



SENATE APPROPRIATIONS SUBCOMMITTEE HEARING

OVERVIEW

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Today, the Senate Appropriations Subcommittee on Financial Services and General Government held a hearing to review the President's FY 2017 funding request and budget justification for the Securities and Exchange Commission (SEC) and the Commodity Futures Trading Commission (CFTC).

Key Takeaways

- Chairman Massad said that by the end of the year, the CFTC plans to finalize a position limits rule that prevents excessive speculation while making sure commercial end-users can engage in *bona fide* hedging (BFH), and that the agency is focused on approving a process for granting exemptions that are not enumerated (as a BFH) but deserve an exemption.
- Chair White said Dodd-Frank Title VII security-based swap (SBS) reforms are a priority, and plans to have the reporting and dealer regime go live by the end of the year.
- On the swap dealer *de minimis* level, Massad stated that staff is working on a final report that should be issued within the next few months to put the Commission in a position to make a decision.
- White explained that the SEC does not have the authority to review and approve FINRA's budget, and whether or not it should have that authority is up to Congress. She said the SEC is transitioning to allow FINRA to exam more broker-dealers (BDs) in order for the agency to focus more on investor adviser (IA) exams.

SUMMARY

Opening Statement and Testimony

[Chairman John Boozman \(R-AR\)](#)

- The SEC is requesting \$1.781 billion, which is \$176 million or 11% higher than FY 2016. Since FY 2000, the SEC budget has grown from \$377 million to now \$1.6 billion.
- While the SEC is a fee-funded agency, Congressional oversight over the Commission's budget is critical. Although those fees come from public companies and exchanges, they are borne by investors, and Congress has a responsibility to ensure those funds are being spent in a manner that protects investors, helps markets operate efficiently, and spurs economic growth for all Americans.
- The CFTC is requesting \$330 million, 32% more than FY 2016 – the CFTC's leasing costs and practices have raised concerns about effective management of Federal funding.
- Inconsistent rules at the SEC and the Department of Labor (DOL) governing fiduciary standards continue to cause uncertainty and confusion.

Ranking Member Christopher Coons (D-DE)

- We should not let down our guard on financial markets just because the economy is recovering.

- It is critical that Congress provide the resources to these agencies to protect investors and to maintain orderly markets.

Mary Jo White, Chair, SEC

- The SEC is charged with overseeing approximately 27,000 market participants with additional duties and expanded jurisdiction. The requested FY 2017 budget will permit the agency to hire 250 additional staff in mission critical, core areas.
- Specifically, the FY 2017 budget request seeks to:
 - Increase examination coverage of IAs and other key entities who interact with retail and institutional investors;
 - Further leverage cutting-edge technology to permit the SEC to better keep pace with the entities, markets, and products we regulate;
 - Protect investors by enhancing our enforcement program's investigative capabilities and strengthen our ability to litigate against wrongdoers;
 - Further bolster the SEC's economic and risk analysis functions; and
 - Hire market and other experts to enable the SEC to more expertly and efficiently discharge its current rulemaking and oversight responsibilities.

Tim Massad, Chairman, CFTC

- The CFTC has taken a number of actions to make sure commercial end-users can use the derivatives markets effectively.
- Sensible regulation requires adequate resources - approximately 36% of the budget increase will be dedicated to technology enhancements.
- The increase will help hire additional staff, enhance surveillance, increase examinations, and allow the CFTC to be more responsive to the concerns of commercial end-users.

Discussion

Position Limits

Boozman: What is the CFTC doing to ensure the rule works for commercial end-users? *Massad:* The CFTC is taking its time to implement a position limits rule (Congressionally mandated) that prevents excessive speculation while making sure commercial end-users can engage in BFH. We are focused on a process of granting exemptions that are not enumerated (as a BFH) but deserve an exemption. It is important to have the most updated deliverable supply estimates. The goal is to complete this rulemaking by the end of this year.

Boozman: The CFTC's inspector general revealed that the Office of the Chief Economist (OCE) is no longer permitted to conduct research that might conflict with the agency's stance on position limits, why? *Massad:* We have no political screen on OCE, simply priorities. OCE must prioritize its research due to limited resources – I want to hear all positions whether it conflicts with my views or not.

Security-Based Swaps Reform

Boozman: Status of Title VII implementation at the SEC? *White:* The SEC has proposed over half of its rulemakings, proceeding via an established roadmap. Title VII is a priority and we envision the reporting and dealer regime to go live by the end of the year.

Lankford (R-OK): Are the SEC and CFTC coordinating in rulemakings? What is the timing of SEC swaps rulemakings? *Massad:* Congress divided jurisdiction on swaps markets, but the agencies are working together issue such as on capital, swap data reporting, and clearinghouse regulations, amongst other things; *White:* The SEC is cognizant on what the CFTC and foreign counterparts have done (i.e. cross-border). The SEC looks closely at everything the CFTC has done – rules will not be identical but will be compatible for market participants.

