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THE COMMODITY FUTURES TRADING COMMISSION: EFFECTIVE ENFORCEMENT AND THE FUTURE OF DERIVATIVES REGULATION

HEARING

BEFORE THE

COMMITTEE ON AGRICULTURE, NUTRITION AND FORESTRY UNITED STATES SENATE

ONE HUNDRED THIRTEENTH CONGRESS

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THE COMMODITY FUTURES TRADING COMMISSION: EFFECTIVE ENFORCEMENT AND THE FUTURE OF DERIVATIVES REGULATION

Wednesday, December 10, 2014

UNITED STATES SENATE,
COMMITTEE ON AGRICULTURE, NUTRITION AND FORESTRY,
Washington, DC

The Committee met, pursuant to notice, at 10:06 a.m., in room 328A, Russell Senate Office Building, Hon. Debbie Stabenow, Chairwoman of the Committee, presiding.

Present: Senators Stabenow, Brown, Klobuchar, Bennet, Gillibrand, Donnelly, Casey, Walsh, Cochran, Roberts, Chambliss, Boozman, Hoeven, Johanns, Grassley, and Thune.

STATEMENT OF HON. DEBBIE STABENOW, U.S. SENATOR FROM THE STATE OF MICHIGAN, CHAIRWOMAN, COMMITTEE ON AGRICULTURE, NUTRITION AND FORESTRY

Chairwoman STABENOW. Well, good morning. I will call to order the Committee on Agriculture, Nutrition and Forestry, and we have several things we need to do today.

First, happy birthday to Senator Boozman. We want to celebrate. As you can see, we have a package of goodies for everyone, and I want to thank my staff and thank Jessie and everybody who put this together from the team as we honor four members that will be leaving us. When we look in this room, we are reminded every day of two—multiple Chairmen but certainly two, Senator Harkin and Senator Chambliss, whose portraits are here in front of us every day. We are losing both of them, which will be a real loss to the Committee, along with Senator Johanns and Senator Walsh, who are four distinguished members.

In their honor today, we did reach out to do something as a snack from each State, so we do have popcorn from Iowa, and Nebraska, caramel corn in honor of Senator Johanns, and we have beef jerky from Montana, and we also have some Georgia pecan pralines in honor of Senator Chambliss.

So I just want to take a moment in all seriousness to say that it has been a wonderful honor to chair this Committee, and with all of you, again, even though it may feel like old news talking about the farm bill, it certainly is an accomplishment that we were able to do together. That was something that was not only difficult

but not replicated in many places, and it is something that we should, I think, together all feel very proud of.

As we are having the change of the guard, I want to also thank Senator Cochran for his leadership as Ranking Member and Senator Roberts, who will be assuming the Chair. I was fortunate to have the opportunity to work with two distinguished Ranking Members in order to be able to get the farm bill passed twice—not once but twice. It reflects a lot of work of people around this table, and I want to start with just mentioning Senator Harkin, who is overseas for a day honoring a gentleman. He will be coming back and joining us tomorrow, but I do want to recognize Senator Harkin first as the—in order of seniority, Senator Harkin not only has chaired the Committee but really is the "Father of Modern Conservation," as he has been called. He has been in both the House and Senate Agriculture Committees for 40 years and chaired the farm bill in 2002 and wrote the Conservation Stewardship Program and strengthened the farm safety net, he really was a driving force around bioenergy and nutrition. The Fresh Fruit and Vegetable Program we have in our schools today would not be there without Senator Harkin, and so we are very, very grateful to him and cannot imagine this Committee without his service.

We equally cannot imagine, I cannot imagine this Committee without Senator Chambliss both as Chair, former Chair, and as someone who as Chair and Ranking Member, you have played an integral role, in fact, in passing this bill, all the way through to the conference committee. I appreciate your advice. I appreciate your involvement both publicly and behind the scenes to be able to help us move forward in a balanced way to be able to get this done. You played a critical role, as you always do, and will be greatly missed.

I appreciate your personal interest in hunger issues and promoting nutrition and healthy lifestyles for young people as well. We share a common interest in that as well. You have made it clear that you are fighting for Georgia always, but understanding the differences in agriculture and working to have something that is an important piece of policy that works for all parts of agriculture. You will be missed, and we are very, very grateful for your leadership.

Let me also mention—I feel like I should say "Secretary Johanns," our only member who is a former Secretary of Agriculture and actually began talking about conservation and ways to modernize and reform it before we ever did a farm bill back when you were Secretary. We took a lot of your ideas and put them into what we did, which I am very proud that we have a Conservation Title that is reformed and streamlined, and I appreciate your efforts. I very much appreciate all of your advocacy around conservation, Sodsaver, and, again, working for a balanced approach but moving us in reform, which I know is very, very important for you as well. Risk management, both your time as Secretary and on the Committee, you have been a big advocate of letting the market and risk management and so on. So we are going to miss you. You have been a very, very important part. I hope you will continue in some way, I hope all of our members leaving will continue in some way to be a part of helping us move forward to support and strengthen agriculture.

Let me finally just mention our newest member, Senator Walsh, who is no stranger to public service, and we thank you first for your incredible service in the Army National Guard and your service in Montana and your passion. One of the things I am proudest of in the farm bill is we actually have a new position and help for veterans who want to go back into farming, and we appreciate your fighting for Montana from day one, Montana agriculture, as well as all of the other issues you have been involved with. But you made it clear to me from the beginning what your focus was in terms of this Committee for Montana, and we are sorry to see you go. We appreciate all four of you.

So I will be happy to turn to Senator Cochran, if he would like to make any comments, but we did not want to let this last official meeting of the Agriculture Committee come and go without saluting tremendous leaders who have made a permanent impact in our country. So in a moment, I will call on Senator Grassley. I do not know if Senator Cochran would want to make a comment, but I certainly would welcome it.

STATEMENT OF HON. THAD COCHRAN, U.S. SENATOR FROM THE STATE OF MISSISSIPPI

Senator COCHRAN. Madam Chairman, I appreciate your continued leadership of our Committee. I want to join you in welcoming the Chairman of the Commodity Futures Trading Commission to this hearing. After being confirmed, I am sure he is off to a good start over there, organizing and pepping up the Commission so that we can be assured of the integrity of the process and the marketplace. We are happy to be able to have this opportunity to thank him for his service.

Chairwoman STABENOW. Thank you.

Senator Grassley?

STATEMENT OF HON. CHARLES GRASSLEY, U.S. SENATOR FROM THE STATE OF IOWA

Senator GRASSLEY. I appreciate the opportunity to say something about our retiring members. I have enjoyed working with them, and what I would like to do now is take an opportunity to say to each of them—I know Senator Harkin is not here, but Senator Harkin would believe I would say this anyway, and the other people that—and I hope I have said this to most every member I have served with when they have left. At least in recent years, I have tried to make a point of saying that to almost everybody. These colleagues after they leave the Senate, as long as I am in the Senate, they are always welcomed in my office, and I hope that they will call on us, whatever their life is after the Senate. I wish them well and have enjoyed serving with them.

Chairwoman STABENOW. Thank you very much.

Well, again, we appreciate it. One of the hallmarks of the Committee is our working together, and the four members that I mentioned—Senator Harkin, Senator Chambliss, Senator Johanns, and Senator Walsh—have been very, very important in that process.

Yes, Senator Hoeven?

STATEMENT OF HON. JOHN HOEVEN, U.S. SENATOR FROM THE STATE OF NORTH DAKOTA

Senator HOEVEN. Madam Chair, I would like to echo the comments of Senator Grassley and point out that to get a farm bill, we needed the North, we needed the South, and we needed the big "I" States, and these four represent the North, the South, and the big "I" States, and so obviously we could not have done a farm bill without them, and we are going to miss them a lot.

Thank you.

Chairwoman STABENOW. Thank you very much.

Any other comments? We will let everybody munch on their goodies and are counting on all of you coming back and being a part in some way of helping us as we move forward here. I do not want to think about the next farm bill because we are still implementing this one, but we have got a lot of work to do moving forward on implementation.

So let us now turn to the business before the Committee today, and we welcome Chairman Massad being back with us.

More than 6 years ago, our country was hit with the largest financial crisis since the Great Depression. Trillions of dollars of wealth evaporated almost overnight, devastating millions of families, leaving them unemployed, underwater, and unable to keep a roof over their head or food on the table. This crisis also caused Americans to seriously doubt our Government's ability to properly oversee all of the players in the increasingly complex global financial system.

Thankfully, we have come a long way since those dark days. We have had 59 straight months of job creation, and we are now creating jobs at a rate that we have not seen since the 1990s. But we still have a lot to do if people are going to have a real opportunity to get back to work and have the American Dream. There is more that needs to be done to ensure our financial markets are safe, transparent, and accountable.

In the wake of the crisis, the CFTC was given important new authority to more effectively oversee and regulate our derivatives markets. Unfortunately, this new authority did not come with new resources. For the past 4 years as Chair of the Committee, I have repeatedly stopped efforts to unwind protections for families and farmers and businesses.

I have made it also my priority to protect the integrity of financial reform and to secure the resources necessary for the Commission to enforce the law we passed in 2010.

Unfortunately, the omnibus released last night does neither. Because of that fact, I do not support the policy rider in the appropriations bill. This policy rider is masked by a meager increase in the CFTC's budget.

But that increase comes with conditions—handcuffs on the agency that Congress tasked with enforcing the law that Congress passed—in such a way that it represents what looks to me actually as a very serious cut.

Given that the funding levels are well below the President's budget request, this should serve as a bucket of very cold water to those of us who want reform in our financial markets.

Let me be clear: Dodd-Frank Wall Street reform is being undermined every day we underfund the agencies responsible for enforcing the law. That is clearly what is happening in the omnibus bill announced in the House yesterday. Failing to properly fund the Commission leaves our families, our farmers, and our businesses vulnerable to bad actors.

We all remember the mass fraud committed by Peregrine Financial and MF Global in 2011 and 2012. Billions of dollars in customers' funds went missing at just those two firms. How can we expect Americans to trust in our markets when all of this money in U.S. accounts simply disappears overnight?

Everyone benefits when our markets are safe and reliable. Financial institutions and end users benefit when our Nation's markets are recognized around the globe as being ultimately the most trusted in the world.

Since the Dodd-Frank Act was signed into law in 2010, the CFTC has been a leader among our financial regulators, completing almost all of its new Wall Street reform rules.

The Commission continues to show flexibility and improve on its earlier work to ensure that our commercial end users, energy firms, and agriculture producers are able to safely use derivatives markets to manage risk without undue burdens.

In just the past 3 months, the Commission has undertaken to resolve several end-user concerns—we appreciate that—including margin and recordkeeping requirements and relief for local, publicly owned utility companies.

Some of the most critical work lies ahead on rules that have serious consequences on all market participants. The Commission continues to work on the position limits rule, which I know has been a focus of the Chairman and the CFTC Commissioners. Whether it is paying for gas at the pump or providing food to feed our families, when these markets do not work, consumers feel the pain.

The CFTC's Enforcement Division, despite limited resources, also continues to work hard to keep our derivatives markets safe from fraud and abuse. Their numbers continue to prove it.

In the past fiscal year, the CFTC collected over $3 billion in monetary penalties against companies across the country.

The Commission also took a hard stance on the manipulation of foreign currency benchmarks, issuing orders that cost unlawful companies over a billion dollars. This is a success given the difficulty and the resources needed to successfully investigate and close a case of this scale.

Despite the recent successes, the Commission has much work to do in 2015 and beyond.

While we discuss the need to give CFTC resources to effectively enforce its responsibilities here at home, we must also be considering resources needed to take on cybersecurity attacks and global threats.

The Commission must have the resources needed to effectively examine clearinghouses and exchanges to keep U.S. markets from being at risk to broader threats.

We look forward to the Chairman's report on yesterday's meeting of the CFTC's Agricultural Advisory Committee, a Committee obviously very important to all the members of this Committee. I was

pleased to see Secretary Vilsack in attendance to address the state of the agriculture economy.

These are considerations that the Commission must focus on as the markets continue to grow and change and market participants continue to get comfortable with the new model of derivatives regulation.

With the right enforcement and resources, I am confident the CFTC will create stronger, more transparent markets.

I would turn to my Ranking Member, Senator Cochran, if he would like to add anything.

Senator COCHRAN. Madam Chair, only to ask unanimous consent that my full statement welcoming our distinguished witness and challenging our Committee to do its job of oversight, as you are leading us, and I thank you for that. I am happy to yield to others—we have a big crowd here—to get their questions in, so I will withhold any questions until later

[The prepared statement of Senator Cochran can be found on page 35 in the appendix.]

Chairwoman STABENOW. Thank you very much, and we will now turn to our first and only witness this morning, Chairman Timothy Massad, who we all know. The Committee held a nomination hearing in March of this year, followed by confirmation in early June. We very much appreciate your coming back before the Committee. We, of course, welcome your public statements, anything for the record as well, and then we will open it for questions. Thank you.

STATEMENT OF THE HONORABLE TIMOTHY G. MASSAD, CHAIRMAN, COMMODITY FUTURES TRADING COMMISSION, WASHINGTON, DC

Mr. MASSAD. Thank you, Chairwoman Stabenow, Ranking Member Cochran, and members of the Committee. I am pleased to testify before you today on behalf of the Commission. I appreciate the opportunities I have had to meet with many of you, and I look forward to this Committee's continued input.

Let me also add my thanks and recognition to the retiring members—Senators Harkin, Chambliss, Johanns, and Walsh. It has been a pleasure working with you.

I also want to thank you, Chairwoman Stabenow, for your leadership of this Committee and your advice and counsel. I look forward to continuing to work with you, and, of course, I look forward to working with Senator Roberts as the new Chair.

In June of this year, two of the other Commissioners and I took office, and the last 6 months have been a busy and productive time for us. I want to thank my fellow Commissioners, all of whom are extremely dedicated and bring good experience and judgment to the table.

Chairwoman Stabenow, I think you really said it best in terms of the importance of the additional responsibilities we were given in light of the crisis, which was the worst financial crisis this country has experienced. In my written testimony, I discuss our work in implementing those new responsibilities to regulate the swaps market.

We have been just as focused on our traditional areas of responsibility: the futures and options markets. These markets cover

many diverse products today, and as they had their origins in agricultural products, and those remain very important to our work. Just yesterday, we did have a very productive meeting of our Agricultural Advisory Committee, of which I am the sponsor.

We were honored to have Secretary Vilsack join us to discuss the state of the agricultural economy. It was an excellent opportunity to gather input directly from farmers, ranchers, and others who rely on these markets day in and day out.

As the Committee knows, Title VII of the Dodd-Frank Act was a response to the part swaps played in the worst financial crisis since the Great Depression. The CFTC was given primary regulatory responsibility for bringing this market out of the shadows. Thanks to the agency's hard-working professional staff, we have made substantial progress in implementing these reforms.

Today swaps transactions are being cleared and reported. We have increased oversight of key market participants. Trading of swaps on regulated platforms is increasing, and transparency and strong risk management are being achieved.

But in all of these areas, there is more work to do. For the last 6 months, we have made it a priority to review our roles, particularly to address some of the concerns of commercial end users.

To that end, the Commission has taken a number of actions designed to make sure that our markets work well for the manufacturers, farmers, ranchers, and other businesses that rely on these markets to hedge commercial risk.

This includes matters related to margin and the posting of collateral, reporting and recordkeeping, forward contracts, and other areas. We have been listening carefully to market participants and working with them to make sure the rules work.

We are also working on the few Dodd-Frank rules that remain to be finalized, including the position limits rule and a margin rule for un-cleared swaps that, consistent with congressional intent, exempts end users.

In all this, a priority is working with our international counterparts to build a strong global regulatory framework. We are currently working with our international colleagues in particular on clearinghouse recognition and regulation, an issue that concerns the futures and options market just as much as the swaps market.

We are also very focused on data collection and analysis and swaps trading issues, and cybersecurity, which is perhaps the single most important new risk to financial stability, is also a priority.

We are also monitoring developing issues, including the increasing use of automated trading strategies and virtual currencies like bitcoin.

We continue to maintain a strong compliance and enforcement program. Robust enforcement is crucial to the integrity of our markets. Most recently, we ordered five of the world's largest banks to pay $1.5 billion in fines and take remedial actions because they attempted to manipulate foreign exchange rate benchmarks.

In all of these areas, there is much more we could and should be doing, but we simply are not able to do so, to do as much as I believe the American public deserves because of resource constraints. We are fortunate to have a dedicated professional staff,

and we will do all we can with what we have. But our current budget significantly limits our ability to respond.

We are grateful that the omnibus currently being considered would provide an increase, but I am convinced the need is far greater than that.

Although this would start to address some of the very dire needs we have, without additional resources our markets cannot be as well supervised, customers cannot be as well protected, our technology cannot keep up, and market transparency cannot be as fully achieved.

The United States has the best financial markets in the world, the most dynamic, innovative, competitive, and transparent. They have been an engine of our economic growth and prosperity. Good regulation is necessary to keep them that way, regulation that ensures integrity and transparency and creates the foundation for the markets to thrive.

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

[The prepared statement of Mr. Massad can be found on page 36 in the appendix.]

Chairwoman STABENOW. Thank you very much.

First let me ask a follow-on as it concerns resources. One of the most frustrating challenges that market participants face is regulatory uncertainty, and a common complaint I hear relates to registration and compliance delays. Given the CFTC's new responsibilities regulating the swaps market and considering the growth of the futures and options markets, does the Commission have the needed resources to provide regulatory certainty to meet deadlines?

Mr. MASSAD. Thank you, Chairwoman Stabenow, for the question. It is very, very difficult. We are stretched in so many areas. We have over 100 applications from swap dealers that are simply provisionally registered that we need to get through.

We have 22 applications for swap execution facilities that, again, are just temporarily registered. We have a variety of other applications pending.

