

COMMODITY FUTURES TRADING COMMISSION

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Executive Director

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Chief Financial Officer

November 2005

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A Message from the Chairman

Thirty years have passed since Congress established the Commodity Futures Trading Commission (CFTC or Commission). The CFTC is an independent agency with the mandate to regulate commodity futures and option markets in the United States. During that time, the Agency's mandate has been renewed and expanded several times, most recently by the Commodity Futures Modernization Act of 2000 (CFMA).

Today, because of the far reaching changes envisioned by the CFMA, trading in futures contracts has expanded rapidly beyond traditional physical and agricultural commodities into a vast array of financial instruments, including foreign currencies, U.S. and foreign government securities, and U.S. and foreign stock indices. As regulators, we play an important role in ensuring the vitality and innovativeness of the futures markets. With effective CFTC oversight, the futures markets serve the important functions of price discovery and offsetting price risk. As this report chronicles, the Commission works very hard to assure the integrity of the futures markets by encouraging their competitiveness and efficiency, protecting market participants against manipulation, abusive trading practices, and fraud, and ensuring the financial integrity of the clearing process.

We also work to ensure that resources we are entrusted with are used wisely and that we focus on results. That is why we are pleased to present our second *Performance and Accountability Report*. It has been prepared following the

guidelines established in OMB Circular A-136, *Financial Reporting Requirements*. It satisfies our statutory requirements for financial and performance management reporting.

Most importantly, this report is a testament to the CFTC's dedication to regulating the markets under our jurisdiction and achieving management excellence while doing so. Of particular note are the leadership contributions made by Commissioner Brown-Hruska serving as Acting Chairman. Her steady hand and good judgment served the Commission well during a transitional year. Thanks to all our Commissioners and the dedicated staff for their successes, many of which are highlighted in the Management's Discussion and Analysis section of this document.

Therefore, it is with pride and confidence in the Commission staff that I certify with reasonable assurance that our agency's systems of management control, taken as a whole, comply with the Federal Managers' Financial Integrity Act of 1982, and that our agency is in substantial compliance with applicable Federal accounting standards and the U.S. Standard General Ledger at the transaction level. The CFTC's financial and performance data is reliable, accurate, and consistent.

A handwritten signature in dark ink, appearing to read 'Reuben Jeffrey III'.

Reuben Jeffrey III
Chairman

November 15, 2005



Fiscal Year 2005 Commissioners



From left; **Sharon Brown-Hruska**, *Commissioner*; **Walter L. Lukken**, *Commissioner*; **Reuben Jeffery III**, *Chairman*; **Frederick W. Hatfield**, *Commissioner*; **Michael V. Dunn**, *Commissioner*

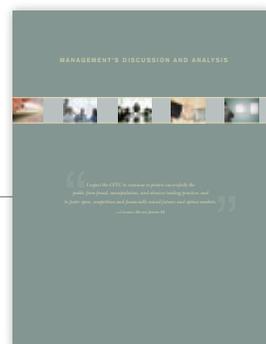


How This Report is Organized

The CFTC's *FY 2005 Performance and Accountability Report* is the second such report published by the Commission. This document is comprised of three primary sections:

Management's Discussion and Analysis

The Management's Discussion and Analysis (MDA) is an overview of the entire Report, as supported and detailed in the Performance Section and Financial Section. The MDA presents performance and financial highlights for FY 2005, in addition to compliance with legal and regulatory requirements and existing or possible effects and challenges facing the Commission in the future.



Performance Section

The Performance Section compares the Commission's performance to the annual goals as set forth in the CFTC Strategic Plan. For more information on this section, please contact Emory Bevill, Deputy Director for Budget and Planning, at 202-418-5187.



Financial Section

The Financial Section is comprised of the Commission's financial statements and related Independent Auditors' report. For more information on this section, please contact Jeanne Ring, Deputy Director for Accounting and Financial Systems, at 202-418-5185.



Questions and comments about this document can be directed to Mark Carney, Chief Financial Officer, at 202-418-5477 or, via e-mail at mcarney@cftc.gov.

An electronic version of this document is available on the Internet at www.cftc.gov/cftc/cftcreports.htm. The Commission's strategic and performance plans are also available at this Web site.



MANAGEMENT'S DISCUSSION AND ANALYSIS



“ *I expect the CFTC to continue to protect successfully the public from fraud, manipulation, and abusive trading practices and to foster open, competitive, and financially sound futures and option markets.* ”

—CHAIRMAN REUBEN JEFFERY III

CFTC 2005 Highlights

Major Power Company Reaches Global Settlement

"The \$81 million penalty assessed today against American Electric Power Company, Inc., (AEP) and AEP Energy Services, Inc., reflects the gravity of the defendant's illegal conduct in the natural gas markets. I applaud the extensive efforts of our enforcement staff to expose the company's wrongdoing, as well as their efforts in assisting the Department of Justice and Federal Energy Regulatory Commission. Over the last three years, Corporate Compliance departments have changed their controls and the way they report sensitive market information. It is obvious that our diligent enforcement actions in this area have had a positive impact on the veracity of traders," stated Director of Enforcement, Gregory Mocek. January 26, 2005

Final Communiqué on Common Work Program to Facilitate Trans-Atlantic Derivatives Business

On June 28, 2005, the CFTC and the Committee of European Securities Regulators (CESR) published the final Communiqué, which sets out a common work program to facilitate trans-Atlantic derivatives business and reflects considerable industry input.

The work program incorporates the views of organized derivatives markets, intermediaries, and end-users

from the United States and the European Union. Under the terms set forth in the work program, a task force drawn from the CFTC and CESR will review issues relating to enhanced transparency and clarity of regulatory developments, simplified access or recognition procedures, and targeted consultation on cross-border issues, as well as issues raised by the derivatives industry and end-users.

Enforcement Actions

The Commission's Enforcement program serves to protect markets, market users, and the public. In fulfilling that mandate, the Division of Enforcement seeks to detect violations quickly, bring immediate action to cease violative conduct, interact with other State and Federal regulators as a force multiplier, and publicize its actions in order to educate the public about possible misconduct and deter future violators. To that end, during FY 2005, the Commission's Enforcement program filed 69 enforcement actions against more than 200 respondents/defendants, and obtained over \$160 million in restitution, disgorgement, and penalties in pending cases.

Approval of New Exchange

The Commission approved the application of the Chicago Climate Futures Exchange, L.L.C., (CCFE) for designation as a contract market. CCFE is an innovative new market



that offers trading of standardized and cleared futures contracts based on emission allowances. For example, the Sulfur Financial Instrument (SFI) futures contract is based on the Environmental Protection Agency's sulfur dioxide emission allowance trading program. CCFE SFI futures contracts are also financially guaranteed. These emission allowance futures contracts provide utilities and other firms with low-cost, financially guaranteed tools for managing the exposure to price volatility in the emission allowance market.

Unqualified Audit Opinion

CFTC earned an unqualified or clean audit opinion on its FY 2005 Financial Statements—the second year that its statements were audited pursuant to the Accountability of Tax Dollars Act. This achievement validates the Commission's commitment to financial integrity and effective program management. Maintaining accounting integrity and quality stewardship of federal funds is tantamount to fulfilling its fiduciary responsibility to the public.

Rule Enforcement Review of Regulatory Compliance Programs

The Commodity Futures Trading Commission notified the New York Board of Trade (NYBOT) of the results of its rule enforcement review. Commission staff found that NYBOT maintains an adequate market surveillance program to prevent manipulations and enforce its speculative position limits and position accountability levels.

The review, which was recently completed by the Commission's Division of Market Oversight, covered the target period from January 1, 2004, to December 31, 2004.

Global Markets

Obtaining input on international market issues that affect the integrity and competitiveness of U.S. markets and firms engaged in global business is a necessity.

In FY 2005, the CFTC worked cooperatively with the U.S. Treasury Department in the continuing efforts to assist China in developing its financial markets.

New Products Pose New Challenges

The Commission has faced the challenge of performing surveillance on a record number of actively traded futures and option contracts—over 900 contracts were listed by U.S. futures exchanges during 2005.

The proliferation of new offerings reflects the continuing evolution of the futures industry in responding to the risk management and price discovery needs of the international economy.

Examples of new futures and option contracts include energy swaps, retail gasoline, weather derivatives, local housing markets and complex financial instruments, as well as new contracts based on the more traditional commodities such as ethanol, wood pulp, freight rates, and corn and soybean production.

NEW FEDERAL GOVERNMENT FINANCIAL EDUCATION WEBSITE



Through a partnership with 19 other Federal agencies, the CFTC helped launch a new financial education Web site and toll-free hotline number.

The mymoney.gov Web site and the 1-888-mymoney toll-free hotline were established to provide Americans easy access to information that can help them better understand their money – how to save it, invest it, and manage it wisely to meet important personal goals.



CFTC Celebrates 30 Years

CFTC Celebrates 30 Years of Service to the American People

On April 21, 1975, with around 200 staff transferred from the Commodity Exchange Authority of the Department of Agriculture, the newly established independent agency opened its doors to regulate the commodity futures and option markets of the United States.

At that time, the vast majority of futures trading took place in the agricultural sector and only on the trading floors of major exchanges.

Today, the Commodity Futures Trading Commission has nearly 500 employees who continue to dedicate themselves to achieving the agency's mission in a world of change.

CFTC CHARTER MEMBERS

There are 26 employees who are deserving of special mention on CFTC's 30th anniversary. They are charter members who have been with the CFTC since its first day on April 21, 1975. Congratulations and thank you for your dedication!

- | | | | |
|--|---|--|---|
| <ul style="list-style-type: none"> • Allen Cooper • Alfonso Holston • Carol Ceropski • Charlotte Ohlmiller • Charles Ricci • David Kass • David Rosenfeld | <ul style="list-style-type: none"> • Donald Nash • Duane Schambach • Elverse Alexander • Frank Zimmerle • James Lammler • Jon Hultquist • Josiane Branch | <ul style="list-style-type: none"> • Judi Payne • Keith Day • Lee Smith • Loraine Leonard • Marshall Horn • Marvin Jackson • Philip Rix | <ul style="list-style-type: none"> • Ralph Der Asadourian • Richard Shilts • Thomas Purcell • Vickie Evans • Walter Maksymec |
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Commission at a Glance

CFTC Mission

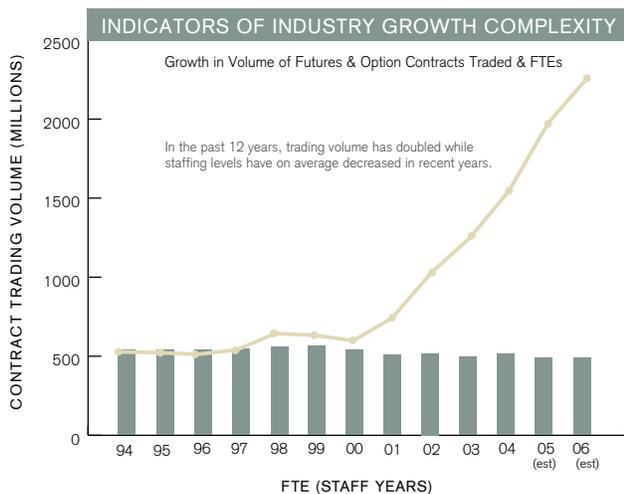
The mission of the CFTC is to protect market users and the public from fraud, manipulation, and abusive practices related to the sale of commodity futures and options and to foster open, competitive, and financially sound commodity futures and option markets.

Keeping Pace with Change

During FY 2005, the Commission continued to focus its actions on modernizing regulation and keeping pace with rapidly changing markets.

In February 2004, the Commission issued *Keeping Pace with Change*, a strategic plan for FY 2004-FY 2009. This plan reflects the new direction of the agency, driven by the CFMA, including three key objectives: 1) modernizing rules affecting trading platforms and market intermediaries; 2) permitting futures based on single stocks or narrow-based stock indices; and 3) providing legal certainty for over-the-counter derivatives.

The plan also reflects the enormous and continuing changes in the markets, including rapid growth in volume, globalization, and the movement from open outcry on exchange trading floors to all-electronic trading from widely dispersed geo-graphic locations.

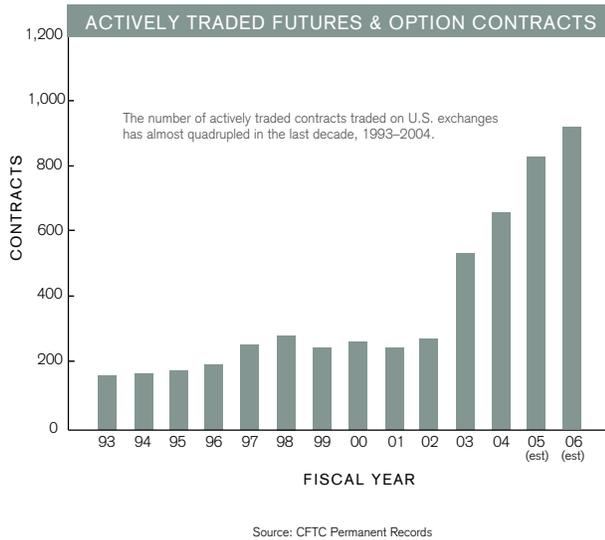


Sources: National Finance Center for FTE data and, Futures Industry Association for Contract Volume data

CFTC History and Transformation

Futures contracts for agricultural commodities have been traded in the U.S. for more than 150 years and have been under Federal regulation since the 1920s. Congress created the CFTC in 1974 as an independent agency with the mandate to regulate commodity futures and option markets in the U.S. At the time of the Commission's founding, the vast majority of futures trading took place in the agricultural sector. These contracts gave farmers, ranchers, distributors, and end-users of everything from corn to cattle an efficient and effective set of tools to hedge against price movements.





Over the years, however, the futures industry has become increasingly complex. While farmers and ranchers continue to use the futures markets as actively as ever to effectively lock in prices for their crops and livestock months before they come to market, highly complex financial contracts based on interest rates, foreign currencies, Treasury bonds, stock market indices, and other products have far outgrown agricultural contracts in trading volume. The latest statistics show that approximately five percent of on-exchange derivatives activity occurs in the agricultural sector, while financial derivatives make up approximately 86 percent, and other contracts, such as those on metals and energy products, make up about nine percent. In recognition of this changing environment, Congress and the President reauthorized the Commission through FY 2005 with the passage of the CFMA in December 2000. The CFMA repealed the ban on single stock futures and instituted a regulatory framework for such products to be administered jointly by the CFTC and the Securities and Exchange Commission (SEC). It codified the principal provisions of a new regulatory framework adopted earlier by the Commission. It also brought legal certainty to bilateral and multilateral trading in over-the-counter markets and clarified the CFTC's jurisdiction over the retail, off-exchange foreign currency market. It gave the CFTC authority to regulate clearing organizations in a way which enables the CFTC to more effectively foster open, competitive, and financially sound markets.

Organization and Locations

The Commission consists of five Commissioners who are appointed by the President to serve staggered five-year terms. All Commissioners are confirmed by the Senate. No more than three Commissioners at any one time may be from the same political party. With the advice and consent of the Senate, the President designates one of the Commissioners to serve as Chairman.

The Commission's organization chart is aligned with its 2004-2009 Strategic Plan, and its functions are divided between program policy and internal management. The Office of the Chairman oversees the Commission's principal divisions and offices that administer the policies, regulations, and guidance regarding the Commodity Exchange Act (CEA). The Office of the Executive Director, by delegation of the Chairman, directs the internal management of the Commission, ensuring that funds are responsibly accounted for and that program performance is measured and improved effectively.

Attorneys at the Commission work on complex and novel legal issues in litigation, regulation, and policy development. They participate in administrative and civil proceedings, assist U.S. Attorneys in criminal proceedings involving futures law violations, and provide legal advice to the Commission on policy and adjudicatory matters.

Auditors examine records and operations of futures exchanges and firms for compliance with the CFTC rules on financial requirements and trade practices.

Economists evaluate filings for new futures and option contracts and amendments to existing contracts to ensure they meet the Commission's regulatory standards. Economists also analyze and advise the Commission on the economic effect of various Commission and industry actions and events. In addition, economists monitor trading activity and price relationships in futures markets to detect and deter price manipulation and other potential market disruptions.

Futures Trading Specialists perform regulatory and compliance oversight of alleged fraud, market manipulations, and trade practice violations.



The CFTC is headquartered in Washington, D.C. Regional offices are located in Chicago and New York; with smaller offices in Kansas City and Minneapolis.

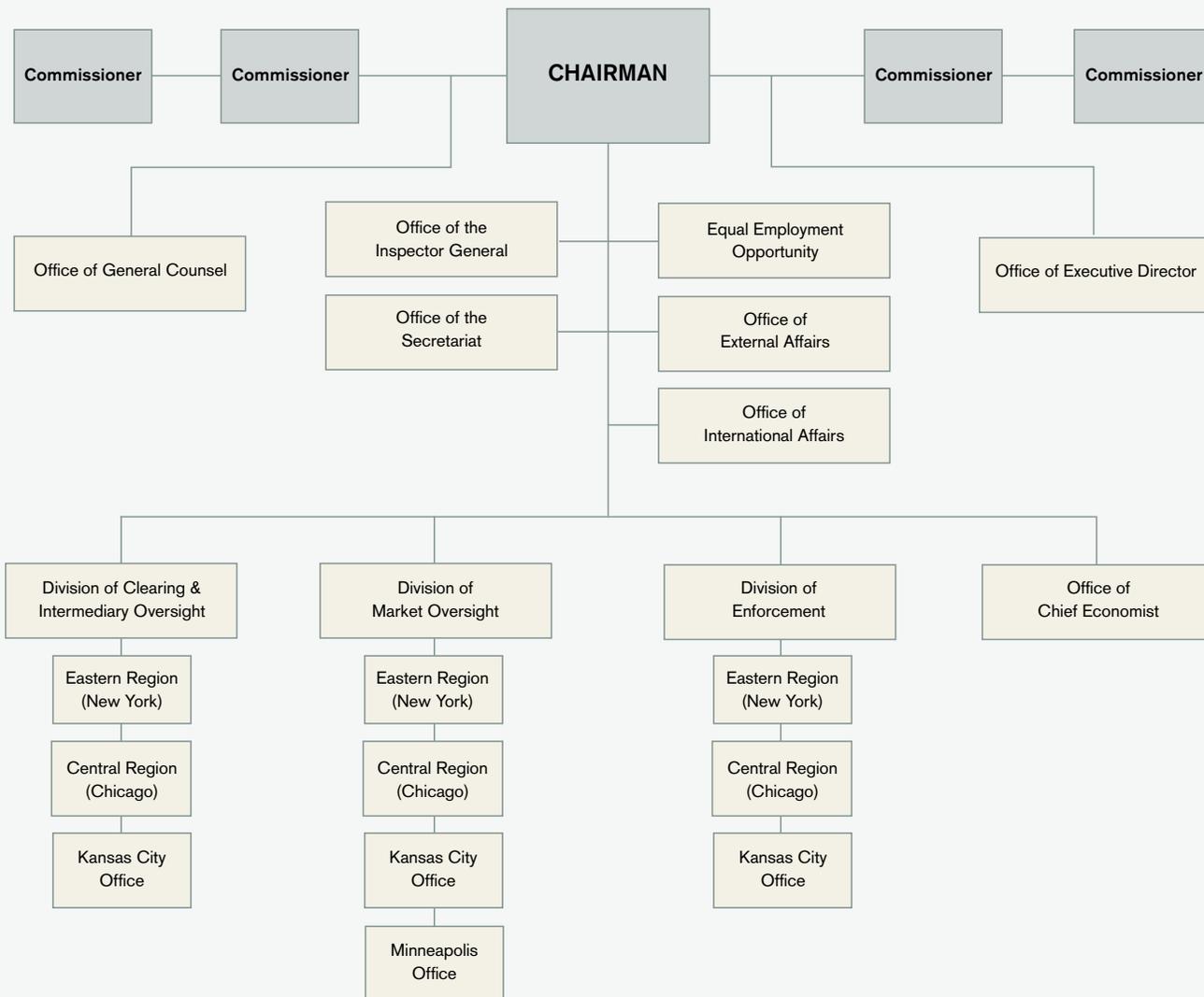
Additional information about the Commission's history and its divisions can be obtained from the Commission's Office of External Affairs or through its Web site, www.cftc.gov.

NUMBER OF CFTC REGISTERED DERIVATIVES CLEARING ORGANIZATIONS 2000–2005

CLEARING ORGANIZATIONS	DEC. 21, 2000	SEP. 30, 2001	SEP. 30, 2002	SEP. 30, 2003	SEP. 30, 2004	JUL. 20, 2005
AE Clearinghouse						✓
BTEX		✓	✓	✓		
CCorp	✓	✓	✓	✓	✓	✓
CBOT					✓	✓
CME	✓	✓	✓	✓	✓	✓
Energy Clear		✓	✓	✓		
FCOM	✓	✓	✓	✓		
GCC			✓	✓		
Hedge Street					✓	✓
ICC	✓	✓	✓	✓		
KCBT	✓	✓	✓	✓	✓	✓
LCH			✓	✓	✓	✓
MGE	✓	✓	✓	✓	✓	✓
NYCC	✓	✓	✓	✓	✓	✓
NYMEX	✓	✓	✓	✓	✓	✓
OCC			✓	✓	✓	✓
ONXCC	✓	✓	✓	✓		
TOTAL	9	11	14	14	10	11



COMMODITY FUTURES TRADING COMMISSION ORGANIZATION STRUCTURE





Performance Highlights

Commission Goals and Objectives

The Commission ensures, through effective oversight, the economic vitality of the commodity futures and option markets and their important function of providing a mechanism for price discovery and a means of offsetting price risk.

The mission of the CFTC is accomplished through pursuing three strategic goals, each focusing on a vital area of regulatory responsibility:

1. Ensure the economic vitality of commodity futures and option markets.
2. Protect market users and the public.
3. Ensure market integrity in order to foster open, competitive, and financially sound markets.

Goal Overviews

Goal One: Ensure the Economic Vitality of Commodity Futures and Option Markets

The focus of this goal is the marketplace. If the U.S. commodity futures markets are protected from and are free of abusive practices and influences, they will better operate to fulfill their vital role in the nation's market economy and the global economy, accurately reflecting the forces of supply and demand and serving market users by fulfilling an economic need.

Desired Outcomes of Goal One:

- Markets that accurately reflect the forces of supply and demand for the underlying commodity and are free of disruptive activity.
- Markets that are effectively and efficiently monitored to ensure early warning of potential problems or issues that could adversely affect their economic vitality.

Performance Summary Highlights for Goal One

- Conducted daily surveillance of 669 active futures and option contracts. Particularly close monitoring was conducted on the energy futures markets, which experienced periods of high prices and high price volatility due to, among other things, low stocks, tight production capacity, geopolitical tension in the Middle East, strong world economic demand, and natural disasters.
- Reviewed, under the Commission's certification procedures for listing new products, 286 new contracts, including 91 security futures products (SFPs), and under its certification procedures, 125 product rule changes. Staff reviewed the terms and conditions of contracts submitted under certification procedures to ensure that statutory and regulatory anti-manipulation requirements were met and to provide essential background information in order to conduct market surveillance.
- Filed ten enforcement actions against a total of 19 individual traders and companies alleging their participation in false reporting and attempted manipulation in



the energy markets. Four energy-related enforcement actions were settled in FY 2005 therein imposing \$45.6 million in civil monetary penalties. Through FY 2005, the Commission's activity in this program area has resulted in 32 enforcement actions, charging 49 defendants and 24 settlements that included a total of nearly \$300 million in civil monetary penalties.

- Provided economic and statistical analysis for enforcement cases involving foreign currencies, energy products, and several recently developed derivatives products, and an examination of the appropriate role for Federal oversight of event-type markets.
- Conducted 72 market move reviews. Such reviews met the objectives of: assuring that registrants and financial intermediaries are not impaired by market volatility or disruptions to meet financial obligations; and detecting any failure by a DCO to meet its obligations or other impairment of a registrant.
- Collected and analyzed approximately 44,000,000 line items of data regarding large trader activity and approximately 16,000 reports identifying the large traders.
- Reviewed three filings by entities that notified the Commission of their intention to operate as exempt markets under the CEA; and reviewed 10 rule amendment approval requests for existing futures and option contracts. In addition, staff: 1) reviewed the terms and conditions of contracts submitted for approval to ensure that the contract terms and conditions were in compliance with Commission regulations and policies and did not raise any public interest issues; 2) reviewed 262 exchange rule submissions that contained 1,237 separate new rule amendments; 3) and reviewed six applications of entities seeking to become a designated contract market.

Goal Two: Protect Market Users and the Public

While our country reaps the rewards of an explosive growth in the futures industry, the risk of fraud and manipulation is always present. The trend toward electronic trading platforms and the expanding complexity of trading instruments have challenged the Commission to reconfigure its ability to identify, investigate, and take action against parties involved in violating applicable laws and regulations. If evidence of criminal activity is found, matters are

referred to state or Federal authorities for prosecution under criminal statutes.

Over the years, the Commission has taken action in a number of cases involving manipulation or attempted manipulation of commodity prices. The Sumitomo copper case and the Hunt brothers silver case are well known examples. A variety of administrative sanctions, such as bans on futures trading, civil monetary penalties, and restitution orders, is available to the Commission. The Commission may also seek Federal court injunctions, asset freezes, and orders to disgorge ill-gotten gains.

Desired Outcomes of Goal Two:

- Violations of Federal commodities laws are detected and prevented.
- Commodity professionals meet high standards.
- Customer complaints against persons or firms registered under the Act are handled effectively and expeditiously.

Performance Summary Highlights for Goal Two

- Typically, the Commission has more than 250 active litigation and investigation matters open at any time. During FY 2005, two-thirds of the Commission's enforcement actions were filed in this performance area. For example, the Commission filed an action closing down Philadelphia Alternative Management, which had hidden trading losses in excess of \$100 million. The CFTC also participated in the joint agency enforcement action as a result of the Bayou hedge fund collapse. The Enforcement program further continued to combat retail foreign currency (forex) "bucket shops" bringing its total, post-passage of the CFMA accomplishments in this area to 79 enforcement actions filed with approximate sanctions of \$115 million in restitution and \$170 million in civil monetary penalties.
- Filed nine enforcement actions related to commodity pools (including "hedge funds"), and commodity pool operators (CPOs); filed eight enforcement actions related to fraud involving commodity trading advisors (CTAs), managed accounts, and trading systems; filed 11 enforcement actions related to futures commission merchants (FCMs), introducing brokers and their associated



persons; and filed a total of 17 enforcement actions involving foreign currency trading. The Commission also filed two enforcement actions involving other illegal off-exchange trading.

- Obtained dismissal of one significant case before the U.S. Supreme Court. The result in that case, *R.J. Fitzgerald & Co. v. CFTC*, 125 S. Ct. 808 (Dec. 13, 2004) (Mem.), preserved the ruling obtained by the Commission in the U.S. Court of Appeals for the Eleventh Circuit in an important anti-sales fraud prosecution. See *e.g.*, *CFTC v. Wall Street Underground*, 128 Fed. Appx. 726 (10th Cir. 2005); *CFTC v. Fremer*, 128 Fed. Appx. 104 (11th Cir. 2005); *CFTC v. Gibraltar Monetary Corp.*, No. 04-13828-I (11th Cir. May 9, 2005).
- Took part in a variety of domestic and international efforts, including task forces and working groups designed to keep market participants abreast of new developments in financial crimes and to coordinate governmental responses to common issues including the Corporate Fraud Task Force, anti-money laundering efforts, Telemarketing and Internet Fraud Working Group, the Consumer Protection Initiatives Committee, and the Securities and Commodities Fraud Working Group.
- Issued 37 opinions and other orders (including orders issued pursuant to delegated authority), 19 of which were final dispositions of cases pending on the Commission's docket.
- Initiated a review of the National Futures Association's (NFA) program for the oversight of CPOs and CTAs for compliance with Commission and NFA rules and regulations. The review specifically focused on: registration of CPOs and CTAs; review of CPO and CTA disclosure documents; and review of CPO annual financial statements, sales practices, and disciplinary process. Staff is currently finalizing its report, which is expected to be presented to the Commission by the close of the first quarter of FY 2006.
- Consulted with staff of the U.S. Treasury Department and various Federal financial regulators to develop anti-money laundering regulations required under the USA PATRIOT Act, including, providing guidance to certain

customers of CTAs and working with other agencies to complete information-sharing agreements.

- Consumer education and outreach is an acknowledged goal of the Commission and part of its effort to protect the public from possible wrongdoing on the part of firms and industry participants. The Commission's Web site is continuously updated with consumer protection advisories and enforcement bulletins to alert and educate the public. The Web site is www.cftc.gov/cftc/cftccustomer.htm

Goal Three: Ensure Market Integrity in Order to Foster Open, Competitive, and Financially Sound Markets

The Commission also focuses on issues of market integrity, seeking to protect: 1) the economic integrity of the markets so that they may operate free from manipulation; 2) the financial integrity of the markets so that the insolvency of a single participant does not become a systemic problem affecting other market participants; and 3) the operational integrity of the markets so that transactions are executed fairly and proper disclosures to existing and prospective customers are made.

Desired Outcomes of Goal Three:

- Clearing organizations and firms holding customer funds have sound financial practices.
- Commodity futures and option markets are effectively self-regulated.
- Markets are free of trade practice abuses.
- The regulatory environment is flexible and responsive to evolving market conditions.

Performance Summary Highlights for Goal Three

- Performed 11 audits (one DCO and 10 FCMs) to test compliance with the Commission's financial requirements for the safekeeping of customer funds. In addition, staff processed approximately 2,700 financial reports filed by registrants. As a result of on-going program efforts such as these, no regulated customer funds were lost in FY 2005, meeting the program's objective of ensuring



sound financial practices of clearing organizations and firms holding customer funds.

