May 17, 2012

The Honorable Spencer Bachus
Chairman
Committee on Financial Services
U.S. House of Representatives
Washington, DC 20515

The Honorable Barkey Frank
Ranking Member
Committee on Financial Services
U.S. House of Representatives
Washington, DC 20515

The Honorable Tim Johnson
Chairman
Committee on Banking, Housing and
Urban Affairs
United States Senate
Washington, DC 20510

The Honorable Richard Shelby
Ranking Member
Committee on Banking, Housing and
Urban Affairs
United States Senate
Washington, DC 20510

Re: Increased and Reliable Funding for the SEC and the CFTC

Gentlemen:

On behalf of the American Bar Association (“ABA”), which has almost 400,000 members, we are writing regarding the pressing need to provide increased and reliable sources of funding for the operations of the Securities and Exchange Commission (“SEC”) and the Commodity Futures Trading Commission (“CFTC”). This issue has become particularly acute in light of the extensive and growing legislative and regulatory demands on those agencies arising out of the recent financial crisis, including new statutory mandates enacted last month in the Jumpstart Our Business Startups Act (“JOBS Act”). As Co-Chairs of the ABA Task Force on Financial Markets Regulatory Reform,1 we have been authorized to express the ABA’s view on this important topic.

Background: The Need for Adequate and Reliable Sources of Funding

Effective regulation of financial markets depends critically on the principle, strongly endorsed by the Task Force and formally approved by the ABA House of Delegates in August 2009, that “Financial services regulators should be independent, with adequate and reliable sources of funding sufficient to carry out their responsibilities.”2 The ability of these regulators to operate in a highly

1 The ABA Task Force is comprised of 15 prominent financial services lawyers who have served in the top levels of government and private practice. The Task Force includes former general counsels of the SEC, the Federal Deposit Insurance Corporation (“FDIC”), and the Treasury Department, as well as members and liaisons who have held high-level positions with the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency (“OCC”), and the SEC. Also included on the Task Force is a founder of Public Citizen Litigation Group and leading academics in the law relating to financial entities and administrative law. The complete Task Force roster is available online at: http://apps.americanbar.org/buslaw/committees/CL116000pub/materials/publicroster.pdf.

effective and proficient manner – with a focus on the long-term stability and integrity of the financial system – is essential to maintaining strong financial markets in which the public can place its confidence. The increasingly rapid pace of change in financial markets in recent years, accompanied by frequently shifting public attitudes, growing marketplace complexity and expanding cross-border capital flows, has posed a serious challenge to the regulators’ ability to perform their functions consistent with the objective of maintaining a stable and dynamic financial system.

As the events of recent years confirm, the pace of regulatory change will necessarily be swift in moments of crisis. At the same time, the broad evolution of regulatory policy requires sustained and deliberate efforts by federal agencies, often over a period of years, to identify and implement regulatory policies that will help assure the stability and efficient functioning of the financial markets central to the nation’s economy. The ongoing development of thoughtful and effective new regulatory approaches thus generally cannot occur if regulators have insufficient ability to plan for longer term developments and must devote all of their limited and unpredictable resources to short-term fluctuations in market sentiment and public attitudes.

Moreover, less than two years ago, as you know, Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”), which assigned mandates for hundreds of new rules and studies and numerous other new responsibilities to the SEC and the CFTC. As a result of the Dodd-Frank Act, the size of the markets to be regulated by the agencies has increased several times over, and the agencies will be responsible for overseeing hundreds of new registrants. Despite calls for increased and independent sources of funding for those agencies at the time, Congress has not authorized these agencies to become self-funding through the use of industry-paid fees. Further, it is increasingly clear that the agencies’ current funding levels are inadequate to meet the growing challenge of overseeing modern financial markets, including the need to complete effectively their congressionally assigned tasks under the Dodd-Frank Act and other legislation, such as the recently-enacted JOBS Act.

SEC and CFTC Funding

The ABA has long favored greater funding for the SEC in order to enable the agency to fulfill its ever growing mission as determined by Congress. In light of the dramatically expanded responsibilities and mandates that the Dodd-Frank Act has imposed on the SEC and the CFTC as outlined above, we consider it urgent and crucially important for Congress to further re-examine its approach to funding these agencies in order to provide them with stable and more predictable sources of revenue. Therefore, the ABA strongly favors authorizing self-funding of these agencies to achieve these objectives.