We are stretched in all these areas. We cannot respond in the timely and thorough manner that we need to do our job well, and that includes not just registrations and applications. But, of course, whenever industry has an issue with how our rules are working, we would like to be able to be very responsive, to look into it quickly, but it is simply very, very challenging with the resources we have.

Chairwoman STABENOW. Thank you. On a different note, 2 weeks ago my colleague from Michigan and friend, Senator Levin, held a 2-day investigative hearing regarding the relationship between banks and commodity ownership, and a significant part of that focused on aluminum prices in the London Metal Exchange. I asked the CFTC over a year ago to report on its authority to regulate the LME, and in December of 2013, you responded, confirming that the CFTC has authority and stated that the LME's foreign board of trade registration was pending.

Can you provide an update on LME's registration status and what the Commission is currently doing to resolve this aluminum issue with its current authority?

Mr. MASSAD. Certainly, Senator. Thank you for the question, and I share your concern about this situation. I have also visited with Senator Levin about it. It is an issue that we are paying a lot of attention to.

Let me just say I have personally met with the Aluminum Users Group, I have met with the LME and their regulator in the U.K., and we are watching this very, very closely. The LME has proposed some reforms. We are looking at how those work as they implement them, and we are looking at whether more is needed.

With respect to our authority, we have indirect authority, given their FBOT application, but their primary regulator is in the U.K., and the contract is one regulated by the U.K. We do not have direct jurisdiction over the warehouses which are at issue here. But I can assure you that we will continue to follow this situation very closely and engage with the LME, the U.K. authorities, and the aluminum users and work toward resolving this problem.

Chairwoman STABENOW. So you are speaking about indirect authority.

Mr. MASSAD. Yes.

Chairwoman STABENOW. But from the American interest standpoint, do you think at this point that you have enough authority to prevent fraud and manipulation of commodity prices?

Mr. MASSAD. Well, we always have the authority to go after fraud and manipulation in the markets, and so we are very mindful of that, and we will use that authority anywhere we can. As I say, in this case, what is going on in part is the LME is looking at trying to reform some of its warehouse arrangements. We are hopeful that can help address this problem, but we will continue to look at whether additional actions are needed if those reforms do not work.

Chairwoman STABENOW. Back to talking about resources, the Commission has recently been very successful, as you said, in closing benchmark manipulation enforcement cases, including benchmarks like foreign exchange and LIBOR which have affected everything from home mortgages to student loans. Can you discuss just a little bit more about the amount of resources and technology that is needed to bring these types of cases?

Mr. MASSAD. It is very challenging. You know, in the foreign exchange benchmark case, we were negotiating with a number of banks. We issued orders with respect to five. We had to have separate teams working on each of those. These are very intensive investigations to look at all the e-mails and all the documents and look at the market practices here. So, again, we are very stretched.

Now, we are also at the same time pursuing all sorts of other matters in our Enforcement Division, whether it is traditional Ponzi schemes or commodity pool fraud, precious metal scams that we have seen a lot of against retirees, spoofing, and other sorts of more sophisticated types of fraud that we are seeing now that our markets are becoming increasingly electronic.

But it is essentially a triage operation. We simply do not have the resources to go after all the things that we should be going after and that would enhance the integrity and strength of our markets. That is why I think additional resources are such a good investment for our economy and for the American people.

Chairwoman STABENOW. Thank you. I could not agree more.

Senator Cochran?

Senator COCHRAN. Let me ask you in reference to the last comments you made, what is your impression of what a fair level of appropriation would be to maintain the staffing and the quality of the staff that is necessary to restore morale at the Commission?

Mr. MASSAD. Well, the President's most recent budget request was for $280 million. I think that was entirely justified, and we are looking with respect to fiscal year 2016 as well.

Again, we are just stretched in all areas. Our markets, our responsibilities were so greatly increased by Dodd-Frank. The swaps market, it depends on how you measure it, but people will say it's a $600 trillion market, in many ways much bigger than the futures market. The complexity of these markets is great. The technology that drives these markets is so important. Things like cybersecurity is such a big risk to our markets. We simply do not have the resources to be examining critical infrastructure such as our clearinghouses and exchanges frequently enough on issues like cybersecurity. So it is just a real challenge for us.

Senator COCHRAN. Well, thank you very much.

Chairwoman STABENOW. Thank you.

Senator Brown is next on the list, but I do not—at this point, unless he appears in 2 seconds, we shall move on.

Let me also say it is wonderful to see so many colleagues here, and we will ask everyone to be mindful of the 5-minute rule. So at this point, Senator Walsh—and Senator Walsh is also not here, so we move on to Senator Bennet.

Senator BENNET. Thank you, Madam Chair. It is nice to be recognized no matter how hard you try to get somebody else to talk.

[Laughter.]

Senator BENNET. Chairman Massad, it is great to see you again. I want the Committee to know that I appreciate very much your help a number of years ago drafting what became the "Pay It Back Act" that made sure that the money that came back from TARP was actually used for deficit, not spent again, and I want to thank you for your help with that.

I was pleased to see in your written testimony that 70 percent of the transactions you regulate are being cleared today compared to 15 percent in 2007. When we worked on Dodd-Frank, we wanted to ensure that the clearinghouses themselves did not become a source of systemic risk.

Could you share with the Committee your sense of just how concentrated the clearing process has become? Are the majority of these transactions occurring through many clearinghouses or just a few? How many clearinghouses are there? I will submit my other questions for the record and yield to my friend, or however you want to do it.

Chairwoman STABENOW. Well, go right ahead, and we will just go back and forth.

Senator BENNET. All right, Mr. Chairman. So that is the question. We did not want the clearinghouses to become a systemic risk. How are things going?

Mr. MASSAD. Senator, that is an excellent question, and I share your concern about clearinghouse risk. It is something that we

need to be paying a lot of attention to; we are paying a lot of attention to it. You know, the mandate that we clear a lot of these transactions I think was a very, very good policy decision. It does allow us, clearinghouses do allow us to monitor and mitigate the risk of these bilateral transactions much better, but they do not eliminate the risk. We have to be very vigilant with respect to CCP risk, and we are focusing on that quite a bit in terms of looking at financial resources that they have, managerial/operational resources. There are systems for margining and measuring the risk, cybersecurity, as I alluded to before.

You asked about the concentration. Most swaps are cleared in just a couple of clearinghouses, and this also goes to our cross-border issues where I have worked very hard with the Europeans on working out a good arrangement on clearinghouse supervision because some of the main clearinghouses are in Europe, and a lot of our transactions are cleared over there.

Senator BENNET. So how would you evaluate the systemic risk?

Mr. MASSAD. Well, again, I think it was the right thing to do to mandate clearing, but we have got to be constantly vigilant on the issue of clearinghouse strength and stability.

Senator BENNET. Is there any evidence—you mentioned your discussions with your European markets. Is there any evidence to indicate that the swap transactions are migrating to less regulated markets than our own?

Mr. MASSAD. Well, in terms of the clearing, a lot of it is happening in a couple of clearinghouses, one in particular in Europe. We are working very closely with the Europeans to make sure we have a good system of regulation, and I think we will land in a good place there.

The other thing I would say about the overall risk is I am working very closely with the Federal Reserve on these questions, too, since we have designated a couple of the clearinghouses as systemically important. That means the Fed does have certain interests here as well. Governor Powell and I in particular maintain a constant dialogue on these issues.

Senator BENNET. Okay. Thank you, Madam Chair.

Chairwoman STABENOW. Thank you very much.

Senator Roberts? Then we will come back to Senator Brown.

Senator ROBERTS. I would be more than happy, Madam Chairman, to yield to my good friend.

Senator BROWN. I have got no more important schedule than the rest of you.

[Laughter.]

Senator BROWN. That is really kind of you. You are going to be the Chairman.

Senator ROBERTS. Well, you are going to have more time since you got off the Ethics Committee, which I bitterly oppose.

[Laughter.]

Senator BROWN. The word is out.

Senator ROBERTS. The word is out. I am sorry. That is all classified. But everything else in the world is not classified now, so it does not make any difference.

Chairwoman STABENOW. All right. Now that you have used your time, we will move on——

[Laughter.]

Chairwoman STABENOW. We will start the clock again. Senator Roberts?

Senator ROBERTS. Madam Chair, I want to thank you for your hard work, your dedication, and your passion for agriculture. If there is a synonym for "perseverance," it has to be "Debbie Stabenow," and I truly want to thank you for that and am looking forward to working with you and also the CFTC. Mr. Chairman, thank you for coming.

I have got quite a bit of commentary here about Dodd-Frank-Bennet—what happened——

Chairwoman STABENOW. He is leaving.

Senator ROBERTS. He just left. I would, too. At any rate, on the regulatory framework that the Commission has created after Dodd-Frank, we made some progress. I call that "low-hanging fruit," so I have some others a little higher up on the branches, but I want to get right to the questions.

Are you worried about the significant number of small and medium-sized future commission merchants—those are the folks that help the farmers and ranchers, the FCMs—which primarily serve agricultural producers that are closing and consolidating? I would point out that 10 years ago, in 2003–04, we had 102; now we have 69. That is a 30-percent reduction. Any comments?

Mr. MASSAD. Thank you for the question, Senator. I share your concern about this. We want to make sure we have a very strong and diverse futures commission merchants sector so that the smaller players can continue to operate effectively and serve their customers.

We have seen concentration. I think it is driven by a number of things. One of them is a very low interest rate environment since a lot of these firms make some of their money on the interest on the funds that they hold.

In terms of our regulation, we have certainly been mindful of this. Recently we proposed amendments to one of our rules that I think will help some of the smaller FCMs in terms of the residual interest issue, and I would be happy to work with you on this because we are——

Senator ROBERTS. Well, I appreciate that. I do not mean to interrupt here, but we are going to be on a time schedule here, and I apologize for doing that.

Mr. MASSAD. Sure.

Senator ROBERTS. Thank you for taking a second look at several of the consumer protection rules. I want to point out that Senator Heitkamp and I introduced legislation so farmers and ranchers would be certain that this would not occur at any point in the future.

I am talking about basically the automatic change in how future commission merchants collect residual interest. But you are studying it after, I think, we have solved it. You are studying it. I would just as soon use that very scarce money for something else if, in fact, we fixed it.

Basically, I wanted to ask you about 140 staff-issued no-action letters that delayed or replaced rulemakings by the Commission. These were issued with little or no oversight and zero trans-

parency. Come to think of it, Madam Chair, I think this is a discussion that we probably ought to have, that this is going to take a little while, I think, in regards to time. But I am very concerned about the no-action letters. Sometimes they work to our favor; sometimes they do not. Many of them just are not—I do not think the members of the Commission are aware of them.

Are you also worried that foreign businesses are choosing to relocate their businesses and capital away from the United States markets?

Mr. MASSAD. Senator, I am very mindful of the cross-border issues, but I think we are working on them, and we are making good progress. I think it is important to remember that we started with a market that was entirely unregulated and that was global.

It is also a highly mobile market. This Congress made the policy decisions—I think they were good ones—that we bring this market out of the shadows, and that was consistent with the commitments of the G–20 nations. But all of these nations are moving at different paces. They all have their own political process and regulatory traditions.

We were first in a lot of ways, which is a good thing, in terms of implementing these rules, and we are working with other jurisdictions to harmonize things, and I think we will get there.

So I think we are addressing the concern, but we are very mindful of it.

Senator ROBERTS. Chairperson Stabenow mentioned the budget. I just want to point out that the CFTC's budget has already seen a 27-percent increase since fiscal year 2010. That is up from $169 million to 215. The new omnibus will add another 16 percent to $250 million.

That is about a 50 percent increase to 2010. I know the CFTC is faced with many new issues, many new challenges. Almost any regulatory agency that we have is in the same boat. But that is a 50-percent increase. Somehow or other we are going to have to learn to live within our means. We are going to try to be as helpful as we possibly can. But I simply wanted to point that out.

For the first time in a long time, I am yielding back with 20—no, I am not. I am 24 seconds in the red. I apologize.

Chairwoman STABENOW. Thank you very much.

Senator Brown?

Senator BROWN. Thank you. Thank you, Madam Chair, and thank you, Senator Roberts. Thanks for the work you have done on this Committee, especially with CFTC and financial rules and enforcing and oversight.

I think a number of us are not happy with how the appropriations process this year is, particularly with potential repeal of the 716 provision, a provision written in this Committee by one of your predecessors, the Chairwoman from Arkansas, on financial regulations and derivatives.

Clearly doing that through the appropriations process rather than this Committee undermines this Committee and also undoubtedly puts taxpayers at risk, something that I would think we would have learned that lesson, so that is unfortunate.

Let me follow up on something that the Chairwoman mentioned, the discussion, Mr. Chairman, of the banks' involvement in phys-

ical commodities, particularly aluminum. Your predecessor told me that CFTC "has clear authority to address fraud, manipulation, and other abuses in the aluminum market." Another Senator from Michigan has had a number of hearings in his oversight committee. I have had a couple of hearings in the Banking Committee on this issue of manipulation in aluminum and oil tankers and electricity generation and other things.

Chairman Gensler specifically cited CFTC's authority over foreign boards of trade, but in an October letter and today's testimony, you say that your authority there is limited.

My first question is: Who is right—Chairman Gensler or you?

Mr. MASSAD. I agree with Chairman Gensler's statements. I do not think mine are inconsistent, Senator. We do have authority over fraud and manipulation. We also have authority with respect to their FBOT status, but that is a different status than our own, than for direct registrants. My comments earlier were simply meant to underscore that we take this issue very, very seriously. We are looking at it in a number of ways, and we will continue to do so and continue to work on it. I know it is a concern. I know it is a concern of yours with respect to the queues that we are seeing in these aluminum warehouses.

As to the issue of banks' ownership, also, as I have said before, I think the issue of whether banks should even be in some of these businesses is an important one for us to consider. It is not under our jurisdiction, but I have always said I would be happy to help the banking regulators—

Senator BROWN. Good. Whatever is in your jurisdiction, time really is of the essence here. The Levin report recently said that Goldman's activity in aluminum—this is just narrowly aluminum—"raises troubling issues involving conflicts of interest, market distortions, and the potential to gain unfair trading advantages."

You can see that if there is a huge oil spill with billions of dollars of liability, what that can do to the stability of the financial markets if owned by one of the large banks. You can see that even though they say there is a wall between the trading desks and the information gleaned from their ownership of energy markets, part of the energy markets, there may be a wall, but somewhere at the top of that firm somebody knows something—knows everything about both sides of that wall.

So the trading desk may be walled off from the ownership decisions, but in the end they are not, and that causes a clearly unfair market—clearly causes unfair market advantages for a bank versus others in the real economy.

So I hope you will be as aggressive as you can be there.

Let me ask one more question, Madam Chair, if I could.

Chairwoman STABENOW. Sure.

Senator BROWN. The need for CFTC's cross-border swaps rules, clearly you were speaking to Senator Roberts at it a minute ago, from Long Term Capital Management in 1998 to AIG to JPMorgan's London whale just a couple years ago. Five of my colleagues in 2013 joined me in warning that banks would "de-guarantee affiliates in order to opt out of CFTC rules." To no one's surprise, they did just that. In September, you said you were con-

sulting with bank regulators on the risks that de-guaranteeing would pose to our whole financial system.

Tell me what specifically you are doing to protect the U.S. financial system and taxpayers from risks in the foreign offices of U.S. banks. Will you make the results of this review public?

Mr. MASSAD. Thank you for the question, Senator. We are very concerned about this. Shortly after I got into office, I asked our staff to look into this, examine it, ask the banks a number of questions.

We got some answers from that. We have shared those with the banking regulators, and I am happy to talk about that. Basically a number of these banks have de-guaranteed a lot of their swaps. I think the question, though, is: Is there still a risk posed when you have an unguaranteed offshore affiliate engaging in these transactions?

Now, it may comply with our rules, but because it is still part of that overall banking enterprise, the bank holding company, I think it is a question for us, for the prudential regulators to think about. That is why I took the action of sharing what we are doing with the banking regulators, and we are engaging with them on that.

Senator BROWN. Thank you.

Chairwoman STABENOW. Thank you very much.

Now we will move to Senator Boozman. Again, happy birthday. Oh, excuse me. I had Senator—did you wish to defer?

Senator BOOZMAN. Well, I think he was here first.

Senator JOHANNS. I think we walked in together.

Chairwoman STABENOW. Well, if you would like to defer to Senator Johanns, that—this is the day of people deferring to other people to speak. I apologize. On the list here, Senator Boozman——

Senator JOHANNS. That is all right.

Chairwoman STABENOW. Senator Johanns.

Senator JOHANNS. I think it was a tie, actually.

Let me start off, Madam Chair, and offer a couple of things. One is my appreciation for the way you have handled this Committee.

I have seen you work the floor, if you will, and I could observe my opinion was as valued as the opinion of anybody on your side of the aisle. I think we all knew that, and we all appreciated that immensely.

The second thing I would say is this is, I think, one of those committees here in the Senate where you just leave your party registration at the door. We worked to solve problems and pass farm bills, do a lot of good things for the country, and that is what has made this Committee so enjoyable.

I am going to miss it, and it is somehow appropriate that my last Committee hearing as a United States Senator is in Agriculture. I have always said that for me working on agriculture, any day is a good day. So it is great to be here.

Mr. Chairman, I will offer an observation on capital, but I really want to talk to you about position limits. The cross-border issues, as you know, are real. I have been talking about the cross-border issues since the idea of Dodd-Frank first came about in my role as a member of the Banking Committee and my role here.

My observation over the years is that capital tends to flow to the areas of least resistance from a regulatory standpoint. You know, I remember as a mayor when we were in competition with the city across the State line, we would offer to fast-track permits and do a whole bunch of things. That regulatory atmosphere had a huge impact on the decision making. The same way when I was Secretary of Agriculture, same way when I was Governor of Nebraska.

So I just offer to you we cannot pass laws that bind Singapore or London. We can ask for their cooperation. We can plead for their cooperation. We can do other things. But at the end of the day, I think in an atmosphere of overregulation, we are always going to lose. That is just the unfortunate reality we are dealing with. So I think it is incumbent upon you to tell us when we are overdoing it, when we have gone too far.