- Filed 12 actions in this performance area during FY 2005 including an action imposing restitution and a civil monetary penalty against an accounting firm for failure to detect fraud perpetrated by a CPO and several statutory disqualification actions against registrants. In addition, the Commission assisted in the successful criminal prosecution of a registered floor broker who illegally converted customer funds in violation of the CEA.
- Completed two rule enforcement reviews of self-regulatory organization (SRO) compliance programs. One of the rule enforcement reviews completed during FY 2005 was a review of OneChicago's market surveillance, audit trail, trade practice surveillance, disciplinary, and dispute resolution programs. The other rule enforcement review completed during FY 2005 was a review of the Chicago Board of Trade's (CBOT) audit trail, trade practice surveillance, disciplinary, and dispute resolution programs. Staff found that both OneChicago and CBOT maintain adequate programs with respect to the areas reviewed.
- Worked with NFA staff regarding retail foreign currency trading by FCMs and their affiliates. The NFA submitted additional rules concerning retail foreign currency on August 22, 2005, which the Commission approved on September 15, 2005. These rules are intended to address on-going problems in the off-exchange retail forex market by allowing NFA to impose stricter net capital requirements on certain persons registered as FCMs engaging in retail forex transactions, and to extend certain antifraud and customer protection rules to a greater number of off-exchange retail forex transactions, where NFA members act as intermediaries but the counterparty is not an NFA member. Members are also required to provide customers with information about NFA's registrant database (BASIC) so that they may review the registration status and disciplinary history of those who solicit them.
- Furthered the development of the offer and sale of foreign futures and option transactions (U.S. customers trading on non-U.S. markets) in FY 2005. The Commission issued an order to NFA authorizing NFA to confirm exemptive relief to certain firms acting in the capacity of an FCM that are subject to regulation by a foreign futures authority or that are members of a foreign SRO in a particular jurisdiction. These firms are referred to in the order as cross-border futures brokers (CBFBs). The Commission previously had authorized NFA to confirm exemptive relief solely to firms subject to regulation by a single foreign futures authority or that are members of a foreign SRO.
- Continued work on the International Organization of Securities Commissions (IOSCO) Multilateral Memorandum of Understanding concerning Consultation, Cooperation and the Exchange of Information (MMOU), which is an important and meaningful undertaking for regulators to expand cooperation by establishing specific minimum standards for securities and futures regulators in the area of information-sharing. During FY 2005, Belgium, with which the Commission previously did not have an information-sharing arrangement, became a signatory to the MMOU.
- Issued or reviewed requests for no-action relief in connection with: 1) foreign exchange-traded foreign stock index futures contracts; 2) the offer and sale of foreign exchange-traded foreign stock index futures contracts in the U.S. requests by foreign boards of trade to permit placement of electronic terminals in the U.S. without requiring contract market designation for those boards of trade; 3) relief from the Commission's default contract reporting levels for futures and option contracts so that Eurex U.S.'s new 3-Year U.S. Treasury Notes (3-Year T-Notes) contract would be subject to a reporting level of 750 contracts, rather than the default level of 25 contracts; and 4) easing the burden of reporting on market participants, while preserving the Commission's ability to effectively surveil trading in the 3-Year T-Note contract.
- Provided technical assistance to foreign regulators from 14 foreign jurisdictions visiting the U.S. and to on-site visits to foreign jurisdictions. Sharing information enhances the



knowledge of other regulators and facilitates the development of high levels of global regulatory protections.

- The Commission had two advisory committee meetings in FY 2005. On January 12, 2005, the Global Markets Advisory Committee (GMAC) met, and on April 28, 2005, the Technology Advisory Committee (TAC) met. The GMAC was created by the Commission for the purpose of obtaining input on international market issues that affect the integrity and competitiveness of U.S. markets and firms engaged in global business. The January 2005 GMAC meeting agenda included developments regarding the currency regime of China, with presentations by officials of the U.S. Treasury Department and a representative of the Chicago Mercantile Exchange; segregated/secured funds discussion lead by the GMAC Subcommittee on Bankruptcy; and CFTC reauthorization, with updates by House and Senate staff. The TAC was created by the Commission in October 1999 to obtain input on emerging technologies, the impact of technology on financial services and commodity markets, and the appropriate legislative or regulatory response to increasing use of technology in the markets. TAC members represent U.S. designated contract markets, SROs, financial intermediaries, market users, and traders. The April 2005 TAC meeting agenda included discussion of: 1) what constitutes “prior art” in the patents process; 2) intellectual property in trading and settlements technology; 3) restrictions on the usage of exchange settlement prices; and 4) market data piracy.

Strategic Planning and Reporting

The three goals of the Strategic Plan 2004–2009 establish appropriate priorities for the Commission in enabling a very small organization to be an effective regulator in a rapidly changing marketplace. The preceding overviews demonstrate a coordinated set of objectives and actions flowing from the goals that shape our work into a cohesive whole.

The Government Performance and Results Act (GPRA) requires the Commission to establish meaningful performance standards for activities for the Commission

as a whole and for the statutorily authorized programs that it administers.

For the end of FY 2005, this *Performance and Accountability Report* shows the extent to which these actions translated into meaningful results and successful investment of public funds. This report also includes a discussion of how the Commission will refine our policy and management activities during FY 2006 to enable us to achieve greater success.

For example, as outlined in the Commission’s *FY 2007 Budget Estimate* to the Office of Management and Budget (OMB), a fourth goal, “Organizational and Management Excellence” will be added to the CFTC’s Strategic Plan in FY 2006. It will clearly articulate goals for ensuring the Commission has the right people, in the right place, at the right time, doing the right work. The plan sets up a framework for how information technology investments can improve the work processes of the Commission and the services for its customers and partners. The plan also focuses the Commission’s efforts to ensure that appropriate internal controls and financial systems are in place to provide managers with accurate and timely financial and performance information for managing day-to-day operations.

The accurate and timely financial and performance information will allow the Commission to integrate performance expectations and funding requirements effectively. Key target results for the proposed fourth goal include the following:

- The Commission will improve internal controls and data integrity, as reflected in three sequential clean audit opinions and the ability to use financial data on a day-to-day basis to help inform management and programmatic decisions Commission-wide.
- The Commission will improve the way it exchanges data and interacts with customers by enhancing the use, management, and security of information technology investments.
- The Commission will identify and refine performance measures for its programs, using data and analysis to inform funding recommendations and focusing on the results expected from the programs.



- The Commission will employ top-notch professionals with strong academic records and excellent analytical and problem-solving skills for its important work.

It will continue to implement Section 10702 of Public Law 107-171, the Farm Security and Rural Investment Act of 2002, which removes the CFTC from coverage under certain provisions of Title V of the U.S. Code that govern basic pay, benefits, and compensation in all pay systems and removes the CFTC from the Senior Executive Service.

This authority allows the Commission to compete with the six agencies subject to the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) of 1989 (12 U.S.C.1833b (a))¹ for the scarce talent required to meet its mission.

Integration of Performance with Budget and Finance

Focusing on results and accountability with performance monitoring and financial reporting is sound practice. One critical gauge of how well taxpayer dollars are being used is for an agency to link the performance of its programs to subsequent budget determinations.

The Commission constantly seeks to strengthen the linkage between financial investments and program quality. We do this not only through the development of program measures, but also through various reporting mechanisms and effective budget management. This report is one example of how we provide comprehensive, accurate information to the American public in a timely manner. The following are some other major activities related to budget and performance integration.

Program Assessment Rating Tool (PART). The OMB has systematically assessed the quality of government programs over the past three years. Through the PART, OMB works with Federal agencies to judge the effectiveness of programs with regard to their stated purpose, strategic planning, internal management, and results and accountability. Although primarily a diagnostic tool for programs, PART reviews provide critical information that can be used to establish funding priorities for the subsequent budget cycle.

In December 2004, the Commission's Enforcement program was evaluated by OMB and the Commission. The program received top scores for purpose and design as well as management. Opportunities for improvement existed in the areas of strategic planning and program results measurement.

Alignment of Financial Data and Performance Priorities. This *Performance and Accountability Report* strengthens the alignment of financial data and performance priorities by again identifying appropriations and net costs for the goals of the CFTC Strategic Plan. Each Commission program is aligned with the same strategic goal(s) as a year ago, enabling both our appropriations and our estimated net costs to clearly reflect the discrete priorities of the CFTC Strategic Plan.

Integrating Performance Plan into Budget. During the past year, the Commission incorporated its performance plan into its submission of the Commission's *FY 2007 Budget Estimate* to OMB. For the FY 2007 budget cycle, the budget and annual performance plan were formulated concurrently and are increasingly integrated.

Measurement Challenges. Commission's challenges of linking performance results to the budget are complicated by the fact it is difficult to separate the Commission's impact from other events affecting futures and option markets.

¹The FIRREA agencies are the Federal Deposit Insurance Corporation, the Comptroller of the Currency, the National Credit Union Administration Board, the Federal Housing Finance Board, the Farm Credit Administration, and the Office of Thrift Supervision.





Financial Highlights

Financial Overview

With U.S.-based jurisdiction for regulating the commodity futures and options trading industry, the CFTC covers a great deal of ground – both domestically and abroad. Unlike many other financial regulators, the Commission relies solely on appropriations to cover salaries, expenses, and on-going operations. Any fees or other monies, totaling many millions of dollars, collected during the year are deposited into U.S. Treasury accounts and flow into its general fund.

Operations in FY 2005 achieved marked improvements in our financial management and reporting capabilities. Key enhancements were achieved with account relationship analysis, timely reporting, and the introduction of new management reports. The Commission derived maximum benefits from these enhancements as they helped streamline reconciliation processes. Moreover, more timely data led us to generate new executive management reports to monitor the progress of our programs.

The Commission's ability to demonstrate that effective controls were in place over financial reporting ensured that an unqualified audit opinion was rendered. The Commission is confident that this will be sustained through effective stewardship. Management recognizes the need for accountability, and fully supports the culture change necessary to implement more thorough assessments of risk factors that can have an impact on financial reporting.

Improved management reporting, in turn, enables managers to be accountable and supports the concepts of the GPRA and the principles of the President's Management Agenda. Both GPRA and the President's Management Agenda require the Commission to: 1) establish a strategic plan with programmatic goals and objectives; 2) develop appropriate measurement indicators; and 3) measure performance in achieving those goals.

During FY 2005, we improved our management reporting to include monthly fiscal reporting for program managers. Improved reporting capabilities enable the Commission to integrate program results with fiscal costs that assist in measuring program results against performance.

Our financial reporting capabilities have become routine, enabling us to extend our financial analysis for both program management and fiscal reporting in less time; thereby utilizing Commission resources more efficiently and effectively.

Lines of Business

The Commission managed an appropriation of approximately \$93.5 million in FY 2005, of which 34 percent went primarily toward market oversight activities. The futures markets continue to grow rapidly, with the 2006 trading volume expected to be twice that of 2000, the year the CFMA was passed.



In 2000, there were 12 U.S. futures exchanges. Today, there are 20 designated contract markets and another 13 trading platforms covered by the CFMA. The number of markets subject to some level of Commission oversight has tripled. Similarly, more than 600 new products have been brought to market since 2000, versus fewer than 200 in the three years preceding the CFMA's passage.

These are very positive developments for market users, but they challenge the human capital resources of the Commission. Moreover, as derivatives markets generally become more global in nature, the Commission is increasingly called upon to register overseas clearinghouses and futures firms, to approve complex cross-border trading and clearing linkages, and to then perform effective on-going supervision. This requires the Commission to invest resources in developing and maintaining effective relationships with foreign regulatory authorities.

Of the Commission's three strategic goals, the largest portion of the Commission's resources, 42 percent, was allocated towards Goal Two, with activities designed to protect market users and the public. The Commission's aggressive enforcement actions in the energy sector reflect an approach to market oversight that emphasizes tough enforcement actions against wrongdoers without creating overly burdensome regulations.

As energy price escalations impact the U.S. economy, the Commission must do its part to ensure that market users and the public are protected. Moreover, retail foreign currency fraud has become an increasing problem particularly with the growth of the Internet, which enables access to foreign scam artists and parties who would evade our safeguards and shift funds to off-shore locations.

The Commission needs to calibrate its resources to actively pursue increasingly sophisticated and global fraud that may have implications on national security as well as customer protection. No less important, but using a relatively few number of people, activities to ensure market integrity in nonexempt markets require the Commission to rely on self-regulation and to leverage technology.

With the CFMA, the Commission was, for the first time, assigned separate supervisory responsibility over futures clearinghouses. Since 2000, seven clearinghouses have been designated, three of which are completely new

institutions and another of which is an overseas institution. Clearinghouses, as central counterparties in the futures markets, are critical to the financial integrity of markets and intermediaries. Their proper supervision requires the Commission to devote about 26 percent of its resources executing oversight programs.

In addition, the USA PATRIOT Act of 2001 assigned to the Commission new responsibilities to work with other Federal financial regulators to develop and then implement rules and practices geared toward effectively enforcing key provisions, such as anti-money laundering protections. Fulfilling this important new national security responsibility requires the Commission to devote resources to developing new workforce competencies, practices, and procedures.

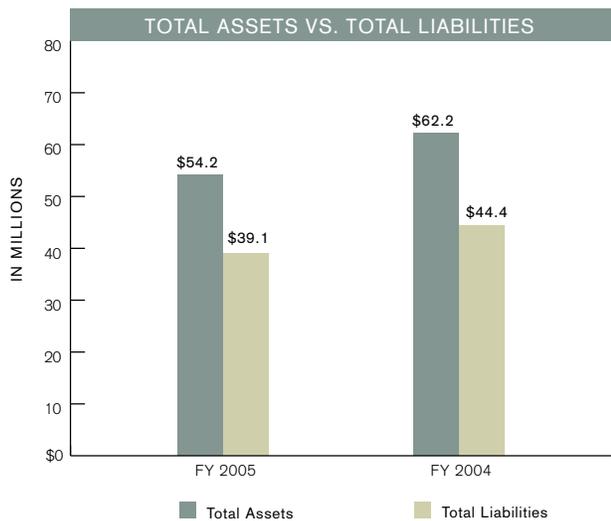
As noted earlier, unlike most other Federal financial regulators who receive fees or other monies collected during the year, the Commission relies on appropriations for 100 percent of its total operating budget. Therefore, management must be diligent in its allocation and administration of resources. This is a key driver behind the adoption of a new fourth goal in FY 2006 addressing management excellence.

Financial Position

The Commission's financial statements, which begin on p. 64, received an unqualified audit opinion, issued by the independent accounting firm of KPMG LLP. In FY 2004, KPMG was only able to render an opinion on the Commission's balance sheet because the other statements were dependent on prior year activity that had not been audited. Preparing these statements is part of the Commission's continuing efforts to achieve financial management excellence and to provide accurate and reliable information that is useful for assessing performance and allocating resources. Commission management is responsible for the integrity and objectivity of the financial information presented in the financial statements.

The financial statements presented in this report have been prepared from the accounting records of the CFTC in conformity with generally accepted accounting principles (GAAP) in the United States. GAAP for Federal entities are the standards proscribed by the Federal Accounting Standards Advisory Board.





Balance Sheet. The balance sheet presents, as of a specific point in time, the economic value of assets and liabilities retained or managed by the Commission. The difference between assets and liabilities represents the net position of the Commission.

The balance sheet displayed on p. 64 reflects total assets of \$54.2 million, a 13 percent decrease from FY 2004. This decrease is attributable to custodial fines and interest receivables from the Civil Monetary Sanctions Program.

The majority of the liabilities, 73 percent, consist of custodial liabilities. Custodial receivables (non-entity assets) are those for which fines and penalties have been assessed and levied against businesses for violation of law. The CFIC litigates against defendants for alleged violations of the CEA, as amended. Violators may be subject to a variety of sanctions including fines, injunctive orders, bars or suspensions, rescissions of illegal contracts, disgorgement, and restitution to customers.

Historical experience has indicated that a high percentage of custodial receivables prove uncollectible. The methodology used to estimate the allowance for uncollectible amounts related to custodial accounts is that custodial receivables are considered 100 percent uncollectible unless otherwise noted in the judgment. An allowance for uncollectible accounts has been established and included in "accounts receivable" on the balance sheet. The allowance is based on past experience in the

collection of accounts receivable and analysis of outstanding balances. Accounts are re-estimated quarterly based on account reviews and determination that changes to the net realizable value are needed.

Several factors influenced the change in the Commission's net position during FY 2005. This includes the timing of the execution of prior year write-offs of old debt and the overall case management and analysis of debt by the Division of Enforcement.

Statement of Net Cost. The statement of net cost is designed to present the components of the net cost of the Commission. Net cost is the gross cost incurred less any revenues earned from Commission activities. The statement of net cost is categorized by the Commission's strategic goals. The Commission experienced a four percent increase in total net costs during FY 2005.

Goal 1, which tracks activities related to Market Oversight, experienced a nine percent increase in costs over FY 2004.

Goal 2 is representative of efforts to protect market users and the public. Costs are spread across three outcomes. However, the majority of costs are related to detecting and preventing violations of Federal commodity laws. These programs experienced a five percent cost increase in FY 2005.

Goal 3, which is representative of efforts to ensure market integrity, spreads costs across the achievement of four outcomes. The distribution of costs for maintaining self-regulated markets was that of costs incurred for other outcomes. Overall, a one percent cost decrease was incurred in FY 2005.

Statement of Budgetary Resources. This statement provides information about the provision of budgetary resources and their status as of the end of the reporting period. Information in this statement is consistent with budget execution information and the information reported in the *Budget of the United States Government*.

The statement displayed on p. 67 shows that the Commission had \$101.8 million in budgetary resources, \$0.77 million of which remained unobligated, with \$3 million not available at year-end. The \$3 million is only available for making upward and downward adjustments



to obligations. The Commission had \$96 million in net outlays for FY 2005.

Statement of Financing. This statement demonstrates the relationship between an entity's proprietary and budgetary accounting information. It links the net cost of operations (proprietary) with net obligations (budgetary) by identifying key differences between the two statements. This statement is structured to identify total resources used during the fiscal year, and then makes adjustments based on whether the resources were used to finance the net obligations or net cost.

This statement, displayed on p. 69, identifies \$95.2 million of resources used to finance activities, \$4.9 million of resources used to finance items not part of the net cost of operations, and \$0.043 million of components of net cost of operations that will not require or generate resources.

Statement of Custodial Activity. This statement provides information about the sources and disposition of non-exchange revenues. Non-exchange revenue at the CFTC is primarily represented by fines, penalties, and forfeitures assessed and levied against businesses and individuals for violations of the CEA, as amended. Other non-exchange revenue includes registration, and filing and appeal fees, as well as general receipts. The statement of custodial activity displayed on p. 70 reflects total non-exchange revenue collected (cash collections) of \$35 million and a transfer of the collections to the U.S. Treasury in the same amount.

Look Ahead – Possible Effects of Existing Events and Conditions

The commodity futures and option markets are burgeoning and dynamic. These trillion dollar markets, of vital importance to the economy, are expanding steadily in both volume and new users, and their complexity is rapidly evolving with new technologies, globalization, product innovation, and greater competition. The integrity of these markets is an essential defense against economic disruption of the marketplace and, by extension, the American economy.

Almost everything in the futures industry has fundamentally changed over the last 20 years – from the products that are trading to the platforms on which they are traded. As the Commission looks ahead, there are even more

broad-based changes on the horizon which will have a dramatic impact on our markets.

Additionally, 20 percent of the Commission's workforce, including 28 percent of its leadership positions, are eligible to retire during FY 2006. The Commission must take immediate steps to preserve its intellectual human capital and expertise in a rapidly changing industry. The Commission must also strive to fully coordinate its strategic technology investments with human capital management.

Rapid development in foreign economies will lead to competition for U.S. exchanges and further lead to cross-border trade in derivatives-related financial services between the U.S. and other countries or multi-nation unions.

Continued technological developments will continue to reduce floor-based trading and increase use of electronic trading systems. The same technology advancement and increased globalization will lead to an even greater number of exchanges and blurring of jurisdictional lines distinguishing foreign and domestic boards of trade.

Increasingly diversified U.S. economic activity will result in added use of exchange-traded and off-exchange derivatives with proliferation of contract-types, trading platforms, and clearing methods.

In recent years, the Commission has been able to operate at a level needed to ensure that it has the tools and resources necessary to do the job expected of it by the Congress, the Administration, and the American people.

Many of the choices the Commission must make about how it will use its limited resources are extremely difficult. Future trends in the market indicate rapid overall growth in trading, computer-based trading, complex contracts, use of international transactions and exchanges, and exploding over-the-counter markets.

The Commission primarily uses its resources to enforce the law aggressively and to pursue wrongdoing in the marketplace. To continue to be an effective regulator, the Commission will need to continue to rely on partnerships and leveraging its resources with those of other agencies and industry groups. That will greatly assist the Commission to confront the jurisdictional challenges created by innovation and the worldwide adoption of futures and option markets. This, coupled with a wide



array of new surveillance issues, will consume significant Commission resources.

From an operational perspective, the Commission must diligently deploy its resources to fulfill its regulatory mandate. To do so, the Commission seeks to transform itself along the following dimensions.

Institutional Transformation. Activities and processes centering on governance, risk management, and compliance with laws and regulations are converging. To be effective, the Commission must excel in all three areas. These long-term management issues require continued focus and sustained management commitment to ensure future success.

The Commission will concentrate on the costs of identifying and controlling institutional risks, specifically, the risk of impairment to the Commission's operations model, reputation, and financial condition from failure to fully comply with laws and regulations, internal controls, and taxpayer expectations. The value of adopting such an approach far outweighs the costs of implementation. Senior management will build long-term value by making investments to comply with relevant regulations, embed compliance within the organization, manage the costs associated with compliance, and identify and address regulatory change. Our progressive focus on compliance will ensure that fewer resources are necessary for remediation activity.

Technology Transformation. Technology improvements will continue to empower the Commission in the future by increasing the availability of our most critical resource – time. Through these improvements, executive management may spend additional time on policy analysis and decision-making rather than on the processing and compiling of key data. This trend at the Commission will continue to accelerate at an increasing rate as many of our investments in systems and E-Government continue to mature.

Major Commission investments currently include replacing the existing financial accounting system and full participation in the on-going E-Government initiative. This model will create public value by optimizing government operations and providing effective oversight in the most efficient manner through a unified data

network. To ensure success, the strategic technology investment plan will be coordinated with human capital management and planning.

Human Capital Transformation. A results-oriented enterprise requires that an organization clearly identify and achieve valuable goals. Our goals continue to reflect the placement of strategic management of human capital at the top of the five key initiatives on the President's Management Agenda.

Specifically, the Commission is focusing significant resources on a consistent approach for the development and implementation of a human capital management plan. The plan integrates human capital management with competitive sourcing and restructuring requirements, and has the solid foundation of data from its first strategic workforce planning competency-based gap analysis and workforce forecasting overview. Along with a talent management action plan, the human capital management plan provides a narrative and literal template for creating a customized, prioritized action plan for the strategic management of human capital in each organizational unit of the CFTC.

As noted in the Technology Transformation section, this planning will continue to be coordinated with other strategic infrastructure investments.

The Commission's continued commitment to strategic investments in both systems and human capital will result in a robust, cost-effective environment. This, in turn, provides taxpayers with an improved return on their investment in the Commission.





Management Challenges

Management Challenges

The major management challenges facing the Commission include:

Financial Management. The Commission has faced many challenges in the past few years related to financial management, including regulatory compliance with Accountability of Tax Dollars Act, requiring the agency to develop financial statements and undergo an annual independent audit.

In addition, regulatory reporting requirements continue to rapidly change through OMB's revisions to financial reporting requirements (OMB Circular A-136, *Financial Reporting Requirements*) and management's responsibility for internal control (OMB Circular A-123, *Management's Responsibility for Internal Control*). The need to comply with these requirements has been extremely difficult and labor intensive to maintain in its existing financial management system environment.

In September 2005, the CFTC entered into an agreement with the Department of Transportation Enterprise Services Center (ESC), an OMB-approved Center of Excellence, to use their systems and services. During the next year, the CFTC will migrate to ESC's integrated financial management system, Delphi. ESC and its Delphi system will provide the agency with a system that supports eTravel, financial transaction processing, and financial reporting – including monthly financial statements, asset

and property management, and procurement. The agency will face many challenges in making the migration to ESC and successfully implementing an integrated system to better meet and serve our financial management needs.

Information Technology. The challenges that face the Commission relating to information technology include investment management, security, critical infrastructure protection, and contingency planning. The Commission has made significant strides relating to its information technology challenges. The Commission accredited its mission-critical systems in July 2005 and is on track to accredit its general support systems by December 31, 2005.

In addition, the Commission completed a management study on mission-essential infrastructure protection that will test critical infrastructure interdependencies within the Commission. The Commission has also initiated several modernization efforts, including eLaw, to increase enforcement case management efficiency.

Program Performance and Accountability. The Commission has several challenges involving data reliability, program monitoring, and program accountability and compliance. As indicated in this report, the Commission will address this issue in the newly proposed fourth goal of the Strategic Plan, and has made accountability a key priority.

Human Capital. To address the challenge of managing and maintaining an appropriately skilled workforce, the Commission has undertaken a comprehensive human



capital management initiative. This initiative includes effective planning for future needs, recruitment, hiring, and the development of the current workforce. It has identified and addressed training gaps and mission-critical leadership positions. The Commission is aware that it still has much to do and is diligently working to achieve its goals..

Management Overview

The CFTC is committed to management excellence and recognizes the importance of strong financial systems and internal controls to ensure accountability, integrity, and reliability. This operating philosophy has permitted the Commission to make significant progress in preparing for an expanded audit of its internal controls over financial reporting next year, as called for under OMB Circular A-123, *Management's Responsibility for Internal Control*.

The Commission relies on its performance management and internal control framework depicted below to:

- Ensure that its divisions and mission support offices achieve their intended results efficiently and effectively.
- Ensure the maintenance and use of reliable, complete, and timely data for decision-making at all levels.

The Commission strongly believes that the rapid implementation of audit recommendations is essential to improving its operations.

Integration of Commission strategic, budget, and performance data permits management to make individual assurance statements with confidence. Moreover, data-driven reporting provides the foundation for Commission staff to monitor and improve its control environment.

Federal Managers' Financial Integrity Act

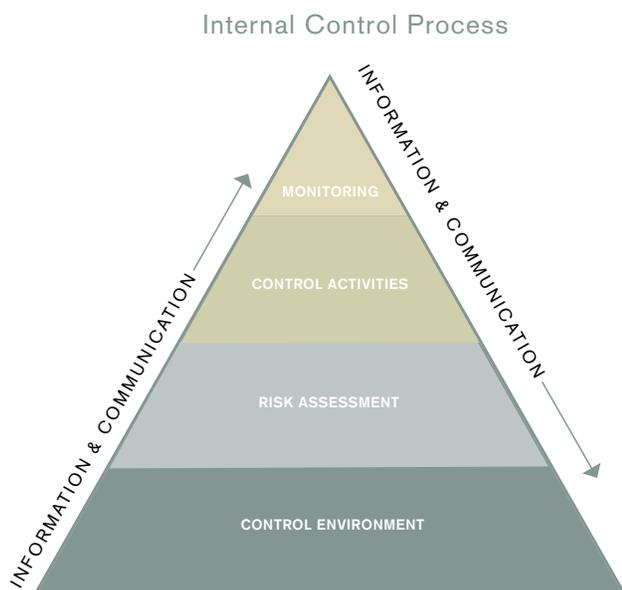
During FY 2005, in accordance with the Federal Managers' Financial Integrity Act (FMFIA), and using the guidelines of the OMB, the Commission reviewed key components of its management and internal control system.

The objectives of our internal controls are to provide reasonable assurance that:

- Obligations and costs are in compliance with applicable laws;
- Our assets are safeguarded against waste, loss, unauthorized use or misappropriation;
- The revenues and expenditures applicable to Commission operations are properly recorded and accounted for to permit the preparation of accounts and reliable financial and statistical reports and to maintain accountability over the assets; and
- All programs are efficiently and effectively carried out in accordance with applicable laws and management policy.

The efficiency of the Commission's operations is continually evaluated using information obtained from reviews conducted by the Government Accountability Office (GAO) and the Office of Inspector General, specifically requested studies, or observations of daily operations.

These reviews ensure that the Commission's systems and controls comply with the standards established by FMFIA. Moreover, managers throughout the Commission are responsible for ensuring that effective controls are implemented in their areas of responsibility. Individual assurance statements from division and office heads serve as a primary basis for the Chairman's assurance that management controls are adequate. The assurance statements are based upon each office's evaluation of progress made in correcting any previously reported problems, as well as new problems identified by the Office of Inspector



General, the GAO, and other management reports, and the management environment within each office.

Commission organizations that have material weaknesses are required to submit plans for correcting those weaknesses. The plans, combined with the individual assurance statements, provide the framework for continually monitoring and improving the Commission's management and internal controls.

The items presented below are illustrative of the review work we performed during FY 2005:

- Implemented key areas of the President's Management Agenda initiatives for strategic management of human capital;
- Assessed gaps in compliance with the pay and benefits provisions called for in Section 10702 of Public Law 107-171, Farm Security and Rural Investment Act of 2002;
- Improved financial performance, expanding electronic government, and integrating budget and performance;
- Complied with the Federal Information Security Reform Act; and
- Corrected material weaknesses and reportable conditions identified in the FY 2004 independent auditors' report of the agency's financial statements and related internal controls.

FMFIA Section 2, Management Control.

The Commission has not declared material weaknesses under FMFIA for FY 2005. However, substantial corrective action has been taken for the three material weaknesses reported in the FY 2004 Financial Statement Audit, and they are no longer considered material:

- Improvements needed in recording accruals and preparing financial statements;
- Improvements needed in financial accounting process over journal vouchers; and
- Financial management systems need improvement.

FMFIA Section 4, Financial Management Systems

Substantial corrective action has been taken to address the material nonconformance reported in the FY 2004 Annual Assurance Statement on the agency's information asset management program. Therefore, this program is no longer considered to be in material nonconformance. This matter was originally reported in the FY 2002 FMFIA Report, and updated in the FY 2003 and 2004 Reports. The Commission did not declare any new material systems nonconformance under FMFIA during FY 2005.



PERFORMANCE SECTION



“

[The CFTC Enforcement Program] is well designed to meet objectives and to maximize the use of its resources.

Through cooperative enforcement with other government and private organizations, the program enhances the impact of its efforts.

”

—OFFICE OF MANAGEMENT AND BUDGET

Mission Statement and Agency Goals

THE U.S. COMMODITY FUTURES TRADING COMMISSION'S MISSION STATEMENT, STRATEGIC GOALS AND OUTCOME OBJECTIVES

MISSION STATEMENT

The mission of the CFTC is to protect market users and the public from fraud, manipulation, and abusive practices related to the sale of commodity futures and options, and to foster open, competitive, and financially sound commodity futures and option markets.

GOAL ONE: Ensure the economic vitality of the commodity futures and option markets.

Outcomes

1. Markets that accurately reflect the forces of supply and demand for the underlying commodity and are free of disruptive activity.
2. Markets that are effectively and efficiently monitored to ensure early warning of potential problems or issues that could adversely affect their economic vitality.

GOAL TWO: Protect market users and the public.

Outcomes

1. Violations of Federal commodities laws are detected and prevented.
2. Commodities professionals meet high standards.
3. Customer complaints against persons or firms falling within the jurisdiction of the Commodity Exchange Act are handled effectively and expeditiously.

GOAL THREE: Ensure market integrity in order to foster open, competitive, and financially sound markets.

