

**REAUTHORIZING THE CFTC: STAKEHOLDER  
PERSPECTIVES**

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**HEARING**

BEFORE THE

SUBCOMMITTEE ON COMMODITY MARKETS, DIGITAL  
ASSETS, AND RURAL DEVELOPMENT

OF THE

**COMMITTEE ON AGRICULTURE  
HOUSE OF REPRESENTATIVES**

ONE HUNDRED EIGHTEENTH CONGRESS

SECOND SESSION

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# REAUTHORIZING THE CFTC: STAKEHOLDER PERSPECTIVES

THURSDAY, JULY 25, 2024

HOUSE OF REPRESENTATIVES,  
SUBCOMMITTEE ON COMMODITY MARKETS, DIGITAL ASSETS,  
AND RURAL DEVELOPMENT,  
COMMITTEE ON AGRICULTURE,  
*Washington, D.C.*

The Subcommittee met, pursuant to call, at 8:29 a.m., in Room 1300 of the Longworth House Office Building, Hon. Dusty Johnson [Chairman of the Subcommittee] presiding.

Members present: Representatives Johnson, Lucas, Austin Scott of Georgia, Bacon, Mann, Nunn, Miller of Ohio, Thompson (*ex officio*), Caraveo, Davis of North Carolina, Costa, Budzinski, and Craig.

Staff present: Paul Balzano, Wick Dudley, Tim Fitzgerald, Nick Rockwell, Kevin Webb, Kyle Upton, Kate Fink, Josh Lobert, Clark Ogilvie, John Konya, and Dana Sandman.

## OPENING STATEMENT OF HON. DUSTY JOHNSON, A REPRESENTATIVE IN CONGRESS FROM SOUTH DAKOTA

The CHAIRMAN. All right. Since everybody is ready to go, we will go ahead and get started. I call this hearing to order.

Welcome, and thanks for coming. I always delight when this Committee does something that is important, but not necessarily sexy. The sexy stuff gets all the headlines, but it is indeed our job to govern a country, and sometimes that means doing things that are really important, even if they don't grab the headlines.

I want to welcome everybody to this Subcommittee hearing. The hearing today, of course, is called, *Reauthorizing the CFTC: Stakeholder Perspectives*.

Everybody here knows that derivatives markets are the backbone of our global financial system, providing essential tools for risk management, for price discovery, and for efficient capital allocation. Those markets allow businesses and investors to use those tools to hedge against price volatility, to promote stability and predictability across various sectors. We have a tendency to think about ag, but of course, it is not just ag. It is also energy. It is finance.

In agriculture, farmers use derivatives to lock in prices for their crops, protecting themselves against unpredictable weather and market fluctuations. In the energy sector, companies use derivatives to stabilize prices for oil, gas, and electricity. That enables steady planning and operation. In finance, derivatives help manage

interest rate risk, currency fluctuations, and credit exposure, and that contributes to the overall stability of global markets.

The U.S. futures and swaps markets are the largest, most liquid markets in the world, and that is not an accident. That is in no small part because of the responsible regulation of the Commodity Futures Trading Commission.

Each day, the Commission works to ensure the integrity, the vibrancy, and the resiliency of the derivatives markets, and in doing so, it protects those people we have been talking about, the farmers, the ranchers, the manufacturers, and other end-users who rely on these markets for robust risk management tools.

Today, we are going to hear from stakeholders who will provide diverse perspectives on the importance of reauthorizing the Commission, and hopefully, they will give us a little insight into the issues and priorities that we should consider during this process.

This past March, CFTC Chair Behnam testified before the Committee, and the Ranking Member asked him about the importance of reauthorization. Chair Behnam put it well, as he often does, when he said this. “We have to reauthorize the agency to ensure the public and our international partners understand that Congress and this Committee take derivatives markets and America’s supremacy in derivatives markets very seriously. We have the biggest markets in the world, and I think we all want to keep it that way, and reauthorization is one step to ensure that that condition remains the same.”

I couldn’t agree more. It is our role as authorizers to continue to examine the work of the Commission and the needs of market users. Reauthorization is how we fill the role. That is how we ripen these conversations. Just as this Committee passed digital asset market structure legislation in a bipartisan manner, both in the Committee and on the House floor, it is my goal to achieve the same bipartisan success with the reauthorization of the CFTC.

I want to thank our witnesses for joining us today. We look forward to hearing from you.

[The prepared statement of Mr. Johnson follows:]

PREPARED STATEMENT OF HON. DUSTY JOHNSON, A REPRESENTATIVE IN CONGRESS  
FROM SOUTH DAKOTA

Good morning. I want to welcome you all to the Commodity Markets, Digital Assets, and Rural Development Subcommittee hearing titled, *Reauthorizing the CFTC: Stakeholder Perspectives*.

Derivatives markets are the backbone of our global financial system, providing essential tools for risk management, price discovery, and efficient capital allocation.

These markets allow businesses and investors to hedge against price volatility, promoting stability and predictability across various sectors, from agriculture to energy to finance.

In agriculture, farmers use derivatives to lock in prices for their crops, protecting themselves against unpredictable weather and market fluctuations.

In the energy sector, companies use derivatives to stabilize prices for oil, gas, and electricity, ensuring steady operations and planning.

In finance, derivatives help manage interest rate risks, currency fluctuations, and credit exposure, contributing to the overall stability of the economy.

The U.S. futures and swaps markets are the largest, most liquid markets in the world, due in no small part to the work of the Commodity Futures Trading Commission.

Each day, the Commission works to ensure the integrity, vibrancy, and resiliency of the derivatives markets. In doing so, it protects farmers, ranchers, manufactur-

ers, and other end-users who rely on these markets for robust risk-management tools and accurate pricing.

Today, we will hear from stakeholders who will provide diverse perspectives on the importance of reauthorizing the Commission, and the issues and priorities we should consider during this process.

This past March, CFTC Chairman Behnam testified before the Committee. Our Ranking Member asked him about the importance of reauthorizing the Commission. Chairman Behnam put it well when he said:

“ . . . we have to reauthorize the agency to ensure the public and our international partners understand that Congress and this Committee takes derivatives markets and America’s supremacy in derivatives markets very seriously . . . we have the biggest markets in the world, and I think we all want to keep it that way. And reauthorization is one step to ensure that condition remains the same.”

I could not agree more. It is our role as authorizers to continue to examine the work of the Commission and the needs of derivatives market users. Reauthorization is how we fulfill this role.

Just as this Committee successfully passed digital asset market structure legislation in a bipartisan manner, both in the Committee and on the House floor, it is my goal to achieve the same bipartisan success with the reauthorization of the CFTC.

I would like to thank our witnesses for joining us today. We look forward to hearing your testimony and the opportunity to discuss this important topic.

The CHAIRMAN. We look forward to the conversation that will flow after that, and without any further ado, I would like to recognize the Ranking Member for her opening remarks.

**OPENING STATEMENT OF HON. YADIRA CARAVEO, A  
REPRESENTATIVE IN CONGRESS FROM COLORADO**

Ms. CARAVEO. Well thank you, Chairman Johnson, for working together to convene this timely and important hearing.

After examining the challenging question of oversight of digital assets, I am pleased that the Subcommittee is turning to the matter of reauthorizing the agency we have chosen to empower with such oversight, the Commodity Futures Trading Commission.

For almost 50 years, the CFTC has been the cop on the beat in protecting the integrity of our futures markets, and the important price discovery and risk management functions they serve. In 2010, in the wake of the financial crisis, Congress empowered the agency to oversee the multi-trillion-dollar swaps market, and ease the market’s transition from an unregulated environment into a more transparent and financially secure market.

Through the years, our markets have shown themselves to be remarkably resilient amongst global volatility from international conflicts to extreme weather events, to the COVID–19 pandemic. However, this agency with such important responsibilities has not been reauthorized for more than 2 decades. For today’s hearing, we will hear from a distinguished panel of stakeholders about the importance of the CFTC and the markets it oversees, and what Congress should consider when reauthorizing the agency.

Thank you, witnesses, for being here this early morning to share your testimony. I look forward to hearing from all of you. As Ranking Member of the Subcommittee, I am particularly interested in how we maintain strong customer protections in our financial markets while we pursue reauthorization, especially for the retail investor. While our nation’s financial markets are vibrant, innovative, and amongst the strongest in the world, they will only remain

that way if the users of these markets have confidence in the customer protections in place and these agencies, like the CFTC, that enforce those protections.

Additionally, as we consider these discussions regarding an agency whose oversight authority we are looking to expand to the digital assets marketplace, we must make sure we are not short-changing the CFTC in our appropriations process. The current agricultural appropriations proposal includes a cut of \$20 million to the agency's budget. Today, we will hear about the importance of this agency, and I hope it will resonate that such a cut will negatively impact the agency's ability to police its derivative markets.

Again, I welcome our witnesses who are here today, and look forward to listening to your testimony. And with that, Mr. Chairman, I yield back.

The CHAIRMAN. Now we turn to the legend of Howard, Pennsylvania, the Chairman of the full Committee, GT Thompson.

**OPENING STATEMENT OF HON. GLENN THOMPSON, A  
REPRESENTATIVE IN CONGRESS FROM PENNSYLVANIA**

Mr. THOMPSON. Okay. Well, maybe I should just yield back at this point. That is the nicest thing anybody has said about me in a long time.

Good morning, everybody, and thank you to Chairman Johnson and Ranking Member Caraveo for convening this Subcommittee hearing. I would like to echo Chairman Johnson's sentiments and extend my thanks to everyone for joining us today.

The U.S. derivatives markets are essential to our economy. They allow businesses, both large and small, to manage the risks associated with price fluctuations for their inputs and outputs. Derivatives enable businesses to focus on their core activities without being unduly concerned with ever-changing commodity prices.

The CFTC—which, by the way, is celebrating its 50th anniversary this year as an independent agency—serves a critical function in regulating derivatives markets both domestically and internationally. The Commission safeguards market participants from fraud, manipulation, and abusive practices while also promoting financial innovation and fair competition.

Earlier this week, a bipartisan group of House Agriculture Committee Members visited the CFTC's D.C. headquarters. We had a terrific visit with the CFTC Chairman, the Commissioners, and agency staff to gain a deeper understanding of how the Commission operates, and the pressing issues that it faces.

The agency's authorization expired more than a decade ago, making it crucial that we address reauthorization now. This process is not merely a bureaucratic formality; it is a reaffirmation of our commitment to robust regulatory oversight. It ensures that CFTC has the necessary tools and resources to adapt to the evolving financial landscape.

With technological advancements, like artificial intelligence, and the rise of new financial products, like digital assets, the CFTC's role is more critical than ever. Further, reauthorization of the CFTC reinforces the global leadership of the United States in financial regulation. It sends a strong message that we are committed to maintaining high standards in our markets, protecting



investors, and fostering innovation. That is why Ranking Member Scott and I have both publicly called for the CFTC to be reauthorized this Congress.

I look forward to hearing our witnesses's testimony, and remain committed to working towards a successful, bipartisan CFTC reauthorization. Together, we can ensure the CFTC remains a cornerstone of integrity and stability in our financial system.

With that, I thank you and I yield back.

The CHAIRMAN. The chair would request that other Members submit their opening statements for the record so the witnesses may begin their testimony and to ensure there is ample time for questions. Ms. Caraveo and I will be running this hearing together, and with that in mind, she will introduce our witnesses.

Ms. CARAVEO. Thank you, Mr. Chairman.

Our first witness today is Mr. Walter Lukken, who is the President and Chief Executive Officer of the Futures Industry Association.

Our next witness is Thomas Sexton, the President and Chief Executive Officer of the National Futures Association.

Our third witness will be Mr. Travis Antonsen, who is Senior Vice President for Grain Marketing and Logistics for the Agtegra Cooperative, and our fourth and final witness today is Ms. Alexandra Thornton, who is the Senior Director for Financial Regulation at the Center for American Progress.

Thank you all so much for joining us.

The CHAIRMAN. Impressive witnesses. You all get situated. You got 5 minutes. The timer in front of you will count down, and when you get to red, you will get gavelled down by either Ms. Caraveo or myself.

With that, Mr. Lukken, please begin when you are ready.

**STATEMENT OF HON. WALTER L. LUKKEN, J.D., PRESIDENT AND CHIEF EXECUTIVE OFFICER, FUTURES INDUSTRY ASSOCIATION, WASHINGTON, D.C.**

Mr. LUKKEN. Chairman Johnson, Ranking Member Caraveo, and Members of the Committee, thank you for allowing me to come today and testify on reauthorization.

Mr. Chairman, I disagree. I believe derivatives regulation is sexy. At least, I have been trying to convince my family of that for many years. So, hopefully by the end of my testimony, I will have you on my side.

I am the President and CEO of FIA, which represents futures, options, and centrally cleared derivatives markets globally.

FIA strongly supports the reauthorization of this important agency. As former acting Chairman of the CFTC, I believe reauthorization serves as an exercise in good government and provides a Congressional stamp of approval of the CFTC's important mission. Today, I want to highlight some of the trends that are happening in our markets that will benefit from your deliberations on reauthorization.

First, our markets have grown significantly. Total trading volume on CFTC-regulated exchanges in the U.S. has doubled since 2008, the last time that this Committee reauthorized the CFTC.

Second, post-crisis reforms have brought more derivatives products under the CFTC's regulation, while at the same time, making the derivatives markets safer and our financial system safer.

Third, our markets have demonstrated tremendous resilience and strength in the face of recent volatility. Our markets have remained stable and working throughout recent stress events, including COVID-19, the war in Ukraine, the Silicon Valley bank failure, and even high inflation.

One reason for this resilience is the CFTC's principles-based regulatory regime enacted by this very Committee. This regulatory framework has enabled flexible oversight tools for the CFTC to keep pace with evolving trends and technological advancements. Now, this adaptability has reduced the need for wholesale changes of the CFTC's statutory authority over time. That said, while the CFTC has this flexibility that has proven effective, the need for this Committee's oversight remains as important as ever.

There are certain trends for this Committee's oversight that are worth noting today. For example, as the American public becomes more accepting of new products, like cryptocurrencies, digital asset platforms bring novel market structures into the traditional futures industry. Increasingly, we are seeing more exchanges, clearinghouses, clearing brokers, and trading firms under one legal entity. FIA has serious concerns that collapsing the existing, multi-tiered ecosystem with its independent checks and balances could undo valuable customer protections of the listed derivatives markets. FIA welcomes Chairman Behnam's comments that the agency plans to propose a new rule to address these potential conflicts.

A second topic worth noting is the pending U.S. bank capital proposals that would dramatically increase the amount of capital held by U.S. banks for client clearing, those folks that access customers in our markets. Without changes to the proposals, the costs of hedging in our markets will likely increase for all end-users, including production agriculture. Our industry appreciates this Committee's leadership in voicing concerns about the impact of these rules.

The last item is the SEC's treasury clearing mandate taking effect over the next 2 years. The cleared derivatives markets are heavy users of treasury securities and the repo markets in the funding, margining, and collateralization of futures trades. This Committee will play a critical role in ensuring that there are no impediments to customers accessing these markets or overlapping jurisdictional issues between the CFTC and SEC with these mandates.

Now, turning to reauthorization, FIA believes the existing CFTC regulatory framework has served as a source of strength for our markets. I believe an appropriate approach would be a simple and straightforward reauthorization bill, one that provides the Congressional stamp of approval of this agency's important mission, and legal authority.

That said, there are three minor adjustments to the Act I would raise for your consideration.

First, FIA joins the NFA in supporting a non-controversial legislative fix to resolve legal uncertainty around FCM bankruptcies and the definition of *customer property*.

Second, FIA supports expanding the way the CFTC might leverage funding for educating farmers about our markets, including the risks and opportunities of derivatives.

And finally, FIA supports legislative efforts to provide flexibility for research and development capabilities of the CFTC in partnering with private-sector, such as those led by Representative Austin Scott. Thank you, Congressman.

Thank you all for allowing me to testify on CFTC reauthorization, and I look forward to your questions.

[The prepared statement of Mr. Lukken follows:]

PREPARED STATEMENT OF HON. WALTER L. LUKKEN, J.D., PRESIDENT AND CHIEF EXECUTIVE OFFICER, FUTURES INDUSTRY ASSOCIATION, WASHINGTON, D.C.

Chairman Dusty Johnson, Ranking Member Yadira Caraveo, and Members of the Committee, thank you for the opportunity to testify about the reauthorization of the Commodity Futures Trading Commission (CFTC), and the state of derivative markets.

I am the President and Chief Executive Officer of FIA. FIA is the leading global trade organization for the futures, options and centrally cleared derivatives markets. FIA's membership includes clearing firms, known in the U.S. as futures commission merchants (FCMs), exchanges, clearinghouses, trading firms and commodities specialists from more than 48 countries. FIA's mission is to support open, transparent and competitive markets, protect and enhance the integrity of the financial system, and promote high standards of professional conduct.

Prior to FIA, I served as a CFTC Commissioner for 7 years and as the agency's Acting Chair for 18 months during the financial crisis and the last reauthorization of the CFTC during the 2008 Farm Bill.

I commend the Committee for continuing your important oversight function over the CFTC and applaud you for holding this hearing to consider the reauthorization of the CFTC. FIA strongly supports the reauthorization of this important agency. Reauthorization is an exercise in good government and provides a Congressional stamp of approval on the CFTC's important mission and legal authority. It also provides the agency, and market participants, with greater certainty about the agency's direction and priorities.

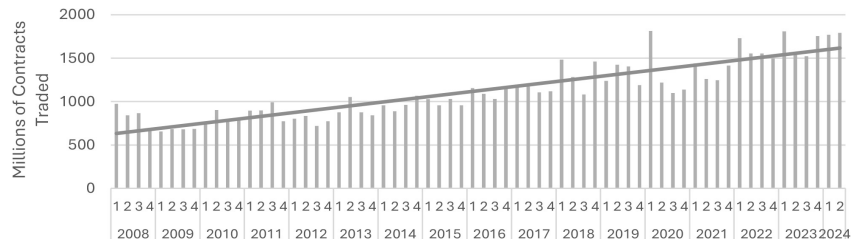
Today, I am honored to provide my counsel to this Committee once again as you deliberate CFTC reauthorization and changes to the Commodity Exchange Act (CEA).

### **The State of Our Markets**

#### *Our Markets Are Growing*

In the decade and a half since the last reauthorization in 2008, the futures and options markets have grown significantly. Total trading volume on CFTC-regulated exchanges in the U.S. has nearly doubled from 3.4 billion futures and options contracts in 2008 to 6.6 billion in 2023. In fact, more contracts were traded on CFTC-registered exchanges in the first 6 months of this year than in all of 2008.