Now, if I do not jump into position limits, we are not going to get there, because we could have a huge conversation, and I would welcome that, but maybe not in this Committee here.

Mr. MASSAD. I would be happy to try to address it briefly, Senator. I share your concern that we have to look at this as a global market, that capital is highly mobile. We also have our responsibilities under the law to implement the reforms, and Congress has made it very clear. They gave us deadlines to do that, and that I think has created a situation where we moved faster than other jurisdictions.

But I am very committed to trying to work this out, and I think we are getting there. I view it as a glass half full. It will take time. It is not going to happen overnight, but I think we are making good progress. We have a new Commissioner in Europe, Lord Hill, who has taken over. He and I are off to a good start. I have had a lot of meetings.

I have been overseas three times on a number of these issues and met with my international counterparts here. There is work going on a lot of fronts to try to harmonize rules.

Senator JOHANNS. Let me shift to position limits before I run out of time here. I appreciate the fact that you have the Agricultural Advisory Committee up and running. Thank you for that. I think that is important, very, very important.

One of the issues—and I think it was yesterday that you had the group together. One of the issues raised probably by a lot of industries, but I will focus specifically on the cattle industry, is the whole issue of position limits. They need liquidity in the marketplace. They need to be able to manage their risk. They worry that the proposed rules are going to damage their ability in the arena of managing risk. You have heard all of this, I am sure.

Explain to us, if you would, where are they right and where do you think they are missing the point? I have heard from both Nebraska cattlemen and national cattlemen on this, and like I said, I suspect you have, too. In fact, I have had copies of the letters sent to your attention. Where are they right and where are they wrong?

Mr. MASSAD. Thank you for the question, Senator. I think we are very mindful of their comments, and as to where they are right and where they are wrong, I guess I would answer in the following way: Position limits are a very important tool in the toolkit to address

excessive speculation, but at the same time, we have to make sure we allow bona fide hedging.

The question is: How do you draw the bright lines that distinguish between true bona fide hedging by commercial players versus what speculators might do? We do not have the resources, we will never have the resources to look at facts and circumstances of every transaction, to look at intent.

So the challenge for us is trying to write bright-line rules in an area that is very complicated so that we allow what is really legitimate hedging versus excessive speculation.

Senator JOHANNS. Madam Chair, thank you. I am out of time.

Chairwoman STABENOW. Thank you very much.

Senator Boozman? Oh, excuse me. You know what? Actually, I was so intent on getting you back in order that I am missing my side of the table, so I am going to retract that. I was trying to get back to you, and I apologize because it is actually Senator Casey's turn.

Senator CASEY. Madam Chair, thanks very much, and I first want to commend your work leading this Committee and your efforts on an ongoing basis, as Senator Johanns noted, to be collaborative on both sides of the aisle. We are grateful for that and your team who made that possible. We are looking forward to a new session of Congress under new leadership, but we are certainly going to miss your leadership. We appreciate that.

Mr. Chairman, I wanted to walk through maybe one fundamental issue, but before that, I do want to touch on the issue of resources. When I was the auditor general of my State, my main job was to audit hundreds and hundreds of State agencies, and we would often conduct financial audits which were kind of routine, but it was a way to discharge the responsibility to be a watchdog. We also did a lot of performance audits where we looked at results and effectiveness.

I was very critical of agencies across the board when they misspent money, when they were not getting the job done, so I think I have pretty good credentials on the "spend taxpayer dollars wisely" concerns that people have. I do think, though, that you need more resources. We were told this morning—and I know this is by way of repetition, maybe—that the omnibus we are considering now would fund CFTC at $250 million, we are told, which would be $30 million below the President's request. I am troubled, more than troubled by that. I am concerned about that, especially in the context of what happened, the prelude of the foundation of the Great Recession and what you and your agency can do to prevent the next Great Recession, God forbid. I believe resources are part of it, so I will be one of many people arguing for the next number of months and years to give you the resources you need.

One of the reasons you need resources is because of enforcement. It is not something new but something that I know has been a priority for you. I am told that in fiscal year 2014 CFTC imposed $3.3 billion in monetary sanctions, almost double the previous record total from fiscal year 2013 of $1.7 billion. I just want to ask you, let us set aside the resource question for now, important though it is: What are the factors driving that increase in the monetary sanctions?

Mr. MASSAD. Well, it is really, Senator, a question or an issue of the fact that there are a lot of things that we are going after. Unfortunately, there is still a lot of fraud out there. You know, a big part of it was the foreign exchange benchmark case. We are continuing to see attempted manipulation with respect to benchmarks, and it is so important that we continue to address that. We addressed it previously with respect to LIBOR. But this will be ongoing.

At the same time, it is compromised, that number is compromised of a lot of smaller actions. We had a number of cases with respect to precious metal frauds. We had a number of—each year we have a number of Ponzi schemes that we go after.

Again, the challenge for us is we simply do not have the resources to go after all the things that we would like to go after, and you are constantly making choices about whether you even investigate something or how far you carry that investigation.

Senator CASEY. Well, I would hope that more of us would be—even as we are advocates for greater resources in the context of law enforcement, for police and other law enforcement across the country, in the world of the markets, in the world of making sure that folks do the right thing in that context, we hope we can continue to provide the resources so that you can be the cop on the beat in this world that we hope you could be.

Lastly, I will just make a comment, and if you want to follow up, you could, and you can do it more extensively in writing. The efforts you have undertaken—I know you still have a ways to go, but the efforts you have undertaken to focus on some regulatory relief for end users, in our State, like a lot of States here, that becomes important to folks in a whole range of different industries, steel being one, often any manufacturing-based industries. So we appreciate that effort.

I know it is difficult to manage when you have new legislation, new regulations to be able to calibrate that, but we are grateful for your efforts.

Mr. MASSAD. Yes, well, thank you, Senator, for that. I am very committed to that. My focus is very much the following: Our task is not simply to implement this regulatory framework and bring the swaps market out of the shadows, continue to oversee the futures and options markets, but to do so in a way that allows these markets to thrive. That means making sure that these markets continue to work effectively and efficiently for end users. That is why we have tried to be very responsive to their concerns.

Again, it does come back to resources. You know, we want to be able to respond as quickly as possible and look into these things and study them and then take the appropriate action. So we are hopeful that we can do all we can in this area.

Senator CASEY. Thank you. I appreciate it.

Thank you, Madam Chair.

Chairwoman STABENOW. Thank you very much.

Finally, Senator Boozman.

Senator BOOZMAN. Thank you Madam Chair, and I want to echo the comments of the rest of the Committee about enjoying working with you and how you have always been very, very open, always willing to listen, and really do your best to solve the problems that

we have. Also your staff, they have done a tremendous job likewise working with our staff, working with myself. So thank you very much.

Mr. Chairman, I also have concerns about the commercial end users, and I know that you have had several questions in that regard. In regard to agriculture, can you talk a little bit about the Agricultural Advisory Committee, if that is going to be a help in that regard of trying to sort some of these things out?

Mr. MASSAD. Absolutely, Senator. Thank you for the question. You know, I am sponsoring that committee because I recognize the importance of the agricultural products in our markets, and I think the committee is a very, very helpful way for us to get input. All of our advisory committees are, and let me just say that the other Commissioners I think are equally committed to using the advisory committees to get good input from market participants.

We had an excellent meeting yesterday. Not only did Secretary Vilsack come and share his thoughts, but we had a good discussion of some of the issues related to position limits, to residual interest, and we will continue to do that and continue to get input, not just through the committee but separately in other meetings. I have made it very clear that my door is open. I will try to meet with people as much as I can to hear their concerns. We have acted on things. We acted on the residual interest issue. We have acted on some reporting and recordkeeping issues that I know were of concern to agricultural interests. The margin rule exempts end users. We will continue to take these sorts of actions.

Senator BOOZMAN. Good. Very good.

In regard to the morale issue, I know that you feel like a situation of maybe not getting the funding that you need. What other areas are out there? What can the Committee help you with in regard to that particular area?

Mr. MASSAD. I am sorry. To the funding?

Senator BOOZMAN. To the morale issue. Funding is one thing, but it goes beyond that. Again, what can we do to help?

Mr. MASSAD. I appreciate the concern. Let me say on the morale issue I think there are probably a number of historical reasons that have affected that. We recently had some feedback on that was done from a survey done in April.

My view of it is the following: that we start from there, we are going to address it. I think a lot of it is just making sure that people understand the mission, they understand how their work is connected to the mission, and they have sufficient opportunity for input.

Obviously the funding issue has been a big one. The sequestration and furloughs were important. But we will address this. I am already seeing some changes.

I appreciate your offer in terms of the Committee's help. Let me give that some thought, but certainly the fact that this Committee does act, as a number of members have said, in a bipartisan fashion and has shown great interest and support for our issues, and obviously your support and increasing our funding, all those things will help.

Senator BOOZMAN. I was going to ask you about your priorities, but you mentioned that right at the very top is the cybersecurity issue.

Mr. MASSAD. Yes, absolutely.

Senator BOOZMAN. That is such an important issue not only for you but the rest of Government. I am almost thinking out loud in asking the question, but do we do that independently? Does your agency do that as an agency and somebody else in a similar situation do that? How do we address this? Talking about funding, there is a finite amount of money to go around. How can we be efficient in solving this huge task that really is the problem of the day?

Mr. MASSAD. That is an excellent question, Senator. I think there is actually a lot of coordination going on among Government agencies. I attended earlier this week a meeting that Treasury Deputy Secretary Raskin holds periodically of a number of the financial regulators to talk about cybersecurity. There is a number of vehicles that have been set up to share information, share ideas, coordinate action.

I am actively coordinating with the Federal Reserve on this, given their interest. Governor Powell and I have met, and our teams have met. Their staff has participated in some of our reviews.

So I think we will continue to coordinate this, and I could not agree with you more as to the importance of this issue. It is clearly an issue that we have to be devoting a lot of attention to.

Senator BOOZMAN. Good. Thank you, Madam Chair.

Chairwoman STABENOW. Thank you very much.

Senator Donnelly?

Senator DONNELLY. Thank you, Madam Chair. I also want to say thank you for your leadership on the Committee, how privileged I felt to be a part of this, how devoted you have been to the ag community in my State and to the whole country, and your staff as well. Thank you very, very much.

Mr. Chairman, good to see you again, sir. As you know, I have had concerns about excessive speculation and its effect on increasing prices for working families for various products. The last time you were here, I asked about finalizing a good position limits rule in a timely manner.

We recently extended the comment period, and I understand that. I understand the need to get this right. But what I am trying to understand is, Are we still committed to finalizing a good position limits rule in a timely manner?

Mr. MASSAD. Absolutely, Senator. Thank you for the question.

What we did on the comment period was simply the following: We had the Agricultural Advisory Committee meeting. As we talked to members about what they wanted to talk about, the issue of deliverable supply came up, and so we decided that we would have some conversation about that.

Simply as a matter of good Government practice—we were not required to do this, but we felt that if that is going to be discussed at the Agricultural Advisory Committee, then it is only fair to open up the comment period on that part of the rule, just on those issues. That will not slow us down. There is a lot of other work——

Senator DONNELLY. So we are making progress.

Mr. MASSAD. Absolutely. There is a lot of other work. This is a very complicated rule. There are a lot of issues. We have received a lot of input. But we are proceeding on multiple tracks here.

Senator DONNELLY. One other thing I wanted to mention is I wanted to thank you for the CFTC's work to create a level playing field between public and investor-owned utilities. The efforts that have been made to make sure that we have a rule that levels the playing field have been extraordinary helpful. We will continue to work on the legislative side, but our municipal utilities are now less likely to be exposed to greater risks, less likely to be exposed to increased prices which are passed on to our families. I just wanted to thank you for your hard work on that.

Mr. MASSAD. Certainly.

Senator DONNELLY. Thank you, Madam Chair.

Chairwoman STABENOW. Thank you very much.

Senator Thune?

Senator THUNE. Thank you, Madam Chair, and thank you for your leadership of this fine Committee and the hard work that we have accomplished here in the last couple years. Hopefully there will be some more to come, and we can get something done on this next year.

But thank you for your leadership, and thank you and Senator Cochran for having the hearing today as we kind of wrap up this year's Congress and look at next year's priorities. I think the Commodities Exchange Act reauthorization will be one of many pieces of legislation that we are going to have to consider.

I want to mention one area of concern which we have discussed before on this Committee, and that has to do with staff guidance letters that are not subject to the Administrative Procedures Act and its mandatory cost-benefit analysis requirements.

The letters have the same regulatory effect as rulemaking. I also want to mention no-action letters, which has been referred to earlier, which are used to amend or withdraw new rules, and I would encourage you, Mr. Chairman, to take a more measured and conventional approach to issuing regulatory guidance.

Commodity futures trading continues to become increasingly important to the agricultural community, especially in States like my home State of South Dakota, with agriculture as its number one industry, and because of currently lower commodity prices, managing risk is even more important to our farmers and ranchers, grain elevators, cooperatives, and suppliers who utilize the trading tools under the jurisdiction of the CFTC to better manage their risk.

I appreciate you being here today and hope you will continue to put that appropriate focus on agriculture.

I wanted to mention your proposed rule excluding certain legitimate hedging activities used by agricultural businesses from qualifying as bona fide hedging. What is the CFTC doing to ensure that those legitimately hedging their risk will qualify for the exemption afforded to bona fide hedgers?

Mr. MASSAD. Well, thank you for the question, Senator. It is a very important area. We have received a lot of comment on the proposed rule, and particularly on the subject of bona fide hedging, and we are taking that very seriously. We had a very good roundtable earlier this summer with a number of industry participants

where we talked about this, and we recognize hedging strategies are often very complex.

The challenge for us is, again, to try to write bright-line rules that work, that distinguish between the bona fide hedging, which we want to allow, and the preventing the excessive speculation.

We are in a situation where we cannot look at people's intent, we cannot look at particular transactions, so we have to come up with that bright-line rule. We have asked industry for suggestions in that regard so that we make sure the rule does work to allow people to hedge commercial risk. It has to. These markets are so fundamental. We recognize the importance of that. I think all the Commissioners recognize the importance of that.

Senator THUNE. The CFTC and banking regulators recently proposed margin rules that would take effect in December of next year. I understand the deadline was set by a group of international regulators sometime ago under the assumption that the rules would be completed by now. I also understand that these changes would force the industry and their end-user clients to implement massive system changes which could take years to develop.

Do you think this timing is realistic given that the rules have not yet been finalized?

Mr. MASSAD. Well, thank you for the question. I think that, first of all, the margin for uncleared swaps rule is extremely important because, although we have mandated clearing of some products, there will always be uncleared swaps, and that is why we need a margin rule. I think it is important that we implement it in a way that works. We do not want to disrupt the market.

But I would say that most financial firms are already taking margin for these uncleared swaps. We are now 5, 6 years after the crisis, and a lot of them were taking margin even before that. Many of them obviously have increased that.

We want, though, to come up with a good implementation timetable. It has delayed implementation as it is written. It generally does not apply to end users, commercial end users. Our rules and the prudential regulators' rules exempt end users. We want to do it in a way where we are coordinating internationally because we do not want a situation of regulatory arbitrage.

I hear the concern. We are working on it. But I think we should try to get this rule in place as quickly as we can.

Senator THUNE. Are any of your international counterparts talking about perhaps a longer implementation period?

Mr. MASSAD. There is discussion currently that we are also part of, and people are balancing, well would this really be needed or not. We have received some comments from industry saying a delay is needed. We will certainly look at that. I think sometimes we have to look at these proposals for delay with a good amount of skepticism. That is part of our job. But we will certainly try to come up with a reasonable approach here.

Senator THUNE. Okay. Yesterday the first Agricultural Advisory Committee meeting took place, and I am wondering if you can share with the Committee what you see as the role of that committee in making future regulatory decisions. Is it going to be a committee that is created simply for symbolism purposes or will you really look in a substantive way to that committee for advice

when it comes to making some of these decisions, particularly with regard to agricultural commodities?

Mr. MASSAD. Well, thank you for the question. I think it is extremely important. It is a very good vehicle for us to get input. We have about 40 members representing a number of interests in the agricultural sector, whether it is producers or the co-ops or financiers or others. We had a very good meeting yesterday. I am committed to having a couple of meetings a year.

We are also consulting with the members about the things that they want to talk about and want to share with us.

So I think it will be extremely important to our efforts together, but I think generally you have a Commission today, four Commissioners who all are very pragmatic, who are all listening to market participants' concerns as well as to this Committee, and who are very committed to working together to try to do the right thing.

Senator THUNE. All right. Thank you, Mr. Chairman.

Thank you, Madam Chair.

Chairwoman STABENOW. Thank you very much.

Senator Gillibrand?

Senator GILLIBRAND. First, I want to thank you, Madam Chairwoman, for your excellent chairmanship. You have done a great job. It has been a privilege to serve on this Committee with you, and I am grateful for all the hard work you did in wielding the gavel, and I really enjoyed it.

Mr. Massad, I want to talk a little bit about two issues: first, cyber; and, second, high-frequency trading.

So on cyber, nearly every week we learn of a data or systems breach by cyber criminals. From Nasdaq to JPMorgan, it is clear that our Nation's financial institutions are prime targets for data and intellectual property theft.

One significant concern for the options market is that the Commodity Futures Trading Commission's budget is so limited that you cannot effectively test the cyber defenses of the entities you oversee. While yesterday we saw that the CFTC could get a 16-percent funding increase, I still believe this is inadequate, and I understand that there may be restrictions on this money.

Considering your budget crunch, how is the CFTC working with market participants, both big and small, to address the growing threat? What are the limits on your systems' safeguards procedures of the entities you regulate? Second, are you seeing the same obstacles in the financial sector with regards to cyber incidents that other sectors are facing, whether the need for capital improvements, better information sharing in the industry, and with appropriate regulators or better training?

