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Testimony

Oral Testimony of Walter L. Lukken, Acting Chairman, Commodity Futures Trading Commission Before the United States Senate

Subcommittee on Financial Services and General Government Committee on Appropriations

May 7, 2008

Thank you, Mr. Chairman and Members of the Subcommittee. I am pleased to be here to testify before you on behalf of the Commodity Futures Trading Commission (CFTC).

The CFTC is the agency charged with overseeing and regulating the U.S. commodity futures and options markets. These markets play a critical role in the U.S. economy by providing important risk management tools for market participants. The futures markets also serve to discover prices that accurately reflect supply, demand, and other economic factors.

These are extraordinary times for our markets with commodity futures prices at unprecedented levels. In the last three months, the agricultural staples of wheat, corn, soybeans, rice and oats have hit all-time highs. We have also witnessed record prices in crude oil, gasoline and other related energy products. Broadly speaking, the falling dollar, strong demand from the emerging world economies, global political unrest, detrimental weather and ethanol mandates have driven up commodity futures prices across-the-board.

On top of these trends, the emergence of the sub-prime crisis last summer led investors to increasingly seek portfolio exposure in commodity futures. As the federal regulator of these products, the CFTC is closely monitoring these growing markets to ensure they are working properly for farmers, investors, and consumers. To date, CFTC staff analysis indicates that the current higher futures prices generally are not a result of manipulative forces. That said, we continue to probe, investigate and gather information from the entire marketplace – and welcome outside analysis and perspectives – so that we can ensure that we have an accurate and full view.

For example, the agency convened an industry agriculture forum two weeks ago to have a full public airing of views as to the driving forces in these markets. The comment period for that event ends today and we hope to announce in the near future agency initiatives to address the concerns we heard at the forum. The CFTC also recently announced the creation of an Energy Markets Advisory Committee and scheduled its first meeting for June 10th to review the functioning of the energy markets.

Despite this tumultuous time in our markets, the agency continues to make advancements on important policy initiatives. Last fall, the Commission delivered an extensive Report to Congress recommending additional authorities for the agency in overseeing exempt energy trading. Through bipartisan efforts, these recommendations became a part of the CFTC's reauthorization legislation, which is contained in the Farm Bill conference report. The enactment of that legislation will improve oversight of the energy markets with the addition of new authorities at the agency. The President's FY09 budget does not take into account these new powers.

Evolution of the Markets

The U.S. futures and options markets of today bear little resemblance to the industry of 1976—the Commission's first year of operation—in terms of complexity, globalization, volume, and economic importance. Yet, staff resources and operating funds over time have not kept pace.

Figure 1 shows the growth in trading volume on U.S. futures exchanges from 1996 to present. Trading volume has increased six-fold during the last decade, while at the same time, Commission staffing levels have fallen to 447 full-time employees. That's 50 fewer staff today than the agency had 30 years ago.

Figure 2 lists the many different components of the futures industry. As you can see from the chart, the growth in these categories from 1976 to present is stunning. For instance, total contract volume has increased more than 8,000 percent in thirty years compared to CFTC staffing and overhead expenses, which have decreased 12 percent and 5 percent respectively.

FY09 Budget

On behalf of the entire Commission, I would like to express my appreciation for the support provided to the CFTC in the FY08 budget. The $111 million appropriated by Congress for the current calendar year is already being put to good use to address critical needs in two major areas – personnel and technology. That focus will continue with the FY09 budget.

The Commission employs highly-trained individuals who work within three program divisions – Market Oversight, Clearing and Intermediary Oversight, and Enforcement.

The Division of Market Oversight ensures that the markets are operating efficiently and free from manipulation and fraud. The Commission's staff economists utilize the Commission's large trader reporting system and one of the Commission's main technology systems, the Integrated Surveillance System (ISS), to detect and deter market manipulation. As you can see in ***Figure 3***, the current atmosphere of rising futures prices across a wide range of products makes these anti-manipulation efforts all the more important.

The Division of Clearing and Intermediary Oversight ensures the financial integrity of the futures industry as a whole. The amount of funds handled by clearing houses has increased significantly of late. During this time, all exchanges have experienced record settlements, including one day in January 2008 in which the Chicago Mercantile Exchange cleared and settled more than $12 billion worth of transactions—nearly six times its normal load. Despite these spikes in cash flow, the clearing system has worked well.

When a manipulation or fraud occurs in the marketplace, it is the job of the Enforcement Division to prosecute the offenders. Since the collapse of Enron, CFTC has brought 39 cases involving energy markets and charged 64 entities or persons with manipulation, attempted manipulation, and false price reporting. The collective civil monetary penalties levied in these energy market enforcement actions exceed $444 million.

Unfortunately, these programs have felt the effects of turnover at the agency. The Commission lost 58 experienced employees in FY06, 49 in FY07 and 15 to date in FY08. Replenishing these losses is critical if this agency is to continue to meet its responsibilities in overseeing the futures markets.

The FY09 President's Budget request, as seen in ***Figure 5,*** is for an appropriation of $130 million and 475 full time staff, an increase of approximately $18.7 million and 10 staff over the FY08 appropriation.

Key changes in the FY09 Budget are:

- $3.2 million to provide for increased compensation and benefit costs for current employees;

- $1.9 million to provide for salary and expenses of 10 additional full-time employees. This increase – although modest – will allow us to build on current key hiring efforts.

- $13.6 million to provide for increased operating costs for technology modernization, office space, and all other services.

In FY09, the requested increased funding will continue to target technology upgrades and staffing increases. It would permit the Commission to improve existing critical technology systems, such as ISS and eLaw. The funds requested would also permit continued development of the new Trade Surveillance System (TSS). Soon, with these investments, we will have the capability to more quickly monitor and analyze a trader's intraday trading activity.

In conclusion, I am very proud of the agency and our highly-skilled staff. Everyday, they carry out the agency's mission of protecting the public and market users from manipulation, fraud, and abusive practices. If the futures markets fail to work properly, all Americans are impacted. Accordingly, it is critical that the CFTC have sufficient resources to hire and maintain skilled talent, as well as provide a steady stream of technology investment commensurate with the agency's expanding and evolving global mission.

Thank you for the opportunity to appear before you today on behalf of the CFTC. I would be happy to answer any questions you may have.