Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Testimony

Written Testimony of

Reuben Jeffery III, Chairman
Commodity Futures Trading Commission

Before the United States House of Representatives
Subcommittee on Agriculture, Rural Development, Food and Drug Administration, and Related Agencies

Committee on Appropriations

May 22, 2007

I am pleased to submit testimony on behalf of the Commodity Futures Trading Commission, and I appreciate the opportunity to address issues related to the Commission's 2008 Budget request.

I would like to review the impact of the commodity futures and options industry on the everyday lives of Americans, the mission and program responsibilities of the agency and, finally, our Fiscal Year 2008 congressional justification for the $116 million funding level requested by the Administration. This proposed funding level will enable the Commission to address its two major needs – staff increases and technology investment.

During the past 10 years, as can be seen in ***Figure 1,*** trading volume on U.S. futures exchanges has quintupled. Today, in a single day of trading, our markets will move more than $5 trillion. The industry has grown from largely agricultural product hedging to a broad array of complex instruments related to both physical commodities and financial instruments. Trading volume, measured by numbers of contracts traded, has more than tripled in just the past six years. At the same time, the Commission's staffing ceiling has fallen to 458 full-time employees. This compares with the 497 FTEs 30 years ago in 1976 – the Commission's first year of operation. Commission employees work hard, work smart, and use technology effectively, but given the complexity of the markets we oversee, they are stretched.