Mr. MASSAD. Well, thank you for the excellent question, Senator. We are very focused on this issue. Resources are a challenge. Let me try to address all of your concerns.

First of all, you have highlighted the need very well. This is just a huge concern. We are seeing cyber risks obviously posed by a number of different types of actors, whether it is theft, whether it is cyber crimes committed in order to profit, whether it is espionage, or whether it is disruption. They are coming from a variety of types of players. So there is a need to be extremely vigilant and active on this.

We, as you say, do not have the money to do independent testing. We cannot possibly do that. You know, some of the big banks are spending more on cybersecurity than our entire budget. So what we are trying to do is do examinations that look at is the institution sufficiently focused on this. We look at things like: Is the board paying enough attention?

Is this rising to the board's attention, and is it rising to the risk committee's attention?

What are the policies? But also are the policies actually enforced? You know, a lot of times institutions have good policies on the books, but they do not really enforce them.

Then when an incident does happen, is the institution responding in a way that not only looks at the incident but at potentially taking a broader look at whether the incident suggests a need to shore up practices more generally?

That is sort of how we are going about it. We are coordinating with other arms of the Federal Government on this. As I mentioned earlier, there is a lot of coordination going on cyber. But the resource challenge is a big one, and it worries me.

Senator GILLIBRAND. Have you guys considered different funding mechanisms like a user fee based on size of actor, making sure it does not sap liquidity but given we have a market that is 450 million trillions, I think there is capacity there. Have you guys thought through that? Would you ever recommend that to Congress?

Mr. MASSAD. It is a very good question. I would be happy to work with you or members of this Committee on this issue. We, I think, are one of the very few financial regulators that does not have a separate fee. Presidents ever since, and including Ronald Reagan, have suggested that fees be used. I think they can be done in a way that works. Obviously we have to be mindful of impact on market liquidity, but I think it is possible. But it is a decision for the Congress. My desire, quite frankly, is to increase the budget however we can.

Senator GILLIBRAND. Okay. So high-frequency trading poses a dual risk: one, by creating a mechanism for bad actors to manipulate the markets through disruptive practices such as spoofing; and, two, by creating propensity to negatively affect market stability. These risks are not confined to the U.S. As a result, risks develop in foreign jurisdictions that have direct impacts on our markets.

What role is the CFTC playing in conjunction with domestic and international regulators in examining the institutionalizing of best practices with the goal of avoiding regulatory arbitrage? Two, as the CFTC works with these different regulators, what are some of the obstacles you are facing as it seeks to avoid the race to the bottom?

Mr. MASSAD. Thank you, Senator. We are looking at automated trading and high-frequency trading both from a policy and regulatory standpoint as well as from an enforcement standpoint. On the enforcement side, just to note that quickly we brought some actions with respect to spoofing and obtained some penalties and remedial actions as a result. In fact, one of our recent cases led to one of the first indictments of an individual for spoofing.

On the regulatory and policy side, we are very focused on this. We had a concept release where we asked for a lot of input on a number of issues to look at market practice. It is important to note that our markets are different than the cash equity markets. We do not have the multiplicity of trading platforms that the cash equity markets have, which is in many people's minds one of the reasons that we have seen some of these high-frequency trading issues.

But, nevertheless, automated trading is increasing in our markets. It is a significant part of our markets, and so we are looking at whether our institutions, the exchanges under our supervision, have adequate policies in place. We recently had a rule enforcement action against one of our exchanges on the fact that we did not feel they were looking enough at their own rules on spoofing and enforcing those rules. But we are also looking at additional rule changes that we might propose to address this issue.

So we will continue to be very focused on this and happy to meet with you further on it and get your ideas.

Senator GILLIBRAND. Thank you, Mr. Chairman.

Chairwoman STABENOW. Thank you very much.

Senator Hoeven?

Senator HOEVEN. Thanks, Madam Chairman. Thanks for your leadership of this Committee and for your hard work and, of course, all your work on the farm bill. It was greatly appreciated. Also to our Ranking Member, Senator Cochran, thank you as well. I have appreciated working very much with both of you. Thank you.

Chairman, my first question is: You have proposed a new margin rule that would take effect in December of next year. The industry is saying that the changes called for in this new margin rule could take years to implement, so talk about it. I mean, are they going to be able to meet that implementation requirement?

Mr. MASSAD. Thank you, Senator, for the question. We are aware that some industry participants have said that, and we will certainly evaluate those comments and work with other regulators on the timetable here. The timetable as it is written, as it is proposed, is phased in over 4 years. Currently most large financial institutions are already collecting variation margin, and so while some have said that they cannot do this, we want to look at, well, why is that if they are already doing it in part.

But we are certainly mindful of the need to implement a rule in a way that does not unnecessarily disrupt the market, and we are mindful of doing it in a way where we are coordinating with other regulators. So I can assure you that we will keep those concerns foremost in mind and try to work on a good solution.

Senator HOEVEN. On an interactive process to make it work.

Mr. MASSAD. Sure.

Senator HOEVEN. So then how does the rule mitigate risk, both systemic risk and product risk, and increase transparency? Then at what cost to the end user?

Mr. MASSAD. Sure. A very good question, Senator. The way the rule does that is the following: While we have mandated clearing for some swaps that are standardized or clearable, there will always be a lot of swaps that are not subject to centralized clearing,

that remain bilateral. That is what we had in the crisis. We had this whole opaque network of bilateral transactions, and what happened was when one participant then had trouble, that risk could easily cascade through the system because of the interconnections among participants.

By mandating clearing, we have dealt with some of that. But there will always be swaps that will not be cleared because there is not enough liquidity in that particular product or they might be new or for other reasons. For those swaps, what this rule does is say you have to evaluate the mark-to-market risk and take margin for that.

Now, a lot of big institutions will tell you they are already doing that. They did not wait around for this rule in many ways. The rule, though, formalizes the practice. We are working with international regulators.

There is a set of international standards that we are all trying to basically use to make sure the rules are the same. One of those standards is that we exempt end users, commercial end users, which is what we have done, and which is what the prudential regulators have done as well.

Senator HOEVEN. So by exempting those end users, you feel that they are not picking up substantial costs for implementation of the new rule.

Mr. MASSAD. That is correct.

Senator HOEVEN. Do you feel that with this new rule you can truly assess both systemic risk and product risk that is out there at any given time. So you can monitor how it is working in terms of the industry, the positions they are taking, the products they are offering. So that if one of them goes down, one, you can reasonably anticipate that, but it does not create any kind of domino effect or you have some kind of firewall to prevent that.

Mr. MASSAD. I guess what I would say, Senator, is this particular rule requires the individual financial institutions to take measures so that they are monitoring their risk. What we are trying to do from a system wide standpoint, I would say we are doing through our overall surveillance and our data collection to try to look at systemic risk and where that might be——

Senator HOEVEN. Well, I should have said you in conjunction with the other regulators because that was the problem before, not truly understanding the ramifications of the new hybrid products and the systemic risk created when one institution went down because they did not have the proper protections in place. So is all that being brought together in a way that I guess is transparent so that you and the other regulators can actually assess what is going on and communicate that to our Committee and other elected officials to make sure that we do not have a similar problem in the future?

Mr. MASSAD. Sure. A very good question. I think we are making good progress on that. It is kind of like a big infrastructure bill.

You do not get it done overnight. But a key piece of it is really the collection of data on this market. We had no data on this market at the time of the crisis, and now we are collecting a lot of data on this market. But our ability to collect that, to make sure it is

standardized, to make sure that we can analyze it and manipulate it is resource-driven in part.

It is a challenge for us under the resources. It also requires a lot of harmonization efforts. We are working very hard to harmonize data collection standards. It also requires making sure industry participants abide by their obligations to give us good data in the first place.

So I would say the data challenge is in particular where we are focused on that. We are working with other regulators on that, and I think, again, we are making very good progress.

Senator HOEVEN. Thank you.

Chairwoman STABENOW. Thank you very much.

Senator Klobuchar?

Senator KLOBUCHAR. Thank you very much, Madam Chairman. Thank you for these baskets, which I am sure you like. Have you ever had a Committee hearing where you got a basket with beef jerky?

Mr. MASSAD. I have not.

[Laughter.]

Senator KLOBUCHAR. All right. Well, feel very welcome. You can report back——

Mr. MASSAD. I hope it continues under Chairman Roberts.

[Laughter.]

Chairwoman STABENOW. That is a real question.

Senator KLOBUCHAR. All right. So I was going to ask you about cybersecurity, but I know my colleagues have—you have gone into that in depth, obviously a serious concern, so I thought I would switch over to a few things.

One you have just talked about, and that is the incredibly important work the CFTC is doing, but also the careful way you have to look at end users. I think our economy has a wide range of businesses in Minnesota that are affected by actions of the CFTC. We have farmers—and, by the way, many of them that were hurt by some of the bad things that were happening with some of the abuse of processes.

But then we also have energy producers, financial institutions, and commercial end users like farmers and rural energy co-ops use commodity markets as a form of insurance against price fluctuations. I want to make sure that the CFTC also takes into account how these commercial end users use hedges and derivatives in their day-to-day business, which you have acknowledged that you are doing.

At your nomination hearing, you committed to work with them, and I am glad that you are doing that to ease that burden, and I hope that as you review the rule on position limits and bona fide hedges, you consider all the ways commercial end users hedge real commercial risk and incorporate that into the final rule.

First of all, my first question would be: Do you think that the list of bona fide hedges should include the types of transactions that are common in agriculture?

Mr. MASSAD. Thank you for the question, Senator. We certainly want to end up with a rule that allows people to engage in legitimate, bona fide hedging, and we have gotten a number of comments about this. The challenge for us is writing the bright-line

rules because we cannot look at facts and circumstances, we cannot look at the individual intent behind particular transactions. We have to write rules that are general.

So the challenge is to write that rule in a way that works in an industry or multiple industries where hedging strategies can often be very complex. Sometimes it is hard to distinguish between what is really a bona fide hedge and what is maybe a cover for excessive speculation.

Senator KLOBUCHAR. Exactly.

Mr. MASSAD. But we are working on it.

Senator KLOBUCHAR. I hope you will continue to work with those that trade physical commodities as well——

Mr. MASSAD. Absolutely.

Senator KLOBUCHAR. —to ensure that the exemption to the position limit rule allows for their normal practices.

Mr. MASSAD. Absolutely.

Senator KLOBUCHAR. I appreciate that.

The second area that I have talked with you about before is speculation, and I have been concerned in the group of Senators that see this as an issue most notably in the gas and oil markets in the past.

Recently you noted in your testimony with Arcadia and Parnon Energy that they had manipulated the crude oil market, and I am concerned that end users who have a stake in the underlying commodity, such as wheat growers, are not able to conduct their business because of the rules put in place to curb the abuses by speculators and financial institutions.

What steps can the CFTC take to ensure that the end users are able to conduct their business and the market best reflect the forces of supply and demand?

Mr. MASSAD. Right. Thank you for the question, Senator. You know, one of the most important things we do is simply that the surveillance that we do on the markets. It is great to have rules such as the position limits rule, but one of our most important jobs is to engage in ongoing surveillance.

Now, we have multiple markets to look at. In the futures market alone, with respect to physical commodities alone, as you know, there are lots of agricultural markets, lots of energy and metals markets. Each of those is different.

Then we have the financial futures and options, and then we have the swaps. So trying to engage in surveillance over all of that is a real challenge, and we simply do not have the resources to do that today. That should really be something that this country funds adequately because it is such a good investment in our markets; it is such a good investment in making sure that end users not only can use these markets but have confidence in their integrity. So that is a real challenge for us today.

Senator KLOBUCHAR. Okay. One last thing. It is the Renewable Fuel Standard. You and I have talked about this in the past. You understand in the Midwest and really all over the country, generating $5 billion in economic output, it is 12,000 jobs in my State alone. We think it is good to have a mix of fuel, and along with the Chairwoman, a number of us have been advocating against

some of the changes that have been suggested last year by the administration. That is all now on hold.

But in the course of that, the Renewable Fuel Standard RINs market, as you know, was extremely volatile, and then the questions were raised about the impact of excessive speculation in the market. Given the CFTC's experience with the commodities market, what improvements could the CFTC recommend to improve the price discovery transparency and liquidity in the RINs market?

Mr. MASSAD. Well, Senator, we are happy to continue to engage with you and others on this. I think we have a very good relationship with EPA on these issues. Obviously they have the primary responsibility on some of these matters. But we will certainly be very mindful in terms of looking for fraud and manipulation in these markets and taking action if we see——

Senator KLOBUCHAR. Well, and if you have any recommendations about how to minimize the volatility and the manipulation that we saw in 2013 that we believe led to some of what we will call sort of an overreaction to what happened—and we believe outside forces may have caused that speculation, and if you have any recommendations how to minimize it, we would really appreciate it.

Mr. MASSAD. Okay.

Senator KLOBUCHAR. Thank you.

Chairwoman STABENOW. Thank you very much, and I would echo what Senator Klobuchar has said. It is very, very important.

This has been a very important hearing. We appreciate your ongoing efforts. I could not agree more with you when we look at the fact that, to be effective, to make sure that we have safety and reliability in the U.S. markets, there has to be the resources to provide the accountability and to make sure things are functioning well for those who need actions from the Commission.

So it is certainly something we will continue to focus on. We encourage you to continue to move forward all of the issues that you have to address, and we appreciate your steps, and thank you for joining us.

Any additional questions for the record should be submitted to the Committee clerk 5 business days from today, which is 5:00 p.m. on Wednesday, December 17th.

The meeting is adjourned.

Mr. MASSAD. Thank you.

[Whereupon, at 11:40 a.m., the Committee was adjourned.]

A P P E N D I X

DECEMBER 10, 2014

Madame Chair, Ranking Member Cochran, it is good to be back here with my colleagues in the committee and I appreciate you calling this hearing to highlight ,and help us better understand, recent actions by the Commodity Futures Trade Commission and its role in shaping policies that affect our agricultural community.

For many in Arkansas, the issues we will be discussing today are very personal. The agricultural community in my home state depends upon available tools to mitigate risk. Without these tools, many in Arkansas would be subject to too great a risk to remain viable. Not only do these tools directly impact our agricultural community, their impact can be felt in the price families pay for gas at the pump and for groceries to put food on the table.

The implications of CFTC's policy decisions are far reaching, both domestically and in global markets. Policy decisions made by the agency with regard to our counterparts abroad, can either help or harm markets right here at home. Furthermore, I believe CFTC should always look to embrace commonsense and sound policies while carrying out its mission, rather than pushing and implementing polices that create more problems than they solve.

Mr. Massad, I am encouraged by your commitment to working with this Committee and being open to constructive dialogue from me and others here today. It is good to see you again.

Opening Remarks for Senator Thad Cochran
Hearing on "The Commodity Futures Trading Commission: Effective Enforcement and the Future of Derivatives Regulation"
December 10, 2014, SR-328A

Madam Chairwoman, thank you for holding this hearing today. First, as today marks the final Senate Agriculture hearing for four of our members, I want to thank my distinguished colleagues, Senators Chambliss, Johanns, Harkin, and Walsh, for their valuable service to this body.

I join Chairwoman Stabenow in welcoming Chairman Timothy Massad to testify before this Committee. The Commodity Futures Trading Commission plays an important part in the regulatory framework that protects American farmers, families, and businesses.

It has been about six months since the Chairman took the reins of the Commission, and it appears the agency is moving in a positive direction due to his leadership. Several rulemakings recently undertaken by the Commission have received favorable reactions by industry stakeholders – including farmers, ranchers, and public utilities – that use these markets on a daily basis to make ends meet. I am hopeful that the Commission will follow through on these proposals by further enacting permanent relief for the marketplace. Temporary, piecemeal approaches to market regulation are not enough.

Chairman Massad, when you appeared before us during your confirmation process, Members of this Committee made it clear that the CFTC needs leadership that is willing to engage all stakeholders – especially those in the agriculture and energy sectors – and to conduct rulemakings in an open and transparent manner with a thorough understanding of costs and benefits.

Under your tenure, the Commission seems to be off to a good start, and we all know that much work remains to be done. If done properly, your efforts will provide much needed certainty to the global marketplace and stability for American families. I am ready to continue to work with you to address these issues, and I look forward to your testimony today.

Thank you.

Testimony of Chairman Timothy Massad before the U.S. Senate Committee on Agriculture, Nutrition & Forestry Washington, DC December 10, 2014

Thank you Chairwoman Stabenow, Ranking Member Cochran, and members of the Committee. I am pleased to testify before you today on behalf of the Commission. I last came before you as a nominee. It is a privilege to be here today as Chairman of the Commodity Futures Trading Commission (CFTC). I appreciate the opportunities I have had to meet with many of you during the confirmation process and since, and value your suggestions on the issues facing the Commission. I look forward to this Committee's continued input going forward.

The CFTC is tasked with oversight of the futures, options, and swaps markets. These are highly complex, global markets that most Americans do not participate in. But these markets are profoundly important to the daily lives of all Americans. They impact the prices we all pay for food, energy and many other goods and services.

The derivatives markets enable businesses of all types to manage risk—whether it is a farmer locking in a price for his crops, the utility managing its fuel cost, or the exporter hedging foreign exchange risk. For these markets to work well, good regulation is essential. That is why the Commission's job is so important. We must do all we can to prevent fraud and manipulation in these markets, to make sure these markets operate with integrity and transparency, and to help them thrive. I am committed to working with this Committee and Congress to make sure our financial markets continue to be innovative, dynamic, and an engine for economic growth.

Today, I would like to review what we have done over the last six months since I, as well as two of the other three Commissioners, took office. It has been a busy and productive time for us. In particular, I will discuss our progress in bringing the over-the-counter swaps market out of the shadows. I will also discuss our work to make sure our rules do not pose undue burdens or unintended consequences for the commercial businesses that rely on these markets. Finally, I will discuss some key priorities.