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4 In February 2003, for example, the ABA House of Delegates adopted ABA Resolution 301 which called for greater financial support for the SEC and urged Congress to fund the Commission “at adequate and reasonable levels to enable it to fulfill its statutory responsibility of protecting investors and ensuring market integrity.” ABA Resolution 301 is available online at: http://www.americanbar.org/content/dam/aba/directories/policy/2003_my_301.authcheckdam.pdf
The Federal Reserve Board, the FDIC and the OCC are self-financed. The Federal Reserve Board primarily derives its income from interest on U.S. government securities it has acquired through open market transactions, and also from interest on foreign currency investments, fees received for services provided to depository institutions, and interest on loans to depository institutions. After it has paid for its operating expenses, the Federal Reserve Board turns the rest of its revenues over to the U.S. Treasury. The OCC is funded primarily through its assessments on national banks. These banks pay for their examinations and pay for the processing of their corporate applications. The OCC is also funded by income from its investments, primarily in U.S. Treasury securities. The FDIC is funded by premiums paid by banks and thrift institutions for deposit insurance coverage and from its own investment in U.S. Treasury securities.

By contrast, the SEC and CFTC are funded by annual congressional appropriations. Yet, the SEC collects more in fees than its annual budget. From 2005 to 2009, the SEC collected approximately $7.4 billion from transaction and registration fees that were turned over to the U.S. Treasury, but Congress appropriated only $4.5 billion for the agency’s budgets during that period. Notably, these amounts are wholly apart from the enormous sums of money that each agency collects in its enforcement cases – which we do not believe should be included in any self-funding mechanism.

When the Dodd-Frank Act was under consideration, there was a strong push for SEC self-funding by SEC Chairman Mary Schapiro, former SEC Chairmen, securities lawyers and some senators. The reasons given for such self-funding include the following: (1) self-funding is necessary to eliminate the chronic under-funding of the SEC; (2) self-funding would enable the SEC to make multi-year commitments to build technology and infrastructure; (3) self-funding for financial regulators is common for other agencies; and (4) the money for self-funding could come from transaction and registration fees already provided for by Congress. Comparable reasons apply to self-funding of the CFTC. The problem with annual congressional appropriations is that overall funding priorities can shift, leaving the agency short-handed when it needs funding the most. During the 1990s, the SEC staff barely grew, even though the volume and value of securities transactions greatly increased. During the next decade, the SEC had flat or declining budgets.

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6 About the OCC, available at http://www.occ.treas.gov/about/about.html.
9 The ABA does not favor inclusion of enforcement collections as part of self-funding in light of the potential conflicts of interest that could arise if an agency had a financial stake in amounts obtained from parties against whom it brings actions. By way of factual background, we note that in fiscal year 2010, the SEC and CFTC collected over $2.9 billion in penalties and disgorgement. U.S. Securities and Exchange Commission, FY2010 Performance and Accountability Report, p. 11, available at http://www.sec.gov/about/secpar2010.pdf#2010review, and U.S. Commodity Futures Trading Commission, FY 2012 President’s Budget and Performance Plan, p. 84, available at http://www.cftc.gov/ucm/groups/public/@newsroom/documents/file/cftcbudget2012.pdf. Although some of these funds are returned to investors, any remainder goes to the U.S. Treasury.
10 Letter from Federal Bar Association Securities Law Committee Executive Council, June 11, 2010 to Sen. Saxby Chambliss et al. This letter was subsequently endorsed by over 100 securities lawyers.
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The CFTC, in turn, reached a low point in staffing in 2007, with 23 percent less staff than the
agency had in 1999 even as the futures and options markets the agency regulated increased five-fold
over that period.\textsuperscript{12} Although it is difficult to assign cause and effect, this lack of reliable and
adequate funding certainly did not assist the agencies in attempting to anticipate the financial crisis
of 2008.

The SEC and the CFTC were not given self-funding authority in the Dodd-Frank Act. Congress
recognized the need for the SEC to at least double its budget and to engage in contingency and
multi-year budgeting, and the SEC was given some greater independence to determine its funding
needs. The CFTC’s budget has also increased since then. Yet, Congress has not given either
agency all of the necessary increased funding identified at the time that the Dodd-Frank Act was
enacted.

**Oversight of the SEC and CFTC**

The absence of adequate and reliable sources of funding for the SEC and the CFTC will, in our
view, substantially detract from the agencies’ ability to achieve the critical regulatory missions
assigned to them by Congress. Self-funding of these agencies can effectively address this concern –
and it can do so consistent with the important congressional interest in ongoing review of the
agencies’ activities, particularly given the ample mechanisms and opportunities established in
recent years for expanded congressional oversight of the agencies outside the annual appropriations
process.