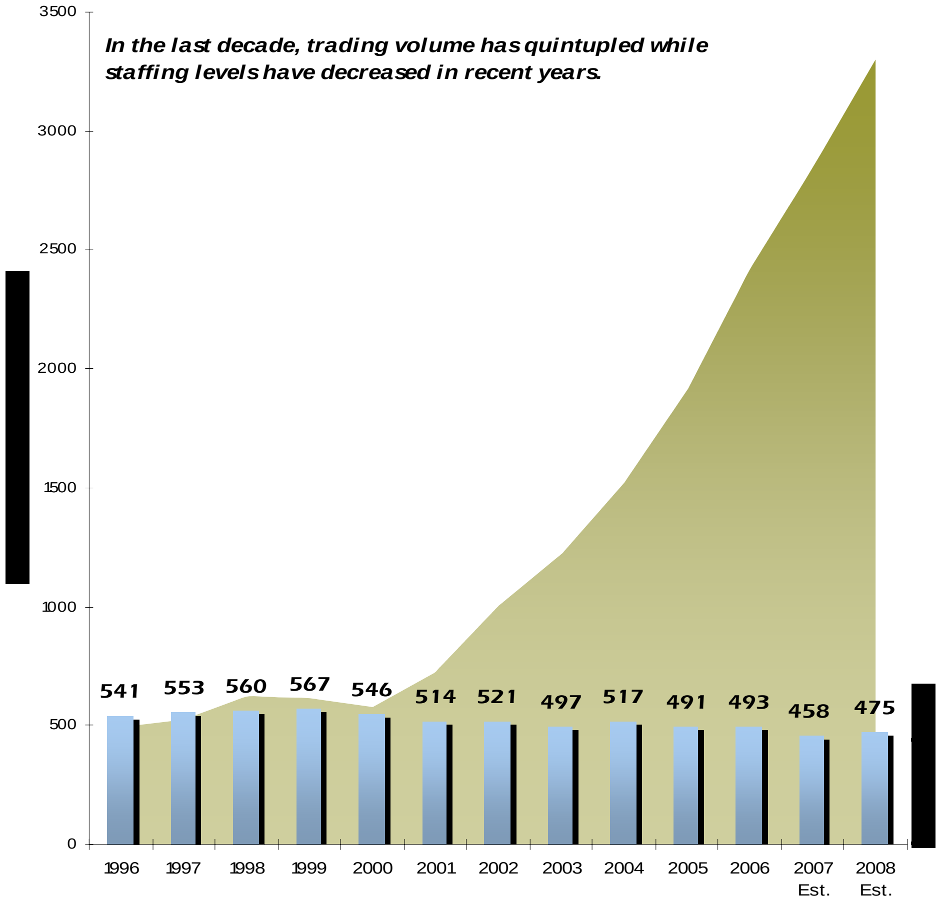

Figure 1: Growth of Volume of Contracts Traded and FTEs

Mission of the Agency

While the daily business of the CFTC can appear from the outside looking in to be somewhat obscure and highly technical in nature, the mission of the agency is very clear: 1.) to protect the public and market users from manipulation, fraud, and abusive practices and 2.) to promote open, competitive and financially sound markets for commodity futures and options. This is important because the futures markets are used in the price discovery process affecting the price of a bushel of wheat, the cost of a gallon of gas, and the interest rate on a student loan. If the futures markets fail to work properly all consumers are impacted.

Congress created the CFTC in 1974 as an independent agency with the mandate to regulate commodity futures and option markets in the United States. The Commission's mandate has been periodically renewed since then. In December 2000, Congress reauthorized the Commission through FY 2005 with passage of the Commodity Futures Modernization Act of 2000 (CFMA).

Commission Structure

The CFTC is the sole federal regulator responsible for overseeing the futures markets by encouraging competitiveness and efficiency, ensuring market integrity, and protecting market participants against manipulation, abusive trading practices and fraud. Through effective oversight, the CFTC enables the commodity futures and options markets better to serve their vital function in the nation's economy – providing an effective marketplace for price discovery and risk management.

To achieve its statutory mandate, the Commission employs a well-trained and dedicated staff who work within three major programs – Market Oversight, Clearing and Intermediary Oversight, and Enforcement.

Market Oversight

Market Oversight ensures that the futures markets are operating efficiently and without manipulation and fraud. One workload indicator is the number of actively traded contracts trading on U.S. exchanges. As can be seen in ***Figure 2,*** this number has more than quintupled in the last decade, with particularly significant growth seen in the last five years, or since the passage of the CFMA. Prior to 2000, the number of contract types traded was relatively stable at a level of around 250. By next year in FY 2008, the number of actively traded contracts is anticipated to climb to nearly 1,600, a record high. There is every indication that this significant growth in new and novel products will continue.