I want to note that, although much of what I will discuss concerns implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd Frank"), and the new regulatory framework for swaps, we are equally focused on our traditional areas of responsibility, the futures and options markets. On a day to day basis, a lot of what we do is to focus on the registrations, examinations, rule reviews, product monitoring, and surveillance of these markets to make sure they operate with integrity. While these markets cover many diverse commodities, they had their origins in agricultural products which remain very important to our work. In this regard, just yesterday we had a productive meeting of our Agricultural Advisory Committee, of which I am the sponsor. We were honored to have Secretary Vilsack as our special guest. It was an excellent opportunity to gather input directly from farmers, ranchers, and others who rely on these markets day in and day out.

Our advisory committees are very important. Commissioner Wetjen recently held a very informative meeting of our Global Markets Advisory Committee, which focuses on matters that affect the integrity and competitiveness of U.S. markets and U.S. firms engaged in global business, and makes recommendations for appropriate international standards for regulating futures, swaps, options, and derivatives markets, as well as intermediaries. He will also be convening a meeting of our Technology Advisory Committee in the coming months. Commissioner Giancarlo has been working to build up our Energy and Environmental Markets Advisory Committee, which advises the Commission on matters of concern to exchanges, firms, end users, energy producers, and regulators regarding energy and environmental markets and their regulation by the Commission. And, Commissioner Bowen, who is sponsoring our new Market Risk Advisory Committee, has requested public comment on its agenda and membership. This committee helps the Commission identify and understand the impact of an evolving market structures and movement of risk across clearinghouses, exchanges, intermediaries, market makers, and end-users.

Before I discuss implementation of reforms, I would like to highlight one item: our recent enforcement action regarding attempted manipulation of foreign exchange rate benchmarks by some of the largest banks in the world. Our investigation revealed that they attempted to manipulate one of the largest markets in the world. We ordered the banks to pay almost $1.5 billion in penalties and to agree to implement reforms designed to prevent the recurrence of this behavior.

This is an important case. As we saw with the investigation and fines in the Libor cases, benchmarks such as these are extremely important to our futures and swaps markets and to the financial system generally. And the system only works if market participants have confidence that benchmarks are not being manipulated. These actions exemplify the CFTC's commitment—and my commitment—to the robust enforcement necessary to safeguard the integrity of our markets. I will further discuss these efforts later in my testimony.

Implementing the New Regulatory Framework

Let me turn now to our efforts to implement financial reform. The financial crisis that began over six years ago stands as the worst since the Great Depression. We must never forget its cost in terms of jobs lost, homes foreclosed and other damage to our economy and to American families. It was during the financial crisis that most Americans first heard about derivatives. That was because over the counter swaps accelerated and intensified the crisis like gasoline poured on a fire. In the absence of regulatory oversight, a global market had developed and some participants took on excessive risk. A bilateral market structure hid the magnitude of these exposures. Because of the interconnectedness among swaps participants, risk associated with one participant's troubles could easily cascade through the system—often across national borders. We faced the possibility of systemic collapse.

The Dodd-Frank Act was a comprehensive response to the market excesses and regulatory gaps that contributed to the crisis. Title VII embodied the four basic commitments that were agreed to by leaders of the G-20 nations to reform the OTC swaps market: require central clearing of standardized swaps through regulated clearinghouses known as central counterparties (or CCPs), require regulatory oversight of the largest market participants; require regular reporting so that regulators and the public can have a view of what is happening in the market; and require transparent trading of swaps on regulated platforms. We have made substantial progress in implementing these reforms.

I want to thank the hardworking, professional staff of the CFTC for their work in each of these four areas. We would not be where we are today without their tireless efforts.

- Clearing of standardized swap transactions.

A primary commitment of Dodd-Frank was to require clearing of standardized swaps transactions through clearinghouses. The use of clearinghouses in financial markets is commonplace and has been around for over one hundred years. The idea is simple: if many participants are trading standardized products on a regular basis, the tangled, hidden web created by thousands of private bilateral trades can be replaced with a more transparent and orderly structure, like the hub and spokes of a wheel, with the clearinghouse at the center. The clearinghouse can then monitor the overall risk and positions of each participant.

Clearing through central counterparties is now required for most interest rate and credit default swaps. Recent data show our progress. About 70% of the transactions in the markets we regulate, measured by notional amount, are being cleared today, compared to about 15% in December 2007.

The CFTC was the first of the G-20 nations' regulators to implement clearing mandates. In doing so, the CFTC has acted in accordance with the Congressional direction and specifically exempted from those mandates most commercial end-users, non-financial companies such as manufacturers or farmers who are using the markets to hedge.

Of course, central clearing is not a panacea. Clearing does not eliminate the risk that a counterparty to a trade will default—but it provides us with powerful tools to monitor and mitigate that risk, and, through the use of mutualized default resources, significantly mitigates the effect of any such default on market participants. To work well, active, ongoing oversight is critical. We must do all we can to ensure that clearinghouses have the financial resources, risk management systems, settlement procedures, and all the necessary standards and safeguards consistent with the Commodity Exchange Act's (CEA) core principles and applicable international standards to operate in a fair, transparent, and efficient manner.

- Increased oversight of major market participants.

Since Congress passed Dodd-Frank, we have increased oversight of major market players through the registration and regulation of major swap participants and swap dealers. More than 100 are now provisionally registered. This list includes many of the largest banks in the world. We have adopted rules requiring these registrants to observe strong risk management practices, and they will be subject to regular examinations to assess risk and compliance with rules designed to mitigate excessive risk.

The new framework requires registered swap dealers and major swap participants to comply with standard business practices, such as documentation and confirmation of transactions, as well as dispute resolution processes. They are also required to make sure their counterparties are eligible to enter into swaps, and to make appropriate disclosures to those counterparties about risks and conflicts of interest.

We have worked with the SEC, other US regulators, and our international counterparts to establish this framework.

- Regular reporting for increased market transparency.

Congress recognized that having rules that require oversight, clearing, and transparent trading is not enough. We must have an accurate, ongoing picture of what is going on in the marketplace to achieve greater transparency and to address the potential systemic risk. A key commitment in Dodd-Frank is ongoing reporting of swap activity. In 2008 regulators and Congress were essentially blind to the size and the risks in this market. Under our rules, all swap transactions, whether cleared or uncleared, must now be reported to registered swap data repositories (SDRs), a new type of entity responsible to collect and maintain this vital information.

There are currently four SDRs that are provisionally registered with the CFTC. The collection and public dissemination of swap data by SDRs helps regulators and the public. It provides regulators with information that can facilitate informed oversight and surveillance of the market and implementation of our statutory responsibilities. Dissemination, especially in real-time, also provides the public with information that can contribute to price discovery, competition and market efficiency. You can now go to public websites and see the price and volume of swap transactions. Further, the CFTC publishes the Weekly Swaps Report that gives the public a snapshot of the swaps market.

- Transparent trading of swaps transactions on regulated platforms.

The Dodd-Frank Act also requires transparent trading of swaps. Congress mandated that certain swaps must be traded on a swap execution facility (SEF) or other regulated exchange. The trading requirement was designed to facilitate a more open, transparent, and competitive marketplace, which will benefit all participants.

Today, there are 22 SEFs temporarily registered, and 2 applications are pending. Each is required to operate in accordance with the same statutory core principles. These core principles provide a framework that includes obligations to establish and enforce rules, as well as policies and procedures that enable transparent and efficient trading. SEFs must make trading information publicly available, put into place system safeguards, and maintain financial, operational and managerial resources necessary to discharge their responsibilities.

Trading on SEFs began in October of last year. As of February 2014, specified interest rate swaps and credit default swaps must be traded on a SEF or other regulated exchange. Through the summer, notional value executed on SEFs was generally in excess of $1.5 trillion weekly. Publicly available data show trading volumes are continuing to increase. In addition, the number of market participants using SEFs is increasing. One SEF recently confirmed that it had exceeded 700 firms as participants.

In all these areas, however, there is more work to do. Our rules are new. We are still phasing in some requirements. As we gain experience with application of new rules in the marketplace, we will see what works well and what doesn't, and we will fine-tune the rules or make other changes as appropriate. And there is substantial work to be done to harmonize rules across national borders.

I believe the Commission today is focused on moving forward. It is comprised of four commissioners all of whom are dedicated to implementing the Dodd-Frank reforms, and all of whom bring good experience and judgment to the table. We are also focused on process. We have already had two open meetings. We are listening to market participants. I commend my fellow commissioners in particular for their efforts to reach out and make sure we are all well informed by a diversity of views, and for their willingness to collaborate and work constructively together. I am committed to continuing in that spirit as well. We will not always agree, but I believe we are working together in good faith to assess what is working and what needs fine tuning, and to do the best job we can in implementing the law.

There may still be those who say that the basic principles of these reforms are misguided, and would repeal these reforms and return us to the days where the industry operated with little oversight. To those who hold that view, I think the history of the securities and futures markets is a useful guide.

In the 1930s, we created a framework for securities regulation and trading, which proved tremendously successful. Many of its mandates were revolutionary, and at the time, many felt those requirements would be the death knell of capitalism. When Congress passed the Securities Exchange Act, which required public reporting by listed companies, the President of the New York Stock Exchange said it was "a menace to national recovery." History has proved otherwise. Today, the public reporting and basic trading requirements of our securities laws are about as controversial as seat belts. Indeed, they have been the foundation for the growth of our securities markets.

The history of the futures market is no different. Congress created a framework for the regulation of the industry, which properly balanced the need to embrace innovation with strong oversight. We have the strongest, largest and most dynamic markets in the world—in part because they have the integrity and transparency that attracts participants.

With this in mind, our challenge is to ensure that we create a regulatory framework that not only meets the Congressional mandate of bringing the swaps market out of the shadows, but also allows our financial markets to thrive. The regulatory framework must ensure transparency, integrity and oversight, and, at the same time, permit innovation, freedom and competition.

Priorities Going Forward: Making Financial Reform Work for End-Users

Let me turn now to one of the ways the Commission is meeting that challenge. For the last six months, we have made it a priority to address some of the concerns of commercial end-users—such as manufacturers, farmers, ranchers, and other businesses that rely on these markets to hedge commercial risks. We have sought to make sure that our rules do not impose undue burdens or create unintended consequences for these participants, and that we are creating better, more transparent markets for them. Let me review some of the actions we have already taken.

Local Utility Companies. In September, the Commission amended its rules so that local, publicly-owned utility companies could continue to effectively hedge their risks in the energy swap market. These companies, which keep the lights on in many homes across the country, must access these markets efficiently in order to provide reliable, cost-effective service to their customers. The Commission unanimously approved a change to the swap dealer registration threshold for transactions with special entities which will make that possible.

Customer Protection/Margin Collection. In November, the Commission proposed to modify one of our customer-protection related rules to address a concern of many in the agricultural community and many smaller customers regarding the posting of collateral. These rules had been unanimously adopted in the wake of MF Global's insolvency and were designed to prevent a similar failure from recurring and to protect customers in the event of such a failure. Market participants asked that we modify one aspect of the rules regarding the deadline for futures commission merchants to post "residual interest," which, in turn, can affect when customers must post collateral. The change was that the deadline would not move to earlier than 6:00 pm the day of settlement without an affirmative Commission action and an opportunity for public comment.

Reporting Requirements. We have proposed to exempt end-users and commodity trading advisors from certain recordkeeping requirements related to text messages and phone calls. This proposal largely tracks staff-issued no-action relief and is designed to make sure we do not impose undue reporting requirements on commercial end-users. The proposal also clarifies, in response to public feedback, that oral and written communications that lead to the execution of a transaction need not be linked to records identifying that transaction.

Volumetric Optionality. We have proposed to clarify our interpretation of when an agreement, contract, or transaction that contains embedded volumetric optionality falls within the forward exclusion from being considered a swap. "Embedded volumetric optionality" refers to the contractual right of a counterparty to receive more or less of a commodity at the negotiated contract price. These types of contracts are important to and widely used by a variety of end users, including electric and natural gas utilities. The proposed interpretation would clarify when forward contracts with embedded volumetric optionality may be excluded from being considered swaps. In this way, the proposed interpretation is intended to make sure commercial companies can continue to conduct their daily operations efficiently.

Treasury Affiliates of End-Users. The Commission staff has recently taken action to make sure that end users can use the Congressional exemption given to them regarding clearing and swap trading if they enter into swaps through a treasury affiliate. It is common for a large corporation with significant non-financial operations to have separate affiliates that enter into swaps and other financing transactions on behalf of the larger corporation and its subsidiaries. We have taken action

to clarify how our rules will be applied to make sure that such companies can utilize the end user exemption.

Interaffiliate Transactions. We have also worked to harmonize the phasing in of certain rules regarding clearing with the requirements in other jurisdictions. The Commission previously adopted a final rule providing an exemption from required clearing for swaps between certain affiliated entities, subject to specific requirements and conditions. One condition, designed to prevent evasion of the clearing requirement, is that any related swap executed with an unaffiliated counterparty must be cleared in accordance with Commission rules or comparable rules of a foreign jurisdiction. Because other jurisdictions had not yet adopted a mandatory clearing framework, the final rule provided a temporary alternative compliance mechanism. We took action because other jurisdictions need more time. While progress continues to be made with regard to the implementation of mandatory clearing regimes in foreign jurisdictions, many do not yet have a clearing mandate in place. For this reason, the Commission staff recently extended the rule's alternative compliance approach to December 31, 2015.

Reporting Requirements for Contracts in Illiquid Markets. We recently granted relief from the real-time reporting requirements for certain less liquid, long-dated swap contracts that are not subject to mandatory clearing and do not yet trade on a regulated platform. This relief was provided in part because while Dodd-Frank requires real-time reporting for swaps, it also requires that such reporting obligations should not lead to identifying market participants, as that could result in competitive harm. We therefore agreed to permit slightly delayed reporting for these swaps.

Aluminum Market. Another issue of concern to end users that we are focused on pertains to the long queues for delivery of aluminum at warehouses in this country licensed by the London Metal Exchange (LME), the relationship of those queues to the pricing and delivery of aluminum, and how those issues impact market integrity and market participants. We do not have direct regulatory authority over those warehouses, and the LME's principal regulator is the Financial Conduct Authority (FCA) in the UK. However, we are looking at these issues closely and speaking with aluminum users, the LME and the FCA on a regular basis. We are examining the actions that LME is taking to address aluminum market conditions as well as what other actions could be taken.

Harmonization with SEC Rules. We continue to work closely with our colleagues at the SEC. For example, in connection with the SEC's efforts to implement the Jumpstart Our Business Startups

Act ("JOBS Act"), we recently took action to harmonize our rules with the new requirements. Specifically, we revised requirements applicable to commodity pool operators that are also registered with the SEC.

In sum, we have been very focused on fine-tuning the rules to make sure they work for commercial end users. These are not major changes, but significant to the overall success of the new regulatory framework.

Finalizing the Remaining Rules

The CFTC has also been working on the few Dodd-Frank rules that remain to be finalized. In September, we reproposed our rule on margin for uncleared swaps, working in close cooperation with the banking regulators. While central clearing is a key mandate of the Dodd-Frank Act, uncleared, bilateral swap transactions will continue to be an important part of the derivatives market. This is so for a variety of reasons. Sometimes, commercial risks cannot be hedged sufficiently through swap contracts that are available for clearing. For example, certain products may lack sufficient liquidity to be centrally risk managed and cleared. This may be true even for products that have been in existence for some time. And there will and always should be innovation in the market, which will lead to new products. So, margin will continue to be a significant tool to mitigate the risk of default, and therefore, the potential risk to the financial system as a whole.

Consistent with Congressional intent, our proposal exempts end-users from the margin requirements applicable to swap dealers and major swap participants. In addition, because Congress mandated that margin requirements be set by different regulatory agencies for the respective entities under their jurisdiction, we worked closely with the relevant bank regulators so that our respective margin rules will be substantially the same. Under the Dodd Frank Act, each swap dealer and major swap participant for which there is a prudential regulator must comply with margin rules established by that prudential regulator. All other swap dealers and major swap participants must comply with margin rules established by the CFTC.

The capital rule and position limits rule are two others that we are working on. We have proposed rules issued in both cases. Congress mandated that we implement position limits to address the risk

of excessive speculation. In doing so, we must make sure that the market works for commercial end-users seeking to hedge routine risk through bona fide hedging.

We have received substantial public input on the position limits rule, and staff is still currently reviewing those comments. We also held a meeting of the Agriculture Advisory Committee yesterday, December 9, and discussed position limits—in particular the parts of the proposal applicable to deliverable supply (as that pertains to agricultural commodities). Accordingly, we reopened the comment period for the CFTC's Position Limit Proposal and Aggregation Proposal with respect to such issues for an additional 45 days to allow public comment on what was discussed at that meeting. I expect this input to be very helpful in enabling us to write rules that can achieve the goals of reducing risk and improving the market without imposing unnecessary burdens or causing unintended consequences.

Commission staff will also be considering next steps on the capital rule as we move forward on the proposed rule on margin for uncleared swaps.

Cross-Border Issues: The Challenge of Regulating a Global Market

As we move forward, implementing the new regulatory framework, a key area is working with our international counterparts to build a strong global regulatory framework. To succeed in accomplishing the goals set out in the 2009 G-20 commitments and embodied in the Dodd-Frank Act, global regulators must work together to harmonize their rules and supervision to the greatest extent possible. We know that what happens in London, Hong Kong and Tokyo can impact all of us here at home. We learned first-hand during the crisis how risks embedded in overseas derivatives transactions can flow back into the United States. We also know that differences in rules between jurisdictions can lead to changes in how business is conducted, given this market's mobility. I have been focused on cross-border issues since joining the Commission, including through three trips abroad and many meetings with international counterparts here.