Outcomes

1. Clearing organizations and firms holding customer funds have sound financial practices.
2. Commodity futures and option markets are effectively self-regulated.
3. Markets are free of trade practice abuses.
4. Regulatory environment is responsive to evolving market conditions.





Introduction to the Performance Section

Strategic Planning Framework

The mission of the CFTC is accomplished through three strategic goals, each focusing on a vital area of regulatory responsibility.

Accomplishing the three long-term strategic goals is evidenced by the progress of nine key outcome objectives. In most cases, due to the broad economic functions that the Commission oversees, it is not a simple task to identify specific detailed objectives that will be accomplished each year; however, it is possible to identify conditions that, if present, are indicators that the Commission's activities are contributing successfully to the health of the industry it regulates.

Commission programs strive to achieve the three performance goals supporting nine outcome objectives through various means and strategies described in the Performance Detail section. Annually, the performance metrics are analyzed to determine the measure of success the program's activities have in accomplishing the Commission's overall strategic mission.

To ensure this level of success, the Commission is committed to a continual in-depth assessment of the agency and its strategic planning structure. In early November 2005, the Commission conducted strategic planning sessions to reassess the agency's strategic planning structure and probe basic fundamental questions, such as: Where are we going? How will we get there? How has our environment changed to adapt to external changes?

In addition, the Commission will continue to scrutinize the current performance metrics to ensure that the metrics adequately challenge the programs to reach the desired results, ensure accountability, and provide information that can be used to make financial decisions and develop future budgets.

How the Commission Reports Performance Results

Performance results are discussed throughout this report. Commission-wide strategic performance measures are discussed at a summary level in the executive summary. They are further amplified in the discussion of each strategic goal in the Performance Detail section.

Although OMB Circular A-11, *Preparation and Submission of Strategic Plans, Annual Performance Plans, and Annual Program Performance Reports*, suggests reporting more than three prior fiscal years of performance metrics, new measurement data was developed in 2004 rendering 2002 performance data obsolete and is, therefore, not included in this report. In 2004, the Commission modified the 2004 strategic measures and targets to better align our measures to our objectives and to adopt replacement measures where data is not available for prior measures. In the Performance Detail section, the 2005 replacement targets, modified in 2004, are identified as "N/A," not available.

Each strategic goal, in the Performance Detail section, reports the percentage of performance measures met. The



performance statistics in this document represent the best assessment of Commission performance obtainable through the use of existing performance measures. Performance data that is still pending is identified as “TBD,” to be determined. Once the performance metrics are finalized, the “TBD” data will be replaced with the final metrics in the FY 2006 Performance and Accountability Report.

The Performance Details section also sets the national context for each of our goals and describes the accomplishments of our programs over the past year. This discussion is followed by the results on the strategic measures. The Commission believes, however, that significant revisions to these measures are necessary to more meaningfully assess its performance.





Program Assessment Rating Tool

The President’s Office of Management and Budget has systematically assessed the quality of government programs over the past three years. Through the Program Assessment Rating Tool (PART), the OMB works with Federal agencies to judge the effectiveness of programs with regard to their stated purpose, strategic planning, internal management, and results and accountability. Although primarily a diagnostic tool for programs, PART reviews provide critical information that can be used to establish funding priorities for the subsequent budget cycle.

OMB did not undertake a PART review of any CFTC program in FY 2005, and the findings of OMB’s PART review of the Enforcement program in FY 2004 were released in December 2004, after the *FY 2004 Performance and Results Report* was published; therefore, we are including these results here for the first time:

PROGRAM ASSESSED: Enforcement

RATINGS: Results not Demonstrated

SCORING	
Purpose	100
Planning	71
Management	100
Results/Accountability	67

By way of comparison, the Commission understands that the category scoring for the Division of Enforcement was the highest of the three Enforcement programs that underwent the 2004 PART.

Assessment Findings:

The OMB found the CFTC Enforcement program is:

“Well designed to meet objectives and to maximize the use of its resources. Through cooperative enforcement with other government and private organizations, the program enhances the impact of its efforts.

Demonstrates through its performance measures that it brings substantive cases in a timely manner. CFTC successfully resolved 99 percent of the cases it closed in the past year.

Lacks performance measures that illustrate whether the program meets its overall objective. Like other enforcement programs, it faces challenges in establishing overall performance measures to indicate the percentage of violative activity deterred, since no way has been devised to measure the total amount of fraud that exits. Thus, while current measures show that markets have been growing, which could demonstrate that they are ‘open, competitive, and financially sound,’ it cannot be determined how free they are from ‘fraud, manipulation, and abusive practice.’”

In response to these findings, OMB has requested that the Commission:

“Work with other similar programs in the government to develop measures that better reflect program effectiveness. The program will consider developing a novel way of measuring results, for instance, surveying industry experts.

Develop a measure that quantifies increased efficiencies.

Develop measures and targets for the collections of fines.”

The Commission is preparing its response to the OMB recommendations for submission in December 2005.





Goal One

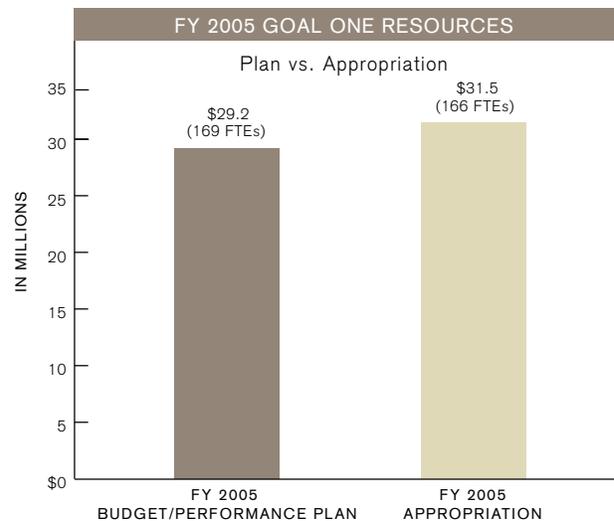
Ensure the economic vitality of the commodity futures and option markets

Public Benefit:

Properly functioning futures markets collect information from around the world, digest it, and respond with judgments about the likely price of commodities at some future time. For example, such judgments could, in turn, trigger decisions to sell a commodity at a certain price; raise capital through an equity rather than a debt offering; increase inventories of various commodities (*i.e.*, copper, soybeans, etc.); use corn syrup rather than sugar or sweetener; or to hold receivables in Deutsche marks rather than British pounds. Thus, futures markets help us plan and make decisions, so that market users avoid uncontrolled risk.

Resource Investment:

In FY 2005, the Commission requested \$29.2 million and 169 full time equivalents (FTEs) and was appropriated \$31.5 million and 166 FTEs for Goal One.



Goal One

Ensure the economic vitality of the commodity futures and option markets.

GOAL ONE: HISTORY OF PERFORMANCE RESULTS¹

OUTCOME OBJECTIVE 1.1

Futures and option markets that accurately reflect the forces of supply and demand for the underlying commodity are free of disruptive activity.

PERFORMANCE MEASURES	FY 2003	FY 2004	FY 2005
Percentage growth in market volume	20%	24%	26%
Percentage of novel or innovative proposals or requests for CFTC action addressed within six months to accommodate new approaches to, or the expansion in, derivatives trading, enhance the price discovery process or, increase available risk management tools	100%	100%	100%
Percentage increase in number of products traded	25%	12%	43%
Percentage of new exchange or clearinghouse organization applications completed within expedited review period	100%	100%	100%
Percentage of new contract certification reviews completed within three months to identify and correct deficiencies in contract terms that make contracts susceptible to manipulation	21%	53%	54%
Percentage of rule change certification reviews completed within three months to identify and correct deficiencies in exchange rules that make contracts susceptible to manipulation or trading abuses or result in violations of the law	70%	70%	84%

OUTCOME OBJECTIVE 1.2

Markets that are effectively and efficiently monitored to ensure early warning of potential problems or issues that could affect their economic vitality.

PERFORMANCE MEASURES	FY 2003	FY 2004	FY 2005
Percentage of DCO applications demonstrating compliance with core principles	100%	100%	100%
Ratio of contracts surveilled per economist	8	10	11
Percentage of contract expirations without manipulation	99.9%	99.9%	99.9%

¹The performance metrics included in this document represent the best current estimate of Commission performance. Additional work is needed to devise better measures and valid current performance measures in order to effectively illustrate program success in meeting overall objectives.



Return on Investment

The Commission's 2005 Annual Performance Plan supports two outcome objectives for Goal One.

OBJECTIVE 1.1: NO PRICE MANIPULATION

FY 2005 Appropriation: \$25.3 Million

FY 2005 Results: Performance results are positive and generally indicate the achievement of results. However, performance plan targets were not developed at the time of the FY 2005 Budget submission in February 2004, as a result of the contemporaneous adoption of the 5-year strategic plan in February 2004.

Number of Measures	Exceeded Goal	Met Goal	Did Not Meet Goal	To Be Determined or Not Available	Percent Meeting or Exceeding Goal
6	0	0	0	6	0%

PERFORMANCE MEASURES	FY 2005 PLAN	FY 2005 RESULTS
1.1.1 Percentage growth in market volume	N/A	26%
1.1.2 Percentage of novel or innovative market proposals or requests for CFTC action addressed within six months to accommodate new approaches to, or the expansion in, derivatives trading, enhance the price discovery process or, increase available risk management tools	N/A	100%
1.1.3 Percentage increase in number of products traded	N/A	43%
1.1.4 Percentage of new exchange and clearinghouse organization applications completed within the expedited review period	N/A	100%
1.1.5 Percentage of new contract certification reviews completed within three months to identify and correct deficiencies in contract terms that make contracts susceptible to manipulation	N/A	54%
1.1.6 Percentage of rule change certification reviews completed within three months to identify and correct deficiencies in exchange rules that make contracts susceptible to manipulation or trading abuses or violations of law	N/A	84%



OBJECTIVE 1.2: EFFECTIVE AND EFFICIENT MARKET SURVEILLANCE

FY 2005 APPROPRIATION: \$6.2 Million

FY 2005 RESULTS: 67 Percent of Performance Results are on target. Performance plan target for Outcome Measure 1.2.2 was not developed at the time of the FY 2005 Budget submission in February 2004, as a result of the contemporaneous adoption of the 5-year strategic plan in February 2004.

Number of Measures	Exceeded Goal	Met Goal	Did Not Meet Goal	To Be Determined or Not Available	Percent Meeting or Exceeding Goal
3	0	2	0	1	67%

PERFORMANCE MEASURES	FY 2005 PLAN	FY 2005 RESULTS
1.2.1 Percentage of DCO applications demonstrating compliance with core principles	100%	100%
1.2.2 Ratio of contracts surveilled per economist	N/A	11
1.2.3 Percentage of contract expirations without manipulation	99.9%	99.9%

Program Contributions to Strategic Goal One:

In 2005, the explosive growth in the futures and option markets continued; total volume in FY 2005 was up 26 percent from FY 2004 with over 2 billion contracts traded. (See measure 1.1.1)

Market Surveillance. Monitoring market activity represents one of the ways the Commission seeks to protect the economic functions of the markets. Market surveillance is conducted to detect attempted manipulation and other abusive practices that could undermine the capacity of these markets to perform their economic function. The Commission takes preventive measures to ensure that market prices accurately reflect fundamental supply and demand conditions, including the routine daily monitoring of large trader positions, futures and cash prices, price relationships, and supply and demand factors in order to detect threats of price manipulation.

In FY 2005, the Commission conducted daily surveillance of 669 active futures and option contracts. Particularly close monitoring was conducted on the energy

futures markets, which experienced periods of high prices and high price volatility due to, among other things, low stocks, tight production capacity, geopolitical tension in the Middle East, strong world economic demand and natural disasters. In addition, very close monitoring was conducted on the cattle futures markets as prices were volatile due to the countervailing pressures of strong demand and the effects of discovery of Bovine Spongiform Encephalopathy (BSE) or "Mad Cow" disease in a single cow in the state of Washington. The surveillance included collecting and analyzing approximately 44 million line items of data regarding large trader activity and approximately 16,000 reports identifying the large traders. In the course of the year, economists prepared approximately 1,500 weekly surveillance reports and compiled 23 special market reports. (See measure 1.2.2)

Commission staff reviewed six applications of entities seeking to become a designated contract market. Staff also reviewed three filings by entities that notified the Commission of their intention to operate as exempt markets under the CEA. (See measure 1.1.4)



Commission staff reviewed 10 rule amendment approval requests for existing futures and option contracts in FY 2005. Staff reviewed the terms and conditions of contracts submitted for approval to ensure that contract terms and conditions were in compliance with Commission regulations and policies and did not raise any public interest issues. Under the Commission's certification procedures for listing new products, 286 new contracts were filed, including 91 SFPs, and under its certification procedures, 125 product rule changes were filed. Staff reviewed the terms and conditions of contracts submitted under certification procedures to ensure that statutory and regulatory anti-manipulation requirements were met and to provide essential background information in order to conduct market surveillance. (See measures 1.1.1, 1.1.2, 1.1.3, 1.1.5, 1.2.1)

The Commission's review of exchange rules is a key aspect of the statutory framework for self-regulation under Commission oversight. The staff reviewed exchange rule submissions with a view toward maintaining the fairness and financial integrity of the markets, protecting customers, accommodating and fostering innovation, and increasing efficiency in self-regulation consistent with the Commission's statutory mandates. During FY 2005, staff reviewed 262 exchange rule submissions containing 1,237 separate new rule amendments. Commission staff are also responsible for providing exemptive, interpretive, or other relief to various markets and market participants to facilitate the continued development of an effective, flexible regulatory environment responsive to evolving market conditions. (See measure 1.1.6)

Derivatives Clearing Organization Oversight. The Commission monitors the potential for, and instances of, market volatility, market disruptions or emergencies which have the potential to impact: 1) the proper capitalization of firms; 2) the proper segregation of customer funds; 3) the ability of financial intermediaries to make payments to a DCO in a timely manner; and 4) issues with respect to systemic risk. Commission staff monitor cases of volatile markets in order to advise the Commission of any potential financial impairment of a registrant or potential systemic risk. It is not possible to estimate in advance the number of such events that will occur

annually because market volatility cannot be predicted. Nevertheless, such events are expected to occur. Commission staff conducted 72 market move reviews in FY 2005. Such reviews met the objectives of assuring that registrants and financial intermediaries are not impaired by market volatility or disruptions to meet financial obligations; and detecting any failure by a DCO to meet its obligations or other impairment of a registrant. (See measure 1.2.3)

Economic and Statistical Analyses. Commission staff performed economic and empirical analyses to evaluate the performance of futures markets and to evaluate the impact of changes in trading rules and in contract specifications on the performance of the futures markets. For example, staff empirically examined the effects of participation by managed money traders in certain U.S. futures markets. Economists in the Office of the Chief Economist also provided economic and statistical consulting services to Commission staff and offered economic and financial research seminars and short courses in futures, options, and financial economics.

Staff also provided economic and statistical analysis on a number of cases involving foreign currencies and energy products, conducted an examination of the appropriate role for Federal oversight of event-type markets, and of several recently developed derivatives products. In addition, Commission staff presented research findings relating to price discovery, hedging, and market microstructure and development issues at industry or academic and industry conferences, as well as through publications available to the public.

Manipulation, Attempted Manipulation and False Reporting. Manipulation investigations and litigations tend to be among the most complex and resource-intensive matters handled by Enforcement staff. During FY 2005, the Commission's Enforcement efforts in this program area are reflected in its handling of alleged misconduct in the agriculture and energy markets. (See Appendices)

Office of the General Counsel. In FY 2005, the Commission continued to review for legal sufficiency and for conformance with the CEA and Commission policy and precedent contract market designation applications and applications for registration as DCOs. In addition, Commission staff continued to advise the Commission



concerning implementation of the rules and regulations issued pursuant to the CFMA. Staff have been instrumental in advising the Commission as it comprehensively modernizes its rules, and particularly the rules governing market intermediaries such as FCMs, CPOs, CTAs and other registrants in light of the study completed by the Commission and submitted to Congress under Section 125 of the CFMA.

Staff also reviewed in excess of 100 proposed enforcement actions, including those alleging manipulation and other abusive trading practices, during FY 2005, to assure their legal sufficiency and conformance with Commission policy and precedent.

Integrated Surveillance System. In FY 2005, the Commission's primary mission critical application to support futures and option data market surveillance, the Integrated Surveillance System (ISS), was significantly enhanced to address changes and growth in the futures industry. This year, those changes included the automation of the collection and review of data from exempt commercial markets. In addition, a number of noteworthy enhancements were established in the ISS that will improve the efficiency of market monitoring and analysis. These modifications include integrated document storage capabilities in support of large trader reporting, consolidated market queries that allow related markets to be grouped together for better market analysis, full search capabilities throughout the application, and comprehensive graphing capability.





Goal Two

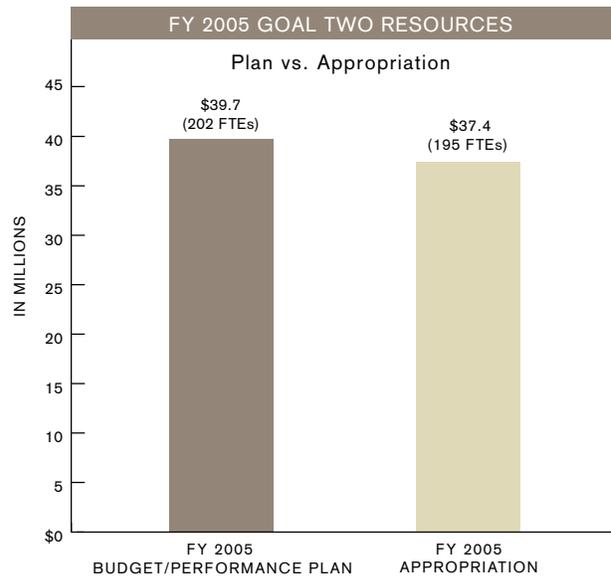
Protect market users and the public

Public Benefit:

Market users must be protected from possible wrongdoing on the part of firms and commodity professionals with whom they deal to access the marketplace, and they must be confident that the marketplace is free of fraud, manipulation, and abusive practices. The Commission plays a crucial role in deterring behavior that could affect market users' confidence by investigating and taking action against unscrupulous commodity professionals who engage in a wide variety of fraudulent sales practices against the public.

Resource Investment:

In FY 2005, the Commission requested \$39.7 million and 202 FTEs and was appropriated \$37.4 million and 195 FTEs for Goal Two.



Goal Two

Protect market users and the public.

GOAL TWO: HISTORY OF PERFORMANCE RESULTS²

OUTCOME OBJECTIVE 2.1

Violations of Federal commodities laws are detected and prevented.

PERFORMANCE MEASURES	FY 2003	FY 2004	FY 2005
Number of enforcement investigations opened during the fiscal year	172	215	131
Number of enforcement cases filed during the fiscal year	65	83	69
Percentage of enforcement cases closed during the fiscal year in which the Commission obtained sanctions	99%	99%	100%
Cases filed by other criminal and civil law enforcement authorities during the fiscal year that included cooperative assistance from the Commission	20	23	20

OUTCOME OBJECTIVE 2.2

Commodity professionals meet high standards.

PERFORMANCE MEASURES	FY 2003	FY 2004	FY 2005
Percentage of SROs that comply with core principles	100%	100%	TBD
Percentage of DCOs that comply with core principles	100%	100%	TBD
Percentage of professionals compliant with standards regarding testing, licensing, and ethics training	100%	100%	100%
Percentage of SROs that comply with requirement to enforce their rules	100%	100%	TBD
Percentage of total requests receiving CFTC responses for guidance and advice	90%	90%	90%

OUTCOME OBJECTIVE 2.3

Customer complaints against persons or firms registered under the Act are handled effectively and expeditiously.

PERFORMANCE MEASURES	FY 2003	FY 2004	FY 2005
Percentage of filed complaints resolved within one year of the filing date	50%	41%	50%
Percentage of appeals resolved within six months	35%	35%	46%

² The performance metrics included in this document represent the best current estimate of Commission performance. Additional work is needed to devise better measures and valid current performance measures in order to effectively illustrate program success in meeting overall objectives.



Return on Investment

The Commission's 2005 Annual Performance Plan supports three outcome objectives for Goal Two.

OBJECTIVE 2.1: VIOLATORS DETECTED & SANCTIONED

FY 2005 Appropriation: \$28.0 Million

FY 2005 Results: Results achieved or slightly below target. It is impractical and infeasible to predict with a degree of precision the exact number of investigations opened, cases filed, cases closed with sanctions obtained, and cases filed with cooperative assistance. Outcome measure 2.1.3 is arguably the strongest measure and the planned results were achieved

Number of Measures	Exceeded Goal	Met Goal	Did Not Meet Goal	To Be Determined or Not Available	Percent Meeting or Exceeding Goal
4	1	1	2	0	50%

PERFORMANCE MEASURES	FY 2005 PLAN	FY 2005 RESULTS
2.1.1 Number of enforcement investigations opened during the fiscal year	135	131
2.1.2 Number of enforcement cases filed during the fiscal year	65	69
2.1.3 Percentage of enforcement cases closed in which the Commission obtained sanctions	100%	100%
2.1.4 Cases filed by other criminal and civil law enforcement authorities during the fiscal year that included cooperative assistance from the Commission	21	20



OBJECTIVE 2.2: COMMODITY PROFESSIONALS MEET HIGH STANDARDS

FY 2005 Appropriation: \$5.8 Million

FY 2005 Results: Results achieved or “to be determined.” Oversight is still on-going and program staff have not completed its review and assessment on measures 2.2.1, 2.2.2, and 2.2.4 to provide sufficient data to report on the percentages that comply with core principles.

Number of Measures	Exceeded Goal	Met Goal	Did Not Meet Goal	To Be Determined or Not Available	Percent Meeting or Exceeding Goal
5	0	2	0	3	40%

PERFORMANCE MEASURES		FY 2005 PLAN	FY 2005 RESULTS
2.2.1	Percentage of SROs that comply with core principles	100%	TBD
2.2.2	Percentage of DCOs that comply with core principles	100%	TBD
2.2.3	Percentage of professionals compliant with standards regarding testing, licensing and ethics training	100%	100%
2.2.4	Percentage of SROs that comply with requirement to enforce their rules	100%	TBD
2.2.5	Percentage of total requests receiving CFTC responses for guidance and advice	90%	90%

OBJECTIVE 2.3: CUSTOMER COMPLAINTS RESOLVED

FY 2005 Appropriation: \$3.6 Million

FY 2005 Results: Slightly above and on target.

Number of Measures	Exceeded Goal	Met Goal	Did Not Meet Goal	To Be Determined or Not Available	Percent Meeting or Exceeding Goal
2	1	1	0	0	100%

PERFORMANCE MEASURES		FY 2005 PLAN	FY 2005 RESULTS
2.3.1	Percentage of filed complaints resolved within one year of the filing date	50%	50%
2.3.2	Percentage of appeals resolved within six months	35%	46%



Program Contributions to Strategic Goal Two:

Oversight of Sales Practices and Registered Futures

Associations. A core part of the Commission's mission is to operate a program that protects market users and the public from fraud and abusive practices related to the offer and sale of commodity futures and options. Commission staff conduct on-going oversight related to screening market professionals for fitness and assuring that DCOs have appropriate risk management programs. The Commission also develops disclosure standards, particularly for managed futures and option products, to assure that market users and potential market users are appropriately and consistently informed of the risks of futures and option trading, and are provided with information about trading managers.

During FY 2005, the Commission initiated a review of the NFA's program for the oversight of CPOs and CTAs for compliance with Commission and NFA rules and regulations. This review has focused on the following NFA programs: registration of CPOs and CTAs, review of CPO and CTA Disclosure Documents, review of CPO annual financial statements, sales practices, and disciplinary process. Staff is currently finalizing its report, which is expected to be presented to the Commission in early FY 2006. (See measures 2.2.1 and 2.2.2.)

Oversight of Intermediary Fitness. In FY 2005, there were 71,264 industry registrants. These registrants included 215 futures commission merchants (15 of which were securities broker-dealers registered with the SEC that "notice-registered" with the CFTC because their only futures-related activity involved SFPs), 1,701 introducing brokers (IBs) (42 of whom were notice-registered), 1,791 CPOs, and 2,661 CTAs. These firms employ 54,823 sales personnel, known as associated persons. In addition, there are 8,524 individuals registered as floor brokers and 1,549 individuals registered as floor traders executing trades on U.S. exchanges.

The Commission is responsible for formal oversight of the NFA registration program. This oversight involves inspection of records and interviews with NFA staff as well as numerous informal contacts between NFA and the Commission staff on a weekly basis. These oversight

activities are designed to protect market participants and the public interest by assuring that persons who deal directly with customers and those who handle customer orders and funds meet the standards for fitness, integrity, and training established under the CEA. Persons who cannot meet these standards may be subject to statutory disqualification from registration and may have their registration denied, conditioned, or revoked.

The Commission seeks to protect market users and the public by requiring futures industry professionals to meet high standards through registration and passing of a proficiency exam by salespersons. When Commission staff uncover persons who are not registered but should be, a letter is sent to the person, and/or the matter is referred for enforcement action. (See measure 2.2.3.)

The Commission chaired the Registration Working Group (RWG), which is composed of Commission and NFA representatives. The RWG was created as a means for the Commission and NFA staff to share ideas and concerns about issues that are not tied to any specific pending registration case. Commission staff participated in four meetings of the RWG during FY 2005, in which the group discussed, among other things: 1) registration holds; 2) conditional registrations; 3) augmentation of the registration database to include a name for regulatory contacts; and 4) fingerprint processing.

Anti-Money Laundering. Commission staff continue to work with other Federal financial regulators on various aspects of a program to combat money laundering and terrorist financing. Specifically, staff continues to participate in developing rules implementing the USA PATRIOT Act and in developing and issuing guidance concerning the application of these rules. For example, staff worked with the SEC and other agencies in drafting a no-action position concerning the customers of certain CTAs and investment advisors that was issued on March 14, 2005. Commission staff also continues to work with the U.S. Treasury to share information about possible terrorist financiers and money launderers. As part of this process, staff maintains and updates a list of FCMs and contact persons, which the U.S. Treasury then uses when issuing a biweekly list of possible money launderers and terrorist financiers.



Commodity Pools (including “Hedge Funds”), Commodity Pool Operators, and Commodity Trading Advisors. Investors continue to fall prey to unscrupulous CPOs and CTAs, including CPOs and CTAs operating self-described hedge funds. In many of these cases, the defendants have pre-existing business, social, religious, or ethnic ties to the individual investors. These personal relationships enable the defendants to gain the investors’ trust and then lull them into a false sense of confidence. The Commission addresses this violative conduct through a combination of enforcement actions and investor education. Some of the scams are operated as “Ponzi schemes” in which early investors are paid purported “profits” with newer investor funds. The schemes generally involve fraud in soliciting the general public to invest in the pools operated by the CPO or CTA, fraudulent statements concerning the results being achieved by the pool for its investors, and/or outright misappropriation of pool funds by the CPO. During FY 2005, the Commission filed nine enforcement actions in this program area, and also achieved significant litigation results in six actions filed in this practice area during previous fiscal years. Examples of these successes are provided in the Appendices.

Commodity Trading Advisors, Managed Accounts, and Trading Systems. During FY 2005, the Commission filed eight enforcement actions in this program area and achieved significant litigation results in four actions filed in this practice area during previous fiscal years. (See Appendices.)

Futures Commission Merchants, Introducing Brokers, and Their Associated Persons. The Commission diligently redresses misappropriation and other violative conduct by futures commission merchants, introducing brokers, and their associated persons. During FY 2005, the Commission filed 11 enforcement actions in this practice area, and also achieved significant litigation results in one action filed in this practice area during previous fiscal years. (See Appendices.)

Foreign Currency Cases. The Commission continued to battle fraud perpetrated on the retail public by firms offering trading in off-exchange forex. While much foreign currency trading is legitimate, numerous companies have fraudulently solicited and traded customer foreign currency futures or option trading accounts. Under the CFMA, it

is unlawful to offer off-exchange foreign currency futures or option contracts to retail customers unless the counterparty to the contract is a regulated financial entity enumerated in the CFMA, such as an FCM or financial institution. In addition, even if the counterparty is appropriate, the Commission has jurisdiction to investigate and prosecute retail foreign currency futures or options fraud. Forex trading scams often attract customers through advertisements in local newspapers, radio promotions, or online. These advertisements often tout purportedly high-return, low-risk investment opportunities in foreign currencies. The Commission has brought enforcement actions against both registered firms (for fraud and for other CEA violations, such as failure to maintain net capital requirements) and unregistered “bucket shops.” (See Appendices.)

During FY 2005, the Commission filed 17 enforcement actions against firms and individuals selling illegal foreign currency futures and option contracts, bringing the total of such actions to 79 since enactment of the CFMA in December 2001. During FY 2005, the Commission also achieved significant litigation results in eight actions filed in this practice area during previous fiscal years. Since the enactment of the CFMA, the Commission has obtained in its 79 forex enforcement actions approximate monetary sanctions of \$170 million in civil monetary penalties and \$115 million in restitution. (See Appendices.)

Precious Metals and Other Illegal Off-Exchange Cases. During FY 2005, the Commission’s Enforcement program prosecuted two actions that alleged non-forex, illegal off-exchange trading. (See Appendices.)

Violation of Commission Orders. The Commission filed one enforcement action in this program area during FY 2005. (See Appendices.)

Quick-Strike Cases. The Commission is committed to responding quickly to enforcement investigations that uncover on-going fraud. Quick-strike cases are civil injunctive actions that generally are filed in Federal district courts within days or weeks of the discovery of the illegal activity, enabling the Commission to stop fraud at an early stage and to attempt to preserve customer funds. During FY 2005, the Commission prosecuted 13 quick-strike cases, which were all filed within four months of opening the related investigation.



Domestic Cooperative Enforcement. The Commission's cooperative enforcement efforts are an important part of its ability to promote compliance with and deter violations of Federal commodities laws. Cooperative enforcement enables the Commission to maximize its ability to detect, deter, and impose sanctions against wrongdoers in cases involving U.S. markets, registrants, and customers. The benefits of cooperative enforcement include: 1) The use of resources from other sources to support Commission enforcement actions; 2) coordination in filing actions with other authorities to further the impact of enforcement efforts; and 3) development of consistent and clear governmental responses and avoidance of duplication of efforts by multiple authorities.

