

February 1, 2017

United States House of Representatives  
Cannon and Rayburn Office Buildings  
Washington, DC 20515  
Attention: Congresswoman Ann Wagner and Congressman Michael Conaway

RE: H.R. 78 and H.R. 238 to yield overdue accountability from CFTC and SEC.

Dear Congresswoman Ann Wagner and Congressman Michael Conaway,

SEC Commissioner Mary Jo White and CFTC Commissioner Timothy Massad had resigned their positions just before Donald Trump was sworn in, and the swamp was officially drained. They left without responding to gross inefficiencies of their respective departments during their oversight. Hopefully H.R. 78 and H.R. 238 to provokes accountability by the new leadership.

Why does regulation often fail to work? To regulate is to control. Regulators, however, use their authority to disperse control to the regulated, and in doing so create an inherent conflict of interest. They receive compensation to simply prescribe rules, let the regulated mess up, and get involved too late after the damage is done.

Consider MF Global which fail to keep customer assets segregated as the regulatory reporting group reported directly to the CEO. If the calculation of customer funds to be segregated and the computation of net capital were done remotely by a SRO like FINRA, there would be no conflict of interest. If regulatory accountants can perform these functions from logging in at home, then they should perform these functions on the premises of FINRA thus removing the conflict of interest.

In the current state of regulation, the participant is working on behalf of the regulator. In an ideal state of regulation, the regulator justifies its own value by working for the taxpayers and participants. It is simply more efficient for the data to be transferred to the regulator, than to send CFTC and SEC to the premises of each participant.

In January of 2014 I sent an email to Mary Jo White "Simultaneously Eliminating Budget and Regulatory Gaps" requesting a "pilot program including just one self-clearing entity willing to disseminate their data should be established as a foundation for the industry. Regulatory staff at the SEC and the SROs would be involved with systems requirements". The SEC department of examinations wrote back to me thanking me for my "recommendations" and the SEC would review. On February 1, 2016 I followed up by email for a for a specific and substantive reason why the recommendations were not implemented, and have never received any reason why not to implement new technology.

This begs the question: *Why is the SEC constantly requesting more funding before capitalizing on every efficiency?* I am still looking for the SEC's participation to work with the college students at the Steven Institute in Hoboken on the automation of data for a specific broker-dealer in Jersey City. This would include automation of SEC rule 15c3-3 which would insure protection of customer cash. I hope

the SEC Regulatory Accountability Act H.R. 78 yields change which shifts control back to the regulators thus alleviating participants of such risk inherent responsibilities.

The CFTC recently passed Regulation AT with the intent of as “codifying existing industry best practices and necessary to ensure market integrity in light of potential market disruptions such as the May 2010 flash crash.” Regulation AT will now be likely repealed and like health care should be replaced with something better at **no cost** to the United States taxpayer.

I offered the CFTC an alternative which would save the expense of CFTC and DOJ source code review. I hold the patent for a system which would calculate the effect of trading positions on net capital in real-time per SEC Rule 15c3-1. The net capital rule is used as a standard for CFTC CFR 1.17 “Minimum financial requirements for many futures commission merchants and introducing brokers.” If the effect of algorithmic trading on net-capital could be calculated in real-time, *then a transmission could be sent to the exchange to halt trading for the participant’s clearing members MPID in real-time.*

There are several letters on the CFTC website for Public Comment on Regulation AT. The CFTC never came back with a specific or substantive reason why my alternative should not be utilized. This begs the question: *Why is the CFTC constantly requesting more funding before capitalizing on every efficiency?*

It is simply more efficient for the regulators to review the code of one single system which perform such the net capital calculation on behalf participants, than for the CFTC to examine net capital for each participant and for the CFTC to maintain a source code repository for each algorithm on the street.

The reason the regulators always request more cash is they simply do not capitalize on technology to keep pace with the modernized trading. The regulators can be provided unlimited human resources and never keep pace with the speed of algorithmic trading. The Federal Hiring Freeze should thus remain in place until every efficiency through automation is implemented.

Regulation justifies its cost when the regulator notifies the participant of a threat to the participant’s capital. It is not the role of the referee (regulator) to have access to the player’s (participants) source code playbook. The referee’s role is to simply blow the whistle when the player steps out of bounds.

I look forward to blow the whistle loudly enough with immediacy so the exchanges hear it when an algorithmic trading error threatens our markets.

As the holder of patent # 6,144,947 which enables the calculation of trading of net capital in real-time, the regulators can have greater visibility and control over the effect of algorithmic trading in Real-time **FREE OF CHARGE**. The cost of the system would be allocated to the algorithmic trading firms so there would be no cost to the Federal Government. The anticipated costs saved on SEC 15c3-1 examinations by the CFTC and SEC could be excluded from their 2017 budgets thus reducing the deficit.

My confidence to finally hear a response lies with you. Then I will no longer be “the forgotten man”.

Sincerely,

Peter Schwartz  
[www.systemicriskregulation.com](http://www.systemicriskregulation.com)