The challenge of harmonizing rules across borders is best understood by remembering the unique historical situation we are in. The swaps market grew to a global scale without any significant regulation. We must regulate what is already a global market, but the new framework can only be implemented through the actions of individual jurisdictions, each of which has its own legal

traditions, regulatory philosophy, political process, and market concerns. While the G-20 nations agreed to basic reform principles, there will inevitably be differences in specific rules and requirements. The challenge is to achieve as consistent a framework as possible while recognizing that our responsibility as national regulators is first and foremost to faithfully implement and observe our own nation's laws. I think we have made good progress in harmonization, but there is much more to do. It will take time.

The timing of implementation of reforms can be a critical issue. We wrote most of our rules faster than other jurisdictions and made many substituted compliance determinations last December. More will eventually follow. But you can't make substituted compliance determinations or meaningfully coordinate regulation until other jurisdictions have their rules in place. For example, while our clearing mandates for key products have been in place now for some time, many jurisdictions are still finalizing or implementing their clearing mandates. This creates the potential for regulatory arbitrage—individual market participants seeking opportunities to avoid regulation and oversight. With many jurisdictions now finalizing their clearing mandates, we expect more progress in this area. And, we will continue to consider the cross-border implications of clearing mandates for additional products.

One of the most important cross-border issues that has been before the Commission over the last several months is clearinghouse recognition and regulation. This is an issue that transcends swaps. It is of equal concern to participants in the futures and options markets.

As you may know, the Europeans have not yet recognized our central clearinghouses as equivalent. Their law, EMIR, requires not only that our rules governing our clearinghouses meet international standards—which they do—but also that our laws have an effective equivalent system of recognition for clearinghouses located in Europe. A few days after I was sworn in, I attended a meeting overseas at which the European Commission announced its intention to recognize the clearinghouses in five jurisdictions—Australia, Hong Kong, Singapore, Japan and India—but not the United States. They said it was because they believed that "effective equivalent system of recognition" meant that the U.S. should not require registration of clearinghouses outside of the U.S. that wish to do clearing for U.S. customers.

That initial position has led us to discuss the rules governing clearinghouses that are located in Europe, but are also registered with the CFTC. There are presently three such clearinghouses.

This dual registration came about because the U.S. did not mandate that clearing of futures—even futures traded on U.S. exchanges—must take place in the U.S.; we simply required that it take place through clearinghouses that are registered with us and that meet our standards. Those standards include provisions related to our bankruptcy laws. They provide protection of customer funds and facilitate quick transfers of customer accounts in the event of a failing firm.

We built our swap clearing mandates on this framework of dual registration in the context of a global market, where clearing for U.S. persons largely takes place overseas. It is noteworthy that, currently, fourteen clearinghouses are registered with the CFTC as derivatives clearing organizations (DCOs) either for swaps, futures, or both. Five of those are organized outside of the United States, including three in Europe, one of which has been registered since 2001.

Dual registration and cooperative supervision have worked. The model has worked to protect customers, it worked during the crisis, and it is a model on which the market has grown to be global. In addition, I believe it is a good approach as a matter of public policy because major clearinghouses are extremely important in the global financial system today. A simple notion of deference—if the clearinghouse sits on foreign soil, then we defer to foreign regulation and supervision—is not sufficient.

We continue to be in dialogue with the Europeans to facilitate their recognition of our clearinghouses. We are making good progress. They have agreed that the framework of dual registration and cooperative supervision should not be dismantled. And we have agreed to consider changes that would further harmonize our rules with European rules governing these clearinghouses. This would in turn facilitate their recognition of our U.S. clearinghouses, as well as our exchanges, which they have also not yet recognized. In the meantime, I am pleased that the European Commission has decided to postpone the imposition of higher capital charges on banks clearing through U.S.-based central counterparties. This was due to take effect on December 15 in the event recognition had not been granted. It was this threat of higher capital charges that was going to fragment the market, not the existence of dual registration, which has actually been the foundation for the growth of the global market.

We are working on the cross-border aspects of other issues, including in some cases by trying to get the rules to be similar from the start. This is the case, for example, in the rules on margin for uncleared swaps. Europe, Japan and the United States have each proposed rules which are

substantially similar, and which reflect a set of standards agreed to by a broader international consensus. There are, however, still issues in the details and in the timing of the implementation of the reforms, which are important.

Another cross-border issue that I am focused on is the potential regulation of financial benchmarks and indices by the European Union (EU). In our markets, thousands of contracts reference these benchmarks and indices, such as LIBOR, S&P 500 and Brent Crude. The integrity of benchmarks and indices is vital to our financial system. That is why we have focused on this issue in our enforcement efforts, as evidenced by our orders against banks that have tried to manipulate LIBOR and the foreign exchange markets. We have also worked cooperatively and effectively with foreign regulators in these enforcement actions. We believe there should be standards for benchmarks that insure good administration and transparency and minimize the risk of manipulation.

The European Union (EU) has recently proposed legislation that would have adverse market consequences. In particular, benchmarks created by administrators located in countries outside the EU could not be used by European supervised entities, such as banks and asset managers; unless the European Commission determines that any non-EU administrator is authorized and equivalently supervised in the non-EU country. As you know, the United States does not have such a government-sponsored supervisory regime for benchmarks. Accordingly, in light of the EU's equivalence standards, the new proposed benchmark regulation could prohibit EU institutions from hedging using thousands of products traded on US futures exchanges and swap execution facilities.

I have expressed these concerns to European officials. I have encouraged them to consider the work of the International Organization of Securities Commissions (IOSCO) in this area, which the CFTC helped lead. IOSCO's recently published Principles for Oil Price Reporting Agencies (PRA Principles) provide a framework for price reporting agencies to address methodology, governance, conflicts of interest, and disclosure. Many price reporting agencies have already begun voluntarily complying with these standards. IOSCO is also doing work in the area of financial benchmark standards.

Because of the potential consequences on financial markets, the CFTC stands ready to work with its counterparts in the US financial regulatory sector to address this issue further. I hope that we can continue to work with our international counterparts to insure benchmark integrity in a way that recognizes that most benchmarks are not administered by a government agency.

Market data reporting and trading rules—each addressed in more detail below—are two additional areas where cross-border coordination is essential to achieve a well-working, global regulatory framework.

Market Data

Data is another vitally important area. Transparency was a cornerstone of the Dodd-Frank Act, and the establishment of swap data repositories in the U.S., and trade repositories abroad, is bringing unprecedented transparency to the swaps market. As I noted earlier, it is providing regulators with information that can facilitate informed oversight and surveillance of the market and implementation of our statutory responsibilities. Dissemination, especially in real-time, also provides the public with information that can contribute to price discovery and market efficiency.

Still, there is a considerable amount of work left to do to collect and use this data effectively. It is an enormous task that will take time. While harmonization with respect to data standards is a challenge, we are focused on it and committed to moving forward.

There are three general areas of activity. First, we must have data reporting rules and standards that are specific and clear, and that are harmonized as much as possible across jurisdictions. Only in this way will it be possible to track the market and be in a position to address emerging issues. The proliferation of data repositories across various jurisdictions makes moving forward in this area more important than ever. We are leading an international harmonization effort to achieve consistent technical standards and identifiers for data in SDRs.

We must also make sure the SDRs collect, maintain, and publicly disseminate data in the manner that supports effective market oversight and transparency. This means a common set of guidelines and coordination among registered SDRs. Standardizing the collection and analysis of swap market data requires intensely collaborative and technical work by industry and the agency's staff. We have been actively meeting with the SDRs on these issues, getting input from other industry participants and looking at areas where we may clarify our own rules.

Finally, market participants must live up to their reporting obligations. Ultimately, they bear the responsibility to make sure that the data is accurate and reported promptly. We have already brought cases to enforce these rules and will continue to do so as needed.

In short, the data collection issues will take time, but we are making progress. Going forward, it must continue to be one of our chief priorities.

Trading of Swaps on Regulated Platforms

With regard to swaps trading, there is also progress as well as work to be done. Increased trading on swap execution facilities provides greater price transparency, which can bring better pricing to market participants and better information to the public at large.

SEF trading is barely a year old, and our mandates requiring trading are only 10 months old. With platform-based trading of swaps still in its infancy, individual SEFs are still developing best practices under the new regulatory regime. The new technologies that SEF trading requires are likewise being refined. Establishing the new platforms, developing the new workflows, creating the administrative infrastructure, and testing and refining to make sure things work smoothly take time, effort, and resources.

While SEF volumes continue to grow and SEF trading continues to mature, we recognize that, ultimately, markets develop and thrive when private actors find it beneficial to transact on those markets. Therefore, we are looking at ways to make sure our rules help achieve that result.

I expect that we will look at several issues here involving execution methods and work flows, so that we strike the right balance between rules that achieve transparency, fairness and integrity while still allowing market innovation and competition. We are also looking to make sure we phase in requirements where appropriate so that we avoid unnecessary disruptions in the marketplace.

An example of this is how we have handled package transactions—that is, complex transactions that include both a swap that has been required to be traded on a SEF or designated contract market and some other swap or other product. Since SEF trading began earlier this year, we have been working with market participants to resolve questions about how the trading mandate applies in this circumstance.

At my direction, CFTC staff extended previous no-action relief to permit additional time for market participants to phase-in SEF trading of swaps executed as part of certain package transactions. This effort reflects the Commission's commitment to pragmatically implementing Dodd-Frank, while listening to market participants, and reviewing what rules work and what rules might require fine-tuning.

Such phasing of both rule implementation and compliance deadlines provides time for an orderly transition and gives market participants the necessary time to develop operational procedures and safeguards, and to transition smoothly to the new framework without creating unnecessary disruption or costs. It has been and should continue to be an important part of our approach.

We will also focus on the cross-border implications of trading rules. In this regard, the timing of the implementation of reforms has been critical. The Commission has implemented its trading mandate, but other jurisdictions have not. For example, Europe's trading mandate will not take effect until 2017. We will seek to harmonize our rules with those of other jurisdictions as much as possible. But more importantly, I believe we should focus on making sure our rules not only achieve the goals of transparency, but also help to create the kind of robust markets that the U.S. has long been known for and that attract participants from around the world.

Cybersecurity

We must also focus on cybersecurity, perhaps the single most important new risk to financial stability. Cybersecurity and business continuity generally are increasingly important aspects of our oversight for futures and swaps markets. The need to strengthen the security and resilience of our financial markets against cyber attacks is clear. We will be focused on this issue in our examinations of clearinghouses and exchanges in particular to make sure they are doing all they can to address this risk. We will also focus on business continuity and disaster recovery plans as a well-executed disaster recovery plan will aid in the recovery of a cybersecurity event.

The risk is apparent. The examples from within and outside the financial sector are all too frequent and familiar: the latest include JP Morgan; Home Depot and Target. Some of our nation's exchanges have also been hit or suffered other technological problems that caused outages or serious concerns. And because of the interconnectedness of financial institutions and markets, a

failure in one institution can have significant repercussions throughout the system. As was seen in the Target attack, the intruder gained access to the Target systems by stealing credentials from a vendor used by Target and the intruder was able to locate customer information and use credit card information. This type of attack launched at an exchange or clearinghouse has the potential to have a significant impact on the operational risks of an exchange or clearinghouse and those entities that use their services.

Our Core Principles have been modernized in recent years to address cyber and information security concerns. Our regulations have similarly been updated by adding more detailed standards addressing various aspects of cyber security.

We require clearinghouses, SEFs and designated contract markets (DCMs), and other market infrastructures to implement system safeguards, which must include four elements: first, a program of risk analysis and oversight to identify and minimize sources of cyber and operational risk; second, automated systems that are reliable, secure, and have adequate scalable capacity; third, emergency procedures, backup facilities, and a business continuity-disaster recovery plan; and fourth, regular, objective, independent testing to verify that the system safeguards program is sufficient to fulfill its regulatory responsibilities. Each entity must also have a risk management program that addresses seven key elements, including information security, systems development, quality assurance, and governance. In addition, these entities must notify the Commission promptly of incidents and have recovery procedures in place. Systemically important clearinghouses, for example, must have plans that enable them to recover and resume daily processing, clearing and settlement activities no later than 2 hours following a disruption. These entities must also maintain geographic dispersal of personnel resources to aid in the recovery efforts of a disruption.

We conduct system safeguards examinations to determine compliance with these requirements. Our oversight, however, is limited. Keep in mind that some of our major financial institutions are reportedly spending more on cybersecurity each year than our agency's entire budget. We do not engage in independent testing. Instead, we look at whether there is evidence to support management's assertions that they are in compliance with the requirements. Our examinations focus on the following areas:

- Governance—Is the board paying sufficient attention to cybersecurity and taking appropriate steps? Does the board have the expertise, and does it devote the time, to do so?

Is it setting the right tone as to the importance of these issues? The same questions apply, needless to say, to top management.

- Resources—Are sufficient resources and capabilities being devoted to monitor and control cyber-related risks across all levels of the organization?

- Policies and Procedures—Are adequate plans and policies in place to address information security, physical security, system operations, and other critical areas? And is the regulated entity actually following its plans and policies, and considering how plans and policies may need to be amended from time to time in light of technological, market or other security developments?

- Vigilance and Responsiveness to Identified Weaknesses and Problems —If a weakness or deficiency is identified, does the regulated entity take prompt and thorough action to address it? Does it not only fix the immediate problem, but also examine the root causes of the deficiency?

There is much more we would like to do in this area. However, our capacity to carry out examinations and address cybersecurity more broadly is significantly constrained by our current budget. We cannot conduct examinations as frequently or in as much depth as we should. Our response to this rapidly evolving area cannot be as proactive as we would like; and, the increasing number of cybersecurity incidents suggests a proactive approach is precisely what is needed.

High Frequency and Automated Trading

Markets are dynamic, and the agency must keep pace in order to oversee the markets effectively. Technology in particular is an important driver, and we have witnessed over the last several years a dramatic increase in automated trading. Keeping up with these developments has meant investing in the appropriate resources, a challenge given the agency's budget constraints. It has also meant reviewing our rules based on changes in market technology. For example, in April 2012, the Commission adopted rules that require certain registrants to automatically screen orders for compliance with risk limits if they are automatically executed. The Commission also adopted rules to ensure that trading programs, such as algorithms, are regularly tested.

In addition to its current rules, the Commission is currently considering comments received in response to its Concept Release on Risk Controls and System Safeguards for Automated Trading Environments. The Concept Release addresses the evolution from human-centered to automated trading environments. It seeks input on a range of protections, including additional pre-trade risk controls; post-trade reports; design, testing, and supervision standards for automated trading systems that generate orders for entry into automated markets; market structure initiatives; and other measures designed to reduce risk or improve the functioning of automated markets. We are still working through comments and will make a determination on what additional measures, if any, might be necessary to address automated trading.

Virtual Currencies

We also continue to respond to market developments such as new products. Virtual currencies, such as bitcoin, are an example. Virtual currencies may raise issues for a number of governmental agencies. The CFTC's jurisdiction with respect to virtual currencies will depend on the facts and circumstances pertaining to any particular activity in question. While the CFTC does not have policies and procedures specific to virtual currencies like bitcoin, the agency's authority extends to futures and swaps contracts in any commodity. The CEA defines the term commodity very broadly so that in addition to traditional agricultural commodities, metals, and energy, the CFTC has oversight of derivatives contracts related to Treasury securities, interest rate indices, stock market indices, currencies, electricity, and heating degree days, to name just a few underlying products.

Derivative contracts based on a virtual currency represent one area within our responsibility. Recently, for example, a SEF registered with us made such a contract available. Innovation is a vital part of our markets, and it is something that our regulatory framework is designed to encourage. At the same time, our regulatory framework is intended to prevent manipulation and fraud, and to make sure our markets operate with transparency and integrity. Our responsibilities at the CFTC in this regard are ongoing. It is important to emphasize that the existence of contract does not mean the CFTC endorses it. As with all new developments, we must remain vigilant to ensure market integrity, and will continue to evaluate these new contracts over time. We will also continue to coordinate with other regulatory authorities regarding the issues raised by virtual currencies as appropriate.

Our Continued Focus on Enforcement and Compliance

Let me return to where I started: the importance of our enforcement and compliance function. Robust enforcement and oversight are crucial to maintaining the integrity of our markets, as well as public confidence.

Our pursuit of those who have manipulated benchmarks such as in our recent foreign exchange cases or our continued efforts with respect to LIBOR , a key global benchmark underlying a wide variety of financial products and transactions, is a prime example of this commitment. So is our successful litigation against Parnon Energy and Arcadia, two energy companies that systematically manipulated crude oil markets to realize illicit profits. Through the outstanding work of CFTC enforcement staff, the CFTC sends the message that the protection of customers and the integrity of the markets are paramount.

Dodd-Frank provided the Commission with a number of new statutory tools to combat manipulation and practices that can distort the markets, and we are using them. We have new authority, for example, to attack "spoofing," where a party enters a bid or offer without the intent to consummate a transaction; unscrupulous speculators do this to create the false impression of liquidity in a particular product or to move the market price. Last year, we brought a civil action against a firm and its principal for spoofing, one of the first such cases, and in October, the U.S. Attorney for Illinois indicted the principal for spoofing, based on a referral from us.

We have also directed self-regulatory organizations to strengthen their efforts to combat spoofing. The CFTC recently recommended, for example, that the CME develop strategies to identify instances of spoofing and, as appropriate, pursue actions against perpetrators. The CFTC also recommended that CME must maintain sufficient enforcement staff to promptly prosecute possible rule violations. The company should take measures to ensure internal deliberations do not delay disciplinary action.

We have used our anti-manipulation enforcement authority to address fraud in the precious metals space as well. These schemes, which often target seniors concerned that they may outlive their retirement assets, purport to offer consumers the ability to buy precious metals like gold using pre-arranged financing. Contrary to Dodd-Frank's mandate, these transactions are typically not

conducted on an exchange. They are structured so that, taking account of fees and interest, the precious metals would have to double in value year after year in order for the investor to make any money. Even worse, in many cases, the transactions are entirely fraudulent: no precious metals are ever bought. In 2014, the Commission tried and won a case against Hunter-Wise, a Florida company that was a trailblazer in the use of this scheme. In addition to Hunter Wise, we have also taken action to shut down a host of boiler room operations used to identify and recruit potential victims.

In all of our efforts, we will also seek to hold not just firms, but also individuals, accountable. We are mindful that there is no stronger deterrent against future misconduct than the possibility of criminal sanctions, including prison. For that reason, in cases involving willful violations of the CEA, we work closely with the Department of Justice and other criminal authorities. The perpetrators who threaten the financial well-being of innocent participants in our markets need to understand that the loss of their own liberty is at stake.

We are equally focused on using our authority to ensure compliance with our rules, such as our reporting rules. Earlier this year, for example, we imposed penalties against a major bank for failing to abide by our reporting requirements.

Overall, the CFTC filed 67 new enforcement actions during fiscal year 2014. We opened more than 240 new investigations. The agency obtained $3.27 billion in sanctions, including $1.8 billion in civil monetary penalties and more than $1.4 billion in restitution and disgorgement. This amount of civil monetary penalties is more than 8 times our current annual budget. We are committed to aggressive enforcement and policing of our financial markets.

As a complement to these efforts, we have also taken steps to enable individuals to help us detect fraud and other misconduct. The agency's whistleblower program, created by the Dodd-Frank Act is one example. The program provides payments—up to 30 percent of any sanction obtained—to eligible whistleblowers. This is a relatively new program so we are still ramping it up. Already though, we are receiving relevant tips, complaints, and referrals. We believe the program will be an important tool going forward in identifying, investigating, and prosecuting violations of the law.

We are also working to help consumers be smarter investors and detect fraudulent schemes on their own. Last month, we launched the CFTC *SmartCheck* campaign. This campaign is designed to help

investors identify and recognize the most common schemes and the top signs of a fraudulent investment. The campaign includes tools, such as an interactive website, to help investors stay ahead of the fraud perpetrators. For example, investors can use the website to check the background of financial professionals and confirm whether any potential advisors have had past violations.

We will continue to focus on enforcement at all levels, whether it is traditional Ponzi schemes and precious metal retail fraud schemes against retirees, to the new challenges like spoofing that come with our increasingly electronic markets. And we will work with other regulators and law enforcement across jurisdictions to leverage our resources and safeguard our markets. The orders I discussed at the outset against five of the largest banks in the world for attempting to manipulate the foreign currency benchmark rates represent a good example of cross-border cooperation, as we worked closely with the Financial Conduct Authority in the UK and FINMA in Switzerland as well as our domestic counterparts.

Going forward, market participants should understand that we will use all the tools at our disposal to ensure compliance with the law.

Resources and Budget

Advancing the goals I have outlined and fully implementing the new regulatory framework depends on having the resources that are proportionate to our responsibilities. In my view, the CFTC's current budget falls short. The CFTC does not have the resources to fulfill our new responsibilities as well as all the responsibilities it had—and still has—prior to the passage of Dodd Frank in a way that most Americans would expect. Our staff, for example, is no larger than it was when Dodd-Frank was enacted in 2010.

We are fortunate to have a talented and dedicated professional staff, and we keep Teddy Roosevelt's adage in mind—to do all we can, with what we have, where we are. But the limits of our current budget are evident.

Specifically, in the absence of additional resources, the CFTC will be limited in its ability to:

- Review and approve in a timely manner the many new registration applications it faces from over 100 swap dealers and over 20 swap execution facilities, as well as from derivatives clearing organizations, designated contract markets, foreign boards of trade, and other market participants.

- Perform thorough examinations of these same participants and other market registrants on a regular basis for compliance with the law and regulations. This is of particular concern when it comes to monitoring critical infrastructure such as clearinghouses and exchanges, which are so important to our financial system and to financial stability.

- Engage proactively on emerging risks like cybersecurity. The CFTC needs resources to conduct compliance examinations of cybersecurity programs of regulated entities, help develop best practices, and respond when attacks occur.

- Respond in a timely and thorough manner to the concerns of the public and the users of derivatives markets. This includes responding to the many requests for rule approvals, rule certifications, requests for new product approvals, and submissions for swap clearing and trading mandates. Delays can have a significant adverse effect on efficiency, customer protection, and financial stability, as well as liquidity and innovation.

- Maintain and improve information technology systems and resources that are vital to its mission, including in particular its ability to receive, store and analyze vast new quantities of data related to the swaps market. Handling massive amounts of swaps data and effective market oversight both depend on the agency having up-to-date technology resources, and the staff—including analysts and economists, as well as IT and data management professionals. Simply put, the financial markets today are driven by sophisticated use of technology, and the CFTC cannot effectively oversee these markets unless it can keep up.

- Engage in the necessary level of market surveillance and oversight to detect excessive risk, fraud, manipulation or other abusive practices, which requires increasingly sophisticated tools and the ability to analyze massive amounts of data given the technological advances in the markets.

- Engage in robust enforcement efforts with respect to fraud, manipulation, abusive or disruptive practices or other threats to market integrity and customer protection.

- Hire and retain enough economists to perform critical analysis of market developments and provide robust assistance in considering the relative costs and benefits of the Commission's regulatory activities.

Simply stated, without additional resources, our markets cannot be as well supervised; participants and their customers cannot be as well protected; market transparency and efficiency cannot be as fully achieved.

Conclusion

We have made substantial progress in recovering from the worst financial crisis since the Great Depression, but there is much work yet to accomplish. As we continue implementing the necessary reforms that Dodd-Frank mandated, we must work to make sure the regulatory framework serves the needs of the commercial businesses that rely on these markets.

The United States has the best financial markets in the world. They are the strongest, most dynamic, most innovative, most competitive and transparent. They have been a significant engine of our economic growth and prosperity. The CFTC is committed to doing all we can to strengthen our markets and enhance those qualities.

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

QUESTIONS AND ANSWERS

DECEMBER 10, 2014

Senate Committee on Agriculture, Nutrition & Forestry
The Commodity Futures Trading Commission:
Effective Enforcement and the Future of Derivatives Regulation

Wednesday, December 10, 2014
Questions for the record

The Honorable Timothy G. Massad, Chairman,
Commodity Futures Trading Commission

Chairwoman Debbie Stabenow

1) Since the signing of Dodd-Frank, cross-border harmonization has been a significant challenge. There certainly have been bumps along the way, both domestically and internationally. As you know, the term harmonization can mean uniformity in rules between agencies here in the U.S., as well as coordination on the international front. What is your approach toward resolving differences in these rulemakings? Can you highlight for the Committee any specific progress you and your staff have made, or expect to make, on achieving global harmonization?

I am very committed to harmonizing our rules with those of other domestic regulators as well as internationally to the extent possible. Since taking office, I have focused on this issue in a number of ways. First, I have made it a priority to engage with domestic and international regulators. I have regular meetings with Chair White at the SEC and with the prudential regulators on harmonization issues. I also participate actively in the international groups that are focused on harmonization and I have regular meetings and phone calls with a number of my international counterparts.

Among the areas of current focus are the rules on margin for uncleared swaps. We reproposed a rule which is quite similar to the rules, proposed concurrently, by the prudential regulators as well as to the rules proposed recently by Japan and Europe. There are some differences, and we are continuing to address those. We did not propose a specific method for applying our rule to cross-border activity, instead stating that we wished to be flexible, consider different approaches and invite comment on the same.

We are involved in active discussions with the Europeans on harmonizing our rules with respect to regulation of clearinghouses. We are making good progress in this area, and I hope a successful conclusion to this issue can be a roadmap for looking at other issues. We are also in dialogue with the Europeans on a number of issues, such as coordinating clearing mandates.

We have also recently reached out to the Europeans to express our concerns with respect to certain legislation they are considering with respect to benchmarks. We believe adoption of this legislation in its current form could disrupt the market, and we have urged them to rethink the approach and have offered to work with them to find an alternate solution.

We are co-chairing an international working group on harmonization of data standards that has wide participation and is working on a number of important issues in the area of data collection.

These are just some of the efforts going on. We will continue to do all we can to harmonize the regulatory framework as much as possible.

2) The Commission's current proposed rule on margin requirements for uncleared swaps includes initial margin for inter-affiliate swaps. I have heard from market participants that requiring initial margin for inter-affiliates would reduce market liquidity, but not materially reduce systemic risk. If the variation margin and capital requirements are crafted properly, will the CFTC consider alternative initial margin requirements, like exempting inter-affiliate swaps? Has the CFTC considered the cross-border implications of imposing initial margin on inter-affiliates in light of some foreign regulators not doing the same? Lastly, will the CFTC conduct an analysis of the impact an inter-affiliate initial margin requirement would have on market liquidity?

The comment period for the proposal closed on December 2, 2014. The Commission received 60 comment letters. A number of them addressed the treatment of inter-affiliate swaps. CFTC staff is currently reviewing the comments and preparing a summary and analysis of comments. CFTC staff is also conferring with staff of the Prudential Regulators to discuss these issues and to attempt to keep the respective rule proposals harmonized.

The CFTC is considering alternative initial margin requirements for inter-affiliate swaps suggested by commenters. The CFTC also is considering the cross-border implications of various approaches. The CFTC will conduct an analysis of the impact an inter-affiliate initial margin requirement would have on liquidity prior to issuing the same in a final regulation.

3) Title VII of Dodd-Frank created several regulatory requirements that serve to protect both the derivatives markets and the broader economy from systemic risk, including central clearing, data reporting, and swap execution facilities. Do you believe the CFTC's central clearing mandate has made clearinghouse's systemically risky entities? How has the CFTC approached regulating and monitoring clearinghouse health to prevent broader financial systemic risk resulting from them?

Risk exists in the bilateral swaps markets, and mandating clearing of certain swaps serves, among other things, to transfer credit risk to an infrastructure that is designed to manage risk. But clearing does not eliminate risk, and therefore the risk that central clearinghouses pose to our economy and to financial stability is a high priority for the CFTC. We are very focused on making sure that the derivatives clearing organizations (DCOs) registered with us have adequate financial, managerial and operational resources to manage risk. These DCOs successfully met their obligations during the financial crisis of 2008 and have continued to meet their obligations since the issuance of the swaps clearing mandates, but we must continue to be vigilant.

The CFTC takes a number of steps to address these issues. These include analyzing for consistency with statutory and regulatory requirements: applications for DCO registration, DCO rule changes, and DCO margin models. The CFTC conducts periodic examinations of DCO operations, reviews clearing member risk management programs and, on an ongoing basis, the CFTC reviews daily position and margin reports and conducts stress tests to identify traders that pose risks to clearing members and clearing members that pose risks to DCOs.

4) G-20 commitments and Dodd Frank require that all standardized and liquid swaps be centrally cleared and traded on electronic platforms. Many participants at the CFTC's GMAC meeting held in October 2014, supported the clearing mandate for non-deliverable forwards. When do you expect to propose the Forex NDF clearing determination and seek public comment?

No decision has been made on proposing a clearing determination for NDFs. On December 22, 2014, the CFTC published the response by the Foreign Exchange Markets Subcommittee (FEM) to the GMAC's request for a recommendation regarding an NDF clearing requirement determination by the CFTC (Response). The Response raised a number of issues as to whether and how the CFTC should propose such a determination, including whether the market was ready for a mandate, and the staff is still evaluating those.

Senator Heidi Heitkamp

1) The Commission recently provided no-action relief to certain firms that are members of designated contract markets (DCMs) from Section 1.35 reporting requirements that some argue are onerous and technologically infeasible. While the no-action guidance has helped provide some degree of certainty, affected firms still have to gather large volumes of data to be compliant. Is the Commission looking at more permanent relief from these requirements? Why is such data considered by the Commission to be necessary to collect from members of a DCM but not other firms?

The Commission on November 3, 2014 proposed an amendment to Regulation 1.35 that makes permanent the no-action relief that the Commission recently granted to members of designated contract markets (DCMs) and swap execution facilities (SEFs) that are not registered, or required to register, with the Commission in any capacity (Unregistered Members). Specifically, under the proposed amendment, Unregistered Members must maintain the records that are prepared in the course of their business, including certain written communications, but Unregistered Members are not required to retain text messages, and they are not required to comply with the recordkeeping form and manner requirements that the rule imposes on other market participants.

Regulation 1.35 has been amended multiple times since it was introduced in 1948, and has always required recordkeeping requirements on members of contract markets in one form or another. This information is valuable to effective market oversight and helping to ensure market integrity. The Commission recognizes there is a balance, and the proposed amendments are intended, in part, to reduce the regulatory burdens on certain market participants, including end-users, while at the same time ensuring that the recordkeeping requirements are sufficient for the Commission to exercise proper oversight of the markets. The public, including all affected market participants, has an opportunity to comment on the new proposed amendment. The comment period remains open at this time. The Commission will consider all of the comments it receives, and may revise the proposed amendment based on its review and analysis of the comments.

Senator Thad Cochran

1) We have heard recently from end users, clearinghouses and clearing members concerned that new "Basel III" banking capital requirements fail to properly account for the treatment of segregated margin. Within the Agriculture Committee's jurisdiction, the Commodity Exchange Act and CFTC regulations require customer margin to be segregated so it cannot be used to leverage the bank as the Basel III ratio seems to assume. Not only does the punitive capital for customer clearing not make sense, it increases the risk as more customers will have to decide whether they can afford to hedge various risks. Has the CFTC engaged in discussions with the banking regulators to ensure they recognize the exposure-reducing effect of margin that is segregated under CFTC requirements?

The CFTC staff are aware of these issues and have been working with colleagues at the Federal Reserve and with foreign colleagues, informally through international groups, in order to encourage banking regulators to consider these concerns. The CFTC staff has raised the issues stated in the question and others, such as how the incentives created by the leverage ratio calculation affect the goals of encouraging CCP clearing of standardized derivatives, the maintenance by CCPs of substantial liquidity resources, and portability of customer positions in the event of a clearing member's default.

2) The public comment period for the CFTC's rule on margin requirements for uncleared swaps recently ended. Many expressed concern with the lack of consistency across regulators and jurisdictions and also pointed out differences between the CFTC's rules and the Basel Committee on Banking Supervision / International Organization of Securities Commissions Final Framework on Margin Requirements for Non-Centrally Cleared Derivatives. This rule is set to take effect in December 2015. Since the derivatives market is global, there are concerns that different rules in varying jurisdictions will result in an uneven playing field. How can the CFTC better achieve consistency and harmonization of its rules and those put out by its international counterparts to avoid any negative impact from inconsistent international requirements?

The CFTC staff are very conscious of the value of harmonizing margin rules that may be adopted by the CFTC and the U.S. prudential regulators as well as by international regulators and is continuing to focus on those issues. CFTC staff participated in the BCBS/IOSCO committee that developed the international standards.

CFTC staff worked closely with the staff of the U.S. Prudential Regulators in developing the proposed U.S. rules and also was in communication with international regulators during this time. CFTC staff is currently working with staff of the Prudential Regulators in reviewing the comments received and continues to be in touch with international regulators. Two key goals of this effort are: (i) developing a harmonized approach to margin requirements within the U.S.; and (ii) developing a harmonized approach to margin requirements internationally.

3) Are you concerned that the CFTC's extraterritorial approach creates incentives for firms to move certain jobs outside of the U.S. in order to avoid regulatory burdens? Are you concerned that market fragmentation will lead to highly concentrated regional pools of risk around the globe?

CFTC staff has been paying close attention to the impact of our new rules with respect to the over-the-counter swaps market and possible market fragmentation. The CFTC is also mindful of its statutory obligation to address the risks that offshore activity can have on the U.S. economy and financial stability. All the G-20 nations have agreed to implement the same basic reforms of the over-the-counter swaps market. However, many jurisdictions have not completed their rules, and differences in timing alone can result in fragmentation. The CFTC will continue to focus on harmonizing rules where possible particularly as other jurisdictions complete their rules. Recently, for example, in its proposed rule on margin for uncleared swaps, the Commission chose to be flexible and not propose specific rules on the cross-border application of the rule in order to invite further comment.

4) How will the Commission work to ensure that the global swaps markets will not be harmed by fragmentation and loss of liquidity, in the event rule sets prove unworkable across jurisdictions?

I have made it a priority to work with our international counterparts to build a strong global regulatory framework. It is very important to harmonize rules to the greatest extent possible. The unique challenge with the swaps market is that the swaps market is already a global market, and while the G-20 nations have agreed to basic reform principles, the new framework can only be implemented through the actions of individual jurisdictions, each of which has its own legal traditions, regulatory philosophy, political process, and market concerns. In addition, many jurisdictions have not completed their rules, and timing differences alone for bringing those rules on-line can create challenges. While we have made good progress in harmonization, we know that there is much more to do.

We are currently engaged in trying to harmonize rules to the extent possible in a number of areas. For example, with respect to margin for uncleared swaps, we reproposed a rule which is quite similar to the rules proposed recently by Japan and Europe. There are some differences, and we are continuing to address those. We also did not propose a specific method for applying our rule to cross-border activity, instead stating that we wished to be flexible, consider different approaches and invite comment on the same.

We are involved in active discussions with the Europeans on harmonizing our rules with respect to regulation of clearinghouses. We are making good progress in this area, and I hope a successful conclusion to this issue can be a roadmap for looking at other issues.

We are co-chairing an international working group on harmonization of data standards that has wide participation and is working on a number of important issues in the area of data collection. .

While we will seek to harmonize our rules with those of other jurisdictions as much as possible, I believe we should also focus on making sure our rules not only achieve the goals of transparency, but also help to create the kind of robust markets that the U.S. has long been known for and that attract participants from around the world.

5) How has the CFTC been coordinating with the Securities and Exchange Commission (SEC) to ensure that the global framework of derivatives regulations is consistent across all types of swap and securities-based swap transactions?

I appreciate the importance of continuing to work closely with the Securities and Exchange Commission to ensure that the global framework of derivatives regulation is consistent. Since I took office, I have made it a priority to communicate frequently with Chair White and have directed my staff to engage regularly with SEC staff toward this end.

Since the passage of the Dodd- Frank Act, the agencies have been working to ensure that the global framework of derivatives regulation is consistent across all types of swap and securities-based swap transactions. This coordination and cooperation builds on a long history of interagency coordination in a wide variety of ways, including in areas of development of complementary rules, surveillance, enforcement, trading in security-related products, and dual-registrants.

Examples of such consult-and-coordinate interaction in the wake of Dodd-Frank include, but are not limited to, meetings between staff and the sharing of draft proposed and final rules, including the following CFTC rules:

- Part 37 (Swap Execution Facilities);
- Part 43 (Real-Time Public Reporting);
- Part 44 (Interim Final Rule for Pre-Enactment Swap Transactions);
- Part 45 (Swap Data Recordkeeping and Reporting Requirements);
- Part 46 (Swap Data Recordkeeping and Reporting Requirements: Pre-Enactment and Transition Swaps);
- Part 49 (Swap Data Repositories);
- Part 39 (Systemically Important Derivatives Clearing Organizations; End-user Exception to the Clearing Requirement for Swaps);
- Part 4 (Compliance Obligations for Registered Investment Companies);
- 17 CFR Chapter 1 (Interpretive Guidance and Policy Statement Regarding Compliance with Certain Swap Regulations);
- Part 50 (Clearing Exemption for Swaps Between Certain Affiliated Entities; Swap Transaction Compliance and Implementation Schedule);
- Part 23 (Confirmation, Portfolio Reconciliation, Portfolio Compression, and Swap Trading Relationship Documentation); and
- Part 75 (Proprietary Trading and Certain Interests in and Relationships with Covered Funds).

Additionally, the CFTC and SEC staff consulted and coordinated on interagency orders authorizing ICE Clear Credit to permit portfolio margining of credit default swaps (CDS) (which are both swaps and security-based swaps) in cleared CDS customer accounts. The two agencies also consulted in connection with the rulemaking on standards for clearing agencies that are systemically important or that engage in complex activities, such as clearing security-based swaps (covered clearing agencies) (the CFTC was engaged in a parallel set of rulemakings for standards for derivatives clearing organizations).

Chair White and I personally participate in numerous meetings with international regulators on matters pertaining to derivatives regulations, and we frequently discuss the matters being considered by these groups. These include meetings of the board of directors of IOSCO, the ODRG and the FSB. Chair White and I also are both members of the Financial Stability Oversight Council, which meets monthly. These meetings provide another opportunity to discuss and coordinate efforts.

We and our staffs are also working on a number of issues that pertain to harmonizing rules internationally as part of efforts by larger international regulator groups. These include: cross-border harmonization of clearinghouse regulation and supervision and data collection standards.

6) What kind of market data is the CFTC analyzing when considering its options in moving forward with its position limits rulemaking, and how will the costs to the broader economy be computed?

The Commission is taking into account a wide variety of types of data in considering the position limits rule. The Commission considers data submitted in comments received on the rule. The Commission also looks at data it collects as part of the exercise of its current oversight responsibilities, much of which is confidential, such as futures trading data from the large trader reporting system under Part 17 of the Commission's regulations and large trader reporting for physical commodity swaps under Part 20 of the Commission's regulations. 17 CFR Parts 17 and 20.

To inform the public consistent with the statutory confidentiality requirements, the Commission published general statistical information regarding derivative positions of unique persons in Table 11 of the notice of proposed rulemaking, Position Limits for Derivatives. See, 78 Fed. Reg. 75680 at 75731 (Dec. 12, 2013). The Commission noted it intends to use data submitted to swap data repositories, as practicable. Id. at 75734.

The Commission considers the costs to the broader economy as part of its considerations of costs and benefits. CEA section 15(a) requires the Commission to consider the costs and benefits of its actions before promulgating a regulation under the CEA or issuing certain orders. 7 U.S.C. 19(a). CEA section 15(a) further specifies that the costs and benefits shall be evaluated in light of five broad areas of market and public concern: (1) protection of market participants and the public; (2) efficiency, competitiveness, and financial integrity of futures markets; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations. The Commission considers the costs and benefits resulting from the discretionary determinations with respect to the CEA section 15(a) factors. The Commission attempts to quantify the costs and benefits of proposed regulations relative to the statutory requirements of the CEA and the Commission's regulations then in effect. Where quantification is not feasible, the Commission identifies and considers costs and benefits qualitatively.

7) As you know, the proposed rule on margin requirements for uncleared swaps includes initial margin for inter-affiliate swaps. This requirement has raised concerns from industry stakeholders and fellow CFTC Commissioners. Industry participants have noted that requiring initial margin for inter-affiliates would unnecessarily drain liquidity from the system and would not materially reduce systemic risk. They suggest that applying variation margin and credit risk capital requirements to a Covered Swap Entity's swaps with its affiliates would mitigate most of the Covered Swap Entity's credit risk to its affiliates without resulting in undue liquidity burdens or creating artificial incentives to execute swaps with third parties. Provided that the variation margin and capital requirements are crafted properly, do you think the CFTC can exempt initial margin for inter-affiliate swaps? Is the CFTC planning a quantitative analysis of the impact an inter-affiliate initial margin requirement would have on liquidity?

The comment period for the proposal closed on December 2, 2014. The CFTC received 60 comment letters. A number of them addressed the treatment of inter-affiliate swaps. CFTC staff is currently reviewing the comments and preparing a summary and analysis of comments. CFTC staff is also conferring with staff of the Prudential Regulators to discuss these issues and to attempt to keep the respective rule proposals harmonized.

The CFTC is considering alternative initial margin requirements for inter-affiliate swaps suggested by commenters, including an exemption for initial margin. The CFTC will conduct an analysis of the impact of inter-affiliate initial margin requirements on liquidity prior to issuing the final regulations.

8) Due to the global nature of systemic risk, it is important to enable the CFTC to effectively identify and mitigate that risk. Industry participants have expressed concern that confidentiality and indemnification requirements contained in Sections 728 and 763 of Dodd-Frank may negatively impact the CFTC's ability to work with foreign regulators to accomplish this goal. CFTC and SEC Commissioners alike have called for a legislative solution to these confidentiality and indemnification requirements. In September, the OTC Derivatives Regulators Group (ODRG) issued a report on cross-border implementation issues that specifically identified concerns with barriers preventing "authorities [from] accessing information from trade repositories" as needing to be resolved. In your opinion, is this the case? If so, what recommendations do you have to improve the ability of regulators to monitor, detect, and mitigate global systemic risk?

The September 2014 ODRG Report ("Report") identified two issues with respect to data and trade repositories: (i) reporting information to trade repositories; and (ii) the ability of authorities to access information from trade repositories.

With respect to reporting information to trade repositories, the Report focused on barriers to trade reporting by market participants—particularly reporting of counterparty information—embodied by data protection, secrecy and blocking statutes in some jurisdictions. The September ODRG report included a copy of the ODRG's letter to the Financial Stability Board (FSB) requesting that the FSB make a clear and unambiguous statement that jurisdictions need to remove all barriers that prevent reporting of counterparty-identifying information and discuss the setting of an ambitious but realistic deadline by which such barriers are addressed. As a Principal of the ODRG, I agree with the ODRG's assessment that barriers which prevent reporting of counterparty-identifying information to trade repositories significantly reduce the effectiveness of reporting obligations and impede the effective supervision of reporting entities, thus contravening the G20's objectives as outlined in the Leaders' 2009 Pittsburgh communiqué. In this regard, Commission staff has issued temporary no-action relief to permit the "masking" of certain counterparty identifying information with respect to swap data reported to registered SDRs, thus permitting reporting parties to fulfill their reporting obligations while acknowledging privacy, secrecy and blocking laws that prohibit the disclosure of counterparty identifying information. Absent such relief, reporting parties could find themselves in the untenable position of having to choose between violations of the CFTC's swap data reporting rules or the privacy laws of foreign jurisdictions. See CFTC Division of Market Oversight, No-Action Letter No. 14-89 (June 27, 2014). However, I would hope that permanent solutions could be found to this problem consistent with the G20 objectives.

With respect to the ability of authorities to access information from trade repositories, the ODRG emphasized in its Report that direct access by authorities to data in trade repositories is the preferred approach to ensuring that authorities are able to access relevant data held in trade repositories. Section 21 of the CEA, added by section 728 of the Dodd-Frank Act, requires that swap data repositories register with the Commission and prescribes duties of registered swap data repositories (SDRs). Among these is the requirement in section 21(c)(7) that SDRs make available all data obtained by them to specified entities on a confidential basis. Section 21(d), however, requires that before making data available to any such entity, the SDR must receive both a written confidentiality agreement and an agreement to indemnify the SDR and the CFTC from any litigation expenses relating to the information provided.

We and other ODRG members continue to explore practical solutions to SDR access issues in light of these legal parameters. For instance, individual jurisdictions have entered into agreements focused on access and information sharing between two or more jurisdictions. We

have also issued guidance that the indemnification provisions should not prevent foreign regulator access to data when they have an independent and sufficient regulatory interest.

Senator Charles Grassley

1) Several Iowa companies have complained about the Midwest premium price of Aluminum. They have expressed great concern that the price has gone from under $8 per pound three years ago to above $23 per pound as recently as last month. Additionally, they have reported that while that has happened in the Midwest, aluminum prices on the London Metals exchange have stayed pretty constant. What specific actions is the CFTC taking on this issue?

I am concerned about the long queues at LME aluminum warehouses, conditions related to the pricing and delivery of aluminum, and how these issues impact market integrity and market participants. I stated in my confirmation hearing that as Chairman of the CFTC, I would investigate these matters and evaluate what the CFTC can do to address them. Since that time, I've been in direct contact with the LME, FCA, Aluminum Users Group, and other involved parties to discuss the most effective steps that all parties could take to address aluminum market conditions.

I've also reviewed the progress of a package of reforms that LME announced in November 2013, which were intended to reduce the load-out times at LME aluminum warehouses, strengthen information barrier requirements for warehouses and related trading companies, and address other related aluminum issues. Several of these reforms have been implemented, while others had been delayed in litigation until a recent UK Court of Appeal decision came out in favor of LME. LME is in the process of implementing these additional reforms, and new requirements begin on February 1st. In addition, LME is currently working on further improvements.

While the CFTC regulates designated contract markets (DCMs) via core principles, the CFTC does not have direct regulatory authority over warehouses licensed by either DCMs, or by foreign boards of trade such as the LME. While our authority may be limited, we will continue to do all we can regarding this situation.

Over the coming months, I will continue to closely monitor the LME's implementation of additional reforms, and will focus on their impact on warehouse queue lengths and, in particular, aluminum market conditions.

2) **Earlier this year, I wrote to you about excess office space at the CFTC office in Kansas City and the three Agency offices in Washington, DC, New York and Chicago. CFTC has entered into long-term leases for a total of 1352 seats at all four locations. Today, over thirty percent of the office space remains vacant. If current staffing levels remain the same, CFTC will spend over $74 million over ten years on vacant office space. What steps have been taken to get rid of excess office space in all four offices?**

In October 2014, CFTC consolidated the Kansas City office to one floor, thereby making the space on an adjacent floor available for immediate release. We have reached out to the previous and current landlord(s) of the Kansas City office on the issue of returning this excess space and the landlord is seeking backfill opportunities. These conversations are ongoing.

With the funding provided in the FY 2015 appropriation, the CFTC will increase staff which will reduce the projected vacancy rate significantly. The Office of the Executive Director continues to look for cost and space savings. We will keep exploring options to reduce space across offices, in a prudent manner consistent with our limited resources, as well as staff, lease and budgetary realities.

3) The Commodity Exchange Act mandates that the CFTC conduct economic research. This research covers matters of national importance like high frequency trading and the impact of trading on the price of commodities such as oil and gas. The Office of the Chief Economist had 39 economists in 2012, including: permanent employees, contractors who were paid to research particular issues, and unpaid consultants doing research. The contractors and consultants were among the brightest economic minds in the nation, with PhDs from the world's top universities. Today the office consists of 12 economists. This dramatic drop in economic expertise could prove detrimental to CFTC's economic regulatory efforts both now and in the future. How many consultants are currently providing unpaid research and what are their backgrounds? Why isn't CFTC making a greater effort to maximize the use of individuals who are willing to work for free? How many new research papers have been written since December 2012? How many of those research papers have been approved by the Office of the General Counsel and published?

I am committed to having a robust economic research program and a strong Office of the Chief Economist.

My understanding is that certain developments in 2012-13 impacted the ability of staff economists to collaborate with the academic community. First, in January 2013, then-Chairman Gary Gensler requested that the OIG investigate how OCE onboards staff, the Division's physical and information security, and a legal review of its papers to ensure that no confidential data was being improperly disclosed. Pending the completion of the OIG investigation, CFTC suspended all contractual engagements with academicians. After the OIG finished its investigation and the CFTC Management team reviewed all aspects related to the OCE Research program, in August 2014, CFTC started hiring academic contractors for research again.

We are currently looking at ways to strengthen and expand the office. There are some vacancies that the office is currently working on filling. In addition, with an increase in the CFTC's FY15 budget, OCE will be able to add additional full time economists. This increase is a key component of an ongoing strategy to rebuild CFTC's research program using both internal and external resources. CFTC also employs staff in other Divisions to conduct economic analysis to help inform the Commission and the public.

Staff has also been relying on regular interactions in the form of research seminars and academic conferences. These also provide opportunities for staff to leverage the expertise of the external research community.

While staff is engaged in multiple research projects, since December 2012, four new papers have been submitted to the Office of General Counsel (OGC) for review. Two of those papers have been approved and disseminated publicly, and OGC is currently reviewing another two papers submitted recently for review. More generally, a total of seventeen papers have been approved and disseminated during this period including papers in progress or completed by OCE Staff and academic consultants and contractors prior to December 2012.

4) According to the CFTC Inspector General's Office, the CFTC eliminated its one remaining Administrative Law Judge in December 2011. The Agency said that it was a cost-saving measure and that there was not enough work. Yet a CFTC employee, who is not an ALJ, was simultaneously retained to preside over cases. This employee lacks judicial independence, and makes more money than any ALJ. The Agency also retained the higher-paid Director of the Office of Proceedings, who currently directs just one judicial official. The CFTC also hired a new ALJ on a temporary basis to hear cases that are outside the jurisdiction of the higher-paid CFTC employee now presiding over cases. Dodd-Frank expanded the CFTC's jurisdiction into multi-trillion dollar swaps markets, meaning that important cases of first impression – cases that may set precedent for decades to come – will be decided by a rotation of Administrative Law Judges with no particular experience or expertise in the relevant law. Recently, the Wall Street Journal reported that the CFTC plans to direct even more cases to ALJs because it would save money. In the article, CFTC's Director of the Division of Enforcement stated "[the] overwhelming reason for this change is resources." The article went on to state, "Administrative cases are typically far faster and cheaper for agencies to litigate than ones in federal court, according to officials." If administrative cases are far faster and cheaper, why was the ALJ eliminated in the first place? From what agencies has CFTC been borrowing ALJs and what drawbacks do you see in using ALJs without commodities markets expertise?

The Commission decided over three years ago, in 2011, to eliminate its two ALJ positions. It is my understanding that this was done because the ALJs' workload had substantially declined (indeed, the number of cases brought to an ALJ by the Division of Enforcement had declined to zero many years before the decision to RIF the program was made), and elimination of the positions could achieve cost savings of approximately $800,000 per year. (The cost savings reflect the salaries of the ALJs as well as their staffs.) The utilization of scarce agency resources was and remains an important consideration in light of the Commission's greatly expanded duties under the Dodd-Frank Act and concomitant budget constraints.

As you indicate, at the time the ALJ program was discontinued, the Commission retained an employee as judgment officer to handle reparations cases and similar matters. Reparations cases involve matters where a member of the public may pursue damages against a CFTC registrant. The Administrative Procedure Act does not require that reparations cases go to ALJs but it does require that, whether heard by a judgment officer or an ALJ, the cases must go to the Commission for ratification. These cases, which had previously been heard by ALJs and judgment officers, had declined significantly, from 155 in 1997 to 34 in 2010 and it was determined that the caseload could be appropriately handled by a judgment officer.

As you also note, the Commission has an Office of Proceedings, including a director, which position has existed since approximately 1984. The Office of Proceedings is responsible for providing an impartial forum for handling customer complaints against persons or firms registered under the Commodity Exchange Act (CEA). The director and employees of the Office of Proceedings have responsibilities broader and more varied than supporting the judgment officer. These responsibilities include handling legal questions that arise in the pleading phase of reparations cases and all relevant agency rulemakings that affect the office.

Since 2011, the CFTC has used OPM's Administrative Judge Law Program to acquire ALJs for two cases. Both cases were assigned to the Chief Administrative Law Judge for the United States Coast Guard on November 14, 2013, and opinions in each case were issued on October 22, 2014.

The Commission's new Director of the Division of Enforcement, who was appointed in June 2014, recently said the Commission would consider bringing certain, appropriate matters administratively rather than in federal court. The Commission's recent experience in some cases litigated in federal court is that defendants use the breadth of the Federal Rules of Civil Procedure's pretrial discovery regime to engage in very burdensome and time-consuming pretrial litigation. Because of the Division's small size, a few cases can consume a disproportionate amount of the Division's available resources. The ALJ process is widely used by administrative agencies, affords adequate procedural safeguards and provides a pretrial discovery process that is more truncated. For these reasons, the new Director decided that it would be beneficial to have the option of bringing certain, selected cases before an ALJ instead of District Court. However, as the Director made clear in his public comments on the issue, the Division expects to continue to bring the vast majority of cases in Article III courts.

As noted above, the Division of Enforcement now has the option of bringing a small number of cases before an ALJ borrowed from the SEC. The law governing enforcement actions by the SEC and CFTC has long included significant overlap, and Dodd-Frank and the regulations issued pursuant to that statute only intensified the shared nature of this jurisprudence.

The cost of using borrowed ALJs in the manner noted above is not expected to approach the cost of the Commission's previous ALJ program and indeed can result in savings overall for the reasons noted above.