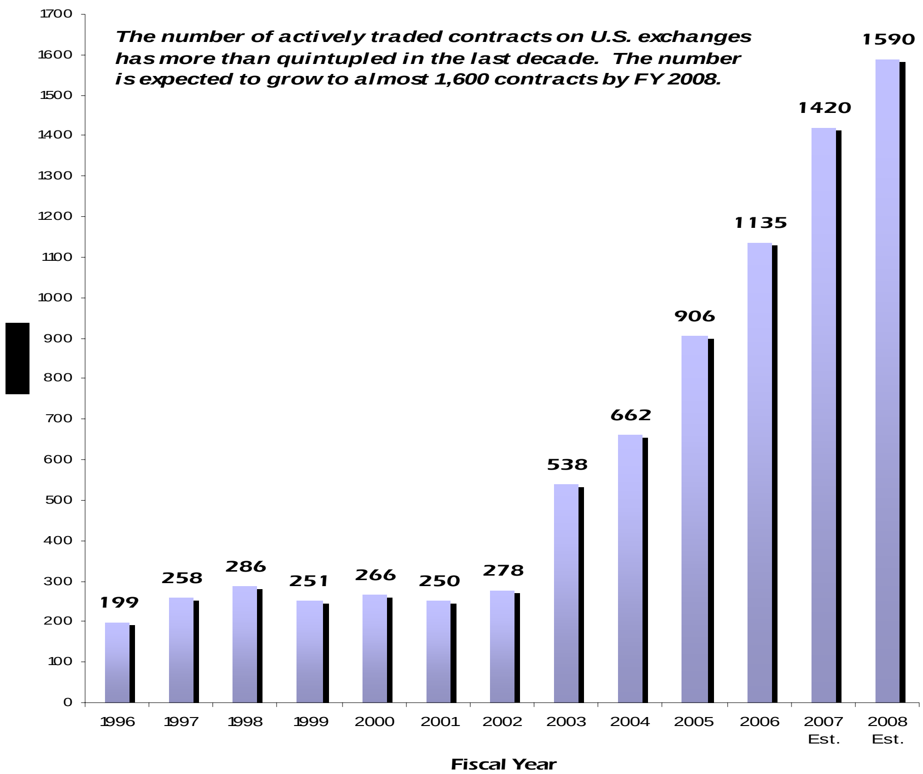

Figure 2: CFTC Actively Traded Contracts

The CFTC must maintain a sufficient level of specialized expertise to review and analyze a very diverse group of instruments and products to ensure that they are not susceptible to manipulation. The types of new products run the gamut from traditional commodity areas, such as new agricultural and energy futures, to novel financial derivatives based on credit risk, weather-related occurrences and effects, pollution allowances, real estate, and instruments having characteristics of both securities and commodities. Our analysts employ various methods to ensure an understanding of how the markets are functioning to develop a flexible, effective regulatory response to market conditions.

Clearing and Intermediary Oversight

Clearing and intermediary oversight ensures the financial integrity of all transactions on the markets that we regulate. The work of the staff is to ensure that the intermediaries managing these funds are properly registered, perform appropriate recordkeeping, have adequate capital, employ fair sales practices, and fully protect the funds their customers invest. The principal clearing operations are associated with the major commodity exchanges in New York, Chicago and Kansas City. Intermediaries overseen by the CFTC include some 200 futures commission merchants, the ranks of which include banks and broker-dealers with specialized futures operations, as well as stand-alone futures trading houses.

In ***Figure 3,*** one can observe that the amount of customer funds held by futures commission merchants has quadrupled over the past decade – meaning more and more Americans are trading in futures markets directly or indirectly through their participation in pension funds, mutual funds, and other institutions.