As in the past, staff have coordinated with numerous Federal, State, and self-regulatory authorities. Historically, program staff have sought assistance from or provided assistance to various Federal agencies, such as the Department of Justice (DOJ), Federal Trade Commission (FTC), Federal Energy Regulatory Commission (FERC), Federal Bureau of Investigation (FBI), SEC, and the U.S. Postal Inspection Service. Similarly, Commission staff have provided assistance to and/or received assistance from State authorities, such as agencies responsible for the regulation of corporations, securities, and banking. The Commission also provided Federal and local law enforcement authorities with testimony or other assistance in connection with criminal investigations. Enforcement program staff worked with the DOJ and various U.S. Attorney's offices throughout the nation, the FBI, the offices of numerous State attorneys general, local police authorities, and task forces focusing on areas such as corporate fraud and foreign currency fraud.

In addition to direct cooperation with domestic law enforcement and regulatory authorities, the Enforcement program also represents the Commission in a variety of domestic and international efforts, including task forces and working groups designed to keep market participants abreast of new developments in financial crimes and to coordinate governmental responses to common issues. Several examples of the efforts of the Enforcement program in this area follow:

- **Corporate Fraud Task Force.** By Executive Order, signed by President Bush on July 9, 2002, the CFTC was named a member of the Corporate Fraud Task Force. This task force was established with the objective of strengthening the efforts of DOJ, Federal, State, and local agencies to investigate and prosecute significant financial crimes, recover the proceeds of such crimes, and ensure just and effective punishment of those who perpetrate financial crimes.
- **Anti-Money Laundering (AML).** The Commission participates in domestic and international AML cooperative enforcement efforts. On the domestic front, the Commission is a member of the Money Laundering Strategy Working Group and the U.S. Treasury Department's Bank Secrecy Act Advisory Group. Internationally, the Commission has aided the U.S. delegation to the Financial Action Task Force on issues including efforts to combat global terrorist financing.
- **Telemarketing and Internet Fraud Working Group.** This Group consists of representatives from Federal, State, and international regulatory and criminal authorities.
- **Securities and Commodities Fraud Working Group.** The Securities and Commodities Fraud Working Group is a vehicle for public and private sector participants to discuss current trends in financial crime in the securities, futures, and option industries and to exchange ideas about enforcement techniques. The group, organized by the Fraud section of the Criminal Division of the DOJ, meets on a quarterly basis, and its members include criminal and regulatory authorities from State and Federal agencies and representatives from various exchanges and other SROs.

Proceedings. The Commission provides a forum for effectively and expeditiously handling customer complaints against persons or firms registered with the Commission at the time of the alleged wrongdoing or at the time the complaint is filed.

During FY 2005, 46 percent of the reparations complaints were disposed of within one year from the date the complaint was filed. The remaining complaints were not resolved within one year as a result of issues beyond the Commission's control. For example, parties requested



additional time for one or more of the following reasons: 1) to submit supplementation to their cases; 2) to prepare pleadings; 3) to complete extensive discovery documents; or 4) to deal with personal or professional responsibilities. (See measure 2.3.1.)

The Commission's administrative law judges (ALJs) are responsible for hearing and rendering decisions in administrative enforcement cases brought by the Commission against alleged violators of the CEA or related regulations. The Commission decided 23 administrative enforcement cases in FY 2005.

Opinions and Review. Through its Opinions program, the Commission drafts opinions and orders in matters appealed to the Commission. The Commission's jurisdiction in adjudicatory matters includes:

- Administrative cases prosecuted by the Enforcement program against alleged violators of the CEA or related regulations;
- Reparations cases brought by customers to recover monetary damages from industry registrants; and
- Adjudicatory actions taken by industry SROs.

Through mid-September 2005, the Commission issued 37 opinions and other orders (including orders issued pursuant to delegated authority), 19 of which were final dispositions of cases pending on the Commission's docket. Among other decisions, in an appeal from an exchange proceeding, the Commission affirmed the default judgment entered against a respondent who challenged a 10-year access denial imposed because he engaged in unlawful trading to cover a mistake in handling a customer order. The Commission rejected the argument that the sanction was unfair because the co-respondent in the exchange proceeding, who settled, faced no access denial. The Commission also found no error in the exchange's decision to impose an access denial period twice as long as the period recommended by the exchange's compliance officials, because the period imposed was permitted by exchange rules. *Caruselle v. NYMEX*, Docket No. 05-E-1 (June 21, 2005).

In another administrative enforcement case, the Commission appealed from the ALJ's refusal to impose a civil monetary penalty on the respondent. Upon review of the record, the Commission determined that it was unable to reliably determine the respondent's net worth and his

consequent capacity to pay a penalty. The Commission elected not to remand the case. Instead, the Commission issued an opinion in which it announced that it would conduct direct fact finding itself. The outcome was that the respondent paid a civil monetary penalty of \$200,000. *In re Nikkhah* (CFTC Mar. 25, 2005).

The Commission refused to find that a closely-held FCM, its owner and his wife violated speculative position limits. The owner, his family and several close friends traded profitably during a corn bull market. The Commission held that similarities in their trading were insufficient to establish either that the owner controlled his wife's trading or that an express or implied agreement existed among the owner and his daughters and friends, all of whom had substantial trading experience and independent financial resources. *In re Bielfeldt*, Docket No. 96-1 (CFTC Dec. 2, 2004) (affirming in part and reversing in part the initial decision, and dismissing the complaint).

Office of General Counsel. Through the litigation program, Commission staff represents the Commission in the U.S. District Courts and the Courts of Appeals and assists the Solicitor General in representing the Commission before the U.S. Supreme Court. Commission staff also monitors litigation of interest to accomplishing the Commission's mission, including the Commission's cooperation with other Federal financial regulators through the President's Working Group on Financial Markets and the President's Corporate Fraud Task Force.

The Commission succeeded in obtaining dismissal of one significant case before the U.S. Supreme Court. The result in that case, *R.J. Fitzgerald & Co. v. CFTC*, 125 S. Ct. 808 (Dec. 13, 2004) (Mem.), preserved the successful ruling obtained by the Commission in the U.S. Court of Appeals for the Eleventh Circuit in an important anti-sales fraud prosecution. The Eleventh Circuit held that a television commercial was fraudulent when its overall message suggested that profits of 200 to 300 percent could be gained by investing in options by looking at known and expected weather patterns. The Court held that the advertising overemphasized profit potential and downplayed the risk of loss. 310 F.3d 1321 (11th Cir. 2002).

Before U.S. Courts of Appeals, the Commission obtained favorable rulings upon a variety of issues. Foremost,



the Commission succeeded in demonstrating that it was substantially justified in defending the statutory registration scheme established under Section 4m of the CEA, *Taucher v. Brown-Hruska*, 396 F.3d 1168 (D.C. Cir. 2005), and in defending the mechanism for evaluating registration applications provided by Congress through Section 8(a) of the Act, *Hirschberg v. CFTC*, 414 F.3d 679 (7th Cir. 2005). The Commission also succeeded in the appellate courts in its defense of challenges brought against injunctions issued by district courts aimed at preventing sales solicitation fraud. *CFTC v. Wall Street Underground*, 128 Fed. Appx. 726 (10th Cir. 2005); *CFTC v. Fremer*, 128 Fed. Appx. 104 (11th Cir. 2005); *CFTC v. Gibraltar Monetary Corp.*, No. 04-13828-I (11th Cir. May 9, 2005).

In support of its oversight of the activities of SROs, the Commission succeeded on appeal in defending its affirmance of an exchange's handling of an altercation that arose at the exchange. *Piccolo v. CFTC*, 388 F.3d 387 (2nd Cir. 2005). In another matter, the Commission was not successful in persuading the Court of Appeals for the Seventh Circuit of the correctness of the Commission's interpretation of a core jurisdictional issue regarding the definition of a futures contract in *CFTC v. Zelener*, 373 F.3d 861 (7th Cir.), reh'g denied, 387 F.3d 624 (2004). The result in that case brought to the fore the need for legislative action to clarify the Commission's ability to combat fraud in the sale of foreign currency exchange investments.

In several cases before the U.S. District Courts, Commission staff defended the Commission's interests in the handling of records it collects while investigating possible violations of the CEA. One case, *In re Application of William R. Tacon*, Misc. No. 05MS00083 (D.D.C.), involved the Commission's defense of the statutory prescriptions application to the Commission's receipt of information. In another case, *In re Subpoena Issued to CFTC*, 370 F. Supp. 2d 201 (D.D.C. 2005), Commission staff continues to defend the Commission's interests where an issue of government-wide interest has been posed, specifically, whether the appellate court should recognize a federal common law right to withhold from third parties records pertaining to settlement under a federal "settlement privilege."

Commission staff represents the Commission in personnel cases before the district courts and before administrative agencies, such as the Equal Employment Opportunity

Commission and the Merit Systems Protection Board and represents the Commission in contract matters before the General Services Board of Contract Appeals.

Commission staff also monitors bankruptcy cases involving futures industry professionals and, as appropriate, assists courts, trustees, and customers in implementing special bankruptcy code provisions that pertain to commodity firms. In FY 2005, Commission staff analyzed the Commission's interests in 22 bankruptcy cases and formally appeared before various bankruptcy courts throughout the country to protect both the Commission's interest in recovering penalties owed due to market misconduct and the interest of public customers in having their funds recovered and returned in 12 such cases.

Finally, through its *amicus curiae* program, Commission staff supported the Commission in assisting the courts in resolving difficult or novel questions arising under the CEA or Commission regulations with the intent of making significant contributions to the development of consistent and accurate legal precedent. In FY 2005, the Commission participated in *Board of Trade of the City of New York v. Klein & Co. Futures, Inc.*, No. 00Civ.5563GBD (S.D.N.Y.), a case involving the rights and duties of parties subject to the Act upon the incidence of a customer's financial default.

Regulatory and Legislative Matters. In FY 2005, Commission staff continued to advise the Commission concerning the implementation of rules and regulations issued pursuant to the CFMA. Commission staff assisted the Commission in new regulatory initiatives to further carry out CFMA mandates, including providing regulatory relief to market intermediaries, such as amendments to the CFTC's Large Trader Reporting rules and revised FCM reporting requirements for risk-based capital.

The Commission consulted with staff of the U.S. Treasury and various Federal financial regulators to develop anti-money laundering regulations required under the USA PATRIOT Act, including in FY 2005, providing guidance to certain customers of CTAs and working with other agencies to complete information-sharing agreements.

During FY 2005, the Commission presented testimony before Congressional committees on the Commission's reauthorization.





Goal Three

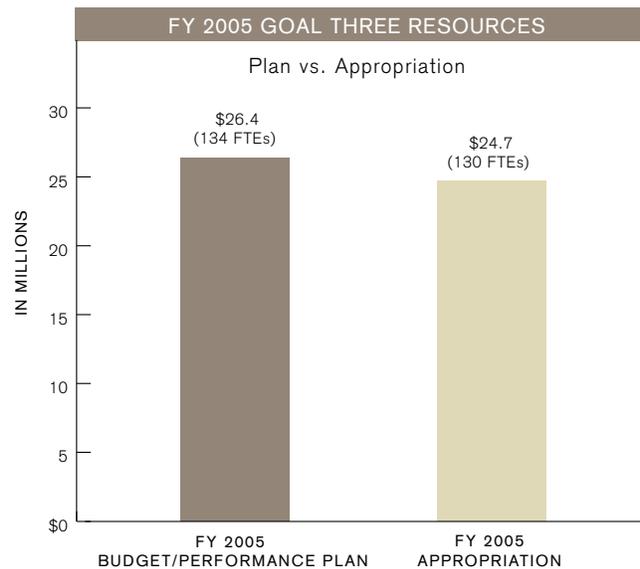
Ensure market integrity in order to foster open, competitive, and financially sound markets

Public Benefit:

The U.S. commodity futures markets must be protected from and free of abusive practices and influences to better operate and fulfill their vital role in the nation's economy, as well as the global economy. The CFTC works diligently to ensure that futures markets do function properly so that the marketplace may be used with confidence by the farmer who wishes to hedge his crop or feed, or the pension fund manager who desires to guarantee a set return on money entrusted for investment.

Resource Investment:

In FY 2005, the Commission requested \$26.4 million and 134 FTEs and was appropriated \$24.7 million and 130 FTEs for Goal Three.



Goal Three

Ensure market integrity in order to foster open, competitive, and financially sound markets.

HISTORY OF PERFORMANCE RESULTS³

OUTCOME OBJECTIVE 3.1

Clearing organizations and firms holding customer funds have sound financial practices.

PERFORMANCE MEASURES	FY 2003	FY 2004	FY 2005
Lost Funds			
Percentage decrease in number of customers losing funds	0%	0%	0%
Amount of funds lost	\$0	\$0	\$0
Number of rulemakings to ensure market integrity and financially sound markets	1	1	3
Percentage of self-regulatory organizations that comply with requirement to enforce rules	100%	100%	TBD

OUTCOME OBJECTIVE 3.2

Commodity futures and option markets are effectively self-regulated.

PERFORMANCE MEASURES	FY 2003	FY 2004	FY 2005
Percentage of intermediaries who meet risk-based capital requirements	100%	100%	100%
Percentage of clearing organizations that comply with requirement to enforce their rules	100%	100%	TBD

OUTCOME OBJECTIVE 3.3

Markets are free of trade practice abuses.

PERFORMANCE MEASURES	FY 2003	FY 2004	FY 2005
Percentage of exchanges deemed to have adequate systems for detecting trade practice abuses	100%	100%	100%
Percentage of exchanges that comply with requirement to enforce their rules	100%	100%	100%

³The performance metrics included in this document represent the best current estimate of Commission performance. Additional work is needed to devise better measures and valid current performance measures in order to effectively illustrate program success in meeting overall objectives.



OUTCOME OBJECTIVE 3.4

Regulatory environment is flexible and responsive to evolving market conditions.

PERFORMANCE MEASURES	FY 2003	FY 2004	FY 2005
Percentage of CFMA Section 126(b) objectives addressed	100%	100%	100%
Number of rulemakings, studies, interpretations, and guidance to ensure market integrity and exchanges' compliance with regulatory requirements	8	6	6
Percentage of requests for no-action or other relief completed within six months related to novel market or trading practices and issues to facilitate innovation	100%	100%	100%
Percentage of requests receiving CFTC responses for guidance and advice	90%	90%	90%



Return on Investment

The Commission's 2005 Annual Performance Plan supports four outcome objectives for Goal Three.

OBJECTIVE 3.1: NO LOSS OF CUSTOMER FUNDS BY DERIVATIVE CLEARING ORGANIZATIONS

FY 2005 Appropriation: \$5.9 Million

FY 2005 Results: Slightly above and on target. Measure 3.1.3 is "to be determined;" program staff have not completed its review and assessment to provide sufficient data to report on the percentages of derivatives clearing organizations that comply with core principles.

Number of Measures	Exceeded Goal	Met Goal	Did Not Meet Goal	To Be Determined or Not Available	Percent Meeting or Exceeding Goal
4	1	2	0	1	75%

PERFORMANCE MEASURES	FY 2005 PLAN	FY 2005 RESULTS
3.1.1 Lost Funds		
1) Percentage decrease in number of customers who lose funds	50%	0%
2) Amount of funds lost	\$0	\$0
3.1.2 Number of rulemakings to ensure market integrity and financially sound markets	1	3
3.1.3 Percentage of self-regulatory organizations that comply with requirements to enforce rules	100%	TBD

OBJECTIVE 3.2: NO LOSS OF CUSTOMER FUNDS BY SELF-REGULATORY ORGANIZATIONS

FY 2005 Appropriation: \$10.6 Million

FY 2005 Results: On target. Measure 3.2.2 is "to be determined;" program staff have not completed its review and assessment to provide sufficient data to report on the percentages of derivatives clearing organizations that comply with core principles.

Number of Measures	Exceeded Goal	Met Goal	Did Not Meet Goal	To Be Determined or Not Available	Percent Meeting or Exceeding Goal
2	0	1	0	1	50%

PERFORMANCE MEASURES	FY 2005 PLAN	FY 2005 RESULTS
3.2.1 Percentage of intermediaries who meet risk-based capital requirements	100%	100%
3.2.2 Percentage of clearing organizations that comply with requirement to enforce their rules	100%	TBD



OBJECTIVE 3.3: MARKETS FREE OF TRADE PRACTICE ABUSES

FY 2005 Appropriation: \$5.1 Million

FY 2005 Results: On target.

Number of Measures	Exceeded Goal	Met Goal	Did Not Meet Goal	To Be Determined or Not Available	Percent Meeting or Exceeding Goal
2	0	2	0	0	100%

PERFORMANCE MEASURES	FY 2005 PLAN	FY 2005 RESULTS
3.3.1 Percentage of exchanges deemed to have adequate systems for detecting trade practice abuses	100%	100%
3.3.2 Percentage of exchanges that comply with requirement to enforce their rules	100%	100%

OBJECTIVE 3.4: REGULATORY ENVIRONMENT IS FLEXIBLE AND RESPONSIVE TO EVOLVING MARKET CONDITIONS

FY 2005 Appropriation: \$3.1 Million

FY 2005 Results: Slightly above and on target

Number of Measures	Exceeded Goal	Met Goal	Did Not Meet Goal	To Be Determined or Not Available	Percent Meeting or Exceeding Goal
4	1	2	0	1	75%

PERFORMANCE MEASURES	FY 2005 PLAN	FY 2005 RESULTS
3.4.1 Percentage of CFMA Section 126(b) objectives addressed	100%	100%
3.4.2 Number of rulemakings, studies, interpretations, and guidance to ensure market integrity and exchanges' compliance with regulatory requirements	2	6
3.4.3 Percentage of requests for no-action or other relief completed within six month related to novel market or trading practices and issues to facilitate innovation	N/A	100%
3.4.4 Percentage of total requests receiving CFTC responses for guidance and advice	90%	90%



Program Contributions to Strategic Goal Three:

Market Surveillance. The Commission staff completed two rule enforcement reviews of SRO compliance programs. Periodic review of SRO compliance programs is a component of the program's oversight activity to promote and enhance effective self-regulation and ensure that SROs enforce compliance with their rules.

One of the rule enforcement reviews completed during FY 2005 was a review of OneChicago's market surveillance, audit trail, trade practice surveillance, disciplinary, and dispute resolution programs. The other rule enforcement review completed during FY 2005 was a review of the CBOT's audit trail, trade practice surveillance, disciplinary, and dispute resolution programs. Market Compliance staff found that both OneChicago and CBOT maintain adequate programs with respect to the areas reviewed.

The Commission's review of exchange rules is a key aspect of the statutory framework for self-regulation. Market and Product Review subprogram staff review exchange rule submissions with the goals of: 1) maintaining the fairness and financial integrity of the markets; 2) protecting customers; 3) accommodating and fostering innovation; and 4) increasing efficiency in self-regulation consistent with the Commission's statutory mandates. To these ends, staff reviewed 262 exchange rule submission packages and, within those packages, staff reviewed 1,237 new rules and rule amendments. (See measures 3.2.1, 3.2.2, 3.3.1 and 3.3.2.)

Commission staff also work to facilitate industry innovations and new trading methods and market structures, thereby meeting the Commission's objective of promoting and enhancing effective self-regulation and competition. During FY 2005, staff was involved in a number of significant matters including issues related to new exchanges and exempt markets, exchange mergers, novel trading procedures and contract designs, and new automated trading systems.

Issuing Exemptive, Interpretive, and No-Action Relief. The Commission is responsible for providing exemptive, interpretive, or other relief to facilitate the continued development of an effective, flexible regulatory environment responsive to evolving market conditions. For

example, in FY 2005, the Commission issued an interpretive letter to the Australian Wheat Board (AWB) which found that AWB's proposal to have its wholly-owned subsidiary, AWB (USA), Inc., conduct over-the-counter trading, both as an offeror and an offeree of agricultural trade option contracts, fell within the exemptive provisions of regulation 32.13(g). The Commission continued the policy initiated in FY 1999 of issuing no-action letters in response to requests by foreign boards of trade to permit placement of electronic terminals in the U.S. without requiring contract market designation for those boards of trade. In FY 2005, the Commission issued a no-action letter to the European Energy Exchange and issued amended no-action letters to Eurex Deutschland and Eurex Zurich, Ltd., to permit, subject to Commission approval, the clearing of Euro products traded on the two exchanges to be cleared by the Clearing Corporation (CCorp) as a special clearing member of Eurex Clearing AG. In FY 2005, the Market and Product Review subprogram also issued an amended no-action relief letter to the Sydney Futures Exchange Limited (SFE) to permit non-clearing SFE members that carry U.S. customer accounts to place SFE terminals with those customers, conditioned on the non-clearing member giving up those trades to a guaranteeing FCM or rule 30.10 firm.

In FY 2005, the Commission issued a no-action letter to U.S. Futures Exchange, LLC (Eurex U.S.) to afford it relief from the Commission's default contract reporting levels for futures and option contracts so that Eurex U.S.'s new 3-Year U.S. Treasury Notes (3-Year T-Notes) contract would be subject to a reporting level of 750 contracts, rather than the default level of 25 contracts. (Subsequently, the Commission adopted a rulemaking formally establishing a 750-contract reporting level for 3-Year T-Notes.) The no-action relief eased the burden of reporting on market participants while preserving the Commission's ability to effectively surveil trading in 3-Year T-Note contract. The Commission also continued the policy initiated in FY 1999 of issuing no-action letters in response to requests by foreign boards of trade to permit placement of electronic terminals in the U.S. without requiring contract market designation for those boards of trade. In FY 2005, the Division's Chief Counsel Office



issued three new no-action letters to the European Energy Exchange, the Winnipeg Commodity Exchange, Inc. and Euronext Amsterdam N.V. In addition, amended no-action letters were issued to Eurex Deutschland (Eurex) and the SFE. The letter to Eurex permitted, among other things, participants of CCorp to carry positions in Eurex products pursuant to the Euro-link agreement between CCorp and Eurex Clearing. On the other hand, the letter to SFE permitted the exchange to make its electronic trading and order matching system, known as SYCOM®, available to non-exchange participants in the U.S.

The Commission responded to a high number of formal and informal requests for guidance concerning the application of regulatory requirements to specific transactions, new products, and market circumstances. Staff issued 170 responses to written requests, including electronic responses, from members of the public and the regulated industry to provide guidance concerning the application of Commission regulations and to provide exemptions. Staff also responded to 1,773 telephone inquiries concerning the application of Commission requirements to commodity professionals. These responses aided market participants and the public by providing guidance concerning the manner in which they may conduct their activities to comply with relevant requirements and by granting relief from requirements where application of the rules would not serve the public interest.

Financial and Segregation Interpretation No. 10 (Interpretation No. 10), issued in 1984, effectively permitted customer margins to be deposited at a bank in a safekeeping or custodial account (otherwise known as “safekeeping account” or “third-party custodial account”), in lieu of posting such funds directly with a FCM, without being deemed to violate the customer funds segregation provisions of Section 4d(a)(2) of the CEA and related Commission regulations. Through analysis and discussions with industry participants, it was determined that third-party custodial accounts are no longer necessary or justified in light of developments since the issuance of Interpretation No. 10 and may present significant cost and burdens for market participants. Accordingly, the Division of Clearing and Intermediary Oversight (DCIO) withdrew Interpretation No. 10 in May 2005 and issued an amended

Interpretation No. 10-1 to prohibit FCMs from depositing, holding, or maintaining margin funds for customer accounts in third-party custodial accounts, with limited exception for FCMs not eligible to hold the assets of their RIC customer (i.e., due to their affiliation with the RIC or its adviser). The ban against the use of third-party accounts is intended to prevent potential delay or interruption in securing required margin payments that, in times of significant market disruption, could magnify the impact of such market disruption and impair the liquidity of other FCMs and clearinghouses. (See measures 3.4.3 and 3.4.4.)

Fostering Sound Business Practices: Oversight of SROs, Market Intermediaries, and DCOs. A key aspect of assuring effective self-regulation is oversight by the Commission of SRO programs to assure compliance by their members with customer and market protection standards. Toward this end, the DCIO oversees, reviews, and reports to the Commission concerning statutorily required self-regulatory programs directed at maintaining the financial integrity of the markets and deterring improper sales practices and other wrongful conduct.

The DCIO staff administer a financial surveillance and audit program that buttresses periodic audit, daily financial surveillance, and other self-policing programs administered by the exchanges and NFA to promote and enhance effective self-regulation of the commodity futures and option markets. The objective of this program is to assure sound financial practices of DCOs and firms holding customer funds. The effort includes oversight of financial compliance programs of SROs and direct quality control audits to assess the efficacy of their programs. The oversight of SRO programs is necessary to ensure that SRO member firms are properly capitalized and maintain appropriate risk management capabilities, and that customer funds are held in segregation by appropriate custodians and are protected from misappropriation.

This oversight function of the Clearing and Intermediary Oversight program has taken on increased importance with the Commission’s new regulatory framework under the CFMA. The CFMA defined a new category of registered entity, DCOs, and set forth certain core principles governing such entities. Similar to the approach of other Federal financial regulators and certain overseas financial



supervisors – indeed, in close consultation with several such peers – the DCIO program has begun enhancing its supervision of exchanges, clearinghouses, and other SROs with risk-based examination cycles and risk-focused reviews. Both the scheduling and scope of the DCIO’s supervisory reviews are now based on careful analysis of the underlying risks to which an institution is exposed and the controls that it has in place to address those risks.

The Major Review unit of the DCIO was created to plan, coordinate, schedule, monitor, and assess major risk-focused reviews. During FY 2005, program staff initiated a review of the Minneapolis Grain Exchange (MGE) in its capacity as a DCO registered with the Commission pursuant to Section 5b of the CEA. The purpose of the review was to determine whether MGE had demonstrated compliance with the core principles for DCOs set forth in Section 5b(c)(2) of the Act and with Part 39 of the Commission’s Rules. While program staff looked initially at compliance with the core principles, generally its risk assessment and scope-setting phases effort led to a focus on MGE’s abilities to demonstrate fulfillment of its responsibilities as a risk-managing central counterparty. The DCIO staff is currently preparing a report of its review for Commission consideration.

The DCIO staff performed 11 audits (one DCO and 10 FCMs) in FY 2005 to test compliance with the Commission’s financial requirements for the safekeeping of customer funds. In addition, program staff processed about 2,700 financial reports filed by registrants. As a result of on-going program efforts such as these, no regulated customer funds were lost in FY 2005, thereby meeting the program’s objective of ensuring sound financial practices of clearing organizations and firms holding customer funds. (See measures 3.1.1, 3.1.2 and 3.1.3.)

Ensuring a Flexible and Responsive Regulatory Environment. In FY 2005, the DCIO supported the Commission’s on-going regulatory reform program, as well as actions required by or appropriate to the implementation of the CFMA. In April 2005, the Commission issued an order registering AE Clearinghouse as a DCO. AE Clearinghouse provides an innovative method for clearing transactions executed on an exempt board of trade or over-the-counter. In October 2004, the Commission issued an order

pursuant to 4d of the CFMA permitting CCorp, a DCO, and its member FCMs to clear trades executed on Eurex, a foreign market, and commingle such positions and associated funds with other positions and funds required to be segregated. The Commission also issued an interpretation clarifying the treatment in insolvency of funds held in segregation pursuant to such an order. In December 2004, the Commission issued an amended order permitting HedgeStreet, a DCO, to clear additional products. In September 2005, the Commission issued an order pursuant to 4d permitting New York Mercantile Exchange (NYMEX), a DCO, and its member FCMs to clear trades executed on NYMEX Europe, an affiliated exchange located in London, and commingle such positions and associated funds with other positions and funds required to be segregated.

The DCIO staff prepared six rulemaking actions during the fiscal year. Two of these were corrections of previously published rule changes, one of which related to closing out of offsetting positions and the other to delegation of authority to the DCIO division director. One order expanded the authority of NFA to exempt certain firms that act as FCMs and that are regulated by multiple foreign futures authorities or foreign SROs from registration under the CEA in accordance with guidelines set forth in the order by the Commission. A rule change simplified the signature requirements for acknowledgment by non-institutional customers of FCMs and IBs of required risk disclosure statements and consent for the firms to take the opposite side of customer trades. An interpretation by the predecessor of the DCIO regarding segregation of customer funds was amended to prohibit the use of so-called third-party safekeeping accounts, except in cases where customers were required by the SEC to use such accounts. Finally, rules were issued that further expanded the range of permissible investments of customer funds by FCMs and DCOs subject to appropriate safeguards.

In September 2005, the Commission published in the *Federal Register* a notice of proposed rulemaking to define the term “client” as it relates to a CTA. The proposed definition provides that a “subscriber” is one type of “client,” thus clarifying apparent inconsistencies in the Act and in the Commission’s regulations concerning the advisees of CTAs. The proposal also clarifies the Commission’s



longstanding view that its antifraud authority extends to all CTAs, irrespective of whether they provide advice on a personalized or non-personalized basis. (See measures 3.4.1 and 3.4.2.)

Remote Clearing. In a matter of first impression, (commonly referred to as “remote clearing,”) a foreign firm requested to become a full clearing member of a combined DCM and DCO to clear trades only for non-U.S. located customers without first registering under the Act. The DCIO staff researched the legal question as to whether a remote clearing foreign firm that would clear trades only for non-U.S. located customers would be required to register with the Commission as an FCM, and addressed the material policy issues of remote clearing with respect to both customer protection and the financial integrity of the markets. After discussions with staff, the foreign firm decided to become registered with the Commission as an FCM.

Foreign Currency. The DCIO continues to work with the Division of Enforcement and NFA staff regarding retail foreign currency trading by FCMs and their affiliates. NFA submitted additional rules concerning retail foreign currency on August 22, 2005, which the Commission approved on September 15, 2005. These rules are intended to address on-going problems in the off-exchange retail forex market by allowing NFA to impose stricter net capital requirements on certain persons registered as FCMs engaging in retail forex transactions, and to extend certain antifraud and customer protection rules to a greater number of off-exchange retail forex transactions, where NFA members act as intermediaries, but the counterparty is not an NFA member. Members are also required to provide customers with information about NFA’s registrant database (BASIC) so that they may review the registration status and disciplinary history of those who solicit them.

The DCIO staff has considered ways to provide additional formal guidance regarding compliance and registration issues pertaining to entities involved in retail foreign currency trading and has met with other divisions to discuss their concerns regarding issues that may be raised in such an advisory. Staff has also discussed issues with NFA concerning NFA examinations and required adjusted net capital for firms engaged in retail forex transactions.

