



## U.S. COMMODITY FUTURES TRADING COMMISSION

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Office of the  
Inspector General

### MEMORANDUM

**TO:** Gary Gensler  
Chairman

**FROM:** A. Roy Lavik   
Inspector General

**DATE:** December 13, 2013

**SUBJECT:** Inspector General's Assessment of The Most Serious Management Challenges Facing the Commodity Futures Trading Commission (CFTC)

#### Introduction

The Reports Consolidation Act of 2000 (RCA)<sup>1</sup> authorizes the CFTC to provide financial and performance information in a meaningful and useful format for Congress, the President, and the public. The RCA requires the Inspector General to summarize the “most serious” management and performance challenges facing the Agency and to assess the Agency’s progress in addressing those challenges.<sup>2</sup> This memorandum fulfills our duties under the RCA.

In order to identify and describe the most serious management challenges, as well as the Agency’s progress in addressing them, we relied on data contained in the CFTC financial statement audit and Annual Financial Report, representations by agency management, and our knowledge of industry trends and CFTC operations. Since Congress left the determination and threshold of what constitutes a most serious challenge to the discretion of the Inspector General, we applied the following definition in preparing this statement:

Serious management challenges are mission critical areas or programs that have the potential for a perennial weakness or vulnerability that, without substantial management attention, would seriously impact Agency operations or strategic goals.

This memorandum summarizes the results of the CFTC’s current financial statement audit, describes the Agency’s progress on last year’s management challenges, and finally discusses the most serious management challenges that we have identified. For FY2014, the most serious management challenge is:

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<sup>1</sup> P.L. 106-531, sec 3, 114 STAT. 2537 (Nov. 22, 2000), *codified at* 31 USC § 3516(a).

<sup>2</sup> *Id.*

- For the CFTC to deliver on Congressional expectations embedded in the Wall Street Reform and Consumer Protection Act (Dodd Frank Act), including expansion of the CFTC's regulatory footprint to the swaps markets, while adhering to government-wide budgetary constraints.

## **CFTC Financial Statement Audit Results**

In accordance with the *Accountability of Tax Dollars Act*,<sup>3</sup> CFTC, along with numerous other federal entities, is required to submit to an annual independent financial statement audit by the Inspector General, or by an independent external auditor as determined by the Inspector General.<sup>4</sup> The results of the Fiscal Year 2013 financial statement audit will be discussed in the Annual Financial Report, and the financial statement audit is expected to result in an unmodified audit opinion.

## **CFTC's Progress on Last Year's Challenges**

Last year, we identified two of the most serious management challenges:

- Efficient Deployment of Information Technology Resources; and,
- Expanding Delivery of Customer Protection Resources and Consumer Education.<sup>5</sup>

CFTC made progress on both challenges, but these challenges remain a concern due to government wide budget cuts which will require management to prioritize increased oversight responsibilities while implementing the Dodd-Frank Act.

In FY2014, under a government-wide continuing resolution, CFTC allocated \$42<sup>6</sup> million towards technological tools-which is unchanged from FY 2013 and a decline of \$9 million from FY 2012 spending levels. However, during FY2013, CFTC's regulatory responsibility over the \$400 trillion<sup>7</sup> swaps market increased with the availability of continuous data on swap transactions that must be analyzed and sifted for anomalous activity to initiate referrals to Division of Enforcement. Therefore, this management challenge remains a concern given CFTC's declining budget under sequestration.

Our FY2013 financial statement audit of the CFTC Customer Protection Fund confirmed that the financial statements presented the fund's financial position fairly, in all material respects, and

<sup>3</sup> P.L. 107-289, 116 STAT. 2049, Nov. 7, 2002, *codified at* 31 USC 3501 note.

<sup>4</sup> The IG's authority is found at § 304 of the CFO Act, P.L. 101-576, 104 STAT.2852, Nov. 15, 1990, *codified at* 31 USC 3521(e).

<sup>5</sup> Section of 748(g) of the Dodd-Frank Act, P.L. 111-203, 124 STAT. 1376, July 21, 2010, added section 23(g) to the Commodity Exchange Act, 7 U.S.C. § 26, to establish within the Treasury of the United States a revolving fund that is available to the Agency for the payment of whistleblower awards and education initiatives. The FY2013 audit is available here: <http://www.cftc.gov/ucm/groups/public/@aboutcftc/documents/file/cpfreport2013.pdf>.