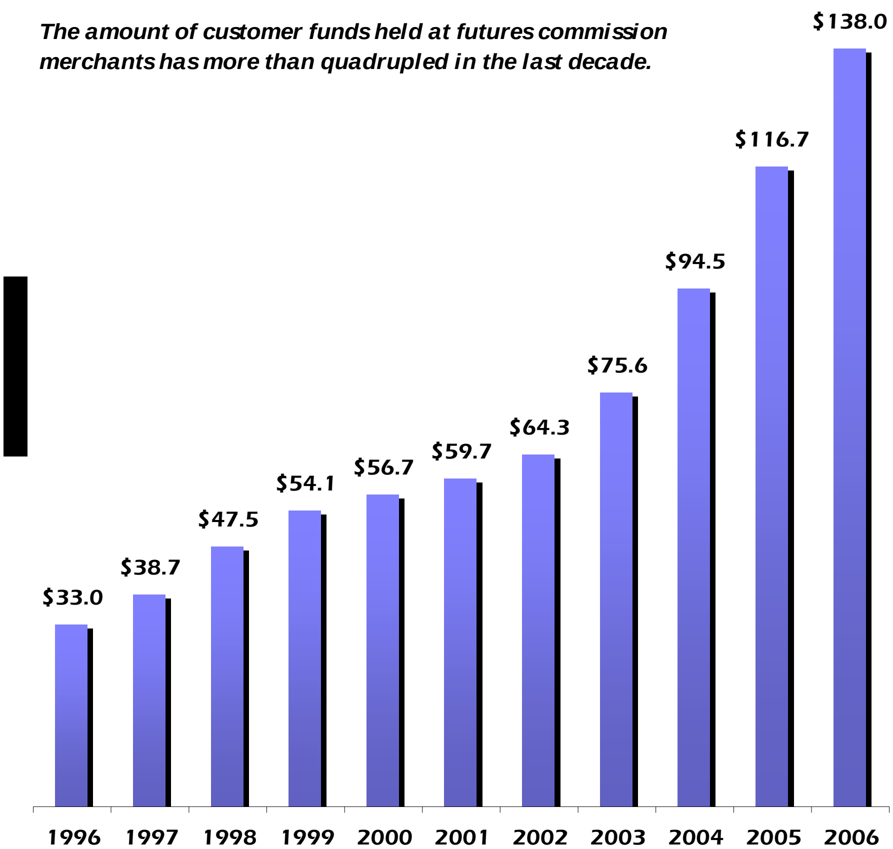

Figure 3: Customer Funds in FCM Accounts

Enforcement

The CFTC prides itself on its vigorous enforcement operation. Through strong enforcement, CFTC polices the markets – going after unscrupulous firms and individuals both on and off-exchange. Manipulation, fraud and other violations of the Commodity Exchange Act undermine the integrity of the markets and the confidence of market participants.

Figure 4 presents the results of the Commission's recent enforcement activity in the foreign currency and energy areas respectively. In the foreign currency or FOREX area, 96 cases involving 362 entities or persons were filed with more than $468 million in civil monetary penalties levied and $257 million in restitution awarded. Since the collapse of Enron, CFTC has brought 35 cases involving energy markets and charged 55 entities or persons with manipulation, attempted manipulation, and/or false price reporting. The collective civil monetary penalties levied exceed $303 million in these matters.

Actions Taken Since Passage of the CFMA in December 2000	**Foreign Currency Markets**[1]
Number of Cases Filed or Enforcement Actions	*96*
Number of Entities/Persons Charged	*362*
Number of Dollars in Penalties Assessed	
• *Civil Monetary Penalties*	*$468,135,562*
• *Restitution*	*$257,147,676*

Actions Taken Since Enron Bankruptcy in December 2001	**Energy Markets**
Number of Cases Filed or Enforcement Actions	*35*
Number of Entities/Persons Charged	*55*
Number of Dollars in Penalties Assessed	
• *Civil Monetary Penalties*	*$303,073,500*

Figure 4: Spotlight on Energy and Foreign Currency Markets

With the demand for enforcement resources exceeding capacity, CFTC must make hard choices every day on how to prioritize our investigative and litigation efforts.

Mission Support

The three major Commission programs are complemented by other offices, including our Office of the Chief Economist, Office of the General Counsel, Office of International Affairs and Office of Proceedings. The Commission's Executive Direction is comprised of the Chairman's and Commissioners' offices providing agency direction, and stewardship over CFTC's human capital, financial management, and information technology resources.

The Commission is headquartered in Washington, D.C., and maintains regional offices in Chicago, New York, and Kansas City. In recent years, budgetary considerations led to decisions to close the Los Angeles and Minneapolis offices.

[1] Since passage of CFMA in December 2000.

When looking at the increased volume of activity across all areas of the CFTC mission, and the scope of the industry change since 2000, the resulting increase in specialized workload is demonstrable. Accordingly, it is critical that the CFTC have sufficient resources to hire and maintain requisite skilled talent, as well as provide a steady stream of technology investment commensurate with the agency's expanding and evolving mission.

<u>FY 2008 President's Budget Request</u>

We are grateful for the Administration's recognition of the need for increased funding for our agency.

The FY 2008 President's Budget request, as seen in ***Figure 5,*** is for an appropriation of $116 million and 475 staff-years, an increase of approximately $18 million and 17 staff-years over the FY 2007 continuing resolution appropriation of $98 million which supports a level of 458 staff-years.