Under the Dodd-Frank Act, the SEC must submit a report annually on its examination of registered
entities, enforcement investigations and corporate filing reviews to its House and Senate oversight
committees. These reports must be certified by the Directors of the Divisions of Enforcement,
Corporation Finance and the Office of Compliance Inspections and Examinations. The purpose of
these reports is to promote complete and consistent staff performance and assure appropriate
supervision of oversight activities. Another reform is the requirement that the Division of Trading
and Markets and the Division of Investment Management have a staff of compliance examiners.\textsuperscript{13}

Further, Congress has supplemented these steps by requiring significant ongoing reports from third
parties independent of the SEC. At least every three years, the Comptroller General must report to
the congressional oversight committees on the SEC’s control structure and attest to the adequacy
and effectiveness of the SEC’s internal supervisory control structure and procedures.\textsuperscript{14} This
 provision resulted from a finding by the Government Accountability Office (“GAO”) of material
weaknesses in the SEC’s internal control structure. Also, every three years the GAO must submit a
report to Congress analyzing, among other things, the effectiveness of supervisors in using the
skills, talents and motivation of employees of the SEC; the criteria for promotions; the fairness of
the promotion criteria; the competence of the professional staff; the efficacy of communications

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\textsuperscript{12} U.S. Commodity Futures Trading Commission, FY 2012 President’s Budget and Performance Plan, p.4, available at

\textsuperscript{13} Dodd-Frank Act, § 965.

\textsuperscript{14} Dodd-Frank Act, § 961(c).
between units of the SEC; and other relevant factors relating to management.\(^{15}\) Within two years from the date of the enactment of the Dodd-Frank Act, the Comptroller General must report to Congress on the SEC’s oversight of national securities associations.\(^{16}\) Another requirement was a study and report by the Comptroller General of the revolving door at the SEC.\(^{17}\) In addition, the Dodd-Frank Act required the SEC to hire an independent consultant to conduct a comprehensive study, now completed, of the present structure of securities regulation, including to examine the internal operations, structure, funding and need for comprehensive reform of the SEC.

While the Dodd-Frank Act did not include similar changes to the oversight of the CFTC, the agency’s oversight has increased since then as a natural consequence of its expanded mandate. For example, since the enactment of the Dodd-Frank Act, the CFTC has been called to testify before Congress more than twice as many times as during the comparable period before the statute was enacted. The Office of the Inspector General for the CFTC also has expanded its oversight efforts to include specialized examination and investigation of the agency’s Dodd-Frank Act implementation efforts, including completing two reports addressing the agency’s cost-benefit analyses and conducting an investigation into the agency’s position limits rulemaking process.

Conclusion

For the reasons described above, we respectfully urge that Congress act promptly to address the need for increased, reliable sources of revenue for the SEC and the CFTC, whether through authorizing self-funding or other appropriate mechanisms.

Thank you for considering the views of the ABA on these important issues. If you have any questions regarding our views, please contact Giovanni Prezioso at (202) 974-1650 or William Kroener at (202) 956-7095.

Very truly yours,

Giovanni P. Prezioso

William F. Kroener III

\(^{15}\) Dodd-Frank Act, § 962.
\(^{16}\) Dodd-Frank Act, § 964.
\(^{17}\) Dodd-Frank Act, § 968.
cc: Members of the House Financial Services Committee
Members of the Senate Banking, Housing and Urban Affairs Committee
The Honorable Daniel K. Inouye, Chairman, Senate Appropriations Committee
The Honorable Thad Cochran, Ranking Member, Senate Appropriations Committee
The Honorable Richard J. Durbin, Chairman, Senate Appropriations Subcommittee on Financial Services and General Government
The Honorable Jerry Moran, Ranking Member, Senate Appropriations Subcommittee on Financial Services and General Government
The Honorable Harold Rogers, Chairman, House Appropriations Committee
The Honorable Norm Dicks, Ranking Member, House Appropriations Committee
The Honorable Jo Ann Emerson, Chairwoman, House Appropriations Subcommittee on Financial Services and General Government
The Honorable Jose E. Serrano, Ranking Member, House Appropriations Subcommittee on Financial Services and General Government
The Honorable Mary L. Schapiro, Chairman, Securities and Exchange Commission
The Honorable Gary Gensler, Chairman, Commodity Futures Trading Commission
Members of the ABA Task Force on Financial Markets Regulatory Reform
Thomas M. Susman, Director, ABA Governmental Affairs Office