Foreign Futures and Option Transactions. The Commission also furthered the development of the offer and sale of foreign futures and option transactions (U.S. customers trading on non-U.S. markets) in FY 2005. The Commission issued an order to NFA authorizing NFA to confirm exemptive relief to certain firms acting in the capacity of an FCM. Specifically, FCMs that are subject to regulation by a foreign futures authority or that are members of a foreign SRO in a particular jurisdiction to which an order under Commission Rule 30.10 has been issued, notwithstanding that such firms may be subject, in part, to joint regulation by a second regulator or SRO in another jurisdiction. These firms are referred to in the order as CBFBs. The Commission previously had authorized NFA to confirm exemptive relief solely to firms subject to regulation by a single foreign futures authority or that are members of a foreign SRO. This order extends the scope of that authority. Specifically, the Commission authorized NFA to grant exemptive relief to any CFBF that solicits or accepts orders (and accepts money, securities or property to margin the trades that result or may result therefrom) from U.S. foreign futures and options customers and that is fully regulated, in the aggregate, by a host and home country regulator, each of which has received a Rule 30.10 Order from the Commission, or is organized in a home country and operating pursuant to certain European Union directives governing cross-border activity (known, collectively, as the European Passport) from a branch located in a host country where the regulator or SRO has received a Rule 30.10 Order, notwithstanding that the Commission has not issued a Rule 30.10 Order to the home country regulator. The Commission determined further to authorize NFA to maintain records pertaining to the functions described in this order and to serve as the official custodian of those Commission records.

Hedge Funds. During FY 2005, the DCIO monitored the SEC’s implementation of new rules requiring registration of hedge fund advisers under the Investment Advisers Act of 1940.

Security Futures Products and Cooperation with the SEC. The CFMA directs the Commission and the SEC to implement a joint regulatory framework for SFPs and narrow-based stock index futures. As part of the on-going SFP



supervisory and oversight process, the Commission and the SEC signed a Memorandum of Understanding (MOU) to clarify the ability of each agency to conduct inspections of notice-registered intermediaries, exchanges, and limited purpose national securities associations. The MOU provides that the CFTC and SEC will notify each other of any planned examinations, advise the other of reasons for an intended examination, provide each other with examination-related information, and conduct examinations jointly, if feasible. The agencies will notify each other of significant market issues and will share trading data and related market information.

The DCIO permitted NFA in FY 2004 to postpone indefinitely updating the Series 3 and Series 30 examinations to include questions on SFPs. Staff has discussed with NFA and the National Association of Securities Dealers how to accomplish eventual updating of the examinations, but, for the time being, salespersons will be permitted to continue to offer SFPs following the taking of a Web-based training module. The SEC is in accord with this approach.

Trade Practice. The legislative history of the CEA notes that one of the fundamental purposes of the Act is to ensure fair practices and honest dealing in the futures market and to control those forms of speculative activity that demoralize the market to the detriment of producers, consumers, and the markets. Consistent with Congress' mandate, the Commission periodically brings trade practice cases to address a variety of unfair, abusive, or deceptive ploys by traders to avoid exposing their orders to market risk. Such actions can create non-competitive prices in the marketplace and have the potential to harm public customers, producers, and others. Improper trade practices include a variety of activities, including trading done in violation of exchange rules, such as trading ahead of a customer order, wash trading, accommodation trading, and fictitious trading. During FY 2005, the Commission filed six enforcement actions in this program area and also achieved significant litigation results in one action filed in this practice area during previous fiscal years. (See Appendices.)

Financial, Supervision, Compliance and Record-keeping. During FY 2005, the Commission filed one enforcement action in this program area and also achieved significant litigation results in two actions filed in this practice area during previous fiscal years. (See Appendices.)

Statutory Disqualifications. During FY 2005, the Commission filed five enforcement actions in this program area. (See Appendices.)

International Cooperative Enforcement. The Commission continues to coordinate enforcement activities with foreign authorities. During FY 2005, the Division of Enforcement made 106 requests for assistance, and it received 18 requests from authorities in foreign jurisdictions. The Commission was successful in obtaining assistance, including bank records, in several jurisdictions where we did not have prior cooperative relationships.

Enforcement also has devoted time and resources to matters involving allegations that persons or entities have committed fraud or other misconduct in their cross-border activities. Such misconduct can adversely affect U.S. firms as well as customers located in the U.S. and overseas.

IOSCO's Screening and Approving MOU Applicants. Commission staff, as members of a Multilateral Memorandum of Understanding Concerning Consultation, Cooperation and the Exchange of Information (MMOU) Verification Team, evaluated the applications of five IOSCO members to become signatories to the MMOU. The Commission also is a member of the Screening Group which makes recommendations to a decision making body of IOSCO concerning whether to accept or reject specific MMOU applications.

During FY 2005, the Commission continued its work on the IOSCO MMOU. The MMOU is an important and meaningful undertaking for regulators to expand cooperation by establishing specific minimum standards for securities and futures regulators in the area of information-sharing. During FY 2005, Belgium, which the Commission did not have an information-sharing arrangement with previously, became a signatory to the MMOU.

Standing Committee 4. During FY 2005, staff also continued to participate in the Standing Committee on Enforcement and Information-Sharing (SC4) of the



Technical Committee of IOSCO. SC4 considers issues and formulates recommendations relating to international assistance in the detection, investigation, and prosecution of securities and futures violations.

Standing Committee 5. Commission staff also continued to participate in IOSCO's Standing Committee 5 (SC5) on Investment Management. Throughout 2005, SC5 continued to consider and issue reports on several topics of importance to collective investment vehicles.

Office of General Counsel (OGC). OGC continued its review of requests for no-action relief to allow the offer and sale of foreign exchange-traded foreign stock index futures contracts in the U.S. In FY 2005, OGC issued three no-action letters for five of these foreign exchange-traded foreign stock index futures contracts.

OGC also advised the Commission with respect to legislative provisions affecting the Commission contained in the Domenici-Barton Energy Policy Act of 2005, which included provisions designed to clarify the Commission's exclusive jurisdiction over futures and option markets and trading data. Furthermore, OGC advised the Commission on the Energy Policy Act's requirement that the Commission and the FERC enter into an information-sharing arrangement.

International Policy. The Commission formulates international policy by: 1) coordinating with foreign regulatory authorities; 2) participating in international regulatory organizations and forums; and 3) providing technical assistance to foreign governmental bodies. In FY 2005, the Commission contributed to this effort by:

- Coordinating Commission representation in the Council of Securities Commissions of the Americas (COSRA), including contributing a paper on the benefits of futures trading to the securitization of small business loans and participating on ways to advance COSRA's regional technical assistance and training initiatives;
- Providing expertise to the Committee of European Securities Regulators (CESR) related to their inquiry into acceptable market practices for commodity markets as part of its deliberations on possible expansion of the Investment Services Directive to commodity markets;
- Promoting access to markets by organizing with CESR a round-table for U.S. and European futures industry

participants to discuss practical operational issues that most affect their conduct of trans-Atlantic business in exchange-traded derivatives and by developing a work program to review issues relating to enhanced transparency, clarity of regulatory developments and simplified access or recognition procedures;

- Providing assistance to the Financial Sector Assessment Program of the World Bank and International Monetary Fund;
- Coordinating the Commission's provision of representations and regulatory information to regulatory authorities in Australia, Austria, Germany, Italy, the Netherlands, Spain and Switzerland that supported the recognition of three U.S. futures exchanges electronic trading systems;
- Coordinating the Commission's comments to the U.S. Treasury on various position papers including U.S.-India and U.S.-China dialogue;
- Participating in and advising the Toronto Centre on leadership with respect to securities and derivatives sector programs; and
- Providing technical assistance to foreign regulators through visits with staff at the Commission by 89 foreign persons representing 14 foreign jurisdictions, two on-site visits by Commission staff to foreign jurisdictions, and a week-long seminar in Chicago that examined the techniques used to promote market, firm, and customer protections.



Methodology for Collecting, Maintaining, and Analyzing Performance Data

Market Oversight

Statistics concerning the large trader and exchange data collection systems are computer-generated based on the number of actual reports processed. Similarly, figures on numbers of market trading reports prepared and new contract and rule change filings analyzed and completed are derived from computer records. Performance data from regional offices and headquarters are collected quarterly and combined into an overall report reflecting performance data included in the *Annual Performance Plan*. Trends in volume, open interest, and number of contracts approved are used to project workload statistics for future periods. Compliance factors, such as audits and letters to traders and reporting firms, are reviewed in the context of total reports processed for anomalous relationships. The number of market surveillance reports and special reports are viewed in the context of the number of markets trading and analyses that are presented at Commission meetings. These reports and comparisons with indicators from previous periods are used to verify data accuracy.

The Market and Product Review subprogram calculates the performance data included in the Commission's *Annual Performance Report* and *Annual Performance Plan* by querying its automated databases: the Filings (FILAC) system and the Designation and Rule Tracking (DART) systems. For each new exchange, these systems record product, rule submission, information on the date re-

ceived, the submission's ultimate disposition, the date of disposition, and the processing time.

During FY 2004 and FY 2005, the Division of Market Oversight (DMO) coordinated with DCIO staff and the Office of Information Resources Management (OIRM) to develop a comprehensive database system for organizations (trading facilities, clearing organizations, etc.), foreign terminal no-action relief, products, and rule amendments. This system ultimately will replace the DART system and provide a more efficient and effective method for tracking the processing of various filings received by DMO and DCIO.

The Market Compliance subprogram's performance data are continuously collected from regional and headquarters staff and are maintained at headquarters for each performance category. The adequacy of SROs' sanctions and a comparison of sanctions across all exchanges are conducted quarterly by regional staff and are also maintained at headquarters.

Clearing and Intermediary Oversight

Compliance and Registration. The Compliance and Registration subprogram compiles data on discrete events, such as letters written, rules promulgated or revised, and RWG meetings held. It should be noted that statistics on numbers of letters issued or rules promulgated may not reflect the complexity of any particular matter or the resources necessary to address one issue versus another

issue. In addition, matters commenced in one fiscal year may overlap into, and be completed during, a subsequent fiscal year, resulting in some imprecision in statistical measures for a given fiscal year. Finally, the timeliness of a response is affected by the speed with which a requester provides additional information sought by staff and the length of time required by other Commission divisions or offices to review a draft response (factors outside the control of the Compliance and Registration subprogram).

Audit and Financial Review. Each branch of the Audit and Financial Review subprogram prepares a monthly report that includes statistics for those projects that can be reported on a numerical basis and also describes special projects, enforcement support, and all other noteworthy matters that staff have worked on during the month. Statistical summaries are also prepared on a quarterly basis.

Clearing Policy. The Clearing Policy subprogram maintains an on-going status report of current and completed projects. Separately, the Commission is close to completion of development of an electronic database to track all exchange and clearinghouse rule filings.

Enforcement

The Enforcement program tracks several types of performance data. For example, the number of investigations and cases opened, closed, case type (*e.g.*, fraud, manipulation, etc.), results obtained, and matters pending is collected and tabulated on a monthly basis and at the end of each fiscal year. Case status information is then cross-checked against status reports submitted by staff to the Office of the Director of the Enforcement program. This information is adapted for use in performance reporting (*i.e.*, individual matters are identified by the goals and activities under which they most reasonably fall).

Other data that are routinely tracked and then adapted for use in performance reporting include sanctions assessed in enforcement matters. In enforcement cases, sanctions can be assessed by resolution of: 1) Commission ALJs; 2) the Commission in settlement or on appeal of an ALJ's decision; and 3) Federal district court actions. Upon final disposition of the enforcement action, unsatisfied judgments are referred to the U.S. Treasury or the DOJ as appropriate for collection.

Finally, additional data tracked by the Enforcement program particularly data reflecting investigation and litigation tasks come directly from the headquarters units and regional offices performing the work. The Enforcement staff from each subprogram and regional office submit monthly status reports on all pending matters. In conjunction with these monthly submissions, staff are required to fill out an electronic form that provides specific information for each matter. While every effort is made to ensure that the data obtained from the investigation and litigation teams is accurate, the integrity of this data is ultimately and primarily the responsibility of the reporting teams.

Office of Proceedings

The Office of Proceedings uses "Repcase," an integrated computerized case tracking system, to collect, maintain, and analyze performance information for each reparations case. The reparations case reports are separated into two sections: complaints and hearings. The data and information collected in the complaints section consist of the number of cases pending on the first day of the month, the number of cases received during the month, the number of cases disposed of in complaints, and the number of cases pending at the end of the month. The data and information collected for the hearings section consist of the number of cases pending with an ALJ or judgment officer (JO) at the beginning of the month, the number of cases assigned during the month (including remands, reassignments, and motions to vacate), the number and type of cases disposed of during the month, and the number of cases pending with each ALJ or JO at the end of the month.

A separate database, Administrative Enforcement Case Tracking system, is used to track administrative cases, (*e.g.*, administrative/enforcement, exchange, statutory disqualification, and Commission review cases). The Administrative Enforcement Case Tracking system records the number of cases received during the month, the number and type assigned during the month, and the number and type disposed of during the month. Case status information is checked on a monthly basis against status reports submitted by the ALJs, JOs, and proceedings clerk to the director of the Office of Proceedings. This information is adapted for use in performance reporting.



Office of the General Counsel

OGC uses Repcase to collect, maintain, and analyze performance information for each reparations, enforcement, exchange review, and NFA case on appeal to the Commission. Statistical data is collected and reported by the total number of: 1) Cases resolved (*e.g.*, final disposition, remand, interlocutory disposition, and miscellaneous disposition); 2) matters received (*e.g.*, merits appeals, interlocutory appeals, and miscellaneous); 3) matters pending; and 4) drafts pending before the Commission.

OGC collects and maintains case data on an on-going basis. A legal program assistant uses this information to prepare periodic reports, which are used by management to monitor and analyze all cases on appeal to the Commission.

Biweekly Report. At the end of each biweekly period, the legal program assistant prepares a report for the General Counsel's signature for submission to the Chairman. The information reported includes significant activity (*e.g.*, legislative, regulatory, litigation-related, and opinions-related) in the office that occurred during that period.

Monthly Opinions Report. At the end of each month, the legal program assistant prepares a report for the General Counsel's signature. The information reported includes all activity (*e.g.*, disposition of cases, matters received, and matters pending) in the Opinions program that occurred during the month.

Quarterly Report. At the end of each quarter, the Deputy General Counsel for Opinions and Review prepares a report to the Commission outlining the status of cases pending on the Commission's docket.

Annual Report. At the end of each fiscal year, the legal program assistant prepares a statistical summary that shows activity in the program during the fiscal year. The report lists by category the number of matters received, Commission orders and opinions issued, and the number of cases pending at the end of the year. All issued opinions and orders are maintained in binders filed alphabetically, monthly, quarterly, and annually.

In preparing these reports, the legal program assistant reviews the statistical data provided by the Repcase tracking system as well as issued opinions and orders maintained in the binders. This staff member also maintains a separate tracking system of the cases on appeal,

which serves as a check against the data provided by the automated tracking system. All reports are reviewed and approved by the General Counsel and/or Deputy General Counsel for the Opinions and Review section.

Executive Direction & Support

Office of Information Resources Management. OIRM acts on the basis of the *CFTC Strategic Plan* and direction from the Executive Management Council. Performance data is collected by comparing the products actually delivered against the requirements identified through the strategic planning of Commission priorities. The resources used to deliver products based on Commission priorities are recorded in the Commission time and attendance data or equivalent OIRM internal records for internal FTEs and the Commission's financial management system or equivalent OIRM internal records for purchased resources. The Commission's technology investment priorities are reviewed through periodic Investment Review Board and Technology Review Board sessions involving key technical and business stakeholders. Analysis of performance data involves comparison of resources expended on projects with the planned expenditures to the products delivered with the products planned.



FINANCIAL SECTION



“ We continue to strive for excellence in the financial management of the Commission as illustrated throughout this Performance and Accountability Report. ”

—MARK CARNEY, CHIEF FINANCIAL OFFICER

A Message From the Chief Financial Officer

From the Chief Financial Officer

The *Performance and Accountability Report* for FY 2005 presents, to the Administration and the public, the status of the CFTC's program performance and fiscal operations. This document is the principal report produced by the Commission delineating our improvements and progress for this year. The Commission recognizes the importance of public disclosure and accountability to the Administration, to Congress, and to the American taxpayer. This *Performance and Accountability Report* is a demonstration of our commitment to fulfill our fiduciary and reporting responsibilities.

I am pleased to present the CFTC's financial statements for FY 2005 as a part of this report. For the first time, an independent public accounting firm, KPMG LLP, selected by our Inspector General, issued an unqualified or "clean" opinion on the Commission's consolidated financial statements, which is the best possible audit result.

The financial statements fairly present the Commission's financial position and were prepared in accordance with standards developed by the Federal Accounting Standards Advisory Board and accounting principles generally accepted in the U.S. These statements are presented in the format required by the OMB and the Government Management Reform Act of 1994.

We continue to strive for excellence in the financial management of the Commission as illustrated throughout this *Performance and Accountability Report*. The Commission continues its efforts to correct our four reportable conditions.



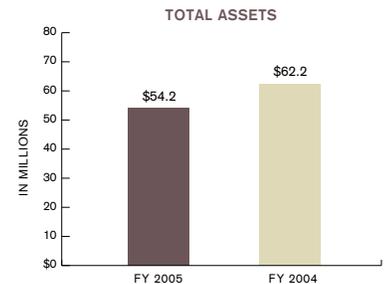
Mark Carney
Chief Financial Officer

November 15, 2005

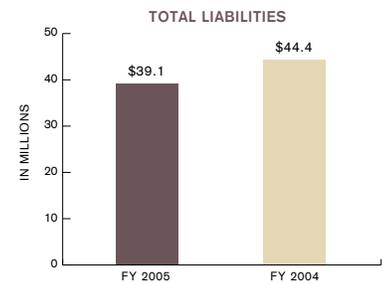


Financial Summary

At End of Year	% Change 2005/2004	2005	2004
CONDENSED BALANCE SHEET DATA			
Fund Balance with Treasury	-11%	\$ 23,464,887	\$ 6,304,227
Property and Equipment	292%	1,919,650	489,638
Accounts Receivable	476%	185,927	32,263
Other (Custodial)	-19%	28,663,845	35,402,939
TOTAL ASSETS	-13%	\$ 54,234,309	\$ 62,229,067

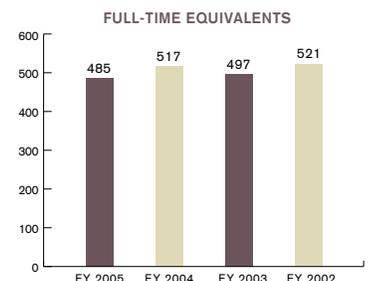
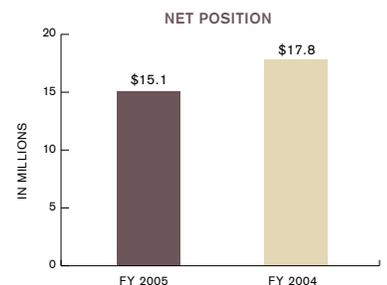


FECA Liabilities	-11%	\$ 629,800	\$ 709,034
Payroll, Benefits and Annual Leave	14%	8,082,514	7,079,766
Contingent & Deposit Fund Liabilities	-89%	20,094	182,426
Accounts Payable	65%	1,692,411	1,025,643
Custodial Liabilities	-19%	28,663,845	35,402,939
Total Liabilities	-12%	\$ 39,088,664	\$ 44,399,808
Cumulative Results of Operations	-24%	(3,939,565)	(5,199,126)
Unexpended Appropriations	-17%	19,085,210	23,028,385
Total Net Position	-15%	15,145,645	17,829,259
TOTAL LIABILITIES AND NET POSITION	-13%	\$ 54,234,309	\$ 62,229,067



FULL-TIME EQUIVALENTS

Market Oversight	-3%	99	102
Clearing & Intermediary Oversight	-10%	62	69
Chief Economist	-11%	8	9
Enforcement	-6%	135	144
Proceedings	-7%	13	140
General Council	-6%	32	34
Chairman/Commissioners	-7%	42	45
Executive Direction & Support	-6%	94	100
TOTAL FULL-TIME EQUIVALENTS	-6%	485	517



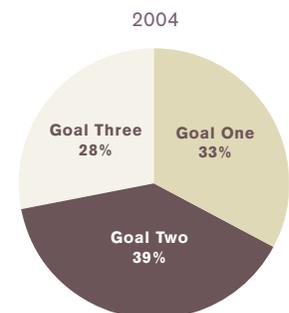
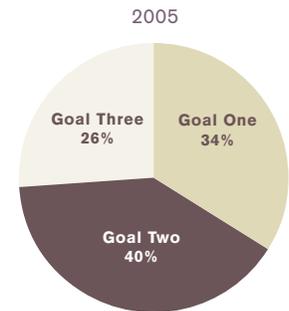
For the Year	% Change 2005/2004	2005	2004
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STATEMENT OF NET COST

Total Cost	4%	\$ 100,412,029	\$ 96,244,924
Earned Revenue	91%	(114,705)	(60,147)
TOTAL NET COST OF OPERATIONS	4%	100,297,324	96,184,777

NET COST BY STRATEGIC GOAL

Goal One - Economic Utility	9%	\$ 34,101,090	\$ 31,402,406
Goal Two - Market User and Public	5%	40,118,930	38,325,786
Goal Three - Industry	-1%	26,077,304	26,456,585
	4%	\$ 100,297,324	\$ 96,184,777



Limitations of Financial Statement

Management has prepared the accompanying financial statements to report the financial position and operational results for the CFTC for Fiscal Years 2005 and 2004 pursuant to the requirements of Title 31 of the U.S. Code, section 3515(b).

While these statements have been prepared from the books and records of the Commission in accordance with GAAP for Federal entities and the formats prescribed by OMB Circular A-136, *Financial Reporting Requirements*, these statements are in addition to the financial reports used to monitor and control budgetary resources, which are prepared from the same books and records.

The statements should be read with the understanding that they represent a component of the U.S. Government, a sovereign entity. One implication of this is that the liabilities presented herein cannot be liquidated without the enactment of appropriations, and on-going operations are subject to the enactment of future appropriations.

Principal Financial Statements

Commodity Futures Trading Commission

BALANCE SHEETS

As of September 30, 2005 and 2004

	2005	2004
ASSETS		
Intragovernmental:		
Fund Balance with Treasury (Note 3)	\$ 23,464,887	\$ 26,304,227
Accounts Receivable (Note 4)	175,595	22,806
Total Intragovernmental	23,640,482	26,327,033
Custodial Fines and Interest Receivable, Net (Note 4)	28,663,845	35,402,939
Accounts Receivable (Note 4)	10,332,	9,457
Property and Equipment, Net (Note 5)	1,919,650	489,638
TOTAL ASSETS	\$ 54,234,309	\$ 62,229,067
LIABILITIES		
Intragovernmental:		
FECA Liabilities	\$ 138,496	\$ 194,102
Accounts Payable	90,950	-
Total Intragovernmental	229,446	194,102
Accounts Payable	1,601,461	1,025,643
Accrued Funded Payroll	2,852,389	2,282,462
Annual Leave	5,230,125	4,797,304
Actuarial FECA Liabilities (Note 8)	491,304	514,932
Custodial Liabilities	28,663,845	35,402,939
Contingent Liabilities (Note 10)	-	182,426
Deposit Fund Liabilities	20,094	-
Total Liabilities	39,088,664	44,399,808
Commitments and Contingencies (Notes 9 And 10)		
NET POSITION		
Cumulative Results of Operations	(3,939,565)	(5,199,126)
Unexpended Appropriations	19,085,210	23,028,385
Total Net Position	15,145,645	17,829,259
TOTAL LIABILITIES AND NET POSITION	\$ 54,234,309	\$ 62,229,067

The accompanying notes are an integral part of these financial statements.



Commodity Futures Trading Commission

STATEMENTS OF NET COST

For the Years Ended September 30, 2005 and 2004

	2005	Unaudited 2004
GOAL ONE: Ensure the economic vitality of the commodity futures and option markets		
Intragovernmental Gross Costs	\$ 5,839,022	\$ 4,297,937
Less: Earned Revenue	(35,169)	(10,605)
Intragovernmental Net Cost of Operations	5,803,853	4,287,332
Gross Costs With the Public	28,301,068	27,124,106
Less: Earned Revenue	(3,831)	(9,032)
Net Cost of Operations With the Public	28,297,237	27,115,074
NET COST OF OPERATIONS - GOAL ONE	34,101,090	31,402,406
GOAL 2: Protect market users and the public		
Intragovernmental Gross Costs	6,869,438	5,245,515
Less: Earned Revenue	(41,375)	(12,943)
Intragovernmental Net Cost of Operations	6,288,063	5,232,572
Gross Costs With the Public	33,295,374	33,104,237
Less: Earned Revenue	(4,507)	(11,023)
Net Cost of Operations With the Public	33,290,867	33,093,214
NET COST OF OPERATIONS - GOAL TWO	40,118,930	38,325,786
GOAL 3: Ensure market integrity in order to foster open, competitive, and financially sound markets		
Intragovernmental Gross Costs	4,465,134	3,621,020
Less: Earned Revenue	(26,894)	(8,934)
Intragovernmental Net Cost of Operations	4,438,240	3,612,086
Gross Costs With the Public	21,641,993	22,852,109
Less: Earned Revenue	(2,929)	(7,610)
Net Cost of Operations With the Public	21,639,064	22,844,499
NET COST OF OPERATIONS - GOAL THREE	26,077,304	26,456,585
GRAND TOTAL		
Intragovernmental Gross Costs	17,173,594	13,164,472
Less: Earned Revenue	(103,438)	(32,482)
Intragovernmental Net Cost of Operations	17,070,156	13,131,990
Gross Costs With the Public	83,238,435	83,080,452
Less: Earned Revenue	(11,267)	(27,665)
Net Cost of Operations With the Public	83,227,168	83,052,787
TOTAL NET COST OF OPERATIONS	\$ 100,297,324	\$ 96,184,777

The accompanying notes are an integral part of these financial statements.



STATEMENTS OF CHANGES IN NET POSITION

For the Years Ended September 30, 2005 and 2004

	September 30, 2005		Unaudited September 30, 2004	
	Cumulative Results Of Operations	Unexpended Appropriations	Cumulative Results Of Operations	Unexpended Appropriations
BALANCES, OCTOBER 1	\$ (5,199,126)	\$ 23,028,385	\$ (2,957,781)	\$ (23,550,666)
BUDGETARY FINANCING SOURCES				
Appropriations:				
Received	-	94,327,000	-	90,435,000
Less: Rescinded	-	(754,616)	-	(533,567)
Less: Canceled	-	(289,267)	-	(339,153)
Used to Acquire and Provide Goods and Services	97,226,292	(97,226,292)	90,084,561	(90,084,561)
OTHER FINANCING SOURCES				
Imputed Financing Sources	4,330,593	-	3,858,871	-
Total Financing Sources	101,556,885	(3,943,175)	93,943,432	(522,281)
Net Cost of Operations	(100,297,324)	-	(96,184,777)	-
Net Change	1,259,561	(3,943,175)	(2,241,345)	(522,281)
BALANCES, SEPTEMBER 30	\$ (3,939,565)	\$ 19,085,210	\$ (5,199,126)	\$ 23,028,385

The accompanying notes are an integral part of these financial statements.



Commodity Futures Trading Commission

STATEMENTS OF BUDGETARY RESOURCES

For the Years Ended September 30, 2005 and 2004

	2005	Unaudited 2004
BUDGETARY RESOURCES		
Unobligated Balances, October 1	\$ 1,395,503	\$ 9,340,776
Recoveries of Prior Year Unpaid Obligations	6,920,117	8,902,248
Total Prior Resources	8,315,620	18,243,024
New Resources:		
Appropriations	94,327,000	90,435,000
Spending Authority from Offsetting Collections		
Collected	69,394	554,529
Change in Federal Receivables	152,789	22,806
Total New Resources	94,549,183	91,012,335
Permanently Not Available:		
Cancellation of Expired Accounts	(289,267)	(339,153)
Enacted Reduction	(754,616)	(533,567)
TOTAL BUDGETARY RESOURCES	\$101,820,920	\$108,382,639

STATUS OF BUDGETARY RESOURCES

Obligations Incurred, Direct	\$ 98,029,681	\$ 106,949,795
Obligations Incurred, Reimbursable	22,698	37,341
Total Obligations Incurred	98,052,379	106,987,136
Unobligated Balance Apportioned	768,613	38,613
Unobligated Balance Not Available	2,999,928	1,356,890
TOTAL STATUS OF BUDGETARY RESOURCES	\$ 101,820,920	\$ 108,382,639

RELATIONSHIP OF OBLIGATIONS TO OUTLAYS

Net Obligated Balance, October 1		
Unpaid Obligations	\$ 24,931,530	\$ 19,713,939
Uncollected Payments from Federal Sources	(22,806)	-
Net Obligated Balance, October 1	24,908,724	19,713,939
Gross Obligations Incurred	98,052,379	106,987,136
Gross Outlays	(96,211,945)	(92,867,297)
Recoveries of Prior Year Unpaid Obligations	(6,920,117)	(8,902,248)
Change in Federal Receivables	(152,789)	(22,806)



STATEMENTS OF BUDGETARY RESOURCES
 For the Years Ended September 30, 2005 and 2004 *(continued)*

	2005	Unaudited 2004
Net Obligated Balance, September 30		
Unpaid Obligations	19,851,847	24,931,530
Uncollected Payments from Federal Sources	(175,595)	(22,806)
Net Obligated Balance, September 30	19,676,252	24,908,724
Unreconciled Differences	\$ -	\$ -
 NET OUTLAYS		
Gross Outlays	\$ 96,211,945	\$ 92,867,297
Offsetting Collections Received	(69,394)	(554,529)
Distributed Offsetting Receipts	(9,474)	(13,541)
NET OUTLAYS	\$ 96,133,077	\$ 92,299,227

The accompanying notes are an integral part of these financial statements.



Commodity Futures Trading Commission

STATEMENTS OF FINANCING

For the Years Ended September 30, 2005 and 2004

	2005	Unaudited 2004
RESOURCES USED TO FINANCE ACTIVITIES		
Obligations Incurred	\$ 98,052,379	\$106,987,136
Less: Spending Authority from Offsetting Collections and Recoveries	\$ (7,142,300)	\$ (9,479,583)
Net Obligations	90,910,079	97,507,553
Offsetting Receipts	(9,474)	(13,541)
Net Obligations After Offsetting Receipts	90,900,605	97,494,012
Other Resources – Imputed Financing from Cost Absorbed by Others	4,330,593	3,858,871
Total Resources Used to Finance Activities	95,231,198	101,352,883
RESOURCES USED TO FINANCE ITEMS NOT PART OF THE NET COST OF OPERATIONS		
Offsetting Receipts	9,474	13,541
Change in Undelivered Orders	6,316,378	(7,483,065)
Resources that Finance the Net Acquisition of Fixed Assets	(1,472,567)	(196,857)
Total Resources Used to Finance Items Not Part of the Net Cost of Operations	4,853,285	(7,666,381)
Resources Used to Finance the Net Cost of Operations	100,084,483	93,686,502
COMPONENTS OF THE NET COST OF OPERATIONS THAT WILL NOT REQUIRE OR GENERATE RESOURCES IN THE CURRENT PERIOD		
Decrease in Accounts Receivable from the Public (Refunds)	(875)	-
Change in Unfunded Annual Leave, FECA Expenses and Contingent Liabilities	171,161	2,364,826
Total Cost of Items That Will Generate Resources in Future Periods	170,286	2,364,826
COMPONENTS NOT REQUIRING OR GENERATING RESOURCES		
Depreciation and Amortization	134,562	128,239
Contract Refund and Other	(92,007)	5,210
Total Components Not Requiring or Generating Resources	42,555	133,449
NET COST OF OPERATIONS	\$ 100,297,324	\$ 96,184,777

The accompanying notes are an integral part of these financial statements.



STATEMENTS OF CUSTODIAL ACTIVITY
For the Years Ended September 30, 2005 and 2004

	2005	Unaudited 2004
REVENUE ACTIVITY		
SOURCES OF CASH COLLECTIONS		
Registration and Filing Fees	\$ 742,133	\$ 768,130
Fines, Penalties, and Forfeitures	34,260,078	122,468,925
General Proprietary Receipts	9,474	13,541
Total Cash Collections	35,011,685	123,250,596
Change in Custodial Fines and Interest Receivable	(6,739,094)	35,376,188
Total Custodial Revenue	28,272,591	158,626,784
 DISPOSITION OF COLLECTIONS		
TRANSFERRED TO OTHERS, BY RECIPIENT:		
Transferred to Treasury	(35,011,685)	(123,250,596)
Change in Custodial Liabilities	6,739,094	(35,376,188)
NET CUSTODIAL ACTIVITY	\$ -	\$ -

The accompanying notes are an integral part of these financial statements.



Notes to the Financial Statements As of and For the Fiscal Years Ended September 30, 2005 and 2004

Note 1. Reporting Entity

The Commodity Futures Trading Commission (CFTC) is an independent agency of the executive branch of the Federal Government. Congress created the CFTC in 1974 under the authorization of the Commodity Exchange Act with the mandate to regulate commodity futures and option markets in the United States. The agency's mandate was renewed and expanded under the Futures Trading Acts of 1978, 1982, and 1986; under the Futures Trading Practices Act of 1992; and under the CFTC Reauthorization Act of 1995. The Commodity Futures Modernization Act of 2000 reauthorized the Commission through FY 2005. Since its inception, the CFTC has continuously operated through authorized appropriations.

The CFTC is responsible for ensuring the economic utility of futures markets by encouraging their competitiveness and efficiency, ensuring their integrity, and protecting market participants against manipulation, abusive trade practices, and fraud.

Note 2. Summary of Significant Accounting Policies

A. Basis of Presentation

The financial statements have been prepared to report the financial position and results of operations for the CFTC, as required by the Chief Financial Officers' Act of 1990 along with the Accountability of Tax Dollars Act of 2002, and the Government Management Reform Act of 1994. They are presented in accordance with the form and content requirements contained in Office of Management and Budget (OMB) Circular A-136, "Financial Reporting Requirements."

The financial statements have been prepared from the agency's books and records in conformity with generally accepted accounting principles in the United States of America as prescribed for the federal government by the Federal Accounting Standards Advisory Board (FASAB), promulgated by the Office of Management and Budget (OMB), and the agency's accounting policies as summarized in this note.

The financial statements report on the CFTC's financial position, net cost of operations, changes in net position, budgetary resources, financing, and custodial activities of the CFTC. The books and records of the agency served as the source of information for preparing the financial statements in the prescribed formats. All agency financial statements and reports used to monitor and control budgetary resources are prepared from the same books and records. The statements should be read with the understanding that they are for a component of the U.S. Government, a sovereign entity.

The Balance Sheets present the financial position of the agency. The Statements of Net Cost present the agency's operating results, the Statements of Changes in Net Position display the changes in the agency's equity accounts. The Statements of Budgetary Resources present the sources, status, and uses of the agency's resources and follows the rules for the Budget of the United States Government. The Statements of Financing present the reconciliation of the agency's use of budgetary resources with its operating results. The Statements of Custodial Activity present the sources and disposition of collections for which the CFTC is the fiscal agent, or custodian, for the Treasury General Fund Miscellaneous Receipt accounts.

B. Budgetary Resources and Status

The CFTC is funded through Congressionally approved appropriations. The CFTC is responsible for administering the salaries and expenses of the agency through the execution of these appropriations.

For these annual statements, there is no material difference between the Statement of Budgetary Resources and related budgetary information reported to OMB, or in the alignment to the Budget of the U.S. Government.

Congress annually enacts one-year appropriations that provide the CFTC with the authority to obligate funds within the respective fiscal year for necessary expenses to carry out mandated program activities. In addition, Congress enacted a permanent indefinite appropriation that is available until expended. All appropriations are subject to quarterly apportionment as well as Congressional restrictions.



CFTC's budgetary resources for FY 2005 consist of:

- Unobligated balances of resources brought forward from the prior year,
- Recoveries of obligations in prior years, and
- New resources in the form of appropriations and spending authority from offsetting collections.

Unobligated balances associated with resources expiring at the end of the fiscal year remain available for five years after expiration only for upward adjustments of prior year obligations, after which they are canceled and may not be used. All unused monies related to canceled appropriations are returned to Treasury and the canceled authority is reported as a line item on the Statements of Budgetary Resources and the Statements of Changes in Net Position.

C. Entity and Non-Entity Assets

Assets consist of entity and non-entity assets. Entity assets are those assets that the CFTC has authority to use for its operations. Non-entity assets are those held by the CFTC that are not available for use in its operations. Non-entity assets held by the CFTC include deposit fund balances and custodial fines and interest receivable, net.

D. Fund Balance with Treasury

Fund Balance with Treasury is the aggregate amount of the CFTC's funds with Treasury in expenditure, receipt, and deposit fund accounts. Appropriated funds recorded in expenditure accounts are available to pay current liabilities and finance authorized purchases. Custodial collections recorded in the deposit fund account and miscellaneous receipts accounts of the Treasury are not available for agency use. At fiscal year end, receipt account balances are cleared and returned to Treasury.

The CFTC does not maintain bank accounts of its own, has no disbursing authority, and does not maintain cash held outside of Treasury. Treasury disburses funds for the agency on demand. Spending authority from offsetting collections is recorded in the agency's expenditure account and is available for agency use subject to certain limitations. (See Note 3.)

E. Accounts Receivable

Accounts receivable consists of amounts owed by other federal agencies and the public to the CFTC and is valued net of an allowance for uncollectible amounts. The allowance is based on past experience in the collection of receivables and analysis of the outstanding balances. Accounts receivable arise from reimbursable operations, earned refunds or the Civil Monetary Sanctions program. (See Note 4.)

F. Property and Equipment

Property and equipment represents furniture, fixtures, equipment, and information technology hardware and software, which are capitalized and depreciated or amortized over their useful lives.

The CFTC capitalizes assets annually if they have useful lives of at least two years and an individual value of \$25,000 or more. Bulk or aggregate purchases are capitalized when the individual useful lives are at least two years and a value of \$25,000 or more. Property and equipment that does not meet the capitalization criteria are expensed when acquired. Depreciation and amortization is computed on a straight-line basis using a five-year life. Agency assets are valued net of accumulated depreciation. (See Note 5.)

G. Liabilities

The CFTC's liabilities consist of actual and estimated amounts that are likely to be paid as a result of transactions; that are covered by budgetary resources for which Congress has appropriated funds or funding, or are otherwise available from reimbursable transactions to pay amounts due.

Liabilities include those covered by budgetary resources in existing legislation and those not covered by budgetary resources (See Note 6). The CFTC liabilities not covered by budgetary resources include:

- Deposit funds,
- Contingent liabilities,
- Actuarial Federal Employees Compensation Act (FECA) liabilities,
- Annual leave benefits which will be funded by annual appropriations as leave is taken,



- Custodial liabilities for custodial revenue transferred to Treasury at fiscal year end.

The CFTC's liabilities that are covered by budgetary resources are considered current liabilities.

H. Accounts Payable

Accounts payable consists primarily of contracts for goods or services, such as leases, utilities, telecommunications, and consulting and support services. Accounts payable to other Federal agencies are designated as "intragovernmental."

I. Accrued Payroll and Benefits and Annual Leave Liability

The accrued payroll liability represents amounts for salaries and benefits owed for the time since the payroll was last paid through the end of the fiscal year. The annual leave liability is the amount owed employees for unused annual leave as of the end of the fiscal year. At the end of each fiscal year, the balance in the accrued annual leave account is adjusted to reflect current balances and pay rates. Sick leave and other types of non-vested leave are expensed as taken.

The agency's employees participate in the Civil Service Retirement System (CSRS) or the Federal Employees' Retirement System (FERS). On January 1, 1987, FERS went into effect pursuant to Public Law 99-335. Most employees hired after December 31, 1983, are automatically covered by FERS and Social Security. Employees hired prior to January 1, 1984, could elect to either join FERS and Social Security or remain in CSRS.

For employees under FERS, the CFTC contributes an amount equal to one percent of the employee's basic pay to the tax deferred thrift savings plan and matches employee contributions up to an additional four percent of pay. FERS employees can contribute 15 percent of their gross earnings to the plan. CSRS employees are limited to a contribution of 10 percent of their gross earnings and receive no matching agency contribution.

J. Deposit Funds

Deposit funds are expenditure accounts used to record monies that do not belong to the Federal government. They are held awaiting distribution based on a legal

determination or investigation. The CFTC deposit fund is used to record and later distribute monetary awards to the appropriate defendants as restitution.

K. Net Position

Net position consists of unexpended appropriations and cumulative results of operations.

Unexpended appropriations are appropriations that have not yet been used to acquire goods and services or provide benefits. Appropriations are considered expended, or used, when goods and services have been acquired by the CFTC or benefits have been provided using the appropriation authority, regardless of whether monies have been paid or payables for the goods, services, or benefits have been established. Appropriations were used primarily to acquire goods and services to operate the CFTC's programs or to provide benefits.

Cumulative results of operations represent the excess of financing sources over expenses since inception. Cumulative results of operations are derived from the net effect of capitalized assets, expenses, exchange revenue, and unfunded liabilities.

L. Revenues

The CFTC receives reimbursement and earns revenue for the following activities:

- Reimbursement for travel, subsistence, and related expenses from federal and non-federal sources for attendance at meetings or similar functions that an employee has been authorized to attend in an official capacity on behalf of the Commission.
- Reimbursement for Intergovernmental Personnel Act Mobility Program assignments from state and local governments, institutions of higher education, and other eligible organizations for basic pay, supplemental pay, fringe benefits, and travel and relocation expenses.
- Reimbursement from non-federal sources for registration fees to cover the cost of expenses related to the CFTC's annual International Regulators Conference.

M. Net Cost of Operations

Net cost of operations is the difference between the CFTC's expenses and its earned revenue. The presentation of program results by strategic goals is based on



the CFTC's current Strategic Plan established pursuant to the Government Performance and Results Act (GPRA) of 1993.

The mission statement of the CFTC is to protect market users and the public from fraud, manipulation, and abusive practices related to the sale of commodity and financial futures and options, and to foster open, competitive, and financially sound futures and option markets.

The mission is accomplished through three strategic goals,

- Ensure the economic vitality of the commodity futures and option markets.
- Protect market users and the public.
- Ensure market integrity in order to foster open, competitive, and financially sound markets.

N. Gross Costs and Earned Revenue by Budget Functional Classification

The CFTC's gross costs, earned revenue, and intragovernmental transactions align with the three strategic goals based on the agency mission statement related to protecting market users and the public.

O. Reconciliation of Net Obligations and Net Cost of Operations

The Statements of Financing reconcile the net obligations with the net cost of operations. Net obligations, reported on the Statements of Budgetary Resources, are calculated by subtracting downward adjustments of prior-period obligations and offsetting collections from gross obligations. The net cost of operations, reported on the Statements of Net Cost represents the difference between gross costs and earned revenue.

Other resources used to finance activity, such as imputed costs from the Statements of Changes in Net Position, are added to net obligations to derive total resources used to fund activities. Resources used to finance items not part of the net cost of operations, such as undelivered orders are added to the reconciliation.

The reconciliation is finalized by adding in items in the net cost of operations that do not generate or use resources in the current period. This includes costs and earned revenues which will never generate or use resources, such as depreciation expense. This also includes those

which will generate or use resources in a future period, such as benefits expense resulting from the increase in annual leave liability, which is accrued for purposes of the Statements of Net Cost, but is not funded until leave is taken.

P. Custodial Activity

The CFTC collects penalties and fines levied against firms for violation of laws as described in the Commodity Exchange Act as codified at 7 U.S.C. § 1, *et seq.*, and the Commodity Futures Modernization Act of 2000, Appendix E of PL.106-554, 114 Stat. 2763. Unpaid fines, penalties and accrued interest are reported as custodial receivables, with an associated custodial liability. The receivables and the liability are reduced by losses determined to be uncollectible. Revenues earned and the losses from bad debts are reported to Treasury.

Collections made by CFTC during the year are deposited and reported into designated Treasury miscellaneous receipt accounts for:

- Registrations and filing fees,
- Fees, fines, penalties and forfeitures, and
- General miscellaneous recoveries and refunds.

At fiscal year end, custodial collections made by CFTC are returned to Treasury. The CFTC does not retain any amount for custodial activities including reimbursement of the cost of collection.

Q. Use of Management Estimates

The preparation of the accompanying financial statements in accordance with accounting principles generally accepted in the United States requires management to make certain estimates and assumptions that directly affect the results of reported assets, liabilities, revenues, and expenses. Actual results could differ from these estimates.

R. Tax Status

The CFTC is not subject to Federal, State or local income taxes. Accordingly, no provision for income taxes is recorded.



Note 3. Fund Balance with Treasury

A. Reconciliation to Treasury:

There are no differences between the Fund Balance reflected in the CFTC Balance Sheets and the balance in the Treasury accounts.

B. Fund Balances:

Fund Balances with Treasury consist of entity assets such as appropriations and reimbursements for services rendered. Obligation of these funds is controlled by quarterly apportionments made by the OMB. Work performed under reimbursable agreements is initially financed by the annual appropriation and is subsequently reimbursed. Other funds include non-entity deposit fund receipts.

Fund Balance with Treasury at September 30, 2005 and 2004, consisted of the following:

	2005	2004
Appropriated Funds	\$ 23,444,793	\$ 26,304,227
Other Funds:		
Deposit Funds	20,094	-
TOTAL FUND BALANCE WITH TREASURY	\$ 23,464,887	\$ 26,304,227

C. Status of Fund Balance with Treasury:

The Status of Fund Balance with Treasury at September 30, 2005 and 2004, consisted of the following:

	2005	2004
Appropriated Funds		
Unobligated Fund Balance		
-Available	\$ 756,075	\$ 16,360
-Expired	12,538	22,253
-Unavailable	2,999,928	1,356,890
Obligated Balance Not Yet Disbursed	19,676,252	24,908,724
Deposit Fund	20,094	-
TOTAL FUND BALANCE WITH TREASURY	\$ 23,464,887	\$ 26,304,227



Note 4. Accounts Receivable

Accounts receivable consist of amounts owed to the CFTC by other Federal agencies and the public. Accounts receivable are valued net of estimated uncollectibles. Non-custodial accounts receivable are primarily for overpayments of expenses to other agencies, or vendors, and repayment of employee benefits. Historical experience has indicated that most of the non-custodial receivables are collectable and there are no material uncollectible amounts.

Custodial receivables (non-entity assets) are those for which fines and penalties have been assessed and levied against businesses for violation of law. The CFTC litigates against defendants for alleged violations of the CEA, as amended. Violators may be subject to a variety of sanctions including fines, injunctive orders, bars or suspensions, rescissions of illegal contracts, disgorgements, and restitutions to customers.

Historical experience has indicated that a high percentage of custodial receivables prove uncollectible. The methodology used to estimate the allowance for uncollectible amounts related to custodial accounts is that custodial receivables are considered 100 percent uncollectible unless otherwise noted in the judgment. An allowance for uncollectible accounts has been established and included in accounts receivable on the balance sheet. The allowance is based on past experience in the collection of accounts receivable and analysis of outstanding balances. Accounts are reestimated quarterly based on account reviews and the agency determination that changes to the net realizable value are needed.

Accounts receivable, as of September 30, 2005 and 2004, consisted of the following:

	2005	2004
Intragovernmental Accounts Receivable	\$ 175,595	\$ 22,806
Custodial Fines and Interest Receivables, Net:		
Civil Monetary Penalty Interest	\$ 2,501,590	\$ 65,253,060
Less: Allowance for Loss on Interest	(2,290,056)	(65,253,060)
Civil Monetary Penalties, Fines, and Administrative Fees	328,168,373	465,735,791
Less: Allowance for Loss on Penalties, Fines and Administrative Fees	(299,716,062)	(430,332,852)
Net Custodial	28,663,845	35,402,939
Other	10,332	9,457
Total Accounts Receivable With the Public	\$ 28,674,177	\$ 35,412,396



Note 5. Property and Equipment, Net

Assets are capitalized annually if they have useful lives of at least two years and an individual value of \$25,000 or more. Bulk or aggregate purchases are capitalized when the individual useful lives are at least two years and a value of \$25,000 or more. Depreciation and amortization is computed on a straight-line basis using a five-year life. The CFIC did not defer any maintenance in FY 2005 and FY 2004. Property and equipment, net, as of September 30, 2005 and 2004, consisted of the following:

2005				
Major Class	Service Life and Method	Cost	Accumulated Amortization/Depreciation	Net Book Value
Equipment	5 Years/Straight Line	\$ 562,894	\$ 176,878	\$ 386,016
IT Software	5 Years/Straight Line	\$ 1,580,271	\$ 46,637	\$ 1,533,634
Total Property and Equipment		\$ 2,143,165	\$ 223,515	\$ 1,919,650

2004				
Major Class	Service Life and Method	Cost	Accumulated Amortization/Depreciation	Net Book Value
Equipment	5 Years/Straight Line	\$ 428,040	\$ 87,830	\$ 340,210
IT Software	5 Years/Straight Line	\$ 284,301	\$ 134,873	\$ 149,428
Total Property and Equipment		\$ 712,341	\$ 222,703	\$ 489,638

Note 6. Liabilities Not Covered by Budgetary Resources

As of September 30, 2005 and 2004, the following liabilities not covered by budgetary resources exist:

	2005	2004
Intragovernmental-FECA	\$ 138,496	\$ 194,102
Annual Leave	5,230,125	4,797,303
Actuarial FECA	491,304	514,932
Contingent Liabilities	-	182,426
Deposit Fund	20,094	-
TOTAL LIABILITIES NOT COVERED BY BUDGETARY RESOURCES	\$ 5,880,019	\$ 5,688,764



Note 7. Retirement Plans and Other Employee Benefits

The CFTC imputes costs and the related financing source for its share of retirement systems accruing to its past and present employees that are in excess of the amount of contributions from the CFTC and its employees, which are mandated by law. The Office of Personnel Management (OPM), which administers Federal civilian retirement programs, provides the cost information to the CFTC. The CFTC recognizes the full cost of providing future pension and Other Retirement Benefits (ORB) for current employees as required by SFAS No. 5, *Accounting for Liabilities of the Federal Government*.

Full costs include pension and ORB contributions paid out of the CFTC's appropriations and costs financed by OPM. The amount financed by OPM is recognized as an imputed financing source. Reporting amounts such as plan assets, accumulated plan benefits, or unfunded liabilities, if any, is the responsibility of OPM.

Liabilities for future pension payments and other future payments for retired employees who participate in the Federal Employees Health Benefits Program (FEHBP) and the Federal Employees Group Life Insurance Program (FEGLI) are reported by OPM rather than the CFTC.

Note 8. Actuarial FECA Liabilities

The Federal Employees Compensation Act (FECA) provides income and medical cost protections to covered federal civilian employees injured on the job, to employees who have incurred work-related occupational diseases and to beneficiaries of employees whose deaths are attributable to job-related injuries or occupational diseases. The FECA program is administered by the U.S. Department of Labor (DOL), which pays valid claims against the Department and subsequently seeks reimbursement from the Department for these paid claims. Accrued FECA liabilities represent amounts due to DOL for claims paid on behalf of the agency.

Actuarial FECA liability represents the liability for future workers compensation (FWC) benefits, which includes the expected liability for death, disability, medical, and miscellaneous cost for approved cases. The liability is determined using a formula provided by DOL annually as of September 30th using a method that

utilizes historical benefits payment patterns related to a specific incurred period to predict the ultimate payments related to that period. The projected annual benefits payments are discounted to present value using OMB's economic assumptions for ten-year Treasury notes and bonds. To provide more specifically for effects of inflation on liability for FWC benefits, wage inflation factors (Consumer Price Index-Medical) are applied to the calculation of projected future benefits. These factors are also used to adjust historical payment so benefits are stated in current-year constant dollars.

Note 9. Leases

The CFTC leases office space in publicly owned buildings for its locations in Washington D.C., Chicago, New York, Minneapolis, and Kansas City. The lease contracts for publicly-owned buildings are operating leases. The CFTC has no real property. Future lease payments are not accrued as liabilities and are expensed as incurred.

As of September 30, 2005, future estimated minimum lease payments through FY 2010, and thereafter, are as follows:

Fiscal Year	Dollars
2006	\$ 10,926,612
2007	11,343,178
2008	11,654,861
2009	11,942,110
2010	12,207,780
Thereafter	40,996,482
TOTAL FUTURE MINIMUM LEASE PAYMENTS	\$ 99,071,023

Note 10. Contingent Liabilities

The CFTC records contingent liabilities for cases in which payment has been deemed probable and for which the amount of potential liability has been estimated, including certain judgments that have been issued against the agency and which have been appealed. In FY 2004, the U.S. District Court held the CFTC liable for \$182,425 for violation of the Equal Access to Justice Act and a contingent liability was established. In FY 2005, the U.S. District Court found in favor of the CFTC and the contingent liability was terminated. As of September 30, 2005, no contingent liabilities exist.



Required Supplementary Information

Detailed Information on Intragovernmental Amounts

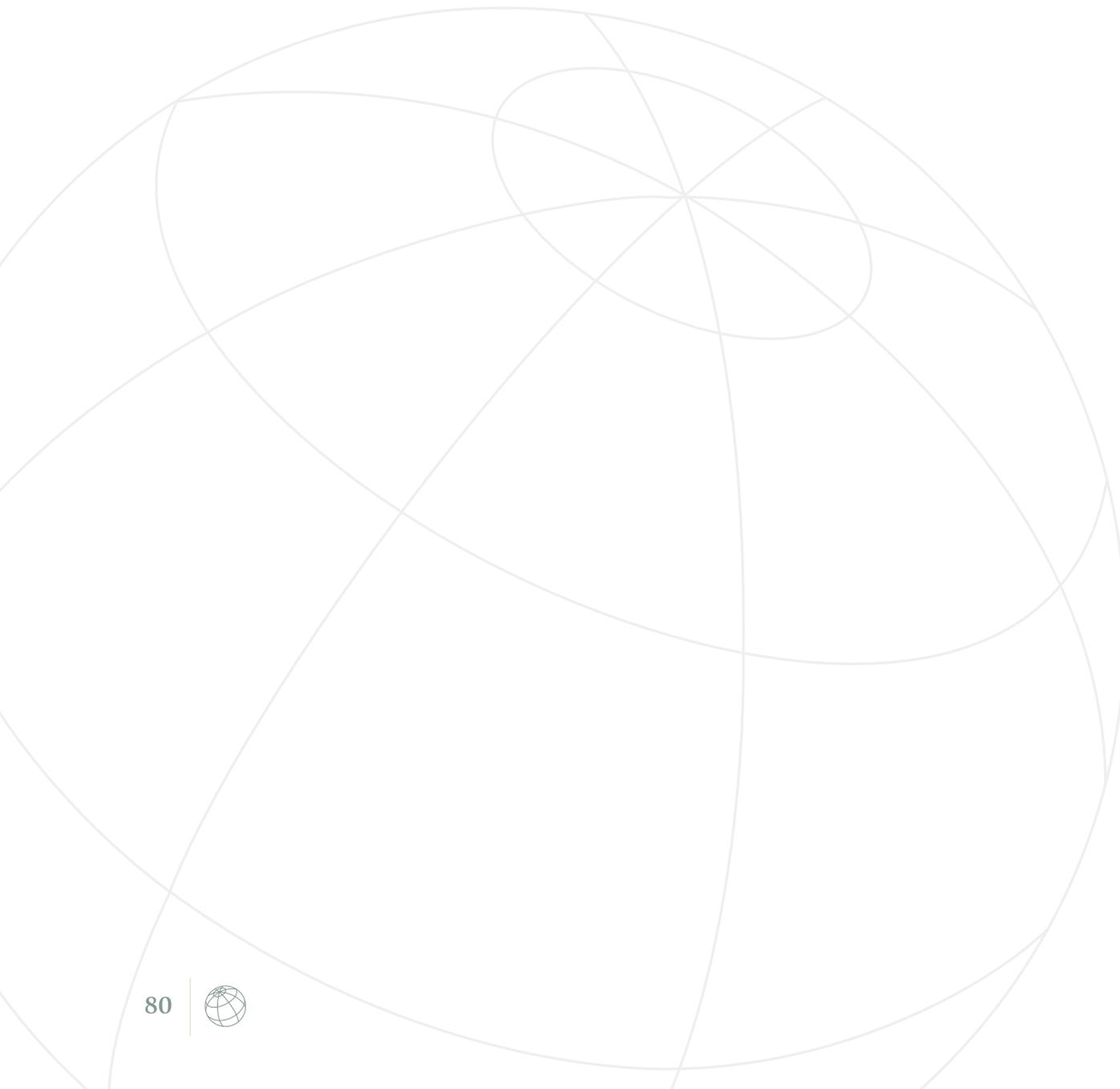
Intragovernmental assets and liabilities as of September 30, 2005 and 2004 consisted of the following:

	2005	2004
ASSETS:		
Fund Balance with Treasury	\$ 23,464,887	\$ 26,304,227
ACCOUNTS RECEIVABLE:		
Postal Service	446	-
Department of Treasury	175,149	-
Executive Office of the President	-	22,806
Total Intragovernmental Assets	\$ 23,640,482	\$ 26,327,033
LIABILITIES:		
Department of Labor (FECA)	\$ 138,496	\$ 194,102
ACCOUNTS PAYABLE:		
General Services Administration	\$ 51,491	-
Government Printing Office	2,451	-
Department of Treasury	11,070	-
Department of Agriculture	16,250	-
Department of Health and Human Services	2,352	-
Library of Congress	1,200	-
Federal Reserve Board	6,136	-
Total Accounts Payable	90,950	-
Total Intragovernmental Liabilities	\$ 229,446	\$ 194,102





A Report of the Independent Auditors





KPMG LLP
2001 M Street, NW
Washington, DC 20036

Independent Auditors' Report

Chairman of the U.S. Commodity Futures Trading Commission and
Office of Inspector General, U.S. Commodity Futures Trading Commission:

We have audited the accompanying balance sheets of the U.S. Commodity Futures Trading Commission (CFTC) as of September 30, 2005 and 2004, and the related statements of net cost, changes in net position, financing, budgetary resources, and custodial activity for the year ended September 30, 2005. The objective of our audits was to express an opinion on the fair presentation of these financial statements. In connection with our audits, we also considered CFTC's internal control over financial reporting and tested CFTC's compliance with certain provisions of applicable laws, regulations, and contracts that could have a direct and material effect on these financial statements.

SUMMARY

As stated in our opinion on the financial statements, we concluded that CFTC's balance sheets as of September 30, 2005 and 2004, and the related statements of net cost, changes in net position, financing, budgetary resources, and custodial activity for the year ended September 30, 2005, are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America. In fiscal year 2004, the scope of our work was not sufficient to enable us to express an opinion on the accompanying statements of net cost, changes in net position, budgetary resources, financing, and custodial activity for the year ended September 30, 2004, because the financial statements of CFTC had not been audited prior to fiscal year 2004, and as a result, we had no assurances as to the asset, liability, and obligation balances at the beginning of the year, which enter into the determination of net position as of the beginning of fiscal year 2004, and the net cost, status of budgetary resources, the reconciliation of net cost to budgetary obligations, and custodial activity for the year ended September 30, 2004.

Our fiscal year 2005 consideration of internal control over financial reporting resulted in the following conditions being identified as reportable conditions:

- Financial Management Systems Need Improvement;
- Improvement is Needed in the Fixed Asset System;
- Improvement is Needed in Evaluating Undelivered Orders; and
- Improvements are Needed in Recording Accruals and Preparing Financial Statements.

However, none of the reportable conditions are believed to be material weaknesses.





The results of our tests of fiscal year 2005 compliance with certain provisions of laws, regulations, and contracts disclosed the following instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*, issued by the Comptroller General of the United States, and Office of Management and Budget (OMB) Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*:

- *Federal Information Security Management Act (FISMA)*; and
- *Federal Financial Management Improvement Act of 1996 (FFMIA)*.

The following sections discuss our opinion on CFTC's financial statements, our consideration of CFTC's internal control over financial reporting, our tests of CFTC's compliance with certain provisions of applicable laws, regulations, and contracts, and management's and our responsibilities.

OPINION ON THE FINANCIAL STATEMENTS

We have audited the accompanying balance sheets of the U.S. Commodity Futures Trading Commission as of September 30, 2005 and 2004, and the related statements of net cost, changes in net position, financing, budgetary resources, and custodial activity for the year ended September 30, 2005.

The financial statements of CFTC had not been audited prior to fiscal year 2004. Therefore, we had no assurances as to the asset, liability, and obligation balances at the beginning of fiscal year 2004, which enter into the determination of net position as of the beginning of fiscal year 2004, and the net cost, the status of budgetary resources, the reconciliation of net cost to budgetary obligations, and custodial activity for the year ended September 30, 2004.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of CFTC as of September 30, 2005 and 2004, and its net costs, changes in net position, budgetary resources, reconciliation of net costs to budgetary obligations, and custodial activities, for the year ended September 30, 2005, in conformity with accounting principles generally accepted in the United States of America. Because of the matter discussed in the second paragraph of this section, the scope of our work was not sufficient to enable us to express an opinion on the accompanying statements of net cost, changes in net position, budgetary resources, financing, and custodial activity for the year ended September 30, 2004.

The information in the Management's Discussion and Analysis and Required Supplementary Information sections, is not a required part of the financial statements, but is supplementary information required by accounting principles generally accepted in the United States of America or OMB Circular A-136, *Financial Reporting Requirements, Part A, Form and Content of the Performance and Accountability Report*. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of this information. However, we did not audit this information and, accordingly, we express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. The information in the Performance Section, other Statutorily Required Reports section, and Appendices is an integral part of CFTC's *Fiscal Year 2005 Performance and Accountability Report*. However, this information is not a required part of the financial statements and is presented for purposes of additional analysis. This information has not been subjected to auditing procedures and, accordingly, we express no opinion on it.





INTERNAL CONTROL OVER FINANCIAL REPORTING

Our consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be reportable conditions. Under standards issued by the American Institute of Certified Public Accountants, reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect CFTC's ability to record, process, summarize, and report financial data consistent with the assertions by management in the financial statements.

Material weaknesses are reportable conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements, in amounts that would be material in relation to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

In our fiscal year 2005 audit, we noted certain matters, discussed in Exhibit I, involving the internal control over financial reporting and its operation that we consider to be reportable conditions. However, none of the reportable conditions are believed to be material weaknesses.

* * * * *

A summary of the status of prior year reportable conditions is included as Exhibit II.

We also noted certain additional matters that we reported to the management of CFTC in two separate letters, addressing information technology and other matters, dated June 30 and November 14, 2005, respectively.

COMPLIANCE AND OTHER MATTERS

Our tests of compliance with certain provisions of laws, regulations, and contracts, as described in the Responsibilities section of this report, exclusive of those referred to in the FFMIA, disclosed one instance of noncompliance that is required to be reported under *Government Auditing Standards* and OMB Bulletin No. 01-02, and is described below.

FISMA, passed as part of the *E-Government Act of 2002*, requires that Federal agencies: (1) provide a comprehensive framework for ensuring the effectiveness of information security controls over information resources that support Federal operations and assets; (2) provide effective government-wide management and oversight of the related information security risks; (3) provide for development and maintenance of minimum controls required to protect Federal information and information systems; (4) provide a mechanism for improved oversight of Federal agency information security programs; (5) acknowledge that commercially developed information security products offer advanced, dynamic, robust, and effective information security solutions, reflecting market solutions for the protection of critical information infrastructures important to the national defense and economic security of the nation that are designed, built, and operated by the private sector; and (6) recognize that the selection of specific technical hardware and software information security solutions should be left to individual agencies from among commercially developed products. OMB Circular A-130, *Management of Federal Information Resources*, provides further information security guidance. We noted that CFTC needs continued improvement with its entity-wide security and contingency planning programs, access controls, segregation of duties, and service continuity, to fully meet these guidelines.

This matter is further described in our separate IT report dated June 30, 2005, and we recommend that CFTC implement the recommendations presented in that report.





The results of our tests of compliance with certain provisions of other laws and regulations, exclusive of those referred to in FFMIA, disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards* or OMB Bulletin No. 01-02.

The results of our tests of FFMIA disclosed instances, described below and in Exhibit I, where CFTC's financial management systems did not substantially comply with Federal financial management systems requirements.

FFMIA mandates that Federal financial management be advanced by ensuring that Federal financial management systems can and do provide reliable, consistent disclosure of financial data, and that they do so on a basis that is uniform across the Federal government from year-to-year consistently, using accounting principles generally accepted in the United States of America. Federal agencies need to comply with FFMIA by adhering to policies established by OMB, such as OMB Circular A-127, *Financial Management Systems*, and OMB Circular A-130. FFMIA requires that Federal agencies implement information security controls and contingency planning capabilities in accordance with OMB Circular A-130. CFTC needs to improve in these areas to be in compliance with Circular A-130. This matter is discussed in further detail in our separate IT report, dated June 30, 2005.

The results of our tests of FFMIA disclosed no instances in which CFTC's financial management systems did not comply with Federal Accounting Standards or the United States Government Standard General Ledger at the transaction level.

We recommend that CFTC implement corrective actions to address the recommendations in our separate IT report, dated June 30, 2005.

RESPONSIBILITIES

Management's Responsibilities

The *Government Management Reform Act of 1994* (GMRA), *Accountability of Tax Dollars Act*, and *Government Corporation Control Act* require agencies to report annually to Congress on their financial status and any other information needed to fairly present their financial position and results of operations. To meet these reporting requirements, CFTC prepares and submits financial statements in accordance with Part A of OMB Circular A-136.

Management is responsible for the financial statements, including:

- Preparing the financial statements in conformity with accounting principles generally accepted in the United States of America;
- Preparing the Management's Discussion and Analysis (including the performance measures) and Required Supplementary Information;
- Establishing and maintaining internal controls over financial reporting; and
- Complying with laws, regulations, and contracts, including FFMIA.

In fulfilling this responsibility, management is required to make estimates and judgments to assess the expected benefits and related costs of internal control policies. Because of inherent limitations in internal control, misstatements due to error or fraud may nevertheless occur and not be detected.





Auditors' Responsibilities

Our responsibility is to express an opinion on the fiscal year 2005 and 2004 balance sheets of CFTC, and the related statements of net cost, changes in net position, budgetary resources, financing, and custodial activity, for the year ended September 30, 2005 based on our audits. As discussed in the Opinion section of this report, the scope of our work was not sufficient to enable us to express an opinion on the accompanying statements of net cost, changes in net position, budgetary resources, financing, and custodial activity, for the year ended September 30, 2004. We conducted our audits in accordance with auditing standards generally accepted in the United States of America, the standards applicable to financial audits contained in *Government Auditing Standards*, and OMB Bulletin No. 01-02. Those standards and OMB Bulletin No. 01-02 require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of CFTC's internal control over financial reporting. Accordingly, we express no such opinion.

An audit also includes:

- Examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements;
- Assessing the accounting principles used and significant estimates made by management; and
- Evaluating the overall financial statement presentation.

We believe that our audits provide a reasonable basis for our opinion.

In planning and performing our fiscal year 2005 audit, we considered CFTC's internal control over financial reporting by obtaining an understanding of CFTC's internal control, determining whether internal controls had been placed in operation, assessing control risk, and performing tests of controls in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. We limited our internal control testing to those controls necessary to achieve the objectives described in *Government Auditing Standards* and OMB Bulletin No. 01-02. We did not test all internal controls relevant to operating objectives as broadly defined by the *Federal Managers' Financial Integrity Act of 1982*. The objective of our audit was not to provide assurance on CFTC's internal control over financial reporting. Consequently, we do not provide an opinion thereon.

As required by OMB Bulletin No. 01-02, in our fiscal year 2005 audit, with respect to internal control related to performance measures determined by management to be key and reported in the Management's Discussion and Analysis and Performance sections, we obtained an understanding of the design of significant internal controls relating to the existence and completeness assertions. Our procedures were not designed to provide assurance on internal control over reported performance measures and, accordingly, we do not provide an opinion thereon.

As part of obtaining reasonable assurance about whether CFTC's fiscal year 2005 financial statements are free of material misstatement, we performed tests of CFTC's compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts, and certain provisions of other laws and regulations specified in OMB Bulletin No. 01-02, including certain provisions referred to in FFMIA. We limited our tests of compliance to the provisions described in the preceding sentence, and we did not test compliance with all laws, regulations, and contracts applicable to CFTC. However, providing an opinion on





compliance with laws, regulations, and contracts was not an objective of our audit and, accordingly, we do not express such an opinion.

Under OMB Bulletin No. 01-02 and FFMIA, we are required to report whether CFTC's financial management systems substantially comply with (1) Federal financial management systems requirements, (2) applicable Federal accounting standards, and (3) the United States Government Standard General Ledger at the transaction level. To meet this requirement, we performed tests of compliance with FFMIA Section 803(a) requirements.

DISTRIBUTION

This report is intended solely for the information and use of CFTC's management, CFTC's Office of Inspector General, OMB, the Government Accountability Office, and the U.S. Congress and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

November 14, 2005



Exhibit I

U.S. COMMODITY FUTURES TRADING COMMISSION

Reportable Conditions

Exhibit I describes the reportable conditions and our recommendations. CFTC management's response is presented following the recommendations.

Financial Management Systems Need Improvement

Effective general information technology (IT) controls add assurance that data used to prepare and report financial information and statements is complete, reliable, and has integrity. Our fiscal year 2005 IT assessment was focused on general IT controls over CFTC's management systems and supporting network infrastructure, using GAO's *Federal Information System Controls Audit Manual (FISCAM)* as a guide. The six FISCAM general IT control review elements are as follows:

- Entity-wide security program;
- Secure access controls;
- Application software development and change control;
- System software;
- Segregation of duties; and
- Service continuity.

We found that CFTC management has not implemented test plans that will allow them to assess their efficiency and effectiveness in carrying out the process steps in its *IT Continuity of Operations Plan*. Additionally, controls in the following areas need to be strengthened: granting system access to users, change management controls, and information security testing.

These weaknesses led to our determination that CFTC was not in compliance with the *Federal Information Security Management Act* and the Federal financial management system requirements called for in the *Federal Financial Management Improvement Act of 1996*, as discussed in the Compliance and Other Matters section of our auditors' report.

Recommendations

Specific recommendations to address IT controls are included in a separate limited distribution IT general controls report dated June 30, 2005, issued as part of the fiscal year 2005 financial statement audit. We recommend that CFTC take steps to ensure effective implementation of our recommendations.

Agency Response

We concur with this finding and agree with the recommendations.



U.S. COMMODITY FUTURES TRADING COMMISSION
Reportable Conditions

Improvement is Needed in the Fixed Asset System

CFTC does not have adequate internal controls to account for, record, track, or monitor its Property, Plant, and Equipment (PP&E). Based on discussions with the Office of Financial Management (OFM), and review of CFTC's fixed asset policy and records, CFTC's assets are comprised of furniture, equipment, computer hardware and software, copiers, and fax machines. CFTC has designated several individuals to track its fixed assets; however, the information maintained by these individuals is not complete or precise as required by Federal Accounting Standards Advisory Board (FASAB) and Joint Financial Management Improvement Program (JFMIP) standards, that requires an accounting and control function that ensures standard transaction processing, accurate valuation, and disclosure of the acquisition and disposition of assets.

In addition, CFTC has not conducted a detailed physical inventory of all property, plant, and equipment within the last four years. Partial inventories performed during the last four years by different CFTC groups have not been uniform or consistent with an established set of physical inventory policies and procedures. For example, the CFTC's Office of Information Management may perform a physical inventory using one set of guidelines, and the CFTC's Office of Management Operations may use entirely different guidelines.

We used a substantive approach in auditing the balance of CFTC's PP&E and the related accumulated depreciation as of September 30, 2005. OFM manually compiled all obligations, purchase orders, and contracts related to fixed asset purchases that were recorded in Federal Financial System (FFS) from 1999 through 2005, to determine total PP&E capitalizable assets. An accumulated depreciation and write-off schedule was also prepared.

During our test work, we noted that OFM incorrectly recorded depreciation expense related to a contractor developed software package, eLaw. CFTC recorded all costs in the current year and began depreciating the asset prior to full implementation of the software package. As a result of our test work, CFTC recorded a current year adjustment to reduce depreciation expense by approximately \$301,000. We determined that adjusted PP&E balances as of September 30, 2005 were fairly stated.

Statement of Federal Financial Accounting Standards (SFFAS) No. 6, *Accounting for Plant, Property, and Equipment* (SFFAS No. 6), paragraph 26 states that all general PP&E shall be recorded at cost. Cost shall include all costs incurred to bring the PP&E to a form and location suitable for its intended use.

The *Federal Managers' Financial Integrity Act of 1982* requires "internal accounting and administrative controls of each executive agency shall be established in accordance with standards prescribed by the Comptroller General." GAO's *Standards for Internal Control in the Federal Government* (GAO Standards) defines internal control as "an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved: effectiveness and efficiency of operations, reliability of financial reporting, and compliance with applicable laws and regulations." GAO Standards provide five standards for internal control, including monitoring. The GAO Standards further state, "internal control should generally be designed to assure that ongoing monitoring occurs in the course of normal operations. It is performed continually and is ingrained in the agency's operations. It includes regular management and supervisory activities, comparisons, reconciliations, and other actions people take in performing their duties."



Exhibit I

U.S. COMMODITY FUTURES TRADING COMMISSION

Reportable Conditions

SFFAS 10, paragraph 8 states that “Internal use software means software that is purchased from commercial vendors off-the-shelf, internally developed, or contractor-developed solely to meet the entity’s internal or operational needs.” SFFAS 10, paragraph 9.b.2 also states that “contractor-developed software refers to software that a federal entity is paying a contractor to design, program, install, and implement, including new software and the modification of existing or purchased software.” SFFAS 10, paragraph 16 indicates that “for internally developed software, capitalized cost should include the full cost (direct and indirect cost) incurred during the software development stage.” SFFAS 10, paragraph 41 further states that “the start of amortization for internal use software as the point when final acceptance testing is successfully completed.”

Recommendations:

We recommend that CFTC:

- Develop a property management system that will do the following: (1) classify PP&E by assets or classes described in SFFAS No. 6 and No. 10; (2) allow user defined transaction types and automatically record the transaction type when the property record is created or updated; (3) provide unique identification; (4) provide a complete audit trail of all changes to property records including, but not limited to modifications, improvements, changes in value, and the individual entering or approving the information; (5) designate property tracked in the property management system as either capitalized or expensed; (6) allow user defined capitalization thresholds to be established for property classes; and (7) notify the user when depreciation, amortization, or depletion thresholds are exceeded.
- Improve internal controls, policies, and procedures related to fixed assets to ensure that assets are recorded in the financial statements on a timely basis. CFTC should also ensure that appropriate personnel are designated to maintain adequate and timely records of inventories and property additions/disposals and that this information is communicated to the OFM on a timely basis for recording in the financial records.
- Improve procedures for property accountability that includes tracking the movement of assets, recording changes in physical condition, and verification of physical counts. In addition, a unique item identification system should be implemented to track each individual asset and assist in performing physical inventories.

Agency Response

We concur with this finding and agree with the recommendations.



U.S. COMMODITY FUTURES TRADING COMMISSION

Reportable Conditions

Improvement is Needed in Evaluating Undelivered Orders

At the end of each quarter, OFM sends correspondence to program office officials responsible for recording obligations to request the status of undelivered orders. The program offices are required to review the obligations and determine if each should be deobligated. We performed test work over balances for a sample of 97 undelivered orders. We recalculated the outstanding balances, without exception. We also obtained a listing of all obligations that had been outstanding for more than two years that were for goods or services that would generally not take two years for the vendor to provide. CFTC could not provide supporting documentation for the management review and status of six items totaling approximately \$1.9 million as of September 30, 2005. No audit adjustment was proposed, because subsequent management review and evaluation determined that the status was appropriately recorded.

CFTC's internal control policies and procedures must ensure the status of its budgetary resources is properly recorded in the general ledger (e.g., FFS) and reported to the Office of Management and Budget on a quarterly and year-end basis. In addition, these policies must ensure that the status of budgetary resources is properly reported in CFTC's Statement of Budgetary Resources and the related notes to the financial statements. Budget execution procedures must be improved for CFTC to ensure that accurate, complete, and timely budgetary accounting entries are made, and that the year-end status of budgetary resources are accurately reported.

Recommendation

We recommend that CFTC improve its process for analyzing its undelivered orders balance on a quarterly and year-end basis, to determine those obligations that should be deobligated. The process should ensure that OFM can accurately and timely identify those outstanding undelivered orders that should be deobligated. In addition, the program office officials should provide necessary documentation in a timely manner to support why outstanding obligations should remain open.

Agency Response

We concur with this finding and agree with the recommendation.



Exhibit I

U.S. COMMODITY FUTURES TRADING COMMISSION

Reportable Conditions

Improvements are Needed in Recording Accruals and Preparing Financial Statements

CFTC has developed and implemented a process for estimating year-end accounts payable and accruals; however, the process needs improvement. At year-end, CFTC makes a rigorous effort to pay all outstanding invoices received prior to September 30. This effort is designed to ensure that CFTC does not have a significant accounts payable balance at year-end. During our test work, we noted that CFTC did not properly record certain items, resulting in an overstatement of accounts payable of \$25,300 and actuarial liabilities related to *Federal Employees Compensation Act* (FECA) of \$261,000. In addition, CFTC did not record a liability for legal fees in the amount of \$36,000, which was awarded by the General Services Board of Contract Appeals; and did not properly record imputed costs from OPM, resulting in an understatement of imputed costs and financing sources of approximately \$1.68 million. As a result of our audit, CFTC recorded an adjustment of \$261,000 to reduce its actuarial FECA liability, and an adjustment of \$1.68 million to increase its imputed costs and financing sources. The need for these and other adjustments in financial statement presentations delayed CFTC in preparing its financial statements timely.

SFFAS No. 5, *Accounting for Liabilities of the Federal Government*, paragraph 19, states that a liability for federal accounting purposes is a probable future outflow or other sacrifice of resources arising from (1) past exchange transactions; (2) government-related events; (3) government acknowledged events; or (4) nonexchange transactions that, according to current law and applicable policy, are unpaid amounts due as of the reporting date.

SFFAS No. 1, *Accounting for Selected Assets and Liabilities*, paragraph 74, states that when an entity accepts title to goods, whether goods are received or in transit, the entity should recognize a liability for the unpaid amount of the goods. If invoices for those goods are not available when financial statements are prepared, the amounts should be estimated.

Recommendation

We recommend that CFTC improve procedures to properly identify and record accrued liabilities when title to goods is accepted. When actual invoices have not been received, a reasonable estimate should be made and recorded. Supporting documentation should be maintained to support all estimates.

Agency Response

We concur with this finding and agree with the recommendation.



Exhibit II

U.S. COMMODITY FUTURES TRADING COMMISSION

Fiscal Year 2005 Status of Prior Year Comments

The status of prior year material weaknesses, reportable conditions, and compliance matters, is presented below.

Internal Control Over Financial Reporting	Fiscal Year 2005 Status
<i>Material Weaknesses</i>	
Record Accruals and Preparing Financial Statements	Repeated as a Reportable Condition in Exhibit I
Financial Accounting Process over Journal Entries	Resolved
Financial Management System	Partially Resolved; Repeated as a Reportable Condition in Exhibit I
<i>Reportable Conditions</i>	
Fixed Asset System	Repeated in Exhibit I
Recording Interest Receivable on Civil Monetary Penalties	Resolved
Evaluating Undelivered Orders	Repeated in Exhibit I
Compliance with Laws and Regulations	
Noncompliance with the <i>Federal Information Security Management Act</i>	Repeated
Noncompliance with <i>Debt Collection Improvement Act</i>	Resolved
Noncompliance with the <i>Federal Financial Management Improvement Act of 1996</i>	Repeated



Other Statutorily Required Reports

Credit Management and Debt Collection Improvement Act

The CFTC has designed and implemented a comprehensive debt collection program that enables us to effectively administer our multimillion-dollar civil monetary sanctions program. The debt collection program covers account servicing, collection, and close-out and it conforms to the government-wide policies in the Federal Claims Collection Standards, the OMB Circular A-129, and the Debt Collection Improvement Act.

The Commission has \$28.7 million in outstanding civil monetary sanctions which accounts for almost 100 percent of its outstanding debt. The other category of debt that it manages, other administrative debt, is negligible. As of September 30, 2005 the CFTC has forwarded approximately 95 percent of all debts eligible for referral to Treasury for servicing.

Federal Information Security Management Act and Agency Privacy Management

The Commission is in substantial compliance with the Federal Information Security Management Act of 2002 (FISMA) also known as Title III of the E-Government Act of 2002. FISMA requires each Federal agency to provide information security for its information technology assets. Our Independent Auditors' Report disclosed one instance of noncompliance with FISMA. The purpose of FISMA is

to provide a framework for enhancing the effectiveness of information security in the Federal government. FISMA also provides a mechanism for effective oversight of Federal agency information security programs. In Fiscal Year 2005, OMB introduced a new privacy management section of FISMA reporting, which removes privacy compliance reporting from the annual E-Government Act report to the annual FISMA report. FISMA requires system owners to annually review certification and accreditation status of all systems, including those that are accredited (*i.e.*, granted an approval to operate).

E-Government Act of 2002

Each year OMB reports to Congress, a summary of the information reported by agencies. In 2005, the Commission provided a brief overview of our process for determining which information will be made available on the Internet as well as our implementation accomplishments.

In FY 2005, the CFTC made significant progress toward implementation of the policies and best practices published by the Interagency Committee on Government Information as required by Section 207(f)(2) of the E-Government Act of 2002. Specifically, CFTC compiled and published a Web site inventory; established a privacy policy in machine-readable format for visitors to the Web site; completed the administration and publication of CFTC forms to the new government-wide forms portal;



and upgraded its search engine to provide improved customer functionality and internal reporting capabilities. In an effort to gather essential information about customer satisfaction, CFTC entered into an agreement with the Federal Consulting Group and its partner, Foresee Results Inc., to publish a survey to the *www.CFTC.gov* Web site. This survey is providing valuable information on customer needs and behaviors for on-going enhancements to the Web site. The CFTC has a long-standing policy of placing as much information as possible and practicable on its Web site.

One noteworthy highlight was implementation of an automated strategic workforce planning system. Support by agency senior leadership of a more transparent and participative approach to resource management guided the selection of an on-line survey that drew on the collective expertise of all employees to inventory the mission-critical competencies needed over the life of the CFTC strategic plan.

The Commission Participated in Several E-Gov Initiatives During FY 2005.

Personnel Security e-Clearance. In FY 2005, CFTC implemented a 100 percent electronic Personnel Security and Suitability process with the installation of electronic fingerprinting units in its Chicago, Washington, D.C., Kansas City and New York offices. CFTC now electronically captures and transmits fingerprints as part of the required background investigations conducted by the OPM. This equipment is certified by the FBI in compliance with the FBI's Integrated Automated Fingerprint Identification System. This technology significantly improved the satisfactory classification rate of fingerprints, as well as the timeliness in processing and receiving results of fingerprint checks.

Financial Management. In FY 2005, CFTC selected an OMB-approved Financial Management Center of Excellence and initiated the migration process. This migration will be completed in FY 2006.

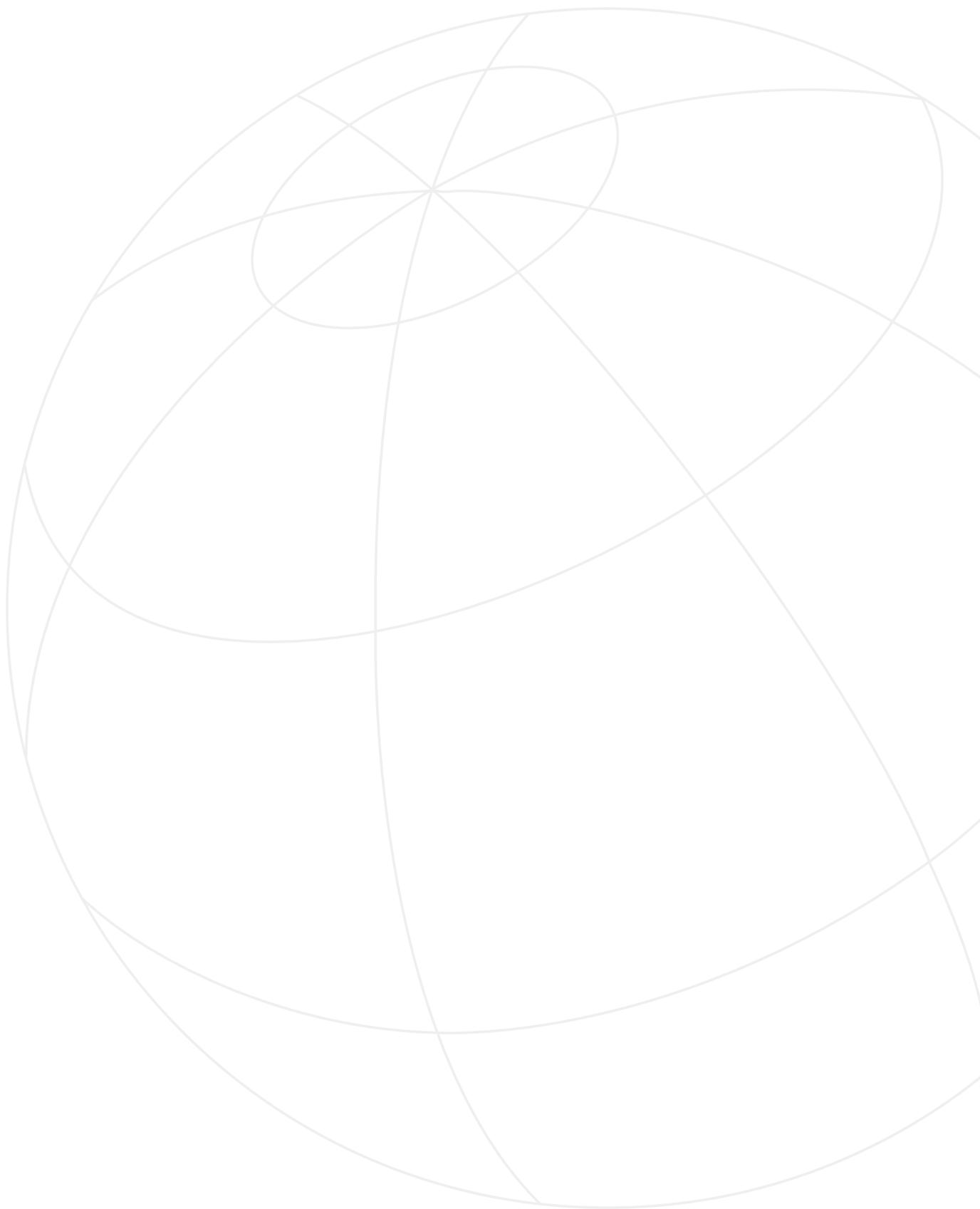
Travel Management. In FY 2005, CFTC initiated migration to an electronic travel system solution through an OMB-approved Financial Management Center of Excellence and initiated the migration process. This migration will be completed in FY 2006.

eLearning. The CFTC offers on-line training consistent with the eLearning initiative and in FY 2005 started planning to broaden the range of on-line course offerings.

Enterprise Human Resources Integration (EHRI). In FY 2005, CFTC participated in the planning activities for the e-Government services that are in the development stage for the EHRI project, including imaging CFTC employee personnel records. Our staff has also contributed to the development of the related e-Payroll and HR Line of Business projects.

Financial Education Web site. Through a partnership with 19 other Federal agencies, the CFTC helped launch a new financial education Web site and toll-free hotline number. The *www.mymoney.gov* Web site and the 1-888-mymoney toll-free hotline were established to provide Americans easy access to information that can help them save, invest, and manage their money wisely to meet important personal goals.





APPENDICES



Appendices

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Inspector General's Assessment of Management Challenges





Office of the
Inspector General

U.S. COMMODITY FUTURES TRADING COMMISSION

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TO: Reuben Jeffery III
Chairman

FROM: A. Roy Lavik *ARL*
Inspector General

DATE: November 10, 2005

SUBJECT: Inspector General's Assessment Of The Most Serious Management Challenges Facing CFTC.

On January 24, 2000, Congress enacted the *Reports Consolidation Act of 2000* to provide financial and performance information in a more meaningful and useful format for Congress, the President, and the public. Included in the Act is the requirement that the Inspector General of each Federal agency summarize what he or she considers to be the most serious management and performance challenges facing the agency and assess the agency's progress in addressing those challenges. In accordance, with the *Reports Consolidation Act of 2000*, we are submitting an annual assessment of the major management challenges confronting the Commodity Futures Trading Commission (CFTC).

Congress left the determination and threshold of what constitutes a most serious challenge to the discretion of the Inspector General. As a result, we applied the following definition in preparing this statement:

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

In Fiscal Year 2002, Congress passed the Accountability of Tax Dollars Act. This Act requires CFTC, along with numerous other federal entities, to have its financial statements audited annually. On January 15, 2004, the Office of the Inspector General (OIG) hired an independent public accounting firm, KPMG LLP, to conduct an audit of the CFTC's financial statements. Fiscal year 2004 was the first fiscal year that the CFTC's financial statements were audited. I am pleased to say that, for fiscal year 2005, the financial statement audit resulted in an unqualified audit opinion. This letter relied on the data contained in the audited financial statements as well as the agency's Performance and Accountability Report (PAR).



Serious Management Challenges

The OIG reviewed all the management challenges listed by program areas as well as external challenges mentioned in the PAR. As a result of our review, the OIG concludes that management fairly stated the challenges faced by the agency and identified in the PAR. Nonetheless, the OIG identifies two management challenges that we consider to be the most serious management challenges facing the agency. Although the PAR identified challenges by program areas, the OIG adopted a broader, agency-wide perspective in selecting two summary management challenges.

We remain steadfast in our concern over Human Resource Planning and attentiveness to Challenges in the Marketplace as the two key management challenges faced by the agency in the near future. These two management challenges in no way diminish other challenges identified by the agency but they ought to guide the agency's efforts in the near future.

I. Human Resource Planning

Last year, we highlighted the forthcoming human resource challenge likely to be faced by the agency in Fiscal Year 2006. This year that challenge is ever more apparent. By March 2006, current estimates are that over twenty percent of CFTC staff including twenty-eight percent of the agency's leadership positions will be eligible for retirement. Consequently, based on these factors, this is a significant challenge faced by a relatively small federal agency which will necessitate careful planning by management. The OIG is heartened by the agency's decision to establish a Human Capital Team to catalogue current skills of existing employees and propose possible pathways for meeting this potential deficit that is likely to occur in the next six months. We look forward to the agency successfully accommodating the approaching wave of employee retirements without materially disrupting the performance of the agency.

II. Challenges in the Marketplace

The Commodity Futures Modernization Act of 2000 (CFMA) transformed the agency from a prescriptive regulator into an oversight regulatory agency. The agency's regulatory mission over the futures industry is guided by core principles stated in the CFMA. Recent innovations in the industry such as the initial public offerings of major Chicago based futures exchanges and futures commission merchants (FCM) have broadened the impact of any malfeasance within the futures industry. How the agency handles unanticipated events such as market disruptions and FCM bankruptcies will be closely watched by a worldwide audience. To date management has handled major turbulences that have occurred during this fiscal year.

When necessary, the OIG has worked with the Government Accountability Office to examine aspects of the agency's operations that members of Congress have expressed a particular interest in understanding, such as the agency's handling of Civil Monetary Penalties and its surveillance of the energy markets. The OIG will continue to provide an independent and constructive review of agency operations so that the agency can continue to improve on its performance in maintaining the integrity and usefulness of the financial products offered by the futures industry.



We take our mission and authority seriously and remain committed to promote integrity, accountability, and transparency within this agency.



Enforcement Litigation for Goal One

Litigation by Goal One

Goal One: Ensure the economic vitality of the commodity futures and option markets.