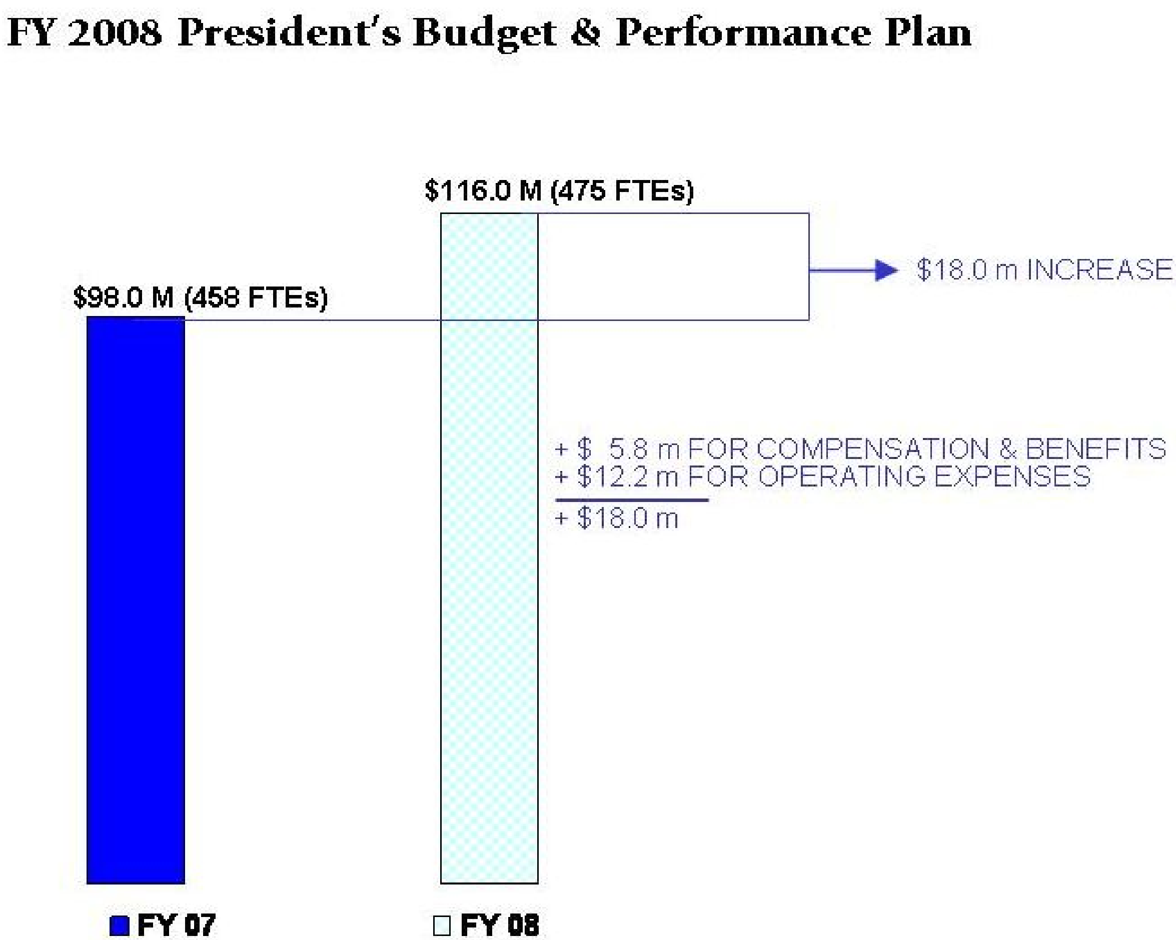

Figure 5: FY 2008 Budget Request Provides for Current Services and 17 Additional FTEs

Compared to the FY 2007 continuing resolution appropriation, key changes in the FY 2008 Budget are:

- $2.8 million to provide for increased compensation and benefit costs for a staff of 458 FTEs;

- $3.0 million to provide for salary and expenses of 17 additional full-time equivalent staff-years;

- $12.2 million to provide for increased operating costs for information technology modernization, lease of office space, and all other services.