High-Frequency Trading (HFT)

Coons: Do you have enough resources to regulate, oversee, and understand significant developments in HFT? *White:* If an HFT engages in bad behavior we have enforcement authority. The SEC is looking at equity market structure and the anti-disruptive trading rule to regulate harmful trading in periods of market volatility; *Massad:* No, the CFTC does not have enough resources to keep up with the marketplace. Almost all trading today is electronic and automated and warrants analyzing huge amounts of data. Our surveillance capacity is not where it needs to be, both IT and personnel. We recently issued a proposal requiring trading firms to maintain adequate risk controls.

Swap Dealer *De Minimis* Level

Moran (R-KS): Does the CFTC intend to issue an interim final rule to maintain the \$8 billion *de minimis* level? *Massad:* The preliminary study is out for comments and staff is working on a final report to put the Commission in a position to make a decision. We are taking the study seriously as the Omnibus bill requires, and do not want the level to be arbitrary or disruptive to the market. The final study should be ready within the next few months. The CFTC wants to provide market participants with adequate time to prepare and to comply.

Market Liquidity

Moran (R-KS): Do new and prudential market regulations contribute to market liquidity, and would this have a price impact for consumers? *White:* Sufficient liquidity is of concern, and we continue to study the cumulative impact of regulations during every rulemaking. Some academics have concluded that Dodd-Frank and other regulations have not impacted liquidity, but more studies are under way.

Clearinghouse Equivalence

Durbin (D-IL): The SEC needs to finalize its rules before receiving clearinghouses recognition in Europe – why is rulemaking taking so long? *White:* This rulemaking is a priority as reflected on the regulatory flex agenda, and we are currently studying comments to a recent proposal. Throughout this period, markets have not been disrupted.

FINRA Oversight

Boozman: Does the SEC review and approve FINRA's budget? If not, should the SEC play a role in the budget with FINRA's increased delegated authority? *White:* The SEC does not review and approve FINRA's budget, but it is reviewed during the examination of FINRA. The SEC is transitioning to allow FINRA to exam more BDs in order for the SEC to conduct more IA exams. Whether the SEC needs the authority to review and approve FINRA's budget is up to Congress.

Cybersecurity

Coons: What is currently underway to enhance cybersecurity protections? *White:* \$14.7 million of the budget request will go towards securing our own data. Recently implemented Regulation SCI enhances the resiliency of critical market infrastructures and how they respond to incidents. For the third year in a row, BD and IA exams have been a priority, and we try to share results in an appropriate way so other participants can take advantage of best practices. The Division of Corporation Finance issued guidance

on disclosing material incidents, and enforcement is active in safeguarding customer data; *Massad*: About \$3 million is spent directly on cybersecurity. We are focused on examinations of exchanges and clearinghouses but simply do not have enough examiners. A proposal was recently issued to enhance cybersecurity testing by registrants.

Leasing

Boozman: Given the CFTC's faulty track record (accounting), are you open to having the Government Accountability Office (GAO) assist in negotiating future leases? Are you willing to support codification of leasing practices? *Massad*: We are working on giving back unused space. The leasing decisions were made in 1994 and we are taking steps to fix the issue. We are open to working with GAO in the future and about discussing codification.

Corporate Political Spending Disclosure Rule

Boozman: The Omnibus bill prevents the SEC from using funds to issue any rules or regulation that pertain to political spending – have you taken any action since the bill was passed? *White*: No.

Enforcement

Durbin (D-IL): How much money was generated from enforcement last year? *Massad*: \$2.8 billion.

Coons: Is your enforcement caseload a signal of more illicit activity or is the agency getting better at enforcement? *White*: The SEC has emphasized proceedings against individuals to deter bad acts, however, deterrence is hard to measure. As the only agency with a standalone collection function, there are significant impediments in collecting some penalties; *Massad*: Benchmark cases have led to dramatic changes to the administration of benchmarks (to prevent manipulation). New forms of manipulation like spoofing have led to the first successful criminal prosecution. To be able to bring those cases, the agency needs to enhance its IT systems. Statutory assistance is needed to raise fines.

Whistleblower

Coons: Importance of whistleblowers? *White*: Whistleblower cases have been successful. We are working to protect against whistleblower retaliation; *Massad*: The challenge is following up on the tips with inadequate resources.

Retroactive Review

Lankford (R-OK): Status on retroactive review of rules? How are you dealing with political pressures on mandatory disclosures (i.e. climate change, gun purchases, etc.)? *White*: The SEC has undertaken a comprehensive review of Regulation NMS, and other rules for impacts on small businesses. We are reviewing these issues simultaneously with implementation of the JOBS Act. The SEC is an independent agency and it is critical that we maintain that independence. We listen to everyone, but make our own decisions – mandated disclosures are based on materiality.

DOL Fiduciary Rule

Boozman: Where is the SEC in the rulemaking process? *White*: I am only one vote of five Commissioners. Personally, I want to advance a uniform fiduciary rule. Staff has been directed to provide a recommendation.