



**AMERICANS  
FOR FINANCIAL REFORM**  
ACCOUNTABILITY \* FAIRNESS \* SECURITY

**Americans for Financial Reform**  
1629 K St NW, 10th Floor, Washington, DC, 20006  
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May 3, 2013

**Re: Reauthorization of the Commodity Futures Trading Commission (CFTC)**

The Honorable Debbie Stabenow  
Chairwoman, Senate Committee on  
Agriculture, Nutrition & Forestry  
328A Russell Senate Office Building  
Washington, DC 20510

The Honorable Thad Cochran  
Ranking Member, Senate Committee on  
Agriculture, Nutrition & Forestry  
113 Dirksen Senate Office Building  
Washington, DC 20510

Dear Chairwoman Stabenow and Ranking Member:

Americans for Financial Reform (“AFR”) appreciates the invitation to provide recommendations on the reauthorization of the Commodity Futures Trading Commission (CFTC). We thank you for your commitment to an open reauthorization process and for reaching out to our coalition for input.

AFR is a coalition of more than 250 national, state, and local groups who have come together to advocate for reform of the financial industry. Members of AFR include consumer, civil rights, investor, retiree, community, labor, faith based, and business groups along with prominent independent experts.

**Background**

The CFTC was reauthorized through 2013 in the Food, Conservation and Energy Act of 2008.<sup>1</sup> This legislation provided the CFTC with substantial additional authority over the futures, options and swaps markets, including measures to close the so-called ‘Enron loophole’ through expanding CFTC oversight to “price discovery contracts” on previously unregulated electronic trading platforms. The 2008 reauthorization also strengthened antifraud prohibitions and increased civil monetary penalties for manipulation or attempted manipulation of commodity markets from \$500,000 to \$1 million per violation

However, most significant changes in the CFTC’s authority since it was last reauthorized occurred in Title VII of the Dodd-Frank Act (the ‘DFA’). This legislation instituted the most comprehensive changes in the Commodity and Exchange Act (CEA) since the Great Depression. The catastrophic events of the financial crisis of 2008-2009 clearly revealed the need for

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<sup>1</sup> Pub.L.110-246

comprehensive regulation of the over-the-counter swaps market. The DFA granted the CFTC authority to regulate the great majority of the over-the-counter swaps market (all swaps with the exception of credit default swaps based on a single security or a narrow index of securities). This change added approximately \$300 trillion in notional derivatives markets to the CFTC's supervision responsibilities – an eight-fold increase in the size of the market the CFTC must supervise. In addition, the DFA granted the CFTC important new anti-manipulation authority and outlined a position limits regime to prevent excessive speculation in the commodity markets.

Below, we outline several initial recommendations for the committee to examine as it drafts a reauthorization bill. AFR would appreciate the opportunity to amend or expand upon this list in the future, both to provide additional detail and potentially to outline new recommendations. Also, these recommendations do not preclude the submission of supplemental recommendations by individual AFR members or their affiliates.

### **Funding of the CFTC**

While the Dodd-Frank Act increased the responsibilities of the CFTC greatly, it did not create self-funding mechanisms for the agency that would guarantee the resources needed to execute these responsibilities. The CFTC is the only significant financial regulator that is not self-funded, and is also by far the smallest of the significant financial regulators. The CFTC is currently funded at approximately \$200 million annually, more than 35 percent below the requested level of \$315 million. This is a level that is inadequate to perform the core monitoring, regulatory, and enforcement functions of the agency. The request of \$315 million is minuscule in comparison to the roughly \$37 trillion U.S. futures market and \$300 trillion U.S. swaps market supervised by the CFTC. A fee sufficient to automatically raise this amount would hardly be noticeable by market participants, and would be proportionally smaller than the SEC's Section 31 fees.

The CFTC's staffing level declined precipitously during the years prior to the financial crisis, even though commodity futures markets were growing rapidly and unregulated swaps markets played a critical role in triggering a collapse of the financial system. Although staffing levels have grown somewhat since 2008, the CFTC's current staffing level is just seven percent higher than it was 20 years ago. But the combination of a five-fold increase in the notional size of the commodity futures market over the past two decades and the addition of the previously unregulated swaps markets means that the total size of the markets overseen by the agency have grown by almost forty times over that period.

AFR strongly supports the President's recommendation to authorize the CFTC to charge user fees to raise its full level of funding. We support measures to make the agency fully self-funding, as is the case for all of the banking agencies and the Consumer Financial Protection Bureau. This would permanently guarantee the agency adequate resources to carry out its mission. As shown by the decline in agency staffing during the years prior to the financial crisis even as the regulated market grew, the CFTC's underfunding problem is chronic and requires a fundamental structural solution. A fee based arrangement would mean that CFTC funding would grow automatically with the size of the markets supervised.

## **Manipulation & Excessive Speculation**

Speculative position limits are important in preserving the overall integrity of the commodity markets, protecting consumers from inflation in commodity prices caused by market manipulation and excessive speculation, and preserving the ability of real economy companies to use commodity derivatives for bona fide hedging without inflated prices due to excessive volatility. Our coalition strongly supports the decision of Congress to mandate speculative position limits under Section 737 of the Dodd-Frank Act.

The CFTC approved a final rule establishing mandatory position limits on October 18, 2011. This rule was to go into effect on October 12, 2012. However, the rule was vacated by a District Court Judge on September 28, 2012 and the decision is currently on Appeal. Our coalition strongly supports the immediate implementation of mandatory position limits and believes that the intent of Congress was clear and unambiguous.

However, even when the October 18<sup>th</sup> final rule is implemented, there are serious doubts about whether the Commission's actions in that rule went far enough in addressing the harmful effects of excessive speculation. Specifically, AFR feels that the October 18<sup>th</sup> rule is overly focused on market manipulation by individual traders and is not oriented to addressing the harmful market dynamics created by excessive levels of speculation in the aggregate. Furthermore, we are concerned that individual position limits set forth by the rule are too high, and that the rule only requires periodic review of established limits.

We believe that a more effective way to prevent excessive speculation from distorting commodity prices and to restore the balance between commercial hedgers and financial investors is to require aggregate limits on all speculation as a class of trader. While the CFTC appears to have the statutory authority to require such speculative class limits under current law, they have chosen not to do so. Yet limits on aggregate speculation are necessary to address all the market effects of excessive speculative interest, which go well beyond the possibility of market manipulation by an individual speculator. In the forthcoming CFTC Reauthorization Act, the committee should require the CFTC to establish class-specific limits on aggregate speculation.

## **Penalties**

Current law allows fines of up to \$1 million per violation for manipulation or attempted manipulation and \$140,000 for other violations under the Commodity Exchange Act.<sup>2</sup> The definition of 'per violation' is open to judicial interpretation. While the amount of these fines vary with the number of violations found by the court in each case, they are generally insignificant when compared to the overall profits of many market participants such as financial intuitions and may be doing little to deter violations of the law.

The committee should increase fines and penalties as appropriate in the CFTC Reauthorization Act in order to more effectively deter unlawful behavior. Given the potentially enormous profits that can be earned through manipulation of these markets, effective deterrence may require stronger steps than simply raising the maximum penalty for a single violation. The Committee

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<sup>2</sup> 7 U.S.C. §13

should also grant the CFTC the authority to escalate penalty levels for repeated egregious or major violations, and should ensure that the CFTC has the ability to ban entities or individuals from future participation in the markets if they engage in repeated egregious behavior.

Additionally, the CFTC is currently restrained by the blanket five-year Statute of Limitations (SOL), which restricts the ability of Commissioners to prosecute violations of the CEA, including cases of fraud and manipulation. The existing five-year SOL challenges the CFTC to prosecute cases despite a limited budget and personnel and the increasing complexity of the markets it regulates. Therefore, the committee should extend the SOL for the CFTC to a minimum of 10 years.

### **Proposed House Legislation**

On March 20, 2013, the House Agriculture Committee approved legislation that would amend the Commodity Exchange Act and, in some cases, intervene in ongoing CFTC rulemakings. Our coalition has taken a position against most of this legislation, which is now pending consideration in the House Financial Services Committee. We understand that some members of Congress, trade associations and special interest groups are recommending one or more of this legislation be included as part of CFTC reauthorization. Below you will find thoughts of our coalition on this legislation.

***H.R.634, the Business Risk Mitigation and Price Stabilization Act*** – H.R.634 would exempt from capital and margin requirements any swap which qualifies for the commercial end user exemption from clearing. AFR believes this legislation is unnecessary given the action of regulators to exempt the vast majority of such ‘end user’ swaps from margin by rule. Furthermore, while this legislation leaves in place prudential authorities to require capital and margin for end user swaps at bank swap dealers, it removes the only statutory authority for the CFTC to require end user margin at CFTC-regulated non-banks. As a targeted use of this authority could prove important in responding to future cases of market disruption, this legislation is potentially harmful as well as unnecessary. AFR opposes this legislation.

***H.R.677, the Inter-affiliate Swap Clarification Act*** – H.R.677 would exempt inter-affiliate swaps from the definition of ‘swap’ under Dodd-Frank for all purposes except reporting. Furthermore, the legislation defines ‘affiliate’ very loosely, as any two entities that report their finances on a consolidated basis. Such consolidated reporting does not even require common majority ownership. The combination of a very loose definition of ‘affiliate’ and a radical narrowing of CFTC jurisdiction for such swaps makes this legislation a significant threat to effective swaps regulation. Furthermore, the CFTC has already used its existing authority to finalize a generous exemption for the great majority of inter-affiliate swaps from clearing and margin requirements, demonstrating that this legislation is unnecessary to accomplish legitimate goals of an appropriate exemption for genuine inter-affiliate swaps. AFR strongly opposes this legislation.

***H.R.742, the Swap Data Repository & Clearinghouse Indemnification Correction Act*** – H.R.742 would remove the indemnification provisions from Sections 728 and 763 of the Dodd-Frank Act to allow data sharing for swaps between U.S. and foreign regulators. AFR does not

oppose this legislation as is it is a non-controversial technical correction that could improve regulatory effectiveness.

***H.R.1003 (no title)*** – H.R.1003 would repeal existing cost-benefit requirements under the CEA and requires the CFTC to conduct more expansive and comprehensive analyses before approving regulations or orders. While comprehensive cost-benefit considerations and analyses of potential burdens on market participants should always be considered by any federal regulator, adequate requirements already exist in the CEA. We believe the legislation is politically-motivated with the intent of slowing down important new derivative market regulations even further than already existing delays, which are unacceptable. AFR strongly opposes this legislation.

***H.R. 1256, the Swaps Jurisdiction Certainty Act*** – H.R.1256 would require the SEC and CFTC to jointly issue rules relating to swaps transacted between U.S. and non-U.S. persons and exempts a non-U.S. person in compliance with the swaps regulatory requirements of a G20 member nation from U.S. swaps requirements unless the SEC and CFTC jointly determine that the regulatory requirements are not “broadly equivalent” to U.S. swaps requirements. This legislation intervenes in ongoing negotiations between U.S. and foreign regulators regarding cross-border oversight of the derivatives markets and could delay or undermine those efforts. Even more important, the substantial new hurdles it creates to effective regulation of swaps conducted off-shore by U.S. entities means that it would create an off-shore loophole that could allow systemically risk entities or financial institutions to evade U.S. regulation. Proper regulation of foreign subsidiaries of U.S. financial institutions is essential to effective derivatives oversight. AFR strongly opposes this legislation.

### **Support For the Full Implementation of Dodd-Frank**

The legislative proposals above have in common that they seek to impede CFTC implementation of the new derivatives framework in Title VII of the Dodd-Frank Act. Despite its lack of funding, the CFTC has been a leader in Dodd-Frank implementation, and has finalized a greater proportion of its assigned rules than any other financial regulatory agency.<sup>3</sup>

Title VII of the Dodd-Frank Act is a common-sense solution to derivatives regulation that relies on market tested tools such as exchange trading, clearing, and entity risk management. Furthermore, ample regulatory discretion is provided to the CFTC in determining exactly which entities and which types of instruments are subjected to these requirements. Indeed, the CFTC has been highly responsive to industry in providing exemptions for small banks, co-operatives, end users, commercial hedgers, dealers with notional swaps volume below \$8 billion, and numerous other situations as well. Given the moderate and measured nature of Title VII and the substantial regulatory discretion permitted to the CFTC to address any technical issues that may arise, statutory intervention that results in impeding CFTC implementation of Dodd-Frank is completely inappropriate.

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<sup>3</sup> See David-Polk, [“Dodd Frank Progress Report”](#), May 2013.

## **Other Areas -- High Frequency Trading And Self Regulatory Organizations**

AFR views the rapid growth of high frequency trading (HFT) as a significant threat to the structure and legitimate purposes of the commodity markets. According to the Tabb Group consultancy, HFT now accounts for over 60 percent of futures market volumes, up from 47 percent five years ago. Evidence is mounting that predatory HFT, rather than improving genuine market liquidity, increase volatility, impedes market functioning, and creates negative externalities for other traders.<sup>4</sup> While the CFTC has statutory authority to regulate HFT, progress in this area has been slow. Adequate data is still lacking and even the definitional decisions needed to properly define the scope of the problem have not taken place. AFR does not have specific policy recommendations concerning HFT at this time, but may submit them in the future. However, we urge the Committee's attention to this important issue. The Committee should seek out opportunities to facilitate and speed CFTC action in this area.

AFR would also like to join Better Markets in urging attention to the problem of excessive reliance on self-regulatory organizations in oversight of the futures markets. As detailed in the Better Markets letter, recent years have seen repeated failures by self-regulatory exchanges such as CME and ICE and associations such as the National Futures Association to properly oversee member organizations and the markets in general. The problem of over-reliance on self-regulatory agencies is fundamentally related to the issue of CFTC underfunding, which as stated above should be addressed through fee-based self-funding. However, even apart from the funding issue, the Committee must reexamine the excessive role of self-regulation in futures markets. As a significant volume of the swaps market could potentially move to the futures markets under 'futurization' initiatives, the need to do so is becoming more pressing.

### **Conclusion**

Again, we appreciate the opportunity to provide input to the committee as it begins its work to draft legislation to reauthorize the CFTC. AFR and its member organizations stand ready to provide additional input to the committee as it continues its work. Should you have any questions, please contact Marcus Stanley, AFR's Policy Director, at (202) 466-3672 or [marcus@ourfinancialsecurity.org](mailto:marcus@ourfinancialsecurity.org).

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<sup>4</sup> Kirilenko, Andrei A. and Lo, Andrew W., Moore's Law vs. Murphy's Law: Algorithmic Trading and Its Discontents (March 19, 2013). Available at SSRN: <http://ssrn.com/abstract=2235963>

## **Following are the partners of Americans for Financial Reform.**

*All the organizations support the overall principles of AFR and are working for an accountable, fair and secure financial system. Not all of these organizations work on all of the issues covered by the coalition or have signed on to every statement.*

- A New Way Forward
- AFL-CIO
- AFSCME
- Alliance For Justice
- American Income Life Insurance
- American Sustainable Business Council
- Americans for Democratic Action, Inc
- Americans United for Change
- Campaign for America's Future
- Campaign Money
- Center for Digital Democracy
- Center for Economic and Policy Research
- Center for Economic Progress
- Center for Media and Democracy
- Center for Responsible Lending
- Center for Justice and Democracy
- Center of Concern
- Change to Win
- Clean Yield Asset Management
- Coastal Enterprises Inc.
- Color of Change
- Common Cause
- Communications Workers of America
- Community Development Transportation Lending Services
- Consumer Action
- Consumer Association Council
- Consumers for Auto Safety and Reliability
- Consumer Federation of America
- Consumer Watchdog
- Consumers Union
- Corporation for Enterprise Development
- CREDO Mobile
- CTW Investment Group
- Demos
- Economic Policy Institute
- Essential Action
- Greenlining Institute
- Good Business International
- HNMA Funding Company
- Home Actions
- Housing Counseling Services

- Home Defender's League
- Information Press
- Institute for Global Communications
- Institute for Policy Studies: Global Economy Project
- International Brotherhood of Teamsters
- Institute of Women's Policy Research
- Krull & Company
- Laborers' International Union of North America
- Lake Research Partners
- Lawyers' Committee for Civil Rights Under Law
- Move On
- NAACP
- NASCAT
- National Association of Consumer Advocates
- National Association of Neighborhoods
- National Community Reinvestment Coalition
- National Consumer Law Center (on behalf of its low-income clients)
- National Consumers League
- National Council of La Raza
- National Council of Women's Organizations
- National Fair Housing Alliance
- National Federation of Community Development Credit Unions
- National Housing Resource Center
- National Housing Trust
- National Housing Trust Community Development Fund
- National NeighborWorks Association
- National Nurses United
- National People's Action
- National Urban League
- Next Step
- OMB Watch
- OpenTheGovernment.org
- Opportunity Finance Network
- Partners for the Common Good
- PICO National Network
- Progress Now Action
- Progressive States Network
- Poverty and Race Research Action Council
- Public Citizen
- Sargent Shriver Center on Poverty Law
- SEIU
- State Voices
- Taxpayer's for Common Sense
- The Association for Housing and Neighborhood Development
- The Fuel Savers Club
- The Leadership Conference on Civil and Human Rights
- The Seminal
- TICAS

- U.S. Public Interest Research Group
- UNITE HERE
- United Food and Commercial Workers
- United States Student Association
- USAction
- Veris Wealth Partners
- Western States Center
- We the People Now
- Woodstock Institute
- World Privacy Forum
- UNET
- Union Plus
- Unitarian Universalist for a Just Economic Community

*List of State and Local Affiliates*

- Alaska PIRG
- Arizona PIRG
- Arizona Advocacy Network
- Arizonans For Responsible Lending
- Association for Neighborhood and Housing Development NY
- Audubon Partnership for Economic Development LDC, New York NY
- BAC Funding Consortium Inc., Miami FL
- Beech Capital Venture Corporation, Philadelphia PA
- California PIRG
- California Reinvestment Coalition
- Century Housing Corporation, Culver City CA
- CHANGER NY
- Chautauqua Home Rehabilitation and Improvement Corporation (NY)
- Chicago Community Loan Fund, Chicago IL
- Chicago Community Ventures, Chicago IL
- Chicago Consumer Coalition
- Citizen Potawatomi CDC, Shawnee OK
- Colorado PIRG
- Coalition on Homeless Housing in Ohio
- Community Capital Fund, Bridgeport CT
- Community Capital of Maryland, Baltimore MD
- Community Development Financial Institution of the Tohono O'odham Nation, Sells AZ
- Community Redevelopment Loan and Investment Fund, Atlanta GA
- Community Reinvestment Association of North Carolina
- Community Resource Group, Fayetteville A
- Connecticut PIRG
- Consumer Assistance Council
- Cooper Square Committee (NYC)
- Cooperative Fund of New England, Wilmington NC
- Corporacion de Desarrollo Economico de Ceiba, Ceiba PR
- Delta Foundation, Inc., Greenville MS
- Economic Opportunity Fund (EOF), Philadelphia PA

- Empire Justice Center NY
- Empowering and Strengthening Ohio's People (ESOP), Cleveland OH
- Enterprises, Inc., Berea KY
- Fair Housing Contact Service OH
- Federation of Appalachian Housing
- Fitness and Praise Youth Development, Inc., Baton Rouge LA
- Florida Consumer Action Network
- Florida PIRG
- Funding Partners for Housing Solutions, Ft. Collins CO
- Georgia PIRG
- Grow Iowa Foundation, Greenfield IA
- Homewise, Inc., Santa Fe NM
- Idaho Nevada CDFI, Pocatello ID
- Idaho Chapter, National Association of Social Workers
- Illinois PIRG
- Impact Capital, Seattle WA
- Indiana PIRG
- Iowa PIRG
- Iowa Citizens for Community Improvement
- JobStart Chautauqua, Inc., Mayville NY
- La Casa Federal Credit Union, Newark NJ
- Low Income Investment Fund, San Francisco CA
- Long Island Housing Services NY
- MaineStream Finance, Bangor ME
- Maryland PIRG
- Massachusetts Consumers' Coalition
- MASSPIRG
- Massachusetts Fair Housing Center
- Michigan PIRG
- Midland Community Development Corporation, Midland TX
- Midwest Minnesota Community Development Corporation, Detroit Lakes MN
- Mile High Community Loan Fund, Denver CO
- Missouri PIRG
- Mortgage Recovery Service Center of L.A.
- Montana Community Development Corporation, Missoula MT
- Montana PIRG
- Neighborhood Economic Development Advocacy Project
- New Hampshire PIRG
- New Jersey Community Capital, Trenton NJ
- New Jersey Citizen Action
- New Jersey PIRG
- New Mexico PIRG
- New York PIRG
- New York City Aids Housing Network
- New Yorkers for Responsible Lending
- NOAH Community Development Fund, Inc., Boston MA
- Nonprofit Finance Fund, New York NY
- Nonprofits Assistance Fund, Minneapolis M

- North Carolina PIRG
- Northside Community Development Fund, Pittsburgh PA
- Ohio Capital Corporation for Housing, Columbus OH
- Ohio PIRG
- OligarchyUSA
- Oregon State PIRG
- Our Oregon
- PennPIRG
- Piedmont Housing Alliance, Charlottesville VA
- Michigan PIRG
- Rocky Mountain Peace and Justice Center, CO
- Rhode Island PIRG
- Rural Community Assistance Corporation, West Sacramento CA
- Rural Organizing Project OR
- San Francisco Municipal Transportation Authority
- Seattle Economic Development Fund
- Community Capital Development
- TexPIRG
- The Fair Housing Council of Central New York
- The Loan Fund, Albuquerque NM
- Third Reconstruction Institute NC
- Vermont PIRG
- Village Capital Corporation, Cleveland OH
- Virginia Citizens Consumer Council
- Virginia Poverty Law Center
- War on Poverty - Florida
- WashPIRG
- Westchester Residential Opportunities Inc.
- Wigamig Owners Loan Fund, Inc., Lac du Flambeau WI
- WISPIRG

***Small Businesses***

- Blu
- Bowden-Gill Environmental
- Community MedPAC
- Diversified Environmental Planning
- Hayden & Craig, PLLC
- Mid City Animal Hospital, Pheonix AZ
- The Holographic Repatterning Institute at Austin
- UNET