This funding increase provides the Commission with the financial wherewithal to hire additional staff and to invest in technology. In staffing, the CFTC must compete for talent not only with the private sector, but also with the SEC and other federal financial regulators. Four years ago, the Congress improved our ability to compete, granting the CFTC comparable pay authority with other financial agencies (so called "pay parity" with the FIRREA agencies). For this authorization to level the compensation "playing field," all of us are deeply grateful. However, the Agency has not yet been fully appropriated to the level of comparable FIRREA agencies.

Second only to our human capital, technology is the single most effective tool in assisting those professionals who oversee the markets. Budgetary constraints have required the Commission over several years to put new systems development initiatives and hardware and software purchases on hold, as indicated in ***Figure 6***.

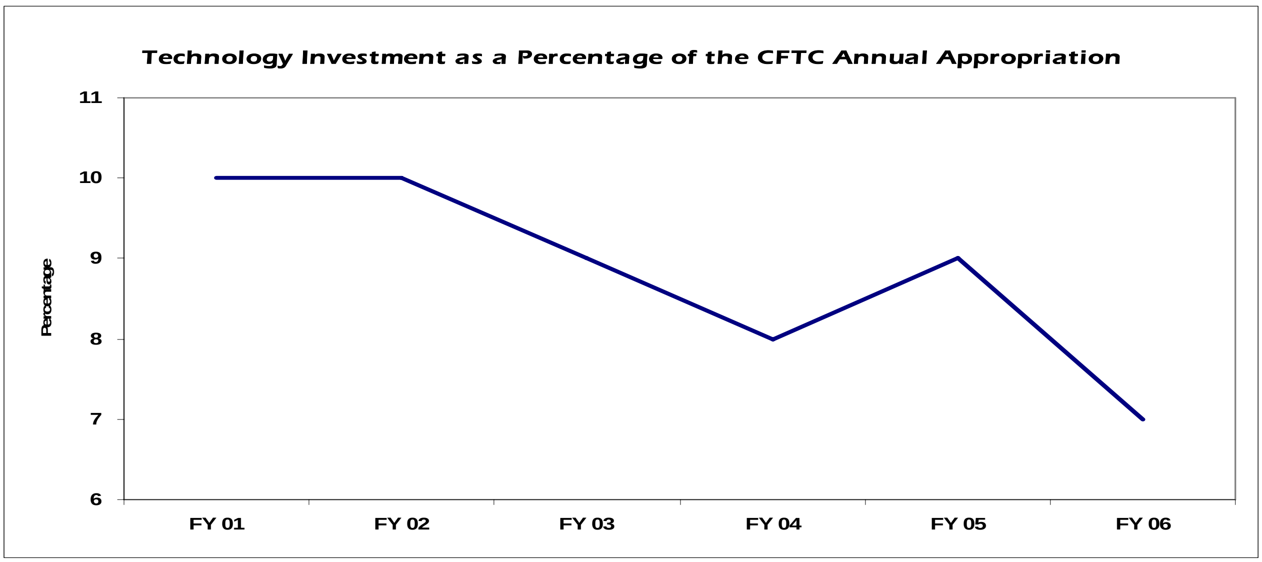

Figure 6: Technology Investment

CFTC analysts rely primarily on two proprietary computer systems for visibility into the markets. One gives us the ability to see who is trading in the markets and who is building leverage in the market or becoming a large trader – thus developing a position that may influence market conditions. The second allows us to pull in all transactional data from regulated exchanges to identify trading patterns that might be indicative of inappropriate or manipulative trading practices. These two major systems are unique in their ability to provide transparency into cross-market trading activity across all futures markets under the Commission's jurisdiction. Their importance to ensuring market integrity cannot be overstated.

The Commission respectfully requests the proposed funding increase for mission-critical investments in people and technology in order to keep up with the dynamic commodity futures and options industry. While relatively small in dollar terms, this funding increment is necessary to ensure that CFTC continues to be able to fulfill its statutory mandate.

All of us at the CFTC take great pride in our work. I can assure you that we are working diligently and efficiently to fulfill the important responsibilities with which the Congress and the American public have entrusted to us.