ensure that this legislation does nothing to narrow the scope of the existing cross-border statutory language and second to ensure that the policy adopted by the CFTC to implement this

provision is fully consistent with the statutory mandate. To achieve that goal, it is absolutely essential that:

- U.S. laws must apply to *all* foreign subsidiaries of U.S. companies. By the same token, U.S. laws must apply to all foreign companies that do more than a *de minimis* amount of business with U.S. entities, including overseas affiliates guaranteed by U.S. companies.
- Substituted compliance must only be granted in those jurisdictions that have genuinely comparable rules, both in terms of the substance of the rules and the vigor of their enforcement. General comparability, along the lines proposed earlier today by the SEC, is simply not adequate.
- The decision to grant substituted compliance must be based on clear and detailed standards through a transparent process in which the rationale for granting substituted compliance is documented. Blanket exemptions must not be granted to jurisdictions that meet some, but not all, of the standards necessary for true comparability.
- Any decision about whether to rely on a foreign regulator under a substituted compliance approach must be deferred until that regulator has adopted and begun to implement its regulatory regime. The United States cannot delay application of its laws while other countries catch up, and it cannot defer to regulations that are not yet being enforced.

CFTC Chairman Gary Gensler has shown that he understands the importance of this issue, and he has fought vigorously to win adoption of a strong cross-border policy at the CFTC. We urge this Committee to use the reauthorization process to reaffirm its support for a strong and comprehensive approach to cross-border application of derivatives rules and to spur the CFTC to speed implementation of a policy that is consistent with the broad scope of the statutory language.

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The CFTC has much to be proud of in its implementation of the Wall Street reform legislation. It has set a standard for relatively timely completion of rulemakings that better funded federal financial regulators cannot approach, let alone match. The reauthorization process offers an opportunity to fine-tune the agencies' operations, providing resources, authority and direction to ensure that it can fulfill its immense and immensely important regulatory responsibilities effectively and efficiently. We look forward to working with the Committee on what we hope will be strong, bipartisan legislation that advances our shared goal of promoting the transparency, integrity, and stability of our nation's futures and swaps markets.

Respectfully submitted,

Barbara Roper
Director of Investor Protection

cc: Members of the Committee