United States Senate

COMMITTEE ON
HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS

WASHINGTON, DC 20510-6250

February 4, 2011

VIA ONLINE SUBMISSION (http://comments.cftc.gov)

Mr. David A. Stawick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, D.C. 20581

RE: RIN Number 3038-AD04, Proposed Rule Implementing the Whistleblower Provisions of Section 23 of the Commodity Exchange Act

Dear Mr. Stawick:

The purpose of this letter is to express support for rules proposed by the Commodity Futures Trading Commission (CFTC) to implement the new whistleblower provisions in Section 23 of the Commodity Exchange Act. Whistleblowers make important contributions to government enforcement programs by providing critical information and leads. With this intent, Section 748 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) amended the Commodity Exchange Act to allow the CFTC to establish stronger whistleblower incentives and protections for individuals who provide the agency with original and relevant information concerning potential violations of federal commodities and futures laws. CFTC's proposed rules effectively outline the procedures and scope of a stronger whistleblower program. This letter respectfully recommends, however, that the CFTC consider (1) providing an incentive to whistleblowers to report claims first through internal compliance programs by offering potentially higher awards to individuals who do so and (2) placing reasonable monetary limits on awards that will protect against inappropriate monetary incentives, while still encouraging potential whistleblowers to come forward.

Whistleblower Contributions. As key federal regulators have noted, whistleblowers may provide important information to government investigators that may not otherwise be uncovered. Further, whistleblowers who are corporate insiders may be able to act as guides within an organization to uncover schemes that were intentionally designed to remain undetected. They may also help uncover major frauds that would otherwise be hidden for years and cause substantial harm to public investors or the U.S. treasury.

The U.S. Senate Permanent Subcommittee on Investigations, which I chair, conducts complex investigations into, among other matters, allegations of corporate misconduct, securities fraud, and misleading accounting. The success of several of the Subcommittee's most important investigations was a result, in part, from leads or information provided by cooperative insiders. Without information from insiders, our investigations would have been more difficult and time consuming. Insider information has enabled our investigative teams to proceed more quickly, make more efficient use of our resources, and has also resulted in a better understanding of the issues and greater accuracy in our findings.

For over five years the Subcommittee has been examining regulated and unregulated commodity markets that trade in U.S. commodities. Specifically, we have examined the role of excessive speculation in causing unwarranted changes in commodity prices that can raise prices at the expense of American consumers and businesses. In 2006, for example, the Subcommittee released a report which found that billions of dollars in speculative trading on the crude oil market had pushed up futures prices in 2006, caused a corresponding increase in cash prices, and was responsible for an estimated $20 out of the then $70 cost for a barrel of oil.[1] A 2007 report showed how a single hedge fund named Amaranth made huge trades on the natural gas market, pushed up futures prices, and increased natural gas prices for consumers and American business.[2] In 2009, we held a hearing using the wheat market as a case history to examine how commodity index trading, in the aggregate, can cause excessive speculation and price distortions.[3] In these types of complex investigations, insiders can play a helpful role.

Corporate Compliance Programs. Some organizations have expressed concerns that the CFTC's proposed whistleblower program may undermine internal compliance programs established after the 2002 Sarbanes-Oxley requirement to encourage employees to report problems internally.[4] The concern is that whistleblowers will go directly to the CFTC with their claims, bypassing corporate internal compliance programs and eliminating any opportunity for companies to self correct identified problems. Although, the CFTC has proposed rules that would allow whistleblowers to report problems to their own companies before the CFTC, its rules do not encourage whistleblowers to do so.

Similar to the Securities and Exchange Commission's (SEC) proposed whistleblower rules, the CFTC's Proposed Rule 165.2 (l) allows whistleblowers to contact their own companies before approaching the CFTC by preserving the whistleblower's "place in line" for a possible reward from the CFTC if they report a violation or potential violation internally to the relevant company first, as long as the whistleblower reports the same information to the CFTC within 90 days of the internal report.

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[1] 2006 Report, "The Role of Market Speculation in Rising Oil and Gas Prices: A Need to Put the Cop Back on the Beat," S. Prt. 109-65 (June 27, 2006).

[2] 2007 Report, "Excessive Speculation in the Natural Gas Market," reprinted in S. Hrg. 110-235 (June 25 and July 9. 2007).

[3] 2009 Report, "Excessive Speculation in the Wheat Market," (June 24, 2009).

[4] See, e.g., comment letter from the Securities Industry and Financial Markets Association (SIFMA) and the Futures Industry Association (FIA), February 3, 2011 and comment letter from the Equal Employment Advisory Council, February 2, 2011.

Also like the SEC's proposed rules, Proposed Rule 165.2, which defines key terms in the proposed rule, protects corporate compliance programs by excluding information from certain employees and others from its definition of "independent knowledge" and, therefore, from receiving an award. These exclusions include: (1) from sources generally available to the public, such as corporate filings and the media; (2) lawyers who obtain the information through privileged communications; (3) individuals who have a legal or contractual duty to report information; and (4) employees who learn about violations through a company's internal compliance program or have the responsibility to take action when the information is reported to them.

However, unlike the SEC's proposed rule, the CFTC's Proposed Rule 165.9, which establishes criteria for determining award amounts, does not take into account, nor offer potential higher awards to, whistleblowers who report potential violations to their internal compliance programs before contacting the CFTC. Such a monetary incentive is intended to encourage employees to first go to their companies' internal compliance programs. Company compliance programs are crucial in preventing violations that could negatively impact investors and markets and operate more effectively if employees provide timely information regarding potential violations. With the award incentive provided under the SEC's proposed rules, but not those of the CFTC, employees are more likely to report the activity to the company first. This will give the company an earlier opportunity to address potential problems and prevent further investor harm.

Reasonable Awards. Section 748 of Dodd-Frank authorizes the CFTC to create a whistleblower program that will pay monetary rewards of between 10 and 30 percent of the penalties collected in successful CFTC enforcement actions to individuals who provide the CFTC with original information that leads to those enforcement actions. To be considered for an award, a whistleblower must voluntarily provide the CFTC with original information that leads to the successful enforcement of an action brought by the CFTC that results in monetary sanctions exceeding $1,000,000 and of certain related actions. Section 23(c)(1)(A) provides the CFTC with the "discretion" to determine the amount of the award from funds collected from wrongdoers in response to monetary sanctions imposed on them by the CFTC.

Because the CFTC may impose large monetary sanctions potentially involving hundreds of millions of dollars, careful thought should be given to how the CFTC should exercise the discretion provided by the law. Persons who envision receiving tens or hundreds of millions of dollars in exchange for information may, even unconsciously, exaggerate a situation and, as a result, unfairly damage the reputation and activities of particular corporations or individuals. Although these persons may ultimately be denied an award, excessive monetary incentives may lead to misreporting that could lead to the waste of investigative resources and unnecessarily harm reputations. Even in the case of a whistleblower who accurately exposes misconduct, an excessive award may deprive victims of the wrongdoing with adequate recovery or deprive the CFTC of funds needed to reimburse investigative expenses. In addressing this problem, the proposed rule should consider using the discretion provided in Section 23(c)(1)(A) to place reasonable limits on the amount of funds that can be awarded to any single whistleblower in any one matter.

The proposed rule to establish greater whistleblower incentives and safeguards, as called for in the Dodd-Frank Act, is well designed to encourage whistleblowers to come forward, strengthen the CFTC's enforcement program, and provide greater investor protections. Thank you for the opportunity to comment on the proposal.

Sincerely,

Carl Levin
Chairman
Permanent Subcommittee on Investigations