<sup>6</sup> CFTC- Fiscal Year 2013 Agency Financial Report, Exhibit 26.

<sup>7</sup> *Id.*, at page 13.

that the fund was fully funded.<sup>8</sup> As a result of this audit our near term goal is to evaluate how the Customer Protection fund is using its available resources to reach potential participants in the commodities markets with impartial and educational information. We have begun an audit to assess CFTC's Customer Protection Resources and Consumer Outreach Program area's emphasis on delivering targeted and educationally useful information to likely participants in the commodities related markets.

### **Most Serious Management Challenges for the coming year**

The most serious management challenge anticipated for FY 2014 is for the CFTC to deliver on congressional expectations in the implementation of Dodd-Frank, including expansion of the CFTC's regulatory footprint to the swaps market, while adhering to government wide budgetary constraints.

CFTC has promulgated over 67 rules, orders, and guidances responsive to the Dodd-Frank Act.<sup>9</sup> Now that these rules are in place, management must develop additional mechanisms to shift agency productivity from rule writing to rule implementation. As we have identified in the past, technological spending can increase staff productivity, but the sheer volume and complexity of industry-supplied data mandates that knowledgeable agency staff be on hand to provide the guidance necessary to efficiently monitor the markets. With the availability of ownership control<sup>10</sup> information across markets, CFTC surveillance of the swaps markets is broader and more complex than the agency's pre-Dodd Frank Act mission of monitoring futures and options on futures markets. Therefore, the agency must adjust its regulatory strategy to reflect its expanded jurisdiction.

Moreover, increased reportable data will increase stakeholders' expectation that CFTC will conduct a robust oversight of the swaps market. On January 1, 2013, certain swap market participants began reporting new and historical swap data to Swap Data Repositories pursuant to 17 CFR Part 45, and the Commission began the process of analyzing these new data and incorporating them into the weekly CFTC Swaps Report available on its website.<sup>11</sup> As a consequence, the agency must now devote labor to the continuous surveillance of the swaps markets. In addition, the agency is expanding its oversight of Swap Execution Facilities (SEFs) - trading platforms that must be registered with the CFTC. Such structural changes will require the CFTC to expand compliance reviews of SEFs as they come online. This reinforces our assessment that the agency, in the near future, will have to examine its current labor skill set and reallocate resources – a challenge during sequestration – towards compliance matters as opposed to rule making.

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<sup>8</sup> The audit report is available here:

<http://www.cftc.gov/ucm/groups/public/@aboutcftc/documents/file/cpfreport2013.pdf>.

<sup>9</sup> See remarks of Chairman Gensler at the CME Global Financial Leadership Conference, Nov. 19, 2013 (available here: <http://www.cftc.gov/PressRoom/SpeechesTestimony/opagensler-153>).

<sup>10</sup> See Remarks of Chairman Gensler, Ownership and Control ("OCR") Reports, Forms 102/102S, 40/40S, and 71, October 30, 2013 (available at: <http://www.cftc.gov/PressRoom/SpeechesTestimony/genslerstatement103013>); see also 78 FR 69177-69266 (Nov. 18, 2013)(Final rules for ownership and control reports, effective date Feb. 18, 2014, available at: <http://www.gpo.gov/fdsys/pkg/FR-2013-11-18/pdf/2013-26789.pdf>).

<sup>11</sup> See <http://www.cftc.gov/MarketReports/SwapsReports/index.htm>.

## **Relevant OIG audits**

My Office plans to contribute meaningful independent analyses towards aiding the agency to explore solutions to its challenges. Toward that goal my office is completing an audit of CFTC compliance with information security management requirements and has initiated an audit to examine the CFTC's recent allocation of resources to information technology. As previously mentioned, we are also conducting an audit to assess CFTC's Customer Protection Resources and Consumer Outreach Program area's emphasis on delivering targeted and educationally useful information to likely participants in the commodities related markets. These audits along with our two financial statement audits and other program audits and reviews provide us with valuable data for evaluating future challenges at the CFTC.

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