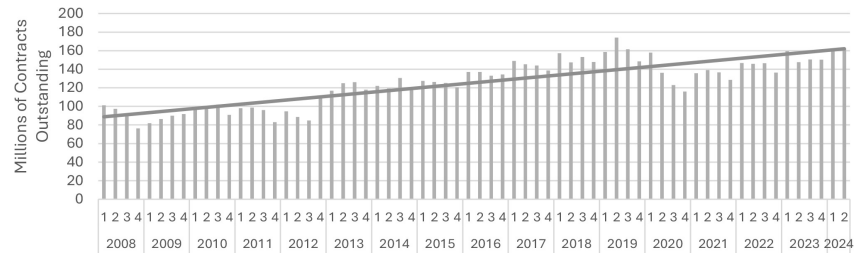
#### **Trading volume on CFTC-regulated exchanges in the U.S. has doubled since 2008**



Open interest is another important metric for these markets because it is a general proxy for commercial hedging among participants. At the end of the second quarter of this year, open interest stands at more than 162 million futures and options contracts at the clearinghouses regulated by the CFTC, compared to 97 million

at the same point of time in 2008. Strong open interest is a sign of a healthy market, so these trends are worth noting.

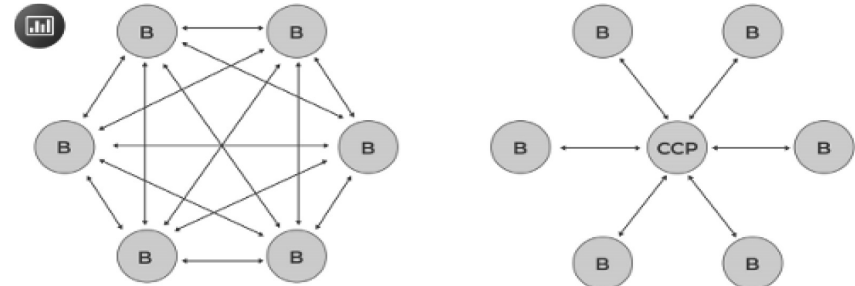
**Open interest, which measures the risk transfer function of futures and options markets, is up over 67% since 2008**



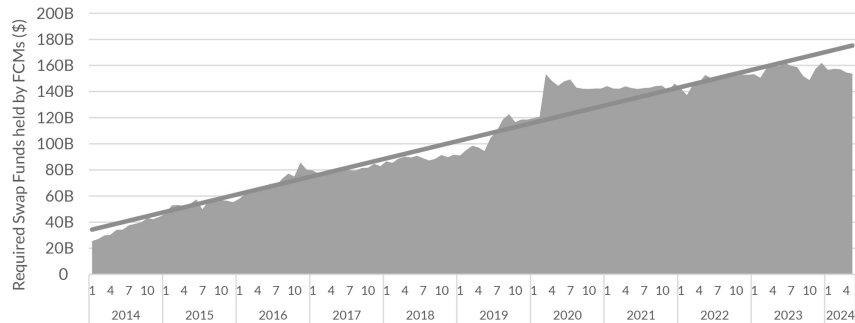
*Our Markets Are Safer*

After the 2008 financial crisis, regulators around the world recognized the need to move more over-the-counter derivatives into central clearing. They understood that central clearing is one of the most effective ways to make the financial system more stable and resilient. After Congress passed the Dodd-Frank Act in 2010, the CFTC implemented a new set of clearing requirements for standardized over-the-counter (OTC) interest rate and credit default swap instruments. Today, roughly 85% of the dollar denominated interest rate swap (IRS) market and roughly 60% of the credit default swap (CDS) market are cleared by central counterparties subject to CFTC oversight. That means all of those swaps are now risk-managed by FCMs and central counterparties, similar to the way futures markets have operated for decades.

**Illustration of the Role Played by Counterparties**



**As required by Dodd-Frank, a majority of the U.S. OTC swaps has migrated to central clearing. Asset managers and other customers holding OTC swaps have deposited more than \$150 billion in collateral to cover the risks of these positions.**



### *Our Markets Are Resilient*

Several factors have introduced incredible volatility to global commodity markets in recent years, including the onset of COVID-19, the war in Ukraine, macroeconomic pressures including supply disruptions and inflation, and the global transition to a low-carbon economy. Effective operation through these powerful, real-world stress tests has demonstrated the resilience of our industry. Market participants have sought access to our markets to manage risk in a safe and regulated environment because of these pressures.

This Committee deserves a lot of credit for the strength of our markets. As noted above, the clearing mandates that were written into law by this Committee following the 2008 financial crisis have expanded the important role of FCMs and CCPs in reducing systemic risk in our markets. By working in partnership with the National Futures Association (NFA), the CFTC, and the broader industry over the last several decades, the cleared derivatives markets have remained robust and resilient despite the extreme market volatility and record trading volumes. And, importantly, end-users in the real economy never lost their ability to access these markets to manage risk and discover prices.

### *Our Markets Are Global*

Just as producers need access to global markets to sell their physical commodities, they too need access to global derivatives markets to hedge risk in times of uncertainty. Knowing they can rely on well-regulated futures and options markets provides American farmers the protection from price volatility they need to compete in the global markets for corn, wheat and soybeans. The reverse is also true: companies all over the world use the agricultural and energy contracts listed on U.S. futures markets as the benchmarks for global trade in these commodities. That brings additional liquidity to these markets, and that is a win-win for both agricultural producers and consumers here in the U.S.<sup>1</sup>

Dating back to my time as a CFTC Commissioner and Acting Chair, and even prior, the derivatives markets have been global. Execution, clearing and settlement often take place in different countries and across different time zones and continents. And, since the last reauthorization, our markets have become even more global in nature. Market participants benefit from the global nature of our markets. The more participants, the stronger the market for those seeking to hedge risks.

FIA appreciates that Members of this Committee, including Ranking Member David Scott and Representative Austin Scott, among others, have worked over the years to engage policymakers in other jurisdictions to ensure a level playing field, reduce market fragmentation and improve collaboration between the CFTC and its international counterparts.

### *Our Markets Are Innovative*

One of the most noteworthy provisions in the Commodity Exchange Act mandates the CFTC to promote fair competition and responsible innovation. There are very few other parts of the Federal Government with such an explicit mandate. I think this has benefited the CFTC throughout its history and something to keep in mind as you consider reauthorization.

The U.S. derivatives markets are nimble, allowing growth and innovation. This is evidenced by the pace of new and novel contracts being listed on our markets today. There are futures contracts based on battery metals such as lithium and cobalt—crucial components for the electric vehicle industry. There are futures on Bitcoin and ether, the two most heavily traded crypto currencies. There are the so-called “ultra” Treasury bond and note futures, which have given asset managers and other institutional investors more ways to hedge their interest rate risks.

Another example is the expanded range of crude oil futures. In 2008, the U.S. was a net importer of crude oil. Today we are a net exporter, thanks to gains in the productivity of the U.S. oil industry. The futures industry has responded by developing new futures contracts based on prices at the export terminals along the Gulf Coast. Those contracts are expressly designed to help companies hedge price risks on international flows of oil.

The biofuels market offers another example. According to the U.S. Department of Agriculture (USDA), approximately 20% to 25% of all soybean oil produced in the U.S. is sold to refineries and converted into renewable diesel. Companies throughout

<sup>1</sup> In 2021 FIA took an in-depth look at cross-border flows and we determined that roughly 25% of the trading in CME's equity index futures and options came from outside the U.S. The ratio was 26% in energy, 30% in agriculture, and 45% in metals. The same held true for ICE Futures U.S. Approximately 34% of the volume in its agricultural contracts originated from outside the U.S.

the supply chain use the well-established futures based on soybean oil and heating oil to hedge the risks in this new and rapidly growing alternative to fossil fuels.

These are just a few examples of the agility, market responsiveness and innovative spirit that has long characterized the U.S. futures industry and will continue to characterize the industry for years to come.

#### **Priorities for Committee Oversight of CFTC**

This Committee plays a crucial role in the oversight of the CFTC as novel and emerging trends present themselves. As the agency's authorizing body, this Committee can provide guidance and Congressional intent to the agency's rulemaking authority as it considers these evolving trends. I want to highlight some of the topics worthy of your attention.

##### *Evolving Market Structures*

Historically, the regulation of the futures markets, as directed by the Commodity Exchange Act, has been by functional registration category. The statute, and its implementing regulations, require market participants who take on certain responsibilities to register in various categories.

Exchanges that bring together buyers and sellers and self-regulate their markets are required to register as designated contract markets (DCMs). Clearinghouses, with their obligations to protect the financial integrity of the system, are required to register as designated clearing organizations (DCOs). Clearing members, those firms that guarantee and safeguard customer funds and serve as their agents, are required to register as futures commission merchants (FCMs).

Given these targeted responsibilities, these registrants have historically been housed in independent legal entities. Increasingly, however, we are seeing more exchanges and clearinghouses that are embedding an FCM within their legal structure.

CFTC Chairman Rostin Behnam has recognized this trend and has indicated his desire to address this issue by rulemaking this fall. He testified before this Committee in March,<sup>2</sup> highlighting that “we are seeing a shift to structures, driven by technology, that combine or compress what have historically been unique and separate activities into a single or fewer entities. This compression raises many important questions including those regarding conflicts of interest within vertically integrated structures.”

FIA has a long history of supporting innovation in the derivatives industry. FIA also strongly believes in the fundamental regulatory principle: same business, same risks, same rules.

In our May 2022 comment letter<sup>3</sup> about the FTX U.S. Derivatives application before the CFTC, which sought to combine several market functions into a single entity, we identified fundamental principles of the derivatives regulatory oversight structure that they could not adequately address. These include principles of segregation of customer funds, conflicts of interest of those entrusted with market operations and customer funds, financial resourcing and capitalization of market operators, appropriately planned and sized default resources, and safeguards of key market operations.

FIA has strong concerns that collapsing the existing multi-tiered ecosystem—with its inherent checks and balances and customer protections—could undo the strong foundation of the listed derivatives markets and, ultimately, put customers at risk. We want to make sure end-users, including those in the agricultural and energy sectors, will continue to have the same protections as customers are guaranteed today.

FIA welcomes Chair Behnam's desire to establish a strong regulatory regime to cover conflicts originating from affiliated entities serving multiple functions within these vertically integrated structures.

##### *Emerging Technology and Artificial Intelligence (AI)*

The Commission's principles-based regulatory framework and flexible approach to regulation has a proven track record when it comes to protecting customers, promoting innovation and preserving market integrity. Regulators and policymakers are rightfully exploring potential uses and risks of emerging technology, such as AI in the derivatives markets that the CFTC regulates and beyond.

In January 2024, the CFTC Divisions of Market Oversight, Clearing and Risk, Market Participants, and Data and the Office of Technology Innovation issued a request for comment (RFC) to better inform them about AI.

<sup>2</sup> <https://agriculture.house.gov/calendar/eventsingle.aspx?EventID=7732>.

<sup>3</sup> <https://www.fia.org/sites/default/files/2022-05/FIA%20FTX%20Request%20for%20Amended%20DCO%20Registration%20Order%205.11.22.pdf>

FIA believes<sup>4</sup> the existing statute and CFTC rules and guidance provide the controls and oversight needed for the Commission to promote and protect the integrity and resilience of our markets. FIA urges the CFTC to take a “technology-neutral” approach and focus on achieving regulatory outcomes, rather than attempting to regulate the technology itself, moving forward.

#### *U.S. Bank Capital Proposals*

On July 27, 2023, the Board of Governors of the Federal Reserve System (Federal Reserve), the Office of the Comptroller of the Currency, and the Federal Deposit Insurance Corporation—together, the U.S. bank regulators—proposed the Basel III endgame capital framework and, separately, the Federal Reserve requested comment on a proposal that would make significant adjustments to the calculation of the global systemically important bank holding companies surcharge. These proposed rules<sup>5</sup> represent a comprehensive rewrite of the regulatory capital standards for the biggest U.S. banks.

While outside the jurisdiction of the CFTC, these rules will harm the CFTC-regulated derivatives markets and the end-users that rely on them. FIA contributed to a report and a set of recommendations<sup>6</sup> adopted by the CFTC Global Markets Advisory Committee (GMAC) at a recent June 2024 meeting.

The report highlights excerpts from the formal comment letters filed by the users of derivatives markets noting concerns about the proposals, including agriculture, energy, insurance, pension funds and others.

We also commend CFTC Chairman Rostin Behnam for his comments in public testimony before this Committee in March 2024, emphasizing the need to “create incentives” for clearing and committing to working with his prudential regulators to ensure new bank capital rules are not “creating unnecessary barriers to clearing and clearing services for end-users.”

#### *Treasury Clearing*

In December 2023, the Securities Exchange Commission (SEC) adopted final rules that will require most market participants to clear U.S. Treasury (UST) repo and cash security transactions in the secondary market. While these transactions are not futures contracts, our industry and its participants utilize treasury securities and repo contracts every day in the collateralization, settlement and cash management of futures positions. Our industry is also exploring whether it can take a more direct role in the clearing of these products given the similarities to the futures and swaps markets.

The SEC’s clearing mandate may seem familiar to Committee Members who were involved in the Dodd-Frank Act that mandated the clearing of OTC derivatives after the financial crisis. Both efforts aimed to move these bilateral, trillion-dollar markets to a client, all-to-all cleared market. In other words, the futures market model. That our markets act as the model for reform demonstrates the importance of our efficient, transparent business practices as an industry.

The incumbent, DTCC’s FICC, has made the most progress to date, having filed several rules with the SEC to build the framework for its clearing model with more rules to come in the fall. CME and ICE also have publicly announced an interest in providing cash treasury clearing.

FIA finds this competition healthy because it will sharpen the discussions with the end-users in mind. We believe we have the expertise and experience to offer in how “done away” client clearing models will work, given their similarity to the agency give-up clearing model of the futures markets.

There are challenges ahead that may require this Committee’s attention. The CFTC and SEC will need to work together to ensure that the Treasury clearing mandate does not conflict with CFTC regulations. Both agencies are working collaboratively to address these concerns.

The second issue is the timeline. Several workstreams need to be addressed before the first deadlines come into place, including capital, accounting, cross-margining, risk and credit controls and netting. Implementing this mandate before June 2026 will be a heavy lift, especially considering the importance of the Treasury and repo markets to the funding of the government and financial markets. Regulators will need to be flexible and aligned with industry to ensure realistic timetables.

Our industry will keep this Committee abreast as this critical rulemaking is implemented.

<sup>4</sup> <https://www.fia.org/sites/default/files/2024-04/FIA-FIA%20PTG-CME-ICE%20Response%20to%20CFTC%20AI%20RFC%204.24.pdf>.

<sup>5</sup> <https://www.federalreserve.gov/newsevents/pressreleases/breg20230727a.htm>.

<sup>6</sup> <https://www.cftc.gov/PressRoom/PressReleases/8918-24>.

## **FIA Views on CFTC Reauthorization**

### *Overall*

As noted earlier in my testimony, our markets have demonstrated incredible resilience given the onset of COVID-19, the war in Ukraine, weather and energy disruptions in the U.S. and abroad, and the commodity market volatility associated with these events. Throughout all these events, the U.S. regulatory framework has proved itself as a source of strength for our markets, and the global clearing system has worked as intended, minimizing the counterparty risk that we witnessed during the crisis of 2008.

As a result, FIA does not believe a broad CFTC reauthorization bill is needed now. Rather, a bill that provides a Congressional stamp of approval on this agency's important mission and legal authority, and that acknowledges the CFTC's proven track record through a period where we have seen record market volatility, is the best approach.

### *Customer Protection*

FIA joins the NFA in supporting legislative clarification to resolve legal uncertainty in FCM bankruptcies as to the definition of "customer property" created by a bankruptcy court decision in the Griffin Trading case. The sanctity of segregated customer funds remains an important tenet of the CFTC's customer protection regime and FIA stands ready to assist the Committee on this clarification.

### *Expanding Access to Educational Resources for Small- and Mid-Size Farmers*

Today's farmers and ranchers are incredibly savvy businesspeople. They want to offset their risk where possible. But they have a lot on their plates. And that's before the food reaches our plates.

FIA supports efforts to expand educational resources about the opportunities and risks of risk management tools like futures and other cleared derivatives. It would go a long way to helping the 2% that feed the 98%—particularly for the small- and mid-size farmers, producers and end-users.

During a March 2023 full Committee hearing titled "Rising Risks: Managing Volatility in Global Commodity Derivatives Markets," FIA's board chair, Alicia Crighton, received a question from Representative Jasmine Crockett about a USDA report from October 2020 that raised concerns about a low percentage of farmers using futures or options to hedge price risk.

FIA took interest in this report and encourages this Committee to consider whether opportunities exist—perhaps through CFTC reauthorization or another vehicle—to expand the manner in which the CFTC might leverage funding through the CFTC Office of Customer Education and Outreach (OCEO) to partner with not-for-profits, private sector educational initiatives or other government entities, like the USDA. Educational resources should be used to highlight both the opportunities and the risks of risk management tools like futures and options.

We believe this may address the concerns raised by Representative Crockett and provide additional resources to farmers during a time when they have experienced, and continue to experience, considerable volatility in their markets.

### *Modernizing the CFTC*

The last CFTC reauthorization was enacted the same year Apple launched its App Store. The technological advancements by market participants have been incredible since that time.

According to former Chairman of the CFTC Christopher Giancarlo, "The CFTC lacks the legal authority to partner and collaborate with outside entities engaging directly with fintech within a research and testing environment, including when the CFTC receives something of value absent a formal procurement."<sup>7</sup>

FIA supports efforts to improve the research and development capabilities of the CFTC. This includes legislative efforts, such as those led by Representative Austin Scott, that would provide the CFTC transaction authority to engage in public-private partnerships with financial technology developers. NASA, the Department of Defense, and other Federal agencies already have this type of authority. This authority would assist the CFTC so it can fully vet and test potential rules and regulations on the technology being utilized by industry.

## **Conclusion**

I am fortunate to represent a wide array of stakeholders in the listed, cleared and regulated derivatives industry—all of whom want to see this industry continue to support the price discovery and risk management needs of their customers in a pro-

<sup>7</sup> <https://www.cftc.gov/PressRoom/SpeechesTestimony/opagiancarlo70>.



ductive way. It is an honor to be with you today and to work with this Committee as you craft a reauthorization of the CFTC and explore reforms to the CEA that strengthen our markets.

The CHAIRMAN. Very good, thank you.  
Mr. Sexton, you are up.

**STATEMENT OF THOMAS W. SEXTON III, J.D., PRESIDENT AND  
CHIEF EXECUTIVE OFFICER, NATIONAL FUTURES  
ASSOCIATION, CHICAGO, IL**

Mr. SEXTON. Good morning, Chairman Johnson, Ranking Member Caraveo, and Members of the Subcommittee. Thank you for the opportunity for National Futures Association to appear at this hearing on the important topic of the CFTC's reauthorization. I am the President and CEO of NFA.

NFA is a registered futures association under the Commodity Exchange Act and the industry-wide independent self-regulatory organization for the derivatives industry. Our overriding objective is to partner with and help the CFTC regulate the derivatives markets. Our main areas of responsibility are described in my written testimony. The CFTC oversees each and every aspect of NFA's regulatory authority.

Our coordination efforts with the CFTC over the years, in part, have built a strong track record of protecting retail customers and prosecuting retail trading abuses and fraud. At this time, I want to thank Chair Behnam for his leadership at the CFTC and thank him and the CFTC's other Commissioners for their support of NFA and for their willingness to work with us to resolve the industry's regulatory issues.

Reauthorization is always an important process for the industry as a whole, and for NFA in particular. NFA firmly believes that customer protection issues should be front and center as Congress works to reauthorize the CFTC. Today, I would like to cover one significant reauthorization topic, strengthening FCM customer protections in bankruptcy.

The 2019 reauthorization bill voted out of the House Agriculture Committee included a key customer protection provision relating to FCM bankruptcies, which we continue to strongly support and believe any future reauthorization bill should address. Over 40 years ago, the CFTC adopted rules regarding FCM bankruptcies. Among other things, those rules provided that if there is a shortfall in customer segregated funds, the term *customer funds* would include all assets of the FCM until customers had been made whole.

Several years ago, a district court decision cast out the validity of the CFTC's authority to adopt this rule. Although that decision was subsequently vacated, a cloud of uncertainty continues to remain over this rule's efficacy. Congress should remove that doubt and ensure that customers have priority if there is a shortfall in segregated funds. Congress can do so by amending Section 20 of the Commodity Exchange Act, which gives the CFTC authority to adopt regulations regarding commodity brokers that are debtors under Chapter 7 of the United States Bankruptcy Code to make clear that the CFTC has the authority to adopt the rule that it did. We believe that there is broad industry support for this approach.

Let me turn to digital asset commodities for just a few minutes. In 1982, Congress and the CFTC gave NFA the authority or responsibility to regulate firms engaging in exchange-traded derivatives. We are appreciative that over the years, Congress and the CFTC have entrusted us with additional regulatory responsibilities over retail forex and swaps.

The Commission's responsibilities are enormous and we will continue to help it in any way we can. The CFTC has led efforts among financial regulators to protect customers by tackling fraudulent schemes associated with retail digital asset commodities activities. We applaud this Subcommittee and under Chairman Thompson's leadership, the House Committee on Agriculture's collaborative work with the House Financial Services Committee to pass legislation governing spot digital assets, including those that are commodities. As this Subcommittee is aware, the FIT Act includes a significant role for an RFA in regulating the digital asset commodity market.

I would like to take this opportunity to reaffirm NFA's willingness to assist the CFTC to the extent requested in developing an appropriate regulatory framework for the digital asset commodity market, if Congress moves forward with legislation in this area.

Our member firms have engaged in spot digital asset commodity activities for over 5 years, and we have taken steps to regulate these members' activities to ensure that appropriate customer protections are in place. We are fully capable of working with the CFTC to perform the responsibilities of an RFA as outlined in the FIT Act (H.R. 4763, Financial Innovation and Technology for the 21st Century Act), and will continue to take a pragmatic regulatory approach with regard to this area.

Thank you again for the opportunity to appear before you today to discuss CFTC reauthorization. I would be happy to answer any questions at the appropriate time.

[The prepared statement of Mr. Sexton follows:]

PREPARED STATEMENT OF THOMAS W. SEXTON III, J.D., PRESIDENT AND CHIEF EXECUTIVE OFFICER, NATIONAL FUTURES ASSOCIATION, CHICAGO, IL

Chairman Johnson, Ranking Member Caraveo, and Members of the Subcommittee, thank you for the opportunity to testify at this hearing on the important topic of the Commodity Futures Trading Commission's (CFTC or Commission) reauthorization. My name is Thomas Sexton, and I am the President and Chief Executive Officer of National Futures Association (NFA), the industry-wide independent self-regulatory organization (SRO) for the derivatives industry.

Before turning to my substantive remarks, please let me provide some background information about NFA. NFA is a registered futures association (RFA) pursuant to Section 17 of the Commodity Exchange Act (CEA). Our global membership includes CFTC registered futures commission merchants (FCMs), swap dealers (SDs), commodity pool operators (CPOs), commodity trading advisors (CTAs), introducing brokers (IBs), retail foreign exchange dealers (RFEDs) and associated persons of these entities. The CFTC requires these registered firms to be NFA Members. We currently have approximately 2,900 NFA Member firms and 38,000 individual Associate Members.

NFA is solely a regulatory body. We do not operate a market, and we are not an industry trade association. Our overriding objective is to partner with and help the CFTC regulate the derivatives markets and, in doing so, we are a resolute customer protection organization. NFA's responsibilities include registering all firms and industry professionals on behalf of the CFTC, passing rules to ensure fair dealing with customers and counterparties, monitoring Members for compliance with those rules

and taking enforcement actions against those Members that violate our rules. Every aspect of our regulatory authority is closely overseen by the CFTC.

As Congress expanded the CFTC's jurisdiction over the years beyond exchange-traded derivatives to include the retail forex rolling spot and swaps markets, Congress and the CFTC also entrusted NFA with additional regulatory oversight responsibilities for these markets.<sup>1</sup> NFA coordinates with the CFTC on a regular basis and worked very closely with the CFTC to develop rules and regulatory programs to effectively oversee these additional areas of regulatory jurisdiction. In addition, the CFTC has delegated numerous responsibilities to NFA including the industry's registration process and the review of CPO and CTA disclosure documents, CPO annual financial filings and SD swap valuation disputes. Our coordination efforts over the years have built a strong track record of protecting retail customers and prosecuting retail trading abuses and fraud. Today, customer complaints and single-event customer arbitrations filed at NFA, as well as CFTC's reparations cases, remain near all-time lows.

The Commission's responsibilities are enormous, and we will continue to help it in any way we can. At this time, I certainly want to recognize Chair Behnam for his leadership at the CFTC and thank him and the CFTC's other Commissioners for their support of NFA and self-regulation and for their willingness to work with us to resolve the industry's regulatory issues. Under Chair Behnam, the CFTC has led efforts among financial regulators to protect customers by tackling fraudulent schemes associated with retail digital asset commodities' (DACs) activities. The CFTC's last formal reauthorization expired over 10 years ago. Since then, NFA, the CFTC and the derivatives industry have established a comprehensive swap dealer regulatory oversight program<sup>2</sup> and navigated a worldwide pandemic. In doing so, we worked collectively to protect customers and counterparties, market integrity and confidence in the derivatives markets.

#### **CFTC Reauthorization**

NFA has always recognized the importance of Congress reauthorizing the CFTC and ensuring that the CFTC continues to have the tools it needs to properly regulate the derivatives industry. As this Subcommittee is aware, on May 22, 2024, the House of Representatives passed the bipartisan *Financial Innovation and Technology for the 21st Century Act (FIT Act)*. This legislation calls upon the Commission to regulate a new area once again—the DAC market. In the past, Congress has used momentous changes to the CFTC's responsibilities to also reauthorize it.<sup>3</sup> In light of the CFTC's potential new responsibilities in the DAC area, NFA strongly believes that now is an appropriate time for Congress to reauthorize the CFTC.

Reauthorization is always an important process for the industry as a whole and for NFA in particular. Today, I would like to cover one significant reauthorization topic—strengthening FCM bankruptcy customer protections. I would also like to take this time to reaffirm NFA's willingness to assist the CFTC to the extent requested in regulating the spot DAC market if Congress moves forward with legislation in this area.

#### *Strengthening Customer Protections in FCM Bankruptcy Proceedings*

NFA firmly believes that customer protection issues should be front and center as Congress works to reauthorize the CFTC. The 2019 reauthorization bill voted out of the House Agriculture Committee included a key customer protection provision that clarifies the Commission's authority to adopt rules that provide customers with priority in the event of an FCM bankruptcy. NFA fully supports this provision, and we believe there is broad-based industry support for this approach. We urge this Subcommittee to include this key statutory change in any future reauthorization bill.

Over 40 years ago, the CFTC adopted rules regarding FCM bankruptcies. Importantly, those rules provide that in the event of a shortfall in customer segregated funds, the term "customer funds" would include all assets of the FCM until customers are made whole. Over 20 years ago, a United States district court bankruptcy decision cast doubt on the validity of the CFTC's rule. Although that decision

<sup>1</sup> Congress originally gave the CFTC anti-fraud jurisdiction over the retail forex markets and expanded its jurisdiction to include regulatory oversight in 2008. Congress gave the CFTC jurisdiction over the swaps markets (except for security-based swaps) after the enactment of the U.S. Dodd-Frank Wall Street Reform and Consumer Protection Act in 2010.

<sup>2</sup> Swap Dealers became registered with the CFTC in early 2013.

<sup>3</sup> For example, the *Commodity Futures Modernization Act of 2000* and *Food, Conservation, and Energy Act of 2008* each made momentous changes to the CFTC's regulatory oversight and/or jurisdiction and reauthorized the CFTC.

was subsequently vacated after the parties in the matter settled, a cloud of doubt continues to linger over the validity of the CFTC's rule.

NFA strongly encourages Congress to remove that doubt and ensure that customers have a priority in an FCM's bankruptcy if there is a shortfall in segregated funds. In our view, this important customer protection can be provided by amending Section 20 of the CEA, which gives the CFTC authority to adopt regulations regarding commodity brokers that are debtors under Chapter 7 of Title 11 of the United States Code. We recommend that Congress amend Section 20 to clarify that the CFTC has the authority to adopt the rule that it did.

#### **NFA's Willingness to Assist the Commission in Regulating Digital Asset Commodities**

At the outset, we applaud this Subcommittee's and under Chairman Thompson's leadership, the House Committee on Agriculture's collaborative work with the House Financial Services Committee to pass legislation governing spot digital assets, including those that are commodities. As this Subcommittee is aware, the FIT Act includes a significant role for an RFA in regulating the DAC market. Among other provisions, the bill requires digital commodity brokers and digital commodity dealers, as well as digital commodity exchanges that accept customer funds, to be Members of an RFA. The bill also provides that any person that files notice with the Commission of its intent to register as a digital commodity broker, digital commodity dealer or digital commodity exchange to be a member of an RFA and comply with the RFA's rules. As a result, the RFA will be solely responsible for oversight of these entities during the period between filing the notice of intent to register and actually becoming CFTC registered.

NFA fully supports providing a role for an RFA to partner with the Commission in developing an appropriate regulatory regime for the DAC market. A cornerstone of effective self-regulation is mandatory membership, and the provisions in the FIT Act that mandate membership in an RFA are essential for ensuring that an RFA can act effectively, and discipline and when appropriate bar Members that do not abide by the RFA's rules. Without mandatory membership, registrants would be able to relinquish their RFA membership if they did not want to follow a rule or were being investigated or disciplined for failing to follow a rule.<sup>4</sup>

NFA looks forward to assisting the CFTC in regulating the DAC market and is fully capable of performing the responsibilities of an RFA as outlined in the FIT Act. The fact is our Member firms have been engaging in spot DAC activities for over 5 years, and we have already taken steps to regulate these Members' activities to ensure that appropriate customer protections are in place. For example, in 2018, we adopted DAC disclosure requirements for our Members because we wanted to make sure that investors fully understood the nature of DACs and DAC derivatives.

Last year, we extended our jurisdiction over Members' spot DAC activities to ensure that NFA could take action if a Member firm committed fraud or similar misconduct with respect to these activities. Detecting and combating fraud is central to our mission. Therefore, our current compliance rules impose anti-fraud, just and equitable principles of trade and supervision requirements on NFA Members and Associates engaged in spot DAC activities. Although we have not observed any significant issues with our Members engaging in spot DAC activities, we will continue to take a proactive regulatory approach with regard to our Members' spot DAC activities.

In conclusion, thank you again for the opportunity to appear before you today and highlight one important provision that NFA believes should be included in any future CFTC reauthorization bill. We also appreciate the opportunity to highlight NFA's willingness to assist the Commission in regulating DACs. We firmly believe our successful regulatory partnership with the CFTC is an effective structure for regulating the derivatives markets and the rolling spot retail forex and spot DAC markets. We look forward to working closely with this Subcommittee to reauthorize the CFTC. I would be happy to answer any questions.

Ms. CARAVEO [presiding.] Thank you, and we will go to Mr. Antonsen next.

<sup>4</sup>Effective government oversight is also essential to self-regulation. As set forth in Section 17 of the CEA, this oversight should cover all aspects of the SRO's regulatory activity. Today, while we may partner with the CFTC to regulate our Members, the CFTC closely reviews and monitors our activities to ensure that we fulfill our regulatory responsibilities.

**STATEMENT OF TRAVIS ANTONSEN, SENIOR VICE PRESIDENT,  
GRAIN MARKETING, AND RAIL LOGISTICS, AGTEGRA  
COOPERATIVE, ABERDEEN, SD; ON BEHALF OF NATIONAL  
COUNCIL OF FARMER COOPERATIVES**

Mr. ANTONSEN. Good morning, Chairman Johnson, Ranking Member Caraveo, and Members of the Subcommittee. Thank you for holding this hearing as you work on reauthorization of the Commodity Futures Trading Commission. I appreciate the opportunity to discuss the role of derivatives markets that CFTC oversees in helping farmers and agribusiness manage commodity price risks.

I currently work for Agtegra, a cooperative owned by 6,700 farmers in the Dakotas. I am also actively engaged in my family farming operation.

Currently, some of our agricultural markets are seeing lower price levels driven by increased international crop production. Mostly favorable weather this year is aiding in crop development and futures contracts are currently pricing in expectations for another large harvest. For example, the futures price in the December 2024 corn contract topped out at \$6.02 a bushel in April of 2022. Yesterday, that price closed at \$4.18, so significant volatility in cash prices.

Thus far, it appears producers who previously forwarded price contracts will likely receive higher prices. Our cooperative is active in offering those pricing tools that allow our members to manage their price risk well in advance of harvesting, or even planting that crop.

To manage such large commodity price risks and movements, we rely on highly functioning derivative markets. For example, Agtegra uses exchange rated futures and options, OTC derivatives, over-the-counter contracts to hedge our price risk for us to protect our grain and storage, manage our future sales, and offset energy and fertilizer risk. We also do this for forward contracting options to our member owners. In the process of buying grain from the farm to selling it to the end-user exporter, that bushel of grain may have had to trade futures four or five times by the time the grain reaches its final destination. The CFTC ensures integrity of those markets.

As the Agriculture Committee has looked to reauthorize the CFTC in the past, we have supported those efforts. Reauthorizing CFTC is how this Committee acknowledges the importance of the agency's critical functions.

While the CFTC's mission has expanded in recent years, we rely on the CFTC to ensure the soundness of our commodity markets. It is essential for the agriculture industry to have well-functioning, commodity derivative markets, and the CFTC performs the essential role of helping to safeguard those markets.

While the Commission's responsibilities have expanded, funding has been flat. While not in the scope of this Committee, we encourage Congress to provide sufficient funding for CFTC's important functions. However, we caution against the imposition of any user fees on the industry to fund CFTC. Agriculture is a high-volume global margin industry. Incremental costs, whether passed on or imposed directly on the participants, eventually trickle down to the

end-users and farmers. Grain represented by underlying futures contracts can be traded multiple times, as I noted before. If there is a user fee, then that selling price received by the producer would go down by the amount of the fee each time the underlying futures contract is traded. We fear a further increase in costs would have the unintended consequences of discouraging prudent hedging practices. To be clear, a user fee would increase risks being absorbed by agriculture.

Additionally, we caution Congress from setting up a situation where the CFTC would see its budget directly impacted by the volume of trading in the products it is tasked with regulating.

I outline several concerns we have with the Basel III Endgame proposals in my written testimony. We appreciate Congress's engagement on this issue, and are hopeful that those capital requirements will be re-proposed.

Thank you again for this opportunity to testify today before the Committee. We appreciate your role in ensuring the industry will continue to be able to effectively hedge commercial risk in supporting the viability of our farmers. I look forward to answering any questions that you may have. Thank you.

[The prepared statement of Mr. Antonsen follows:]

PREPARED STATEMENT OF TRAVIS ANTONSEN, SENIOR VICE PRESIDENT, GRAIN MARKETING, AND RAIL LOGISTICS, AGTEGRA COOPERATIVE, ABERDEEN, SD; ON BEHALF OF NATIONAL COUNCIL OF FARMER COOPERATIVES

Chairman Johnson, Ranking Member Caraveo, and Members of the Subcommittee, thank you for the invitation to testify today with respect to the reauthorization of the Commodity Futures Trading Commission (CFTC) and, in particular, the importance of the agriculture industry's ability to use and offer risk management tools.

I am Travis Antonsen, Senior Vice President of Grain Marketing and Rail Logistics of Agtegra Cooperative. Agtegra Cooperative is a local farmer-owned agricultural cooperative headquartered in Aberdeen, South Dakota. It is owned by over 6,700 farmers and ranchers, predominantly in North and South Dakota, with a network of over 70 locations and 900 employees. With four main divisions, we buy grain from our farmer-members and provide farmers and ranchers with grain, agronomy, energy and feed products and services. In addition, I was born and raised on a family farm in South Dakota where I continue to farm with my family. We grow corn and soybeans and raise livestock.

Today, I am testifying on behalf of Agtegra Cooperative and the National Council of Farmer Cooperatives (NCFC). NCFC represents roughly 1,700 farmer-owned cooperatives across the country whose members include a majority of our nation's more than two million farmers. Agtegra Cooperative is an NCFC member, and also a member of the National Grain and Feed Association (NGFA). I currently serve on the NGFA Risk Management Committee and have previously served on the NGFA Country Elevator Committee and Board of Directors.

Farmer cooperatives—businesses owned, governed and controlled by farmers and ranchers—are an important part of the success of American agriculture. Through their cooperatives, producers are able to improve their income from the marketplace, manage risk, and strengthen their bargaining power, allowing them to compete globally in a way that would be impossible to do individually.

Commodity price risk management tools are essential to help mitigate commercial risk in the production, processing and selling of a broad range of agricultural, energy and food products. America's farmers and ranchers must continue to have access to new and relevant risk management products that enable them to feed, clothe and provide fuel to consumers here at home and around the world. Mostly favorable weather this year appears to be aiding crop development and futures contracts are pricing in expectations for large crops. Thus far it appears producers who previously forward priced crops, which is made possible by derivatives, will likely receive higher prices for their crop. Not everyone forward prices crops, but having the pricing

tools available as part of a multi-layered risk management strategy is important for agriculture.

#### **Use of Derivative Markets**

As processors and handlers of commodities and suppliers of farm inputs, agriculture firms are commercial end-users of the futures exchanges, as well as the over-the-counter (OTC) derivatives markets. They use exchange-traded futures and options and OTC derivatives to hedge the price risk of commodities they purchase, supply, process or handle.

For example, Agtegra uses exchange-traded futures and options and OTC derivatives to hedge the price risk for the cooperative to protect grain in storage, manage future sales, and to offer forward contracting options to our member-owners. In the process of buying grain from the farm to selling it to the end-user or exporter, that bushel of grain may have had to trade futures four or five times by the time the grain reaches its final destination. The cooperative is also active in offering pricing tools that allow its members to manage their price risk well in advance of harvesting or even planting a crop.

While not used to the extent as exchange-traded contracts, the swaps markets also play a vital role in the ability of cooperatives to hedge in the various commodity markets, in both the agricultural and energy markets. Swaps are especially important in times of extreme price volatility that puts stress on the industry—and allows working capital to be freed up so cooperatives can continue to offer forward pricing options for farmers to manage their own production risk.

In addition, swaps serve as important tools in agriculture markets that may not have sufficient trading volume on the futures exchanges, as well in being able to customize hedges to address situations that may not match up well to conventional futures contract specifications. To access the OTC market, cooperatives use a variety of commercial counterparties as well as registered swap dealers, including large banking entities.

Currently some of our agricultural markets are in a period of lower price levels driven by increasing international crop production. For example, the futures price on the December 2024 corn futures contract peaked at \$6.02/bushel on April 25, 2022 and as of the close on July 19, 2024 is down to \$4.05/bushel. To manage such large commodity price risks and movements, cooperatives rely on highly functioning derivatives markets.

As a producer, the ability to customize risk management tools through OTC derivative contracts has been an invaluable tool for my operation by giving me the confidence to price grain well before it is planted. The ability to set a price floor and participate in future market rallies over a timeframe that I get to choose has been a game changer to our farm's risk management plan.

#### **CFTC Reauthorization**

As the Agriculture Committee has previously looked to reauthorize the CFTC on a number of occasions since authorization expired in 2013, NCFCA has supported the Committee's efforts.

Reauthorizing CFTC is the way in which this Committee acknowledges the importance of the agency's critical functions. Continued delay unnecessarily withholds that vote of confidence. While the current trend is to focus on new shiny objects such as cryptocurrency, we continue to rely on the CFTC to ensure the soundness of the bedrock of our commodity markets. As outlined above, it is essential for the agriculture industry to have sound, well-functioning commodity derivatives markets, and appreciate that the Agriculture Committee continues to provide that oversight. The CFTC performs the essential role of helping to safeguard U.S. futures, options and swaps markets that our industry relies on for critical risk management and price discovery functions. For the U.S. agricultural and energy contracts that are utilized extensively by our members to manage their market and business risks, this regulatory oversight is crucial.

Throughout Dodd-Frank implementation, now a decade ago, NCFCA has advocated that the agriculture industry does not fit in a one-size-fits-all regulatory regime meant for Wall Street. As such, we continue to encourage you to help ensure that regulatory burdens don't impede the ability of farmers, their cooperatives and others involved in the agriculture industry to have access to the risk management tools they need. Reauthorizing CFTC would reassert this Committee's oversight of this role.

#### *Costs to End-Users*

The CFTC performs the critically important role of helping safeguard U.S. futures and swaps markets, which benefits all Americans with more stable prices and a sound financial system. And while the Commission's responsibilities have continued

to expand dramatically, adequate funding has remained stagnant. While outside the jurisdiction of this Committee, we encourage Congress to provide sufficient funding through appropriations for CFTC to perform its important functions. Without sufficient resources to staff the Commission and invest in these areas, the CFTC's ability to perform these important functions, as well as ensuring the integrity of the more traditional commodity markets our members rely on for risk management purposes, will be diminished.

However, aggregate regulatory costs and market liquidity are an ongoing concern for farmers and their cooperatives. Agriculture is a high-volume, low-margin industry, and incremental increases in costs trickle down and impact farmers. Taken incrementally, the costs may not seem unreasonable, but those costs are evident to those who have to absorb or pass them on to the farmer. Even as end-users, significant resources must be used just to comply with the additional paperwork requirements called for under Dodd-Frank. In fact, a number of NCFC members have had to greatly increase spending on compliance staff and technology due to additional regulations.

Therefore, we would like to caution the Committee against imposition of any type of user fee on the industry to fund the CFTC. We fear a further increase in cost structure due to higher transaction costs would discourage prudent hedging practices. While the President's 2025 budget request calls for user fees: "CFTC fees would be designed in a way that supports market access, liquidity, and the efficiency of the nation's derivatives markets," it does not indicate how that would be achievable. We believe the opposite to be true.

There are many users of futures contracts in the agricultural supply chains. In grain alone, there are producers, agricultural cooperatives, country elevators, processors, exporters and poultry and livestock feeders who use futures contracts to reduce price risk. Grain represented by underlying futures contracts can be traded multiple times. If there was a user fee associated with a trade, the likely result is the net selling price received by the producer would go down by the amount of the fee each time the underlying futures contract is traded.

In addition to lower farm gate prices farmers would receive, a user fee would result in an increase in risk being absorbed in the agriculture community in general, and would likely reduce the desire for participants, such as agricultural producers, to hedge their price risk.

#### *Basel III End Game*

Throughout the Dodd-Frank Act implementation process, NCFC advocated for rules that would allow for continued access to a robust and diverse set of hedging options, contracts and counterparties. Therefore, NCFC echoes the concerns of the proposals (Federal Reserve, Federal Deposit Insurance Corporation, The Office of the Comptroller of the Currency) raised by other end-users that use derivatives to hedge their commercial risks. While the goal of ensuring and improving financial system integrity is strongly supported by our members, we are concerned our industry would be subject to unintended consequences of what has been proposed.

We appreciate CFTC's engagement with the Prudential Regulators on this issue and are optimistic to hear that those agencies recently signaled their willingness to take another look at those proposals. If they were to go forward in their current form, potential impacts include:

- (A) increased end-users' costs of hedging;
- (B) fewer banking organizations acting as futures commission merchants (FCMs) to the agriculture industry and as swap dealers in commodity OTC derivative contracts, thereby reducing end-users' risk management options; and
- (C) less liquid and more volatile markets.

The impact of increased capital costs for derivative contracts as a result of proposals may create a disincentive for banking organizations to continue to offer designated contract market (DCM) clearing services through their FCMs, or act as market-makers in OTC commodity derivative contracts, which would result in less liquidity in commodity derivative markets, and fewer options for end-users.

Unnecessarily high capital requirements that do not match the associated risk also will create a barrier to entry for certain market participants, such as farmer-owned cooperatives and private companies. Farmer cooperatives are businesses owned, governed, and controlled by farmers and ranchers. Thus, we are particularly troubled by the determination of "Investment Grade" for Unlisted Corporate Exposures (the "Public Listing Requirement"). The Basel III Endgame Proposal would provide a preferential 65% risk weight for investment grade corporate exposures based on a large banking organization's internal assessment of creditworthiness. However, the Proposal would require that the preferential 65% risk weight can only



be applied if the counterparty has shares that are publicly traded on a national securities exchange or foreign equivalent.

Due to the impact of increased capital costs, we fear bank affiliated FCMs would be disincentivized from doing business with entities that are not publicly traded, while their swap dealing entities reduce, or altogether eliminate, offering those hedging services to cooperatives. Given the arbitrary nature of the public listing requirement and the likely unintended consequences on otherwise highly creditworthy entities, we have urged that this requirement be eliminated.

Thank you again for the opportunity to testify today before the Committee. We appreciate your role in ensuring our industry will continue to be able to effectively hedge commercial risk in supporting the viability of our farmers. I look forward to answering any questions you may have.

Thank you.

Ms. CARAVEO. And finally, Ms. Thornton.

**STATEMENT OF ALEXANDRA THORNTON, J.D., SENIOR DIRECTOR, FINANCIAL REGULATION, CENTER FOR AMERICAN PROGRESS, WASHINGTON, D.C.**

Ms. THORNTON. Thank you. Chairman Johnson, Ranking Member Caraveo, and esteemed Members of the Subcommittee, thank you for the opportunity to appear before you today.

The CFTC plays a central role in overseeing agriculture and other physical commodities markets which are essential to our economy, as well as overseeing the complex financial products known as swaps, which were at the heart of the 2007–2008 financial crisis.

The Commission oversees dozens of entities where derivatives are traded, ten organizations that clear those trades, and five more outside the U.S. It also oversees the registration and compliance of thousands of derivatives markets participants, and oversees self-regulatory organizations such as the Chicago Mercantile Exchange and the National Futures Association.

Yet, the CFTC is critically under-funded, and would remain so even if Congress were to grant all the funding that it has requested. The agency simply does not have adequate resources to fulfill its existing mission and statutory obligations. Because of this under-funding, many important protections and functions that should be performed by the Commission are not today, such as comprehensive review of designated contract market rule changes and products to ensure their compliance with the law and the core principles, and development and enforcement of detailed advertising performance and fee rules.

And since the financial crisis, the markets overseen by the CFTC, of course, have become larger, faster, and more interconnected. The Commission's responsibilities are essential to maintaining the integrity, resilience, and vibrancy of our derivatives markets, and ensure that these markets never again threaten the stability of our financial system or wreak havoc on our economy. The Commission should be reauthorized and adequately funded to carry out its existing responsibilities.

This is a major reason why the agency's authorized activities should not be expanded into new areas, as proposed recently in connection with digital assets and voluntary carbon credits. We already know there is rampant fraud and abuse in the crypto industry. Protecting retail investors, consumers from this fraud and abuse should be the guiding principle of any new special digital

asset regulatory regime. Yet, the CFTC in its self-regulatory organization currently lack comprehensive marketing and sales practice rules like those of FINRA and the SEC because the agency has never had to protect retail—has seldom had to protect retail investors from the information asymmetries they confront in financial transactions.

In addition, digital assets are promoted by market intermediaries that are often acting in multiple conflicting roles. Most rules designed to reduce such conflicts of interest, along with rules that combat terrorism, financing, and money laundering, require transparency and accountability that the industry does not want, but are essential to investor protection. These are just two parts of the extensive regulatory framework that the Commission would have to develop in order to adequately protect retail investors in crypto. This framework would take years to develop and absorb significant time and energy away from the agency's existing duties, and the rules developed could raise regulatory risk if challenged in court. Thus, a new CFTC regime for crypto could actually introduce more uncertainty around these assets, rather than less. It would also be extremely inefficient and costly to taxpayers and market participants to create a duplicate investor protection regime at the CFTC when there is a robust investor protection regime at the SEC that has been perfected continuously over 9 decades. A CFTC regime could incentivize players in the securities markets to restructure assets and deals to take advantage of a weaker CFTC regime, which could spread the risk to retail securities investors. Finally, a new CFTC regime would create a new veneer of legitimacy and safety, further confusing retail investors who are finally beginning to understand the risks of crypto.

Any perceived gaps in the current Federal financial regulatory framework as it applies to digital transactions could lead to larger gaps and greater risk to our capital markets.

The CFTC also should not be authorized to take a wider role on voluntary carbon credit derivatives, as the agency's recent proposal might inspire. The underlying assets, the voluntary carbon credits themselves, cannot readily be traded in a manner that is consistent with the core principles, primarily because a material percentage of the underlying projects that purportedly give rise to the credits simply do not generate the carbon savings claimed by those who market them. That is, the amount of carbon actually being removed and for how long is not sufficiently known to form a reliable market, and is far beyond the agency's expertise to fix. Until the problems are fixed by other responsible public and private parties in a global—in a unified global system, voluntary carbon credit derivatives should not be listed or traded.

Thank you again for inviting me to testify today. I look forward to answering your questions.

[The prepared statement of Ms. Thornton follows:]

PREPARED STATEMENT OF ALEXANDRA THORNTON, J.D., SENIOR DIRECTOR,  
FINANCIAL REGULATION, CENTER FOR AMERICAN PROGRESS, WASHINGTON, D.C.

Chairman Johnson, Ranking Member Caraveo, and esteemed Members of the Subcommittee, thank you for the opportunity to appear before you today to discuss reauthorization of the Commodity Futures Trading Commission (CFTC).

I am senior director of financial regulation at the Center for American Progress, an independent, nonpartisan policy institute dedicated to improving the lives of all Americans through bold, progressive ideas, as well as strong leadership and concerted action.

While reauthorization presents an opportunity to assess the funding of an agency and ensure that those financial resources are adequate for the responsibilities Congress has given it, as explained below we strongly caution against using the CFTC reauthorization process to expand the agency's authorities, into areas significantly beyond its current expertise and capabilities.

**The CFTC should be reauthorized in order to protect our economy**

The CFTC plays a central role in oversight of physical commodities markets which are essential for our economy, including our manufacturing, transportation, and agriculture. And since the enactment of the Dodd-Frank Act and through subsequent rule makings, it has come to play an essential role in overseeing the complex financial products known as swaps, which were at the heart of the 2007–2008 Financial Crisis.

The Commission oversees 41 registered entities, including 16 designated contract markets (DCMs), 21 registered swap execution facilities (SEFs) and four provisionally registered swap data repositories.<sup>1</sup> It currently has ten registered derivatives clearing organizations (DCOs), two of which have been designated by the Financial Stability Oversight Council as systemically important.<sup>2</sup> And it regulates five registered DCOs located beyond U.S. borders.<sup>3</sup> The Commission's market participants division oversees the registration and compliance of thousands of derivatives market participants, such as swap dealers, major swap participants, futures commission merchants, retail foreign exchange dealers, introducing brokers, commodity trading advisors, commodity pool operators, floor brokers, and floor traders.<sup>4</sup> In addition, it oversees futures industry self-regulatory organizations, such as the Chicago Mercantile Exchange and the National Futures Association.<sup>5</sup>

Yet, the CFTC is critically under-funded and would remain so even if Congress were to grant all the funding it has requested. Frankly, the agency does not have adequate resources to fulfill its existing mission and statutory obligations.

The challenge with the CFTC is that it has been so chronically under-funded that many important protections and functions that should be performed by the Commission are not today. For example, the Commission does not comprehensively review all DCM rule changes and products to ensure their compliance with the law and the Core Principles. These changes may include changes to market data access and costs, trading operations changes, or listing of new products. The rules and processes adopted by the CFTC currently do not allow for adequate Commission or public consideration of these changes now, leading to DCM practices that unnecessarily burden market participants with costs and complexities that are inconsistent with the law and Core Principles.<sup>6</sup>

Other functions that one might expect have also never been done, likely because the target users of the markets it has traditionally overseen have been sophisticated businesses. For example, the agency and the SROs it oversees have never developed or enforced detailed advertising, performance, and fee rules. This stands in stark contrast to the detailed requirements imposed upon brokers and asset managers in the securities markets.<sup>7</sup>

Unfortunately, the inadequate budgeting and staffing at the agency have led to inadequate examinations, leading to several high profile, years-long abuses and misconduct in some of its core markets, such as U.S. Treasury futures and metals futures markets.<sup>8</sup>

<sup>1</sup> Commodity Futures Trading Commission, *President's Budget, Fiscal Year 2025*, March 2024, available at [https://www.cftc.gov/sites/default/files/CFTC%20FY%202025%20President's%20Budget\\_Final\\_for%20Posting.pdf](https://www.cftc.gov/sites/default/files/CFTC%20FY%202025%20President's%20Budget_Final_for%20Posting.pdf).

<sup>2</sup> *Ibid.*

<sup>3</sup> *Ibid.*

<sup>4</sup> *Ibid.*

<sup>5</sup> *Ibid.*

<sup>6</sup> See, e.g., Letter from Chris Nagy, Healthy Markets Association, to Hon. Heath Tarbert, CFTC, December 11, 2020, available at <https://healthymarkets.org/wp-content/uploads/2020/12/CME-Historical-Data-12-11-2020-4.pdf>.

<sup>7</sup> FINRA, Rule 221: Communications with the Public, available at <https://www.finra.org/rule-221>. Notably, in those markets, registered securities exchanges are not soliciting orders from the public for transactions or generally making claims related to asset performance.

<sup>8</sup> See, e.g., Abhishek Manikandan and Michelle Price, "JPMorgan to pay \$920 million for manipulating precious metals, Treasury market," *Reuters*, September 29, 2020, available at <https://>

The 2007–2008 Financial Crisis is more than 16 years in the rearview mirror. As this Committee considers reauthorization of the CFTC, it should remember the details of how the Financial Crisis happened and the devastation of the financial system and the economy that followed. The dangerous combination of deregulation and weakening of regulators’ authorities that preceded the crisis led to a collapse of major portions of our financial system and ultimately a lengthy recession. Between 2008 and 2009, the U.S. lost 7.6 million jobs, and it took until 2014 for employment to recover to pre-crisis levels.<sup>9</sup> And from 2008 to 2013, more than 5 years later, gross domestic product (GDP) per capita remained below the 2007 level.<sup>10</sup> Economists at the Federal Reserve Bank of San Francisco have estimated that the long-term effects of the Financial Crisis led to a lifetime income loss per capita in present discounted value terms of about \$70,000 (in 2017 dollars).<sup>11</sup> Wealth gaps between the middle class and wealthy Americans worsened significantly all because the rules that placed guardrails on risk-taking had been gutted and the agencies responsible for overseeing the financial system had been weakened.

This Committee should also keep in mind that, since the crisis, the markets overseen by the CFTC have become larger, faster, more interconnected, and more retail in focus. In other words, the demands on the CFTC are already greater than they have ever been.

My colleagues Marc Jarsulic and Lilith Fellowes-Granda at the Center for American Progress recently estimated the present-day costs of a repeat of the Great Recession.<sup>12</sup> They found that a 2007-scale financial shock today would result in 8.7 million people losing their jobs by 2026, and employment would not recover to current levels until 2031.<sup>13</sup>

As we all know by now, previously unregulated over-the-counter derivatives played a central role in the Financial Crisis. Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act<sup>14</sup> called for a comprehensive regulatory framework for these derivatives, granting the CFTC regulatory authority over swaps and the Securities and Exchange Commission (SEC) regulatory authority over security-based swaps.<sup>15</sup> Through transparency, business conduct standards, clearing requirements and much more,<sup>16</sup> the framework sought to eliminate or reduce risky practices that led to the crisis, including price opacity, the sale by large firms of credit default swaps with inadequate capital or liquidity to back the trades, practices that undermined the ability to net trades thus increasing counterparty risk, and the commingling of client margins with dealer assets.<sup>17</sup>

By 2021, the CFTC had fulfilled a large part of its initial responsibility to drag implementing rules required by the Dodd-Frank Act.<sup>18</sup> But its job is still not finished. It has a responsibility to continue overseeing swaps and other derivative markets, as well as major market participants. The agency must monitor the markets and market participants for compliance with its existing rules, and impose appropriate disclosure requirements, margin and capital rules, risk management standards, and other safeguards on the firms and products under its jurisdiction. These

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[www.reuters.com/article/business/jpmorgan-to-pay-920-million-for-manipulating-precious-metals-treasury-market-idUSKBN26K321/](https://www.reuters.com/article/business/jpmorgan-to-pay-920-million-for-manipulating-precious-metals-treasury-market-idUSKBN26K321/) (reflecting Treasury and metals market manipulations lasting from 2008 to 2016).

<sup>9</sup>Marc Jarsulic and Lilith Fellowes-Granda, “Project 2025 Would Allow Financial Disaster To Bolster Wall Street’s Bottom Line,” Center for American Progress, July 1, 2024, available at <https://www.americanprogress.org/article/project-2025-would-allow-financial-disaster-to-bolster-wall-streets-bottom-line/>.

<sup>10</sup>*Ibid.*

<sup>11</sup>Regis Barnichon, Christian Matthes, and Alexander Ziegenbein, “The Financial Crisis at 10: Will We Ever Recover?,” Federal Reserve Bank of San Francisco, August 13, 2018, available at <https://www.frbsf.org/research-and-insights/publications/economic-letter/2018/08/financial-crisis-at-10-years-will-we-ever-recover/>.

<sup>12</sup>Marc Jarsulic and Lilith Fellowes-Granda, “Project 2025 Would Allow Financial Disaster To Bolster Wall Street’s Bottom Line,” Center for American Progress, July 1, 2024, available at <https://www.americanprogress.org/article/project-2025-would-allow-financial-disaster-to-bolster-wall-streets-bottom-line/>.

<sup>13</sup>*Ibid.*

<sup>14</sup>Dodd-Frank Wall Street and Consumer Protection Act, Pub. L. 111–203, July 21, 2010, available at <https://www.congress.gov/111/plaws/publ203/PLAW-111publ203.pdf>.

<sup>15</sup>Michael S. Barr, Howell E. Jackson, and Margaret E. Tahyar, *Financial Regulation: Law and Policy*, West Academic (St. Paul: 2021) at pp. 1265–66.

<sup>16</sup>Legal Information Institute, “Dodd-Frank: Title VII—Wall Street Transparency and Accountability,” Cornell Law School, available at <https://www.law.cornell.edu/wex/dodd-frank-title-vii-wall-street-transparency-and-accountability> (last accessed July 2024).

<sup>17</sup>Barr, 2021, at p. 1263.

<sup>18</sup>“Final Rules, Guidance, Exemptive Orders & Other Actions,” Commodity Futures Trading Commission website, available at <https://www.cftc.gov/LawRegulation/DoddFrankAct/DoddFrankFinalRules/index.htm> (last accessed July 2024).

responsibilities are essential to maintaining the integrity, resilience, and vibrancy of our derivatives markets—and ensure that these markets never again threaten the stability of our financial system or wreak havoc on our economy.

Recognizing the additional responsibilities it had imposed, Congress significantly increased the budget of the CFTC after passage of the Dodd-Frank Act and enacted several increases beyond the rate of inflation over the years since then. The percentage change in the last 5 years—from 2019 to 2024—was 36 percent or 11 percent, when adjusted for inflation.<sup>19</sup> Still, as mentioned above, these amounts are insufficient for the Commission to carry out its existing responsibilities.

For this reason and for other reasons explained below, we strongly encourage Congress to avoid expanding the authority of the CFTC at this time, especially for purposes of authorizing new areas of responsibility that are beyond its current expertise and jurisdiction, such as new authorities relating to digital assets or voluntary carbon credits (VCCs). Expansion of the agency's jurisdiction in such areas may lead to regulatory inefficiencies, the creation of negative market signals and incentives, and general market confusion. More important, it would divert the Commission's resources away from its existing responsibilities, which are so essential to our economy.

My remaining remarks focus on the importance of avoiding inefficiencies, dis-incentives, and market confusion associated with such expanded authorities.

**CFTC authorization should not be expanded for purposes of setting up a special regime for crypto assets or regulating voluntary carbon credits.**

Proposals to expand the jurisdiction of the CFTC are often justified on grounds of promoting innovation and the claim that rules to protect investors stifle innovation. But this is not a binary choice: innovation or investor protection. It is possible to have both. The greater risk is not of stifling innovation. The greater risk is unleashing something that puts investors or worse the financial system and the economy at risk. That is what happened prior to the Financial Crisis. In the Commodity Futures Modernization Act of 2000, Congress exempted most over-the-counter (OTC) swaps from CFTC and SEC jurisdiction, allowing the exemption as long as the participants were sophisticated, as defined broadly in the legislation.<sup>20</sup> By 2008, the gross amount of OTC derivatives outstanding had increased by 630 percent, and credit default swaps had increased 100-fold.<sup>21</sup> Financial lobbying played a major role in this state of affairs, which severely undermined regulators' ability to see what was going on and stem the fallout.<sup>22</sup>

This lesson from recent history must guide current debates in which financial market participants seek weaker regulation.

Agricultural markets are so important, and they depend upon the CFTC to ensure that derivatives markets function well and are free of fraud and manipulation. It is important for this Committee to understand that expanded authorities of the types the agency has sought would distract it from its foundational responsibilities.

**Digital asset regulation**

Whatever promise the digital asset industry may hold, we already know for certain that it contains rampant fraud and abuse. Digital assets are promoted by conflicted market intermediaries that are often acting as introducing broker, executing broker, transfer agent, custodian, and more.

If Congress is to develop a new, specialized regime for the regulation of digital assets, ensuring some integrity of the claims made to customers should be a top priority. But, while the CFTC does not generally have such a regime, the Financial Industry Regulatory Authority (FINRA), the self-regulatory organization that oversees registered securities broker-dealer firms, and the SEC do.

Because there are many registered broker dealers that engage with digital assets, FINRA has already begun to examine issues related to their crypto marketing claims. In particular, in November 2022, as part of a targeted exam, FINRA reviewed over 500 crypto asset-related retail communications by its registered broker-dealer members.<sup>23</sup> It found that over 70 percent of those communications contained potential substantive violations of FINRA's rule on communications with the pub-

<sup>19</sup> Author's calculations based on actual budget figures in annual White House budget proposals since FY 2009, adjusted for inflation using the Employment Cost Index.

<sup>20</sup> Barr, 2021, at p. 1259.

<sup>21</sup> *Ibid.*

<sup>22</sup> *Ibid.*

<sup>23</sup> FINRA, "FINRA Provides Update on Targeted Exam: Crypto Asset Communications," January 2024, available at <https://www.finra.org/rules-guidance/guidance/targeted-examination-letters/sweep-update-jan2024>.

lic.<sup>24</sup> These included, for example, false statements or implications that crypto assets functioned like cash or cash equivalent instruments; comparisons of crypto assets to other assets, like stock investments, without providing a sound basis to compare the varying features and risks of these investments; failure to provide a sound basis to evaluate crypto assets by omitting clear explanations of how crypto assets are issued, held, transferred, or sold; and misrepresenting that the protections of the Federal securities laws or FINRA rules applied to crypto assets.

These findings related only to the handful of crypto firms that are also already registered broker-dealers in the securities markets, who would seem to be the most likely to comply with regulatory requirements. It does not include the “native” crypto firms that have declined to make such registrations.

Again, the CFTC and its self-regulatory organization lack comprehensive marketing and sales practices rules like those of FINRA and the SEC. This is just one part of the extensive regulatory framework that the agency would have to develop in order to adequately protect retail investors in crypto. Yet, developing such rules would take years and absorb significant time and energy of the agency, and the rules that would be developed could raise regulatory risk if challenged in court. All of this raises the distinct possibility that such a new CFTC regime for crypto would actually introduce more uncertainty around these assets, rather than creating clarity.

In the 116th Congress, the last time CFTC reauthorization legislation was considered, the drag bill at that time, H.R. 6197, included provisions that would have provided for the regulation of digital commodities, though the full implications of that language are not clear. The industry has worked with like-minded legislators since then to craft a more detailed regulatory regime under the jurisdiction of the CFTC for digital commodities. These proposals have serious potential ramifications for retail investors, consumers, and the stability of the financial system. Any perceived gaps in the current Federal financial regulatory framework as it applies to digital transactions would pale in comparison to the potential negative impacts of these proposals.

The crypto industry has long argued for a special regulatory regime under the CFTC. But the CFTC by design has never focused on retail investors. The commodity laws do not even contemplate the idea of an issuer who is selling to a retail investor; thus, the agency has never had to protect people from the information asymmetry that arises in such situations. The CFTC was created in 1974 to regulate derivatives, which are complex financial contracts that are based on the value of an underlying asset. They are used to hedge against the risk of changing prices in a wide range of industries, but very seldom by retail investors and consumers. Increasingly, derivatives are used for speculation. They are just too complicated, potentially volatile, and risky for retail investors.

By contrast, the SEC—also by design—has focused on protecting retail investors since it was created 90 years ago. It has decades of experience with protecting investors and the public, and it has developed a robust framework of rules for doing so—rules that can and do apply to the vast majority of digital asset transactions. It would be extremely inefficient—and costly to taxpayers and market participants—to create a duplicate investor protection regime for digital assets at the CFTC.

It is also highly likely that authorizing a special regulatory regime for crypto under the CFTC would create negative market signals and incentives, as players in other markets sought to restructure assets and deals to take advantage of the vacuum of rules and capacity to protect retail crypto investors. The industry has defied the SEC rules that already apply to them,<sup>25</sup> and, if the CFTC’s jurisdiction over digital assets were expanded, there is no reason to believe that the crypto industry would not resist rules designed to accomplish similar investor and consumer protection goals at the CFTC.

If the CFTC’s jurisdiction is expanded to allow it to develop a special regulatory regime for crypto, this would likely provide a veneer of credibility and safety around crypto. This could result in even more harm to retail crypto investors, who may think they are fully protected.

Finally, as alluded to above, the implementation of a comprehensive regulatory regime for digital assets within the CFTC’s jurisdiction would be unprecedented in

<sup>24</sup> FINRA, Rule 221: Communications with the Public, available at <https://www.finra.org/rules-guidance/rulebooks/finra-rules/2210>.

<sup>25</sup> Chair Gary Gensler, “Statement on the Financial Innovation and Technology for the 21st Century Act,” U.S. Securities and Exchange Commission, May 22, 2024, available at <https://www.sec.gov/newsroom/speeches-statements/gensler-21st-century-act-05222024> (last accessed July 2024).

the agency's history, and both the burdens on the agency and the risks to the capital markets could be exceedingly large.

### Regulation of voluntary carbon credit derivatives

Voluntary carbon credit (VCC) derivatives pose a different problem. As the responses to the CFTC's proposed guidance for voluntary carbon credit derivatives make clear,<sup>26</sup> the underlying assets—the voluntary carbon credits themselves—cannot readily be traded in a manner that is consistent with the Core Principles.<sup>27</sup>

It is well established that a material percentage of the underlying projects that purportedly give rise to the credits simply do not generate the carbon savings claimed by those who market them.<sup>28</sup> They are not certain and verifiable and thus not fungible enough to ensure that trading in them will be consistent with the Core Principles. It would be similar to an aluminum futures contract being traded despite the warrant for the aluminum being tied to only half of the promised amount, or no aluminum at all, perhaps a small hunk of granite.

Already, the commodity futures markets are occasionally rocked by scandals where it is later revealed that the physical metal underlying futures contracts has disappeared or of improper form or volume. But these cases should be relatively easy to identify and quickly end, given that the actual metal is supposed to be stored at a warehouse that could be quickly and easily inspected. There is no credible way for this verification function to exist either on an initial or ongoing basis for the vast majority of projects claiming some reduction of carbon in the air.

Worse, unlike in the physical commodities markets, where the ultimate purchaser of a contract may take physical delivery and use the metal, for example, that simply does not happen in the VCC markets. The end-user in the metals markets very much wants the metal to be of the specified quality and quantity, so as to be potentially useful. However, there is no such market protection built into VCCs, as the carbon saved is not directly used. To the contrary, many users of VCCs may have incentives to accept exaggerated claims of carbon saved.

The problem cannot be solved by delegating a standard setter, which the CFTC cannot do, or by allowing the accrediting of VCC derivatives contracts by the exchanges, which are equally lacking in the scientific knowledge and capacity to ensure that the underlying assets are certain and verifiable. Under these circumstances, allowing the designated contract markets to approve the listing of voluntary carbon credit derivatives would only result in market confusion and fraud.

VCCs are likely to continue inviting waste and fraud. Unlike carbon credits traded under government cap and trade regimes, by definition VCCs do not involve governments, do not have corresponding government emissions caps, and can be created anywhere in the world, making them nearly impossible to verify and monitor. One recent study found that the vast majority of voluntary carbon credits are not valid.<sup>29</sup> Before carbon credits can form the basis for derivative contracts, there must be an independent, reliable, fact-based entity that verifies carbon emission reductions on a global basis. To date, that does not exist, despite efforts under the auspices of the United Nations.<sup>30</sup>

VCC derivatives should not be listed or traded under the auspices of CFTC authority until there is a clear, consistent, and reliable methodology for creating voluntary carbon credits and establishing their permanence, as well as how to verify,

<sup>26</sup> Letter to The Honorable Rostin Behnam, Center for American Progress Comments on Commission Guidance Regarding the Listing of Voluntary Carbon Credit Derivative Contracts, February 16, 2024, available at <https://comments.cftc.gov/PublicComments/ViewComment.aspx?id=73324&SearchText=progress>.

<sup>27</sup> Designated Contract Markets (DCMs), Commodity Futures Trading Commission website, available at <https://www.cftc.gov/IndustryOversight/TradingOrganizations/DCMs/index.htm> (last accessed July 2024).

<sup>28</sup> See, e.g., Natasha White, "Carbon Offset Gatekeepers Are Failing to Stop Junk Credits," *Bloomberg*, March 21, 2023, available at <https://news.bloomberglaw.com/esg/carbon-offset-gatekeepers-are-failing-to-stop-junk-credits>; Patrick Greenfield, "Revealed: more than 90% of rainforest carbon offsets by biggest certifier are worthless, analysis shows," *The Guardian*, January 18, 2023, available at <https://www.theguardian.com/environment/2023/jan/18/revealed-forest-carbon-offsets-biggest-provider-worthless-verra-aoe>; and Debra Kahn, "Offsets' promise and peril," *Politico*, January 1, 2023, available at <https://www.politico.com/newsletters/the-long-game/2023/01/20/offsets-promise-and-peril-00078763>.

<sup>29</sup> Patrick Greenfield, "Revealed: more than 90% of rainforest carbon offsets by biggest certifier are worthless, analysis shows," *The Guardian*, January 18, 2023, available at <https://www.theguardian.com/environment/2023/jan/18/revealed-forest-carbon-offsets-biggest-provider-worthless-verra-aoe>.

<sup>30</sup> Eklavya Gupte and Agamoni Ghosh, "COP28: Lack of progress on Article 6 likely to further limit carbon market growth," *S&P Global*, December 13, 2023, available at <https://www.spglobal.com/commodityinsights/en/market-insights/latest-news/oil/121323-cop28-lack-of-progress-on-article-6-likely-to-further-limit-carbon-market-growth>.

register, and retire credits in a unified global system. Without these prerequisites, the most essential terms of a derivative contract based on those carbon credits, the amount of carbon actually being removed and for how long, will not be sufficiently known to form a reliable market that is consistent with the Core Principles.

At the same time, the CFTC should aggressively pursue cases of obvious fraud and manipulation in VCC markets that have impacts on its derivatives markets, including for contracts that have already been identified as being tied to credits that were awarded for fraudulent or erroneous reasons. This should be a significant priority for the understaffed and under-funded examinations and enforcement staff. Again, the agency appears to not have the resources to protect its existing jurisdictions, even though it already has sufficient existing authorities.

To conclude, we strongly support a clean reauthorization of the CFTC, without new authorities, so that the agency can focus on its existing responsibilities to ensure the integrity, resilience, and vibrancy of U.S. derivatives markets.

Thank you again for inviting me to testify today. I look forward to answering your questions.

The CHAIRMAN [presiding.] We will now recognize Members for questions. We will begin with my favorite portrait from the south wall, Mr. Frank Lucas.

Mr. LUCAS. Thank you, Mr. Chairman, and thank you, Ranking Member, for holding this hearing, and the witnesses for agreeing to testify.

The CFTC regulates markets that impact nearly every part of the economy, and reauthorizing the Commission will give us an opportunity to provide meaningful oversight, and give certainty to market participants. The derivatives market faces a number of potential stresses: the Basel Endgame, the GSIB surcharge, the treasury market structure reform, along with substantial SEC rule-making agenda that will decrease market liquidity and increase costs.

In the context of CFTC reauthorization, it is worth considering the full regulatory environment that the markets are confronted with. So, there is a lot to discuss.

Starting with the Basel proposal, an issue I have discussed with Chairman Behnam, Secretary Yellen, Chairman Powell, and all of the Prudential Regulators, is the impact this will have on our capital markets, including reduced access to derivatives products for end-users, and further concentrations of FCMs. It seems like the regulators would be open to a re-proposal, but FDIC and OCC will have to join with the Fed on that decision.

Mr. Lukken, you are no stranger to the Agriculture Committee room, so thank you for joining us today and touching on Basel during your testimony. Could you expand on why it is so important that the regulators reopen the proposal for public comment?

Mr. LUKKEN. Well, Congressman Lucas, you have been a leader on this topic on capital, and this Committee has been a leader. To point out the obvious fact from the financial crisis, which is that our markets in clearing and essential counterparties actually mitigate risks. They reduce risk in the financial system, and so, the capital is an important component of the financial reforms coming out of the financial crisis, that banks should hold more capital for risky activity. But they just have it wrong. I think the Prudential Regulators are overtaxing clearing activity to make it so there is going to be a capacity issue, that banks are going to stop offering this service to hedgers.

We heard Travis talk about this, that end-users may have limited access to hedging vehicles, to hedge volatility and commodity



markets as a result of Basel capital. So, our hope is that the Prudential Regulators are listening to the reasonable voices of the CFTC, Chair Behnam, and others that have said you have to get this right. It has to be proportional to the risks brought by our markets, and we are hopeful that it gets fixed in the coming months.

Mr. LUCAS. Mr. Sexton, you are a member of the CFTC's Global Markets Advisory Committee. One suggestion, among many, that GMAC had for the Commission last month was to hold a roundtable with the bank regulators focused on derivatives issues impacted by Basel.

Could you explain broadly to the importance of stakeholder feedback on matters that will have a significant impact on the market?

Mr. SEXTON. Thank you for the question, Congressman Lucas. I certainly endorse the concept of GMAC and its recommendation to hold this roundtable to further determine the impacts of these capital rules.

As Mr. Lukken and Travis have indicated, this is extremely important to the farmers, ranchers, and end-users and hedgers because of the consolidation that may occur among firms if these capital rules are put into place.

So, stakeholder impact and comments are extremely important, and something that we should be looking to do.

Mr. LUCAS. The CFTC's enforcement authority has been a closely watched issue during the past several years. Reauthorizing the CFTC gives us the opportunity to closely examine what the Commission is doing, and identifying improvements that can be made.

Mr. Lukken, back to you. Do you think the Commission's current cross-border authority is effective from a regulatory and enforcement perspective?

Mr. LUKKEN. I can only speak from my experience at the CFTC, but we were able to work closely with our regulatory authorities overseas to partner with them to make sure they had the appropriate information. But the important thing is, does the CFTC have direct authority when there is a strong nexus to the United States? And I believe they do, that they have the ability to go after bad behavior overseas when it is a strong nexus to the United States.

So, I think the CFTC does have appropriate authority.

Mr. LUCAS. Mr. Chairman, before I yield back, I would simply note that I have spent much time screaming about the potential impacts of the Basel capital requirements on the American economy. This is one of those things that if we don't get it right, the damage that would be inflicted will be extremely difficult to address later.

With that, I yield back, Mr. Chairman.

The CHAIRMAN. One hundred percent right.

With that, we yield 5 minutes to the Ranking Member.

Ms. CARAVEO. Thank you, Mr. Chairman, and thank you all once again for being here this morning as we consider this important reauthorization of the CFTC. Your testimony is invaluable.

Now, the last attempt by the Committee to reauthorize the CFTC included provisions to harmonize some of the enforcement authorities between the CFTC and the SEC. One provision would clarify the CFTC's authority to prosecute fraud and manipulation outside

of the United States, where such activities impair our futures markets, and another would establish a *reckless standard* for those who aid and abet fraudsters and manipulators of our markets, the same standard that currently applies to those who actually perpetrate the fraud or manipulation.

For the whole panel, what are your thoughts on whether we need to harmonize such enforcement activities, and whether these are appropriate?

Thank you. Anyone who wants to answer, go ahead.

Mr. SEXTON. [audio malfunction].

Mr. LUKKEN. I would just chime in; I agree with Tom that it is important for the CFTC to have clear authority to go after bad behavior overseas. I can't speak to the specifics of whether harmonizing with the SEC's enforcement authorities is the right approach. As I had mentioned, when I was chair we had plenty of authority to go after actors. We did not feel impeded in any way of going—

The CHAIRMAN. Mr. Lukken, is your microphone on?

Mr. LUKKEN. Pardon me. Sorry.

We did not have any impediments during my tenure for going after bad behavior overseas, or if we were able to share with foreign authorities. So, we certainly support the premise, though, that it is important for the CFTC to have a robust authority to go after manipulative behavior overseas.

Mr. ANTONSEN. I would agree with both gentlemen.

Ms. CARAVEO. Perfect, thank you.

Ms. Thornton?

Ms. THORNTON. We don't really have a strong opinion on that, but I am really interested to learn more about it.

Ms. CARAVEO. Perfect, thank you.

Now, Mr. Lukken, your testimony raises concerns about conflicts of interest within vertically integrated structures, particularly futures commission merchants owned by exchanges and clearinghouses, and embedded in their trading and legal structures. Can you speak more to these concerns and the impact of such structures on our financial systems, and then Mr. Antonsen, if you could follow up as to whether your members have any concerns?

Mr. LUKKEN. We are seeing this more and more where through efficiencies of a lot of these crypto platforms that they are combining both being an exchange, a clearinghouse, and an FCM into one legal entity.

The problem is that exchanges and clearinghouses have self-regulatory authorities over FCMs. So, in essence, you would be policing yourself and those authorities. We saw some of this, and we raised concerns with the FTX application where they had registered—not registered, but a trading arm within their legal structure that were combining the exchange, the clearinghouse, and a trading arm within their legal structure. And that ultimately led to some of the issues we saw with their demise.

So, we think it is good for the CFTC to take a close look at this to see if there are conflicts of interest that need to be addressed, if there are governance challenges we need to implement as part of this, are we needing to separate certain functions because of that dual role of self-regulatory agency over these authorities.

Mr. ANTONSEN. Could you repeat your question for me, just so I am clear?

Ms. CARAVEO. Just whether your members have any similar concerns around what Mr. Lukken just discussed.

Mr. ANTONSEN. No, I think having guardrails and double-checks in that, I think we would agree with that. We use multiple FCMs. At times there are options to have FCMs that are not exchanges. So, I would agree with Walt on them.

Ms. CARAVEO [presiding.] Thank you all again for your testimony, and I will yield back the remainder of my time.

I am pleased to turn it next to our esteemed Chairman Thompson for his questions.

Mr. THOMPSON. I thank the gentlelady, and once again to all our participant panelists, thank you so much.

Mr. Lukken, in your testimony you mentioned serving as acting Chairman of the CFTC during the last CFTC reauthorization in 2008. You also discussed the increasingly global nature of derivatives markets. Could you please elaborate on how the derivatives markets have evolved since that time, and addressing the importance of reauthorizing the CFTC as these markets evolve?

Mr. LUKKEN. Well, certainly since that time it has gotten much more global, since I was at the agency. I think the addition of over-the-counter derivatives has added challenges to the CFTC's legal authority. I shouldn't say challenges, but given them—

Ms. CARAVEO. Sorry. Mr. Lukken, I don't think your microphone is on. Oh, it is.

Mr. LUKKEN. I am having some microphone problems today, sorry.

But no, I think the markets are definitely more global. They are larger. As I mentioned—but we are seeing that the framework has upheld very well, really, since the Commodity Futures Modernization Act of 2000 (Pub. L. 106-554, Appendix E—H.R. 5660), which but in those flexible approaches. The CFTC is allowed to evolve itself with these market trends, so even though we are seeing more global volume, the CFTC has been able to keep pace with those changes. And that is why I think many of us, if not all of us on this dais, are saying that there doesn't need to be a huge overhaul of the Act, that it has actually kept pace with the big global growth.

Mr. THOMPSON. Yes, those core principles really have sort of made it resilient, and adaptable to—as things have evolved.

Mr. Sexton, could you please share with us your perspectives on this question?

Mr. SEXTON. Thank you, Chairman Thompson. Certainly, I admire you for being involved.

This is a turning point in the process. It is great that this Committee is seeking stakeholder interest in this process, a process that is not easy—by Congress to handle this reauthorization process. The Act has stood up well. I do have one recommendation with regard to *Griffin*, and I agree that—with Chair Behnam and the others testimony today that reauthorization signals the importance of our regulatory structure here to the global derivatives markets, and it gives that acknowledgment of the CFTC's critical role in that market.

So, I think it is very important to reauthorize the CFTC.

Mr. THOMPSON. Well, thank you. I think reauthorization also reflects our responsibility to do our job, and to make sure that we can—we should have done it before.

Mr. SEXTON. Yes.

Mr. THOMPSON. So, I look forward to accomplishing it here, even with just the remaining days we have in the 118th.

Mr. Antonsen, in your testimony you mentioned your concerns regarding the negative potential impacts of Basel III Endgame rules may have on the derivatives markets and the end-users that rely on them. Could you please share with us some of those negative potential impacts?

Mr. ANTONSEN. Yes, I think when the information first came out, speculation was that we were going to lose many FCMs due to the regulations. From our standpoint, we have seen FCMs get out of the business in the last 5 years. Many of them have. We have seen consolidation in the industry, and that—as a user of that, again, I mentioned we use multiple FCMs. To limit our resources and limit our options on who we can use, if one of those goes away, it—we look at potentially higher hedging costs, less people to do business with.

Mr. THOMPSON. Very good. Thank you.

Mr. Lukken, are your members concerned about the impacts of these proposals on end-users and other market participants?

Mr. LUKKEN. This is one of our top concerns as an industry. I think rarely does our industry all get on the same page on a topic, but from end-users to FCMs to exchanges to clearinghouses, this is going to limit the capacity of people to hedge in our markets. And so, as Travis mentioned, we have seen shrinking number of FCMs, those people that access production agriculture, allow them access to our markets. And if we lose more of those folks, it is going to make the framework of our system less safe.

And so, we think this is incredibly important to get this right. Give capacity to FCMs to get more access to more farmers, more commercial end-users in this marketplace. This is a no-brainer. Hopefully, the Prudential Regulators figure this out and fix these proposals.

Mr. THOMPSON. Am I correct in saying—I mean, the root cause of this would be increasing costs, but it would result in more systemic impacts as you described on a derivatives market?

Mr. LUKKEN. Yes. You are going to see less FCMs, and as a result, you are going to see more concentration in firms.

So, we want as broad—it is like insurance. You want as broad of a system of FCMs out there so that there are healthy FCMs across the board, and so that Travis has lots of choices of where he can bring his business.

Mr. THOMPSON. Very good. Thank you very much.

Ms. CARAVEO. Thank you, and we will go next to my colleague from California, Mr. Costa, for 5 minutes.

Mr. COSTA. Thank you very much. I think it is appropriate that we get together this morning and discuss the future of the CFTC.

I wanted to, folks, to begin with the question that has been raised. I guess, Mr. Lukken, you might be the first to respond or Mr. Sexton, about the under-funding. There was a discussion ear-

lier in the reauthorization effort that would allow you to charge fees to register companies to raise resources for the new level of oversight. The Appropriations Committee, I understand, as was noted in the opening comment by my colleague, cut it by \$20 million from the current budget.

When we consider the reauthorization of the Commission and discuss expansion of the authorities, what do you think we need to do to ensure that the CFTC is an appropriately funded regulator?

Mr. LUKKEN. Well, FIA supports the full and appropriate funding of the CFTC. When I was acting Chairman of the CFTC, it was important for us to talk to the appropriators about why our markets matter. And so, I think for us we do have concerns with user fees in that it would cause less hedging. As I mentioned about capital, it is the same issue that if you are directly taxing hedging capabilities, that is problematic for farmers.

Mr. COSTA. So, the user fees then *versus* the reduction of the \$20 million is the tradeoff, and do you think it is—

Mr. LUKKEN. No, I think appropriators should find ways to appropriately fund the CFTC and to—as they have lots of tradeoffs they have to think about, because it is taxpayer dollars. But we think a case should be made and is made that the CFTC should be appropriately funded.

Mr. COSTA. Yes.

Mr. Sexton, do you think the agency's lack of reauthorization since—and this is our fault, as the Chairman noted. Our responsibility, I guess I would say, since 2008, could impact your current funding challenges?

Mr. SEXTON. [inaudible] could impact NFA's funding challenges? Is that the question?

Mr. COSTA. Yes.

Mr. SEXTON. So, we are funded in two significant ways. I know there are two major regulatory programs. Our overall budget is about \$140 million to assist the CFTC—regulate the markets.

Our swaps regulatory program or swaps dealers is wholly funded by the swap dealer industry, by those dealers, and that is about \$47 million or so through membership dues paid to NFA.

Mr. COSTA. Self-funded?

Mr. SEXTON. Self-funded, yes.

Mr. COSTA. Yes.

Mr. SEXTON. The other component are futures is funded in part by membership dues, but the large portion of that funding program at about \$82 million is from what we call an assessment fee. We place a very small fee of what we call public trading volume. It is about 25 percent—

The CHAIRMAN [presiding.] Mr. Sexton, your microphone isn't working, we are being told. It is not broadcasting. So, if you could share—or grab a microphone with—

Mr. SEXTON. Sure. I don't know if I want yours, though. I don't know. Let me see what I can do here.

So, futures assessment fee—I am sorry—is a very small proportion, 25 percent, about a quarter of contract market value, that is public value, and that is at 4¢ around turn. So, it is a very small amount with regard to that fee.

Mr. COSTA. So, if the Financial Innovation Technology for the 21st Century, the FIT 21 were to become law, how much additional resources would the NFA need to effectively tackle these additional responsibilities in a new market?

Mr. SEXTON. That is a great question. We would—that is going to be dependent on how many new member firms we have and what our oversight regulatory responsibilities are.

Each of our regulatory programs needs to self-fund, however, and so, we will find a way with regard to our new members to get a revenue source in order to pay for what we need.

Mr. COSTA. Ms. Thornton, you talked about crypto fraud in your comments. How extensive do you describe it today, and what do you think we need to do about it?

Ms. THORNTON. I think it is quite substantial, and I think it is something that really needs to be focused on is the use of arbitrage, because these spot markets in tokens, non-crypto asset—sorry, tokens are actually—they have different streams, different data streams. And what that means is that when you buy a token, if you are a consumer and a retail investor and you buy a token, you get offered a price but you may not know what prices are being offered on the other platforms.

Mr. COSTA. So, how do we protect against that fraud?

Ms. THORNTON. I am sorry?

Mr. COSTA. How do we protect against that fraud?

Ms. THORNTON. Well, basically, the SEC does that by requiring a national market system. It actually was started in 1975. Congress authorized it in 1975. The idea that the different securities platforms would have to submit data so that a broker would know what the prices are that are being offered for that same security across the different exchanges, and would be able—and then also was given fiduciary duty of best interest—best execution, excuse me, so that they would have to execute the trade, picking the best price for the customer. But that doesn't exist at all with respect to crypto platforms.

Mr. COSTA. Well, Mr. Chairman and the Ranking Member, my time has expired but I think this is something that we need to look at in greater depth. When Mr. Lukken made his comment about prudence and overcapitalization, I am very curious about how he measures prudence or is that in the eye of the beholder? And then how do you measure the risk?<sup>1</sup>

But thank you very much. I appreciate the opportunity.

Ms. CARAVEO [presiding.] Thank you. The gentleman's time has expired.

We will go next to Mr. Miller of Ohio for 5 minutes.

Mr. MILLER of Ohio. Thank you. I want to thank the Chairman and the Ranking Member and the witnesses for being here this morning.

American agriculture utilizes a range of tools to manage risks. They employ vital on-farm strategies and Federal farm bill programs, including risk management commodity support programs, crop and livestock insurance, and disaster assistance prove critical in today's volatile marketplace. Our farm sector and other indus-

<sup>1</sup> **Editor's note:** the information referred to is located on p. 43.

tries can also access vital measures such as futures, options, and marketing contracts to manage risk from product and input price fluctuations.

In the modern world with input and production costs soaring and tight commodity prices, it is crucial to control the variables we are able to through commodity derivative markets. In the last years, conditions globally and other instabilities have led to exceptionally large price volatility and many commodity markets underscoring the role of the Commodity Futures Trading Commission.

To any of the witnesses, commodities derivatives markets are essential to help manage price risk and hedge exposures as these vital tools assist agriculture producers in hedging exposure to rising input costs, severe weather incidents, and volatile prices in fuel, fertilizer, and other essentials. Could the witnesses elaborate on the importance of derivatives products to your operations, and to those of your end-users? And just really quick also, if a bad actor in the derivatives industry is causing significant harm or allowing for illegal and unregulated activity to take place, does the CFTC have the ability and resources to swiftly address and prevent harm from occurring through effective enforcement?

Mr. ANTONSEN. I can address your first part of that question.

Derivatives, futures, options, over-the-counter contracts are paramount in what we do every day at Agtegra for both ourselves and for our cooperative members. So, purchasing grain, hedging grain, storing grain, getting all the way through the system, it is probably the most important thing we do from a cooperative in managing risk.

You mentioned volatility. Whether it is weather, global markets, global geopolitical events, volatility is through the roof and as farm margins are tightening down, it is more important than ever to have the right tools in place and available, and also to use them with everything that a producer has to use, like crop insurance. You multi-layer those risk programs in there to make that happen. So, we utilize those every single day, and we rely on a healthy marketplace to get in and out of those efficiently.

Mr. MILLER of Ohio. Thank you for that answer.

Can anyone address the second part of that question? I can just say it again.

The bad actor in the derivative industry is causing significant harm. Does the CFTC have the ability and resources to swiftly address it, prevent harm from occurring through effective enforcement?

Mr. SEXTON. Congressman, certainly we are all, as regulators, worried about bad actors and the impact it can have. I can tell you that NFA works very closely with the CFTC's Division of Enforcement to ensure that we find those bad actors, punish those bad actors, to the extent that we closely coordinate with them. We have quarterly meetings with that division.

So, as far as the partnership with NFA and the CFTC, we are very focused on bad actors, and I can't say enough about the Division of Enforcement and its dedication to doing so.

Mr. MILLER of Ohio. Thank you. I really appreciate that.

Second question. Given the importance of the United States agricultural production and the magnitude of U.S. exports of agricul-

tural products to global consumers, America's farmers and global end-users are not strangers to market volatility. Can any of you please elaborate on means to withstand these global uncertainties in the commodities market, and tools for agricultural producers, energy users, and others to deal with such instability?

Mr. ANTONSEN. I would say, from the worldwide standpoint, volatility is—can you repeat the question? I am sorry.

Mr. MILLER of Ohio. Yes, absolutely.

So, just to get right to it. Could you elaborate on what it means to withstand global uncertainties in the commodity markets and the tools for agricultural producers, energy users, and others to deal with the instability that we are currently seeing?

Mr. ANTONSEN. Yes, I am sorry.

We see the days when a producer wants to sell is not the same time that an end-user wants to buy. There are huge, huge gaps in volatility and derivatives get us across that line. The volatility we have seen with weather, our export markets come and go. Being in South Dakota, we export most of our production. We are relying on getting it at least out of the state, and most of that goes to the world market. We get to that point and that is our biggest challenge.

Mr. MILLER of Ohio. Yes. I think if we can continue—I am out of time, Mr. Chairman, but we can continue to hold people accountable for agreeing to, say, the USMCA but taking advantage of us with GMO corn, and actually bring them to a dispute panel probably would help out as well for a little bit.

Thank you for your time. I yield back.

Ms. CARAVEO. The gentleman yields back.

We will go next to the gentleman from Kansas, Mr. Mann, for 5 minutes.

Mr. MANN. Thank you, and thank you very much for having this hearing. Thanks for the panel for being here this morning.

This is a very important topic. We have to make sure that we get it right and it impacts not just folks all over the country but certainly my ag producers throughout Kansas as well that rely on markets to make sure that they are managing the risks that are just ever present and continue to increase in agriculture.

First question for you, Mr. Lukken. I want to circle back to enforcement for a moment, and drill in on CFTC's existing authorities. Do you see any current gaps in the Commission's authorities to address overseas fraud that affects markets here in the U.S.?

Mr. LUKKEN. Yes. I am not aware of any current impediments for the CFTC going after bad behavior overseas. They have, again, a nexus on American participants or citizens. I know when I was acting Chairman of the agency, there were times when we needed to use prosecutorial discretion on whether we went after activity overseas. But if there was a strong nexus to American consumers, of course we would take strong interest and the CFTC would go after that. We brought several cases in the international front on that case—on that basis. But, we oftentimes would work in partnership. It is one of those things—and we were talking about appropriate funds. The CFTC should not be the police force of the world for all activity. It really has to come back to whether there



is a U.S. interest in that, and I don't think they have a lack of authority in that area.

Mr. MANN. Great, thank you.

Next question for you, Mr. Sexton. In your testimony, you described a court opinion that called into question how *customer property* is defined by the Commodity Exchange Act, CEA, relative to the U.S. Bankruptcy Code. Could you please share with us some additional background on that issue and why it is potentially problematic for customers?

Mr. SEXTON. I certainly can, and this is in the context of FCM bankruptcies, which are rare, thank God. And the importance of the proposal with regard to reauthorization that we are making is that in the *Griffin Trading Co.* case, the one that I am referencing, there was a hole in customer segregated funds caused by a rogue trader many years ago. And obviously, the firm did not have sufficient funds to make customers whole at that point in time, and the issue was whether or not customers would step in front of the firm's general creditors in the bankruptcy in order to get whatever funds existed from the company to go into segregated funds in order to make customers whole. Very important with regard to customer protections in our view, and the court in that case, the district court essentially said that the CFTC has a rule that would say yes, customers can step in front of the general creditors. They called into question the CFTC's legal authority with regard to making that rule in the context of some provisions of the Bankruptcy Code.

So, what we are asking for is just that that cloud of uncertainty be removed and extremely important from a customer funds safeguard perspective we believe.

Mr. MANN. Okay, thank you.

Next question, back you to you, Mr. Lukken. In your testimony, you discuss the globalization of our derivatives markets. How important is it for global regulators to be able to coordinate and share information with one another as they surveil and regulate these markets?

Mr. LUKKEN. It is incredibly important. Information is really the currency for the regulatory authorities around the world, and so, the CFTC, by statutory grant from this Committee has the ability to get a lot of information from our [inaudible]. This ensures [inaudible] to see trends in the markets. And so, it is important that they are able to share that information globally, as long as it is for an enforcement. It is not just an information grab, but it is for an enforcement purpose, and that happens quite frequently.

Mr. MANN. In your mind, would detailing staff to and from foreign regulators, the EU or the UK, support the global sharing of knowledge and experience?

Mr. LUKKEN. Yes, that would be helpful. I think I sent details from the CFTC over to the UK when I was chair. We benefitted from that because during the crisis, we were able to utilize those folks to help with what was happening in European markets. So, that kind of information and personnel sharing is incredibly important.

Mr. MANN. Thank you. I yield back the 3 seconds of my time. Thanks.

Ms. CARAVEO. Thank you. The gentleman yields back.

And with that, I will hand the steering wheel back to our esteemed chair.

The CHAIRMAN [presiding.] Just in time for me to yield myself time. How very exciting.

I will go with Ms. Thornton for just a little bit. Ms. Thornton, you talked a fair amount about how creating this new regulatory regime and duplicative efforts with the SEC might be complicated, troublesome, problematic. What agency today has jurisdiction over fraud and manipulation in commodity spot markets?

Ms. THORNTON. That is the CFTC, of course.

The CHAIRMAN. Okay. So, that is the CFTC. What about who has jurisdiction over derivatives for non-securities, those markets?

Ms. THORNTON. CFTC.

The CHAIRMAN. The CFTC. When we look at Bitcoin, have there been any reports that have held that Bitcoin is a security?

Ms. THORNTON. No, there is just one—no.

The CHAIRMAN. Has the SEC ever asserted jurisdiction over Bitcoin?

Ms. THORNTON. It should have.

The CHAIRMAN. Has the SEC ever asserted jurisdiction over Bitcoin?

Ms. THORNTON. I don't believe so.

The CHAIRMAN. Do you know what volume of the digital assets trading Bitcoin constitutes?

Ms. THORNTON. Roughly 90 percent.

The CHAIRMAN. Okay.

Ms. THORNTON. But there are hundreds of other tokens.

The CHAIRMAN. There are, there are. Does the legislation—of those hundreds of other tokens that are not generally considered to be commodities, would FIT 21 continue to place the jurisdiction over those other tokens with the SEC?

Ms. THORNTON. I think the problem with FIT 21 is it is a way of resolving the jurisdiction between the CFTC and the SEC so that it makes no difference what the SEC thinks because by the time it weighs in, the tokens are already being traded on the spot market and the CFTC has to unwind something. And there are hundreds of other tokens—

The CHAIRMAN. Ma'am, I just—I don't think that is an accurate description, and in fact, alleging that the creation of this brand-new regime is problematic is just not consistent with the facts on the record. What we know now is by your own answers, the CFTC already has a robust role in this arena, and in fact, in the wake of Dodd-Frank when they were provided grand new authorities to deal with OTC swaps, there were no failures. There were no problems. I think the broad-based assessment by industry is that they did a magnificent job stepping up and filling that gap, because it built on their already existing expertise. That is—they are already doing so much of this. Again, 90 percent of the volume, I probably would have said 70 or 80, but we can take your assertion at face value.

And so, I just want to provide greater context around the robust role the CFTC is already playing in commodity spot markets, and in digital assets, the overwhelming majority of digital assets.

Sir, Travis, I would like to come to you. We are South Dakotans so we get to be buddies with one another.

You noted that CFTC reauthorization would really be a vote of confidence. Tell me more of what you mean by that.

Mr. ANTONSEN. Yes. I think knowing that whether it is farmers or agribusinesses knowing that we get to come to the table and talk about changes that need to be made, adjustments that should happen, that that is happening from the reauthorization process. I think from our standpoint I think we are happy with—we are okay with the regulatory environment around what is going on with—in the markets and in the regulations around that. So, I think just knowing, giving us the confidence that there is going to be integrity in the marketplace and it is going to be efficient.

The CHAIRMAN. Very good.

Mr. Sexton and Mr. Lukken, share you thoughts on this vote of confidence idea. Do the markets really care? Do market participants really care?

Mr. LUKKEN. There is some uncertainty out there. I mean, I just think the lack of confidence for the CFTC, as Chairman Behnam noted, going overseas to his colleagues knowing that there hasn't been a Congressional blessing of the agency in over 15 years. I mean, that is something I think that it would be easy to do for this Committee, straightforward to do for this Committee, and long overdue.

Mr. SEXTON. I would agree that reauthorization recognizes the critical role of the CFTC, both domestically as well as internationally, and it is very important for Congress to do.

The CHAIRMAN. We have a couple of other Members on their way who I know want to ask some questions, so I may exceed my time a little bit here, because I do—we want to fill out the record—oh, Mr. Nunn is here. Very good.

I have questions about the bankruptcy thing, the issues that you brought up, Mr. Sexton. Mr. Lukken, I think you mentioned it as well. But let's go to Mr. Nunn and we can always double back.

[The information referred to is located: for Mr. Lukken, p. 43; Mr. Sexton, p. 44.]

Mr. NUNN. Well, I want to thank the chair, and I believe strongly here that CFTC does have an important role here, particularly when it comes to those lanes in the road that our industry is asking for, particularly when it comes to digital assets. I think that CFTC has a better role to play than where the SEC has tried to insert itself. So, I will begin with that.

I also want to thank everybody here from the Commodity Futures Trading Commission to ensure that our markets are safe and strong. I know you are each committed to this.

Our derivatives markets remain the envy of the world, and that is something we should be very proud of. We should also work to maintain. I want to thank the stakeholders of this Committee who have helped our marketplace weather some pretty tough storms in recent years. Our markets are stronger, more resilient, but there is more to be done to make sure that we don't unintentionally hinder them.

With that, I want to move to farmers in my district in Iowa. One of the programs that I think has really worked well here has been

this Internal Whistleblower Program that CFTC oversees. The program is crucial for the accountability and protecting of agricultural and financial markets. It also benefits Iowans and all Americans.

Just last month, they uncovered a corruption at a company thanks to a whistleblower that resulted in a \$55 million fine, meaning the American taxpayers aren't paying for this. We are calling out bad actors and those bad actors then have to pay for their own policing. As I understand it, a large bulk of the policing comes from the Whistleblower Program. If we don't act before October 1, though, this Whistleblower Program could become defunct due to it not having enough funds to continue.

So, I introduced, along with Representative Don Davis from North Carolina, a colleague on the other side of the aisle, and my senior senator, Senator Chuck Grassley, H.R. 4935, the CFTC Whistleblower Fund Improvement Act, to permanently address this accounting flaw.

Very quickly, I want to ask each member of the panel, do you see yourselves committing to make sure the Whistleblower Program remains solvent? Could I get a yes, or if there is an equivocation, let me know that.

Mr. LUKKEN. Yes.

Mr. SEXTON. Yes.

Mr. ANTONSEN. Yes.

Ms. THORNTON. It is an important program, but obviously the details would need to be clear before we would have a strong opinion.

Mr. NUNN. Let me ask then, what things would you see needing to be done to make sure the program remains solvent, Ms. Thornton?

Ms. THORNTON. Well, I just think one should consider whether it is sustainable as a long-term way to fund enforcement and find enforcement. That is more along the lines of what I am thinking.

Mr. NUNN. If not for this program, how would we discover more of the bad actors inside? I mean, I think that is the fundamental part where both of us would agree, this is highly important. We don't want to incentivize folks to have to go out there and police themselves, but we do want to recognize there has got to be a clean pathway for folks to be able to raise their hand and say, the Federal Government or my agency is not working. I need somebody to come and investigate this.

Ms. THORNTON. Yes, that is certainly a fair question, but I also think that the CFTC needs more funding to carry out its existing duties, one of which is enforcement.

Mr. NUNN. Well, I think that bad actors have a responsibility in helping shoulder that far more than the taxpayer, but I hear what you are saying there.

Mr. Antonsen, I would like to now turn to capital market formation. I share your concerns about the potential impact here of rules proposed by some unelected bureaucrats in Washington making a lot more red tape for everyday working Americans and farmers.

With the average price of one tractor in my home State of Iowa at nearly \$1½ million, this is a major investment for anyone, whether you are a small farmer or whether you are a beginning farmer, and it directly hurts our ability to grow. Let me ask this. How can we ensure that the CFTC operates in a way that supports the mar-

kets while avoiding unnecessary burdensome red tape coming out of Washington?

Mr. ANTONSEN. That is a good question. I mean, we are coming today that we don't really have an ask, right, on CFTC reauthorization. We feel it is working correctly. I agree with you as a farmer in South Dakota, I know the economics of that as well. So, I think current *status quo* is okay for regulations on agribusinesses and those trading with farmers to make sure the system works well.

I feel it is—we are getting into tougher times. I think the next year or two is going to be even tougher than the past couple years at the farm-gate, so I would agree with you.

Mr. NUNN. As we highlighted with our Chairman, my home state a bushel of corn, \$3.89. A break-even point is \$4.85. Three years ago, we were over \$8 a bushel. America's farmers, farming communities, and the entire country is going to experience a spike in costs if regulation is one of the reasons that it causes an American farmer to have to spend more time filling out paperwork than actually being in the field. I know you know that.

Thank you very much, Mr. Chairman. I yield the remainder of my time.

The CHAIRMAN. Of course, we care about Iowa corn farmers and the prices your folks have, Mr. Nunn, but coming from a state where our yields are 30 percent less than yours, would you just stop? We are not going to feel bad for you.

Mr. NUNN. Mr. Chairman, you have an entire palace to corn. I appreciate everything you do.

The CHAIRMAN. Well, that is true.

Mr. NUNN. Thank you.

The CHAIRMAN. I think we are prepared to close the hearing. With that, I would offer the Ranking Member to make any closing comments she would have.

Ms. CARAVEO. Well, thank you again to the witnesses for your testimony. It is really important to hear from you all as we consider this very important reauthorization, and I would like to thank the Chairman again for his collaborative approach, not just to the way that this Subcommittee is run, but in the way that he approaches legislation, and I look forward to continuing to collaborate as we look at this very important reauthorization as the CFTC—as we look at the CFTC's need to regulate all commodities, including digital assets.

The CHAIRMAN. Yes, so many of our colleagues—not on this Committee, of course, this Committee is great. But so many of our other colleagues, they like fighting more than they like governing, and of course, people on this dais actually understand that it is our job to try and govern a country. And of course, our panelists have helped with that today. You have all to a person provided good, specific recommendations for how we can advance and we are going to take that under advisement. Obviously, it will be an ongoing conversation. It is not just like your 5 minutes under the clear lights are the only way that you can feed into this process.

So, with that, I would note that under the Rules of the Committee the record of today's hearing will remain open for 10 calendar days. That gives us an opportunity to receive additional ma-

terial and written responses from the witnesses, to the extent that any Member wants to follow up for the record.

The hearing of the Subcommittee on Commodity Markets, Digital Assets, and Rural Development is adjourned.

[Whereupon, at 9:45 a.m., the Subcommittee was adjourned.]

[Material submitted for inclusion in the record follows:]

SUPPLEMENTARY INFORMATION SUBMITTED BY HON. WALTER L. LUKKEN, J.D.,  
PRESIDENT AND CHIEF EXECUTIVE OFFICER, FUTURES INDUSTRY ASSOCIATION

**Insert 1**

The CHAIRMAN. We have a couple of other Members on their way who I know want to ask some questions, so I may exceed my time a little bit here, because I do—we want to fill out the record—oh, Mr. Nunn is here. Very good.

I have questions about the bankruptcy thing, the issues that you brought up . . .

In your testimony, you discussed the bankruptcy protections afforded to derivatives contract customers and futures commission merchants beyond that provided by the U.S. Bankruptcy Code. Can you please describe the bankruptcy protection framework provided by the Commodity Exchange Act and Commission regulations, and the importance of this framework from your perspective?

The sanctity of segregated customer funds in the event of an FCM bankruptcy is a critical tenet of the CFTC's customer protection regime.

There are various rules enacted by the CFTC that ensure that customer funds are—at all times—segregated and protected in the event of a default. These include a prohibition of an FCM from using the funds of one customer to meet the obligations of another customer. FCMs are also required daily to “top-up” customer margin amounts under a given CFTC “residual interest” formula to serve as a buffer against a shortfall in the customers’ accounts. Under CFTC rules, FCMs guarantee their customers’ trades by stepping into the shoes of a customer during a default and using the FCM’s funds to meet a failing customer’s obligations to a DCO.

If one or more customers of an FCM default on their obligations to the FCM and the loss is so great that, notwithstanding the application of the FCM’s available funds, there is a shortfall in the amount of customer funds, the FCM will likely default and be placed into bankruptcy.

In these circumstances, the Bankruptcy Code and Commission rules provide that, in the event of an FCM’s bankruptcy, losses within each fund—the U.S. Customer Segregated Account, the Foreign Exchange Customer Account, and the Cleared Swaps Customer Account—are walled off and treated separately from other customer account classes.

The Bankruptcy Code also provides that all FCM customers with funds in each account class with losses, including non-defaulting customers, shall share in any shortfall *pro rata*. However, customers whose funds are held in another account class that has not incurred a loss will not be required to share in such a shortfall.

This segregation of account classes allows failing FCMs to “port” these protected customer account classes to another healthy FCM—another important feature of clearing that prevents the fire sale of positions during stressed markets.

The collective attributes of clearing, in combination with these noted bankruptcy protections, have been shown to protect customers and the clearing system from disorderly defaults and contagion during market turmoil.

**Insert 2**

Mr. COSTA. Well, Mr. Chairman and the Ranking Member, my time has expired but I think this is something that we need to look at in greater depth. When Mr. Lukken made his comment about prudence and overcapitalization, I am very curious about how he measures prudence or is that in the eye of the beholder? And then how do you measure the risk?

Post financial crisis, the G20 nations came together on certain pillars of reform of the financial markets to improve the safety and integrity of the financial system. Congress enacted these reforms as part of the Dodd-Frank Act, which sought to bring more products onto regulated clearinghouses, increase capital for certain bank activities, and improve the transparency of over-the-counter trades through centralized trade repositories. Since Dodd-Frank’s enactment, we have seen tremendous growth in the number of OTC trades that clear in a safer and more predictable manner. This has been positive for the integrity of the markets and has led to other clearing mandates, such as the recent SEC requirement to clear certain U.S. treasury securities and repo transactions. The Basel capital reforms also aimed to increase the amount of bank capital post-financial crisis and align the capital levels with the riskiness of the activity.

Unfortunately, recent “End Game” Basel Capital proposals by Prudential Regulators failed to recognize the risk mitigation effects of clearing, suggesting reforms that disincentivized clearing. This could lead to higher costs for hedgers and less clearing capacity in the system. There has been broad consensus among derivatives

end-users and commodity producers that these capital reforms impacting hedgers' ability to clear need to be amended. Recent remarks by Federal Reserve Vice Chair Barr indicate that the Federal Reserve plans to revise the proposed Basel reforms on client clearing to better recognize the risk reducing effect of this activity. FIA strong supports these changes.

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SUPPLEMENTARY INFORMATION SUBMITTED BY THOMAS W. SEXTON III, J.D.,  
PRESIDENT AND CHIEF EXECUTIVE OFFICER, NATIONAL FUTURES ASSOCIATION

**Insert**

The CHAIRMAN. We have a couple of other Members on their way who I know want to ask some questions, so I may exceed my time a little bit here, because I do—we want to fill out the record—oh, Mr. Nunn is here. Very good.

I have questions about the bankruptcy thing, the issues that you brought up . . .

In your testimony, you discussed the bankruptcy protections afforded to derivatives contract customers and futures commission merchants beyond that provided by the U.S. Bankruptcy Code. Can you please describe the bankruptcy protection framework provided by the Commodity Exchange Act and Commission regulations, and the importance of this framework from your perspective?

Section 20 of the CEA gives the Commission the authority to promulgate regulations regarding the bankruptcy of certain CFTC registrants. The Commission has promulgated bankruptcy regulations pursuant to this authority under Part 190 of the CFTC's regulations. The CFTC's Part 190 regulations contain key provisions that govern FCM bankruptcies and are designed to provide critical customer protections.

Part 190 contains an overriding objective for a bankruptcy trustee to transfer customer assets including open futures contracts to a solvent FCM rather than liquidating the customers' assets—a key protection that helps ensure market stability and protects customers from losses related to a sudden liquidation event. However, in certain instances (*e.g.*, a shortfall in customer funds), a bankruptcy trustee may not be able to effectuate this transfer. Therefore, in the event there is a shortfall in customer funds in an FCM bankruptcy, Part 190 provides a critical customer protection that gives FCM customers priority over essentially all other claimants (*e.g.*, general creditors) until bankruptcy estate assets are available to make customers whole.

As noted in NFA's written testimony, NFA believes there is one aspect of the CEA that needs to be strengthened by Congress to better protect customers in the event of an FCM bankruptcy. While the Part 190 regulations provide that customers shall have priority over essentially all other claimants, a bankruptcy court in the past found that the Commission lacked statutory authority to give this protection by regulation to customers. *See In re Griffin Trading Company*, 245 B.R. 291 (Bankr. N.D. Ill. 2000). Although this decision was subsequently vacated on other grounds, 270 B.R. 882 (N.D. Ill. 2001), a cloud of doubt continues to linger over the validity of the CFTC's rule. NFA, the CFTC and industry participants have consistently urged Congress to include a fix to this *Griffin* issue in any CFTC reauthorization legislation. We believe an effective solution is to amend Section 20 of the CEA, which gives the CFTC authority to adopt regulations regarding commodity brokers that are debtors under Chapter 7 of Title 11 of the United States Code, to clarify that the CFTC has the authority to adopt the regulation providing customers with priority over essentially all other claimants (*e.g.*, general creditors) until bankruptcy estate assets are available to make customers whole. A proposed amendment to Section 20 of the CEA has been included in previous reauthorization bills voted out of both the Senate and House Agriculture Committees, and NFA believes there is a broad base of industry support for this approach.



## SUBMITTED QUESTIONS

**Response Submitted by Hon. Walter L. Lukken, J.D., President and Chief Executive Officer, Futures Industry Association**

*Questions Submitted by Hon. Dusty Johnson, a Representative in Congress from South Dakota*

*Question 1.* Could you please comment on the adequacy of the examinations carried out by both the CFTC's and NFA, whether they have suffered from a lack of funding, and whether those examinations should or could uncover all market abuse?

*Answer.* The CFTC and NFA are important 'cops on the beat' in their oversight of our growing risk management markets. These complementary regulators partner with other self-regulatory organizations, such as exchanges and central counterparties, to provide broad oversight coverage of the markets and their participants. While it is difficult to comment on the adequacy of the examinations carried out by both the CFTC and NFA, I have found this self-regulatory model to be an incredibly cost-effective way to police these markets for fraud, manipulation, and abuse. I am not aware of instances where funding has caused a lapse in examinations or adequate oversight using this structure.

*Question 2.* As both a member of the Commission and as the head of a major trade association, you've had a front row seat to the Commission's activities for over twenty years. Are you familiar with any instance where the Commission failed to fulfill its mission and statutory obligations because of a lack of funding?

*Answer.* I fully support ensuring the CFTC is fully funded to accomplish its mission and oversee our growing markets. From my time as a Commissioner and Acting Chair of the Commission, and now as the President and CEO of FIA, I am not aware of an instance where the Commission failed to fulfill its mission and statutory obligations because of a lack of funding.

*Question 3.* Could you please explain for us the process under the Commodity Exchange Act (CEA) and Commission regulations for exchanges seeking to list new contracts or make changes to their rulebooks?

*Answer.* With the passage of the Commodity Futures Modernization Act of 2000, Designated Contract Markets (DCMs) were allowed to list for trading new contracts or make changes to their rules by self-certifying with the Commission that the new contracts or rules comply with the core principles of the Commodity Exchange Act (CEA) and the Commission's regulations. The Congressional enactment of self-certification was meant to address concerns that U.S. exchanges were at a competitive disadvantage to foreign exchanges caused by lengthy delays in contract or rule approvals. To ensure compliance with the CFTC's core principles, Congress required DCMs to file a written self-certification with the CFTC that shows the rule or contract filings comply with the core principles except for such files that are seen as complex or novel. This process has proven to be a cost-effective way for U.S.-registered exchanges to innovate and stay competitive with foreign competitors while also ensuring compliance with the core principles of the Act.

*Question 3a.* Are you familiar with any instance where the CFTC failed to meet its requirements under the CEA and regulations with respect to the listing of new contracts or rule changes because it didn't have the funding to do so?

*Answer.* I am not aware of any instance where the CFTC failed to meet its requirements under the CEA and regulations with respect to the listing of new contracts or rule changes because it didn't have the funding to do so. In fact, I would contend the self-certification process has freed up valuable staff time of the CFTC to focus on more substantive abuses in the markets, instead of the administrative tasks associated with product or rule approvals.

*Question 3b.* Do you or your members find that the CEA's processes for listing contracts and making rule changes "unnecessarily burden market participants with costs and complexities that are inconsistent with the law and core principles?"

*Answer.* Generally, the self-certification process for exchanges to list new products or amend their rules has served the markets and industry well, allowing for greater innovation and enhanced competition.

Regarding rule changes, specifically, I would like to flag a discrepancy in the current process for Systemically Important Derivatives Clearing Organizations (SI-DCOs) and Derivatives Clearing Organizations that are not deemed to be systemic. Under CFTC Rule 40.6, non-systemic DCOs that submit rules or rule amendments that raise novel or complex issues for approval require an opportunity for public comment. However, SI-DCOs are not required to seek public comment for novel and complex rule changes that affect their members.

FIA believes the Commission's approval process for SI-DCO rules under CFTC Rule 40.10 should require an opportunity for public comment when a SI-DCO rule raises novel or complex issues similar to non-systemic DCOs. This is particularly important for rule changes impacting the risk profile and responsibilities of a DCO's clearing members who are charged to collect margin from customers and contribute to a mutualized default fund aimed at protecting the clearing system from contagion risk. We believe a time-limited comment period would result in a more informed and deliberative rulemaking process that ultimately benefits both DCOs and market participants and we encourage the CFTC to reconcile these rules accordingly.

*Question 4.* Could you please describe for us the marketing and other restrictions placed upon market participants in their solicitation and servicing of customers under the CEA, CFTC regulations, and NFA regulations?

*Answer.* The NFA and CFTC have robust rules in place related to marketing and other restrictions placed upon market participants in their solicitation and servicing of customers. This includes NFA regulatory obligations around sales practices and promotional materials, NFA disclosure requirements for Members engaging in activities related to virtual currencies or virtual currency derivatives, and CFTC rules for introducing brokers to maintain tape records of all oral communication with clients.

*Question 5.* Could you please explain the requirements that the CEA imposes on the CFTC with respect to how it manages the confidential information from market participants that it holds?

*Answer.* Section 8(a) of the CEA prohibits the Commission from disclosing information that would separately disclose the business transactions or market positions of any person or trade secrets or names of customers. This section is incredibly important because of the sensitive market information the CFTC receives from large traders in our markets, which, if not protected and publicly disclosed, could distort prices and harm the public. For this reason, the CFTC must be diligent in its enforcement of Section 8 protections and periodically review the information it collects to ensure the information continues to meet a public need.

*Question 6.* Could you provide your thoughts on if elevating the position of Chief Information Security Officer at the CFTC would ensure that information security issues are front of mind for the Chairman and Commissioners?

*Answer.* For the reasons stated in the previous answer, I would support elevating the position of Chief Information Security Officer at the CFTC so that the position reports directly to the Chairman.

*Questions Submitted by Hon. David Rouzer, a Representative in Congress from North Carolina*

*Question 1.* Mr. Lukken, you mention we have seen an increase in new technologies under the CFTC's purview, such as digital assets and artificial intelligence. To me, the best approach when it comes to these novel technologies is for the CFTC to set clear, enforceable rules of the road while also knowing when to get out of the way and allow firms the flexibility to innovate. I fear failing to provide clarity will only lead to uncertainty and firms looking elsewhere to create—a loss for American industry and consumers.

In a previous hearing, I asked Chairman Behnam about the possibility of the CFTC creating an AI sandbox to allow firms to test products. He mentioned that there could be legal limitations on creating such a sandbox.

As we look towards reauthorization, how could Congress help give the CFTC the tools it needs to allow firms to responsibly experiment with emerging technologies?

*Answer.* According to former Chairman of the CFTC Christopher Giancarlo, "The CFTC lacks the legal authority to partner and collaborate with outside entities engaging directly with fintech within a research and testing environment, including when the CFTC receives something of value absent a formal procurement."<sup>1\*</sup>

FIA supports efforts to improve the research and development capabilities of the CFTC. This includes legislative efforts, such as those led by Representative Austin Scott, that would provide the CFTC transaction authority to engage in public-private partnerships with financial technology developers.

Jurisdictions outside of the U.S., like the Monetary Authority of Singapore, have established FinTech Regulatory Sandboxes. Singapore has established a framework

<sup>1</sup> <https://www.cftc.gov/PressRoom/SpeechesTestimony/opagiancarlo70>.

\* **Editor's note:** the link refers to Mr. Giancarlo's prepared statement submitted for the May 1, 2019, hearing before the Subcommittee on Commodity Exchanges, Energy, and Credit of the House Committee on Agriculture entitled, *The State of the Commodity Futures Trading Commission*, pp. 8–15. The hearing, in its entirety, is retained in Committee file.

that enables financial institutions and FinTech players to experiment with innovative financial products or services in a live environment but within a well-defined space and duration.

*Question 2.* Agriculture is an industry that can carry a lot of risk and heavy upfront costs, especially for a new or young farmer starting from scratch. I wonder if more can be done to educate our next generation of farmers about the derivative products that may be available to them to manage their risk and avoid catastrophic losses, one of the major barriers for many looking at entering the industry. This is especially important today as slumping crop and livestock prices, record high input and labor prices, and increasingly volatile markets have pushed many out of production.

You mention FIA's support of efforts to expand educational resources for producers. How could Congress encourage additional partnership between the CFTC, organizations and governmental entities such as Farm Credit or the Farm Service Agency to help better inform our farmers about these available tools?

*Answer.* FIA strongly supports additional education for farmers and ranchers on the use of the derivatives markets for hedging market risk in production agriculture. This can be improved by expanding the CFTC's ability to partner with not-for-profits, private sector educational initiatives or other government entities, like the USDA, to provide educational resources about the opportunities and risks of these hedging tools like futures and other cleared derivatives. FIA believes the CFTC Office of Customer Education and Outreach (OCEO) would be a good place for Congress to target. We understand this office is, by statute, able to pay for "customer education initiatives designed to help customers protect themselves from fraud or other violations." We have heard concerns that this narrow language limits the OCEO's ability to provide education to help customers beyond protecting them from "fraud or other violations." Congress could consider expanding the mandate of the OCEO beyond fraud or other violations to areas designed to educate farmers on the use of these risk management tools.

**Response Submitted by Thomas W. Sexton III, J.D., President and Chief Executive Officer, National Futures Association**

*Questions Submitted by Hon. Dusty Johnson, a Representative in Congress from South Dakota*

*Question 1.* Could you please comment on the adequacy of the examinations carried out by both the CFTC and NFA, whether they have suffered from a lack of funding, and whether those examinations should or could uncover all market abuse?

*Answer.* NFA's examinations, in conjunction with our day-to-day oversight activities, are designed to identify instances of NFA Member non-compliance with NFA's rules and CFTC regulations, which include instances of Members engaging in market abuse.<sup>1</sup> In instances in which our examinations uncover fraud, NFA and the CFTC work together to promptly address any ongoing fraudulent activity and limit customer harm. While no oversight program can guarantee that all instances of market abuse and fraud will be uncovered, NFA's rigorous risk-based Member monitoring program is designed to detect fraud and market abuse as early as possible, take immediate action to stop fraudulent activity, and ensure that bad actors are appropriately disciplined.

NFA's ability to conduct examinations has never been impacted by a lack of funding. The CFTC relies primarily upon NFA to conduct examinations of NFA Member firms. See NFA's response to *Question 4* regarding the CFTC's oversight of NFA.

NFA is not in a position to answer this question's funding part, which we opine should be directed to the CFTC.

*Question 2.* You've been with the NFA for over 33 years and have served as President and CEO for 7 years. NFA clearly has a very close relationship with the CFTC and are keenly aware of its operations. Are you familiar with any instance over the past 33 years where the Commission failed its mission and statutory obligations because of a lack of funding?

*Answer.* NFA is not in a position to answer this question, which we opine should be directed to the CFTC.

*Question 3.* Can you elaborate on how NFA uses mandatory membership requirements to police the derivatives markets and impose essential customer protections?

<sup>1</sup>NFA is not responsible, nor do we have access to the information necessary, for overseeing trading activity on the derivatives exchanges. Instead, derivatives exchanges have their own self-regulatory responsibilities and surveil their markets. If our examination work uncovers any indicia of market abuse occurring on an exchange, we would refer that information to the relevant exchange and the CFTC for follow-up.

*Answer.* Part 170 of the CFTC's Regulations requires that, with few exceptions, each registered futures commission merchant (FCM), swap dealer (SD), introducing broker (IB), commodity pool operator (CPO) and commodity trading adviser (CTA) become and remain a member of a registered futures association (RFA). Section 2(c)(2)(B) of the CEA imposes a similar requirement for retail foreign exchange dealers (RFEDs). As a result, these industry participants are prohibited from conducting derivatives business unless they are NFA Members.

A mandatory membership requirement is essential for NFA to oversee derivatives market participants. NFA's basic mission is to impose ethical and business conduct standards on its Member firms, and take disciplinary actions against those Members that fail to abide by those standards. In the absence of a mandatory membership requirement, firms most in need of NFA's oversight would evade it by choosing not to become NFA Members.

*Question 4.* How does the CFTC work to ensure that NFA is effectively carrying out its regulatory responsibilities?

*Answer.* Given the important role that NFA plays in the U.S. financial regulatory structure, it is essential that NFA's activities are closely reviewed and monitored by the CFTC to ensure NFA is fulfilling its regulatory responsibilities. The Commission's oversight of NFA includes both formal actions, required by the statute or regulations, and informal actions, which have evolved over time.

Formally, NFA's most significant actions are subject to the CFTC's direct review and approval. For example, NFA is required to submit all new and amended NFA rules to the Commission prior to implementation, and the Commission may prevent NFA from making a rule effective. Additionally, the Commission has the authority, in part, on its own motion to review NFA disciplinary and registration/membership decisions.

The CFTC also performs rule enforcement reviews (RERs) to ensure that NFA is effectively carrying out its regulatory responsibilities. In the last 2 years, the CFTC has performed several RERs covering NFA's registration processes; FCM, CPO, CTA and IB programs including examinations, processing of financial statements, FCM notice filings and SD disciplinary actions; and the SD oversight program including exams, staffing and disciplinary actions.

Informally, NFA is in daily contact with the CFTC to discuss ongoing investigations, registration applications, examinations, rulemaking issues or any myriad of issues that can arise. Further, we generally meet quarterly with the CFTC's Chair and Commissioners to discuss NFA's activities and industry regulatory issues. We also have regularly scheduled coordination meetings with the Division of Enforcement (DOE), Market Participants Division (MPD), Division of Market Oversight (DMO), Office of International Affairs (OIA), Office of Public Affairs (OPA), Office of Legislative and Intergovernmental Affairs (OLIA), and the Office of Technology Innovation (OTI).

*Question 5.* Could you please explain for us the process under the CEA and Commission regulations for NFA rule changes? Are you familiar with any instance where the CFTC failed to fulfill its duties under the CEA and regulations with respect to NFA rule changes because it didn't have the funding to do so?

*Answer.* When NFA staff or our Member firms identify an issue or a problem that may require additional rulemaking, we work with NFA Member Advisory Committees, industry trade associations and the CFTC to draft proposed rules and then present those rule proposals to NFA's Board of Directors.

Section 17(j) of the CEA sets forth the requirements for NFA to adopt a new rule or amend an existing rule (Rule Proposal). NFA is required to submit all Rule Proposals to the Commission. In most instances, NFA will submit the Rule Proposal and notify the Commission that we intend to make it effective as early as 10 days after submission unless the Commission notifies us that it has determined to review the Rule Proposal for approval. NFA may also submit a Rule Proposal and specifically ask for Commission review and approval of the Rule Proposal. The Commission is required to approve the Rule Proposal if the Commission determines that it is consistent with Section 17 and not otherwise in violation of the CEA or regulations. The Commission must approve a Rule Proposal or institute disapproval proceedings within 180 days after receiving the Rule Proposal or such longer period that the Commission and NFA agree upon.

NFA is not in a position to answer this question's funding part, which we opine should be directed to the CFTC.

*Question 6.* Could you please describe for us the marketing and other restrictions placed upon market participants in their solicitation and servicing of customers under the CEA, CFTC regulations, and NFA regulations?

*Answer.* NFA and the CFTC work collaboratively to oversee market participants' customer-facing activities. NFA initially adopted requirements in 1985 regarding its Members' solicitation activities and promotional material usage. Further, NFA's rules require FCM and IB Members to provide customers with Commission Regulation 1.55's risk disclosure statement.

NFA's solicitation and promotional material rules govern our Members' conduct with both retail and institutional (*i.e.*, eligible contract participant) customers and counterparties. NFA Compliance Rule 2-29 and its numerous related interpretive notices addressing specific issues are the cornerstone of NFA's solicitation and promotional material requirements. This rule prohibits Members from engaging in any communications related to commodity interests that are fraudulent, deceitful, employ or are part of a high-pressure approach or make any statement that commodity interest trading is appropriate for all persons. Further, the rule establishes specific requirements that are designed to ensure that promotional material is not deceptive, appropriately addresses trading risks and provides all material information. The rule also sets forth specific requirements regarding the use of hypothetical trading results, statements of opinion, and audio and video promotional material that makes specific recommendations.

Over the last 40 years, NFA has adopted numerous interpretive notices related to NFA Compliance Rule 2-29, which address solicitation and promotional material abuses, many of which involved retail customers. These notices prohibit a Member from touting a strong likelihood of profits to customers when its actual trading experience does not support those claims and from using high-pressure sales tactics. Further, they place restrictions upon Members' use of radio and television advertisements and website and electronic communications. Additionally, we require FCMs and other intermediaries to disclose the full costs of trading to customers.

*Question 7.* Can you please describe the retail-focused markets that the CFTC and NFA oversee? Please describe the customer protection requirements that the CFTC and NFA impose on intermediaries in these markets.

*Answer.* Both the exchange-traded derivatives and retail foreign exchange (forex) markets include retail participants. Investor protection is a critical component of NFA's mission. Today, industry-wide interest in discussing retail participation and related topics remains high. To facilitate discussion across the industry, NFA co-hosted FIA's second annual Retail Roundtable event in February 2024, which was attended by representatives from NFA Member firms with significant retail customer bases, exchanges, law firms and clearing firms. Topics addressed at the event included proposed significant market structure changes like direct clearing DCOs, gamification, new products, the need for further customer education and more.

A slight rise in retail interest and participation may be occurring, but protecting investors has been part of the CFTC's and NFA's mandate since inception. NFA and the CFTC have numerous customer protection requirements, which we impose on intermediaries engaging in exchange-traded derivatives. These requirements focus on the following: anti-fraud and anti-manipulation protections; associated person registration requirements; business conduct standards (*e.g.*, solicitation and advertising); conflicts of interest prohibitions and management; customer asset protections (*e.g.*, segregated funds; qualified third-party custodians hold customer assets/property and acknowledge they are holding customer assets/property; limitations on how customer funds may be invested; and bankruptcy protections); know-your-customer and appropriate risk disclosure; maintenance of books and records; minimum FCM and IB capital requirements; risk management procedures; supervision requirements; trade practice surveillance (*e.g.*, detect abusive and manipulative trading practices); and full fee disclosures.

NFA and the CFTC also apply, as permitted by law, many of these customer protection requirements to RFEDs that act as a counterparty to retail participants. Moreover, NFA has requirements in place to monitor RFED trading platforms, which are designed to ensure that RFEDs execute customer orders fairly and at prices that reasonably accord with prevailing forex market prices.

*Question 8.* How does NFA help the Commission meet its regulatory obligations? How important is NFA's cooperative role providing oversight in new markets? What efficiencies and cost savings does NFA's regulatory efforts provide to the CFTC?

*Answer.* NFA partners with the CFTC to regulate our Members' derivatives activities. Our FY 2025 operating budget is approximately \$145M, and we have approximately 525 employees. NFA began operations in 1982 when Congress and the CFTC gave us the responsibility to regulate firms engaging in activities with customers in the exchange-traded derivatives markets. As Congress expanded the CFTC's jurisdiction over the years to include the retail rolling forex spot and swaps markets, Congress and the CFTC also entrusted NFA with additional regulatory oversight re-

sponsibilities for these markets. If future legislation establishes a CFTC regulatory framework for spot digital asset commodities (DAC) and a role for a registered futures association, then NFA looks forward to assisting the CFTC in regulating the DAC market and is fully capable of performing the responsibilities required of an RFA.

NFA works very closely with the CFTC to develop rules and regulatory programs to effectively oversee our Members. NFA currently has seven primary functions—registration, rulemaking, monitoring Members, enforcement, market regulation, investor protection and education and dispute resolution. Our successful regulatory partnership with the CFTC is an effective structure for regulating the derivatives markets and the rolling spot retail forex and spot DAC markets. In the absence of this critical partnership, the CFTC would need to undertake NFA's current functions.

*Question 9.* Could you provide your thoughts on if elevating the position of Chief Information Security Officer at the CFTC would ensure that information security issues are front of mind for the Chairman and Commissioners?

*Answer.* NFA's Information Security staff meets regularly with the CFTC's Information Security group, and based on our interactions, NFA believes that the CFTC recognizes the significant security risks posed to the agency and has measures in place designed to mitigate these risks. Moreover, NFA believes that the CFTC Chair and Commissioners currently recognize the magnitude of security threats. We are not able to opine about the CFTC's Chief Information Security Officer's reporting lines but believe this individual should work closely with the CFTC's Chief Information Officer to mitigate any security threats.