Manipulation Attempted Manipulation & False Reporting. Manipulation investigations and litigations tend to be among the most complex and resource-intensive matters handled by Enforcement staff. During FY 2005, the Commission's Enforcement program's efforts in this program area are reflected in its handling of alleged misconduct in the feeder cattle and energy markets.

Potential Cattle Market Misconduct - *CFTC v. DeLay, et al.*, No. 05C 5619 (N.D.Ill. filed Sept. 29, 2005). On September 29, 2005, the Commission filed an action charging Todd J. Delay, a futures broker located in Columbus, Ohio, with engaging in a scheme to manipulate the price of the October 2003 Feeder Cattle futures contract traded at the CME. The futures contracts at issue involve "feeder cattle" as defined in the CME contract, which are young steers that are sent to feedlots for finishing into "fed" or "fat" cattle that, in turn, are sent to packers for slaughter. Futures contracts enable cattle producers, meat packers, bulk beef purchasers and others to manage their price risk more effectively, and foster price discovery in the livestock industry. The Commission action charges that Delay caused Feeder Cattle futures contracts to trade at an artificially high price at the end of October 2003 by conspiring with two Nebraska feedlot

managers, Jack McCaffery of North Platte and John D. Lawless of Imperial, to report phony sales of feeder cattle to the U.S. Department of Agriculture (USDA). According to the complaint, the USDA included these sales in its public cash market feeder cattle report, which the CME used to price the CME's Feeder Cattle Index, which ultimately determined the final settlement price for the October 2003 Feeder Cattle futures contract. According to the complaint, the reports of phony sales caused an increase of \$2.85 in the final settlement price of the CME's October 2003 feeder cattle contract, to \$106.98 per hundredweight of feeder steers. The Commission lawsuit also alleges that, as part of the manipulation scheme, Delay violated CFTC-approved speculative position limits for the Feeder Cattle futures contract, in that Delay and other trading accounts he controlled bought twice as many contracts as permitted, all of which benefited from the rise in futures prices. The Commission received invaluable assistance throughout the investigation from the CME's Market Regulation Department.

Potential Energy Market Misconduct. During FY 2005, the Commission's Enforcement program continued its rigorous investigation of the energy industry to determine whether any companies and individuals had engaged in any conduct violative of the CEA. In particular, the Enforcement program investigated conduct that potentially involved false reporting of natural gas trading to companies that compile and publish natural gas index



prices for delivery hubs throughout the U.S. and/or attempts to manipulate and/or manipulation of natural gas index prices.

As a result of extensive investigative work in this area, during FY 2005, the Commission achieved significant success (see discussion below) including: filing a total of 10 enforcement actions; achieving significant litigation results in one action filed in this practice area during the previous fiscal year; and achieving a significant victory in a related subpoena enforcement action.

Administrative Cases Against Energy Companies Filed During FY 2005

- *In re Mirant Americas Energy Marketing LP*, CFTC Docket No. 05-05 (CFTC filed Dec. 6, 2004). On December 6, 2004, the Commission simultaneously instituted and settled an action against Mirant Americas, a wholly owned subsidiary of Mirant Corporation, charging it with attempted energy marketing manipulation and false reporting in connection with its false reports of information concerning natural gas transactions to price compiling publications. The order requires Mirant Americas to cease and desist from further violations as charged and imposes a \$12.5 million civil monetary penalty.
- *In re Cinergy Marketing & Trading, LP*, CFTC Docket No. 05-03 (CFTC filed Nov. 16, 2004). On November 16, 2004, the Commission simultaneously instituted and settled an action against Cinergy Marketing & Trading, LP (Cinergy) charging it with false reporting of trade information concerning natural gas transactions to two price compiling publications. The order requires Cinergy to cease and desist from further violations as charged and imposes a civil monetary penalty of \$3 million.
- *In re BP Energy Co.*, CFTC Docket No. 05-02 (CFTC filed Nov. 4, 2004). On November 4, 2004, the Commission simultaneously instituted and settled an action against BP Energy Company charging it with illegal wash sales involving electricity contracts and the reporting of non-bona fide prices. The order requires BP Energy Company to cease and desist from further violations as charged and imposes a \$100,000 civil monetary penalty.

Previously Filed Administrative Case Resulting in Sanctions During FY 2005 - *CFTC v. American Electric Power Company and AEP Energy Services, Inc.*, No. 2:03-cv-891, Final Judgment and Consent Order (S.D. Ohio filed Jan. 26, 2005). On January 26, 2005, the Commission settled an action brought on September 30, 2003, against American Electric Power Company, Inc. (AEP) and AEP Energy Services, Inc. (AEPES), a subsidiary of AEP. The Final Judgment and Consent Order requires the defendants to pay a \$30 million civil monetary penalty in settlement of charges that defendants falsely reported natural gas trades and attempted to manipulate natural gas prices. In addition, in related actions, AEPES agreed to pay an additional \$30 million to the DOJ to avoid federal criminal prosecution, and \$21 million to the Federal Energy Regulatory Commission.

Individual Energy Trader Enforcement Actions.

During FY 2005, the Commission filed seven enforcement actions charging a total of 16 individual energy traders and charging them with false reporting and attempted manipulation. All the individual defendants are or were natural gas traders working for various energy companies, which are identified below (and most of which were previously sued by the Commission). The traders are charged with submitting reports to various natural gas price compilers, including Gas Daily, Inside FERC, Natural Gas Intelligence, Btu Daily and Natural Gas Week, that contained false information such as fictitious trades or the alteration of price or volume for actual executed trades, all in an attempt to manipulate prices.

- *CFTC v. Whitney*, No. H-05-333 (S.D. Tex. filed Feb. 1, 2005). On February 1, 2005, the Commission filed an action charging that Michael Whitney, formerly an energy trader with Duke Energy Trading and Marketing, LLC, submitted or caused to be submitted false or misleading or knowingly inaccurate price and volume information to Gas Daily and Enerdata, Ltd. concerning natural gas transactions he executed on behalf of Duke Energy between June 2001 and approximately August 2002. As alleged, Whitney submitted the false trade information in an attempt to manipulate the price of natural gas in interstate commerce.



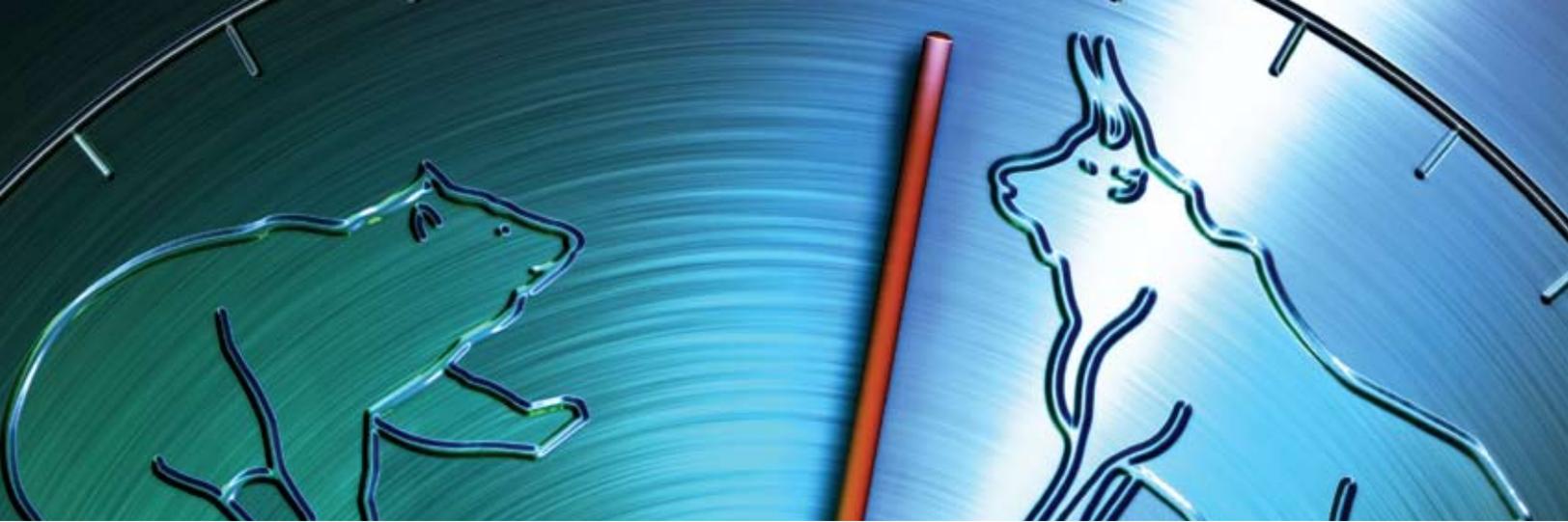
- *CFTC v. Bradley, et al.*, No. 05CV62-CVE-FHM (N.D.Okla. filed Feb. 1, 2005). On February 1, 2005, the Commission filed an action charging that, between January 2001 and October 2002, Jeffrey A. Bradley, formerly the manager of marketing for CMS Field Services, Inc., knowingly submitted false, misleading or knowingly inaccurate transaction information regarding hundreds of natural gas transactions to multiple natural gas reporting firms, including but not limited to Gas Daily, Btu Daily, Natural Gas Intelligence and Natural Gas Week. The action alleges that Bradley did this by reporting fictitious trades as if they were bona fide transactions, by altering the prices and volumes for actual trades, or by reporting non-fixed price trades as if they were fixed price trades. On at least one occasion, Robert L. Martin, formerly the director of gas supply for the same company, allegedly conspired and coordinated with Bradley, and caused reports to be submitted to the same natural gas reporting firms.
- *CFTC v. Atha, et al.*, No. 1:05-CV-0293 (N.D.Ga. filed Feb. 1, 2005). On February 1, 2005, the Commission filed an action charging Paul Atha, Christopher McDonald, and Texas resident Michael Whalen, all formerly Mirant Americas Energy Marketing, LP, energy traders, with false reporting and attempted manipulation of the natural gas markets between January 2000 and late 2000 or early 2001. As charged, Whalen departed Mirant in May 2000 and his alleged violations occurred during his subsequent employment with Cinergy Corporation in Texas. The complaint alleges a series of revealing telephone calls between the Mirant traders and Whalen wherein they conspire about how they should report to Inside FERC to benefit their positions and discuss how to make their reports believable.
- *CFTC v. Johnson, et al.*, No. H-05-0332 (S.D.Tex. filed Feb. 1, 2005). On February 1, 2005, the Commission filed an action charging Denette Johnson, Courtney Cubbison Moore, Robert Harp, Anthony Dizona, John Tracy, and Kelly Dyer with knowingly delivering dozens of reports containing knowingly inaccurate fixed-price, physical, baseload trade information for at least nine locations in the Western United States between October 2001 and June 2002. The complaint also alleges that defendants attempted to manipulate the price of natural gas in interstate commerce by reporting biased information to price reporting companies. Specifically, the complaint alleges that defendants regularly circulated an e-mail with directions to the traders to report prices in such a way that it would benefit their positions. The complaint charges that all these activities occurred while defendants were employed by the energy company Shell Trading Gas and Power Company in providing services for Coral Energy Resources, L.P.
- *CFTC v. Reed, et al.*, No. 05-D-178 (D.Colo. filed Feb. 1, 2005). On February 1, 2005, the Commission filed an action charging that, between May 2000 and October 2002, Matthew Reed, Darrell Danyluk and Shawn McLaughlin engaged in false reporting and attempted manipulation while employed by Enserco Energy Services. McLaughlin engaged in this conduct while acting as President of Enserco. The complaint further alleges that Reed continued the false reporting and attempted manipulation scheme while employed by Concord Energy, LLC, which is also charged with liability for his acts. As alleged, while at Enserco, with McLaughlin's knowledge and consent, Reed, located in Enserco's Colorado office, and Danyluk, located in Enserco's Calgary office, coordinated on an almost daily basis how they wanted to report fictitious trades to numerous reporting firms, including Gas Daily and Natural Gas Intelligence, to benefit trading positions they held.
- *CFTC v. Richmond*, No. 05-M-668 (D.Colo. filed April 12, 2005). On April 12, 2005, the Commission filed an action against Andrew Richmond charging false reporting and attempted manipulation of the price of natural gas. Specifically, the complaint alleges that, between approximately April 2000 and February 2001, while he was the director of marketing at Western, Richmond pressured his subordinates to submit false or misleading or knowingly inaccurate price and volume information to Gas Daily in an attempt to manipulate the price of natural gas.
- *CFTC v. Foley*, No. 2:05 cv 849 (S.D.Ohio filed Sept. 14, 2005). On September 14, 2005, the Commission filed an action charging that between November 2000 and



September 2002, Joseph P. Foley, a former natural gas head trader at AEPES, engaged in attempted manipulation and false reporting of natural gas prices. Foley is alleged to have directed those he supervised to submit false reports of natural gas trading, including false prices and volumes, to index reporting firms that compile energy price surveys or indices (indices), such as Platts. According to the complaint, price and volume information is used by Platts and others in calculating indexes of natural gas prices for various hubs throughout the U.S. The complaint alleges that Foley knowingly directed the delivery of false information to firms such as Platts in an attempt to skew those indexes for his and his company's financial benefit. According to the complaint, Foley knowingly directed those he supervised to deliver thousands of purported natural gas trades to the energy price indexes. The complaint alleges that, of those trades, a substantial number were false or misleading or knowingly inaccurate. Foley went so far as to direct the creation of a computer spreadsheet, titled "IFERC Bogus", to record certain false trade information Foley wanted submitted, according to the complaint.

Subpoena Enforcement Action - CFTC v. The McGraw-Hill Companies, Inc., No. 1:05MS00235 (D.D.C. filed June 16, 2005). On June 16, 2005, the Commission filed an application in the U.S. District Court for the District of Columbia seeking to enforce a subpoena it served on McGraw-Hill in April 2005. The subpoena, issued as part of the Commission's on-going investigations of reporting by energy corporations, seeks information regarding the reporting of natural gas trading records to Platts, an entity owned by McGraw-Hill. The information is being sought in connection with a non-public investigation. The Commission subpoena also seeks McGraw-Hill's documents concerning Platts' use of that data in the indices that Platts calculates and disseminates. Following oral argument on September 27th, the Honorable Judge Lamberth, on October 4th, granted the Commission's motion and ordered McGraw-Hill to provide the requested documents. McGraw-Hill subsequently moved for reconsideration, and the matter is still pending.





Enforcement Litigation for Goal Two

Litigation by Goal Two

Goal Two: Protect market users and the public. Commodity Pools (including “Hedge Funds”), Commodity Pool Operators, and Commodity Trading Advisors. Investors continue to fall prey to unscrupulous CPOs and CTAs, including CPOs and CTAs operating self-described hedge funds. In many of these cases, the defendants have pre-existing business, social, religious, or ethnic ties to the individual investors. These personal relationships enable the defendants to gain the investors’ trust and then lull them into a false sense of confidence. The Commission addresses this violative conduct through a combination of enforcement actions and investor education. Some of the scams are operated as “Ponzi schemes” in which early investors are paid purported “profits” with newer investor funds. The schemes generally involve fraud in soliciting the general public to invest in the pools operated by the CPO or CTA, fraudulent statements concerning the results being achieved by the pool for its investors, and/or outright misappropriation of pool funds by the CPO. During FY 2005, the Commission filed nine enforcement actions in this program area, and also achieved significant litigation results in six actions filed in this practice area during previous fiscal years. Examples of these successes are provided below:

- *CFTC v. Eustace, et al.*, No. 05CV2973 (E.D.Pa. filed June 21, 2005). On June 21, 2005, the Commission filed an

action against Philadelphia Alternative Asset Management Co., LLC (PAAM), a registered commodity pool operator, and Paul M. Eustace, a registered associated person and president of PAAM, alleging fraudulent solicitation and false reporting involving a hedge fund and commodity pools. PAAM is alleged to have accepted over \$230 million from participants and started sustaining massive losses that mounted to over \$140 million by May 2005. On the same day that the complaint was filed, the Commission obtained a statutory restraining order freezing defendants’ assets, preventing the destruction of books and records, and appointing a receiver to take control of defendants’ assets.

- *CFTC v. Bayou Management, LLC*, No. 05 CIV. 8374 (S.D.N.Y. filed Sept. 29, 2005). On September 29, 2005, the Commission filed an action alleging misappropriation and fraud involving Connecticut hedge fund manager Bayou Management, LLC (Bayou Management), its principals, Samuel Israel III and Daniel E. Marino, and Richmond Fairfield Associates, Certified Public Accountants PLLC (Richmond Fairfield). The complaint alleges that the defendants misappropriated customer funds, acquired funds through false pretenses, engaged in unauthorized trading, and misrepresented material facts to actual and prospective investors, including the rates of return the hedge funds earned, the value of assets under management, and the existence and identity of the



accounting firms that had purportedly audited the hedge funds. On the same date that the action was filed, the defendants consented to a preliminary injunction that included an asset freeze. Also on the same date, Israel and Marino, based upon the same conduct, pleaded guilty to criminal charges brought by the U.S. Attorney's Office for the Southern District of New York, White Plains Division. The Commission coordinated its investigation with the U.S. Attorney's Office and the SEC.

- *CFTC v. Princeton Global Management, Ltd., et al.*, No. 99CIV.9669 (S.D.N.Y. filed Sept. 18, 1999). On March 14, 2005, the Commission and SEC announced that a court-appointed receiver in the pending actions against Princeton Economics International, Ltd. and Princeton Global Management, Ltd. (the Princeton Companies) and Martin Armstrong was in the process of distributing over \$50 million as part of an interim distribution to former customers of the Princeton Companies. The distribution stems from actions filed by the Commission and SEC alleging that Armstrong and his companies violated the Commodity Exchange Act and Federal securities laws, respectively, by engaging in unauthorized commodity futures and options trading and then hiding their trading losses of several hundred million dollars by, among other things, the issuance of false net asset value letters. Separately, Mr. Armstrong has been held in civil contempt of a district court order for failing to produce more than \$14 million in assets that the Commission and SEC contend were proceeds of the fraud.

Other FY 2005 Commission Enforcement Actions Alleging Illegal Activity Involving Commodity Pools (including "Hedge Funds"), Commodity Pool Operators, and Commodity Trading Advisors. During FY 2005, the Commission also filed the following actions in this program area: *CFTC v. Schotz, et al.*, No. 04-08889 SJO (SSx) (C.D.Cal. filed Oct. 27, 2004); *CFTC v. Remco Capital Management, et al.*, No. 04 CV 09029 (S.D.N.Y. filed Nov. 16, 2004); *CFTC v. Heffernan*, No. 4 04 23302 25 (D.S.C. filed Dec. 16, 2004); *In re Allen*, CFTC Docket No. 05-08 (CFTC filed April 6, 2005) (simultaneous file and settle; commodity pool operator/commodity trading advisor fraud; sanctions including cease and desist order, five-year personal trading ban and permanent ban from

trading for others); *CFTC v. Steele*, No. 05-3130 (N.D.Ill. filed May 25, 2005); *CFTC v. Beasley, et al.*, No. C 05 02142 (N.D.Cal. filed May 25, 2005); *CFTC v. Eustace, et al.*, No. 05CV2973 (E.D.Pa. filed June 21, 2005); *CFTC v. Pippin*, No. CV 05 4120 (E.D.N.Y. filed Aug. 29, 2005); and *CFTC v. Linuxor Asset Mgt., et al.*, No. 005 CV 8091 (S.D.N.Y. filed Sept. 19, 2005).

Commodity Trading Advisors, Managed Accounts, and Trading Systems. During FY 2005, the Commission filed eight enforcement actions in this program area and achieved significant litigation results in four actions filed in this practice area during previous fiscal years. An example of the Commission's enforcement success in this practice area appears below:

- *CFTC v. Charles*, No. 2:05-cv-02144 (C.D.Ill. filed June 23, 2005). On June 23, 2005, the Commission filed an action against Cameron Charles alleging that he defrauded Watseka Farmers Grain Co. Cooperative (Watseka) by engaging in unauthorized and illegal speculative trading. Specifically, according to the complaint, Charles, a Watseka manager, engaged in unauthorized and illegal speculative trades for Watseka in the soybean market between January and May 2004. The complaint further alleges that Charles concealed from and failed to disclose these trades to Watseka's board of directors and the Illinois Department of Agriculture by making misrepresentations and falsifying Watseka's records to make it appear that Watseka was not at risk in the futures market. The Commission complaint further alleges that in mid-May 2004, a sharp decline in the soybean futures market caused Watseka to receive margin calls on the speculative long futures positions that Charles had created. As alleged, Watseka could not meet the margin calls, thus forcing Watseka into liquidation. According to the complaint, the liquidation resulted in a loss of at least \$1 million to shareholders of Watseka, who were mainly local farmers. The complaint also alleges that Charles solicited and accepted orders for futures transactions from local farmers that Charles executed through Watseka's futures account. In so doing, the complaint alleges, Charles acted illegally as an associated person of a futures commission merchant without proper registration with the Commission. The



Commission's investigation was done in coordination with the Illinois Department of Agriculture and the Illinois Attorney General's office.

Other FY 2005 Commission Enforcement Actions in This Program Area. The Commission's FY 2005 enforcement actions in this program area also included the following: *CFTC v. Jade Trader, et al.*, No. CV04-8213 (C.D.Cal. filed Oct. 1, 2004); *CFTC v. Longhorn Financial Advisors, LLC, et al.*, No. 1:04CV00911 (M.D.N.C. filed Oct. 5, 2005); *In re Berg, et al.*, CFTC Docket No. 05-07 (CFTC filed Jan. 18, 2005) (simultaneous file and settle; commodity trading advisor distribution of inaccurate and outdated disclosure document; sanctions including cease and desist order and \$10,000 civil monetary penalty); *CFTC v. Gemancer, Inc., et al.*, No. CV05 2660 (C.D.Cal. filed April 12, 2005); *CFTC v. Smithers, et al.*, No. 05-80592 (S.D.Fla. filed June 29, 2005); *CFTC v. Lovett*, No. CV05-5074 GHK (MANx) (C.D.Cal. filed July 12, 2005); *CFTC v. Poole*, No. 1:05CV00859 (M.D.N.C. filed Sept. 30, 2005).

Futures Commission Merchants, Introducing Brokers and Their Associated Persons. The Commission diligently redresses misappropriation and other violative conduct by futures commission merchants, introducing brokers, and their associated persons. During FY 2005, the Commission filed 11 enforcement actions in this practice area, and also achieved significant litigation results in one action filed in this practice area during previous fiscal years. An example of the Commission's enforcement success in this practice area appears below:

- *CFTC, et al. v. Cromwell Financial Services, Inc., et al.*, No. 1:05-cv-00210-JD (D.N.H. filed June 12, 2005). On June 12, 2005, the Commission, along with the State of New Hampshire, filed an action against registered introducing broker Cromwell Financial Services, Inc. (Cromwell), its founder and owner (Phillip Tuccelli), and several of its registered associated persons (Michael Saryk, Dennis Gee, Richard Peluchette, and Richard Astern) alleging fraudulent solicitation to trade commodity futures contracts and failure to supervise. Specifically, the complaint alleges that, from at least January 1, 2002 through December 2003, Cromwell fraudulently solicited at least 900 customers who collectively incurred approximately \$19 million in trading

losses. The day after the complaint was filed, the court issued a statutory restraining order, which CFTC representatives executed at four locations in Florida with the assistance of Florida law enforcement.

Other FY 2005 Commission Enforcement Actions in This Program Area. The Commission's FY 2005 enforcement actions in this program area also included the following: *CFTC v. Brickell Key Financial, LLC, et al.*, No. 04-22549 (S.D.Fla. filed Oct. 8, 2004); *CFTC v. United Investors Group, Inc., et al.*, No. 05-80002 (S.D.Fla. filed Jan. 3, 2005); *CFTC v. Lanier*, No. 5:05-CV-516 (W.D.Okla. filed May 10, 2005); *In re Mueller*, CFTC Docket No. 05-09 (CFTC filed June 3, 2005) (simultaneous file and settle; associated person unauthorized trading; sanctions including case and desist order, permanent trading ban and \$30,000 civil monetary penalty); *CFTC v. Commodity Investment Group, Inc., et al.*, No. 05 CV 5741 (S.D.N.Y. filed June 21, 2005); *In re Lochmann*, CFTC Docket No. 05-12 (CFTC filed July 6, 2005) (unauthorized trading by introducing broker associated person); *CFTC v. Musorofiti, et al.*, No. CV 05 3917 (E.D.N.Y. filed Aug. 16, 2005); *CFTC v. American Derivatives Corp., et al.*, No. 1 05-CV 2492 (N.D.Ga. filed Sept. 26, 2005); and *CFTC v. Int'l Currency Exchange, Inc., et al.*, No. 05 CV 8446 (S.D.N.Y. filed Sept. 30, 2005).

Foreign Currency Cases. During FY 2005, the Commission continued to battle fraud perpetrated on the retail public by firms offering trading in off-exchange forex. While much foreign currency trading is legitimate, numerous companies have fraudulently solicited and traded customer foreign currency futures or option trading accounts. Under the CFMA, it is unlawful to offer off-exchange foreign currency futures or option contracts to retail customers unless the counterparty to the contract is a regulated financial entity enumerated in the CFMA, such as a FCM or financial institution. In addition, even if the counterparty is appropriate, the Commission has jurisdiction to investigate and prosecute foreign currency futures or options fraud. Forex trading scams often attract customers through advertisements in local newspapers, radio promotions, or online. These advertisements often tout purportedly high-return, low-risk investment opportunities in foreign currencies. The Commission has brought enforcement actions against both registered firms (for fraud and for other CEA violations,



such as failure to maintain net capital requirements) and unregistered “bucket shops.”

During FY 2005, the Commission filed 17 enforcement actions against firms and individuals selling illegal foreign currency futures and option contracts, bringing the total of such actions to 79 since enactment of the CFMA in December 2000. During FY 2005, the Commission also achieved significant litigation results in eight actions filed in this practice area during previous fiscal years. Since the enactment of the CFMA, the Commission has obtained in its 79 forex enforcement actions approximate monetary sanctions of \$170 million in civil monetary penalties and \$115 million in restitution.

Among the Enforcement program’s successes in this area during FY 2005 were the following:

- *CFTC v. White Pine Trust Corp., et al.*, No. 04-CV-2093 (S.D.Cal. filed Oct. 20, 2004). On October 20, 2004, the Commission filed an action against White Pine Trust Corporation (White Pine) and Richard Matthews charging them with fraudulent solicitation, misappropriation of customer funds, and illegally offering foreign currency options. According to the complaint, since at least February 2003, defendants fraudulently solicited at least \$650,000 from customers. As alleged, defendants also misappropriated funds to pay for personal and business expenses. Moreover, as asserted in papers filed by the Commission, shortly after receiving the subpoena to testify before the Commission, \$1.4 million was withdrawn in cash from an operating account. The complaint alleges that defendants control multiple corporate accounts into which defendants have deposited over \$30 million and upon information and belief, those funds may consist in part, or entirely, of customer funds obtained from hundreds of customers. According to papers filed by the Commission, defendants paid millions out of these accounts for extravagant personal and purported business expenses, including NFL football tickets, nightclubs, and Saks Fifth Avenue purchases. According to an October 28, 2004 report filed by the court-appointed receiver, the receiver has control over real property exceeding \$3 million in value, and also has possession of a yacht owned by White Pine, which was purchased for \$390,000 in cash in 2003. The receiver’s report also states it is investigating the possible diversion of substantial funds to Mexico and Belize. On October 28, 2004, the court entered a preliminary injunction against White Pine enjoining it from further violations as charged, and also confirmed a restraining order entered on October 21 against White Pine and Richard Matthews that freezes defendants’ assets and appoints a temporary receiver.
- *CFTC v. World-Wide Currency Services Corp., et al.*, No. 03-80032-CIV-HURLEY, Order Adopting Magistrate Judge’s Report & Recommendation (S.D.Fla. entered Jan. 4, 2005). On January 4, 2005, the court entered an order assessing a total of \$6,141,748 in civil monetary penalties against defendants World-Wide Currency Services Corp., its president (Genady Spivack) and its vice-president Ellison Kent Morris. This Commission filed this enforcement action on January 13, 2003, and on August 5, 2004, the court granted the Commission’s summary judgment motion finding that the defendants fraudulently sold foreign currency futures contracts to customers under the guise of conducting spot currency transactions. Also, according to the summary judgment order, defendants solicited customers using telemarketing tactics and claims urging customers to act quickly to take advantage of current market conditions and make substantial profits, with minimal risk. One customer was promised a monthly return of one to two percent, another was told to expect an annual profit of 20 percent, still others were promised anywhere from doubling their money to earning as much as five times their investment in just a few months, according to the order. The summary judgment order required repayment to defrauded customers of \$1,092,880.
- *CFTC v. Sonoma Trading Corp., et al.*, No. 05-60342 (S.D.Fla. filed March 9, 2005). On March 9, 2005, the Commission filed an action against Sonoma Trading Corporation (Sonoma) and its owner, William David Seigler, Jr., charging that they wrongfully solicited and sold foreign currency options. The Commission complaint alleges that since December 2002, Sonoma and Seigler, through a Web site operated in the name of Sonoma, solicited retail customers to trade



foreign currency options contracts, touting Sonoma as “The Premier Foreign Exchange Options Dealer in the Americas.” As further alleged, in connection with these solicitations, the defendants instructed customers to wire transfer funds to a U.S.-based bank for routing to a Sonoma bank account located in San Jose, Costa Rica. To conduct these activities lawfully, the complaint charges that Sonoma and Siegler either were required to execute the options transactions on a contract market or a foreign board, or were required to register with the Commission as a futures commission merchant. The complaint alleges that they did neither. On the same day the complaint was filed, court issued an order freezing the defendants’ assets and preventing the destruction of their books and records.

- *CFTC v. Emerald Worldwide Holdings, Inc., et al.*, No. CV03-8339 AHM (C.D.Cal. entered April 19, 2005). April 19, 2005, the court issued a default order requiring defendant City Trust and Investment Co. Ltd. (CTI) of Tokyo, Japan, to repay defrauded customers more than \$3.2 million, and to pay a civil monetary penalty of \$8.2 million, in connection with a forex scam operated by CTI and Emerald Worldwide Holdings, Inc. (Emerald). The order stems from an amended complaint filed by the Commission on May 10, 2004, alleging that defendants CTI and Emerald Worldwide Holdings, Inc. (Emerald) operated together in fraudulently soliciting customers in Japan and China to invest more than \$5 million to trade illegal off-exchange foreign currency futures contracts in the United States. Specifically, the Commission’s amended complaint alleged that Emerald’s promotional materials, which were disseminated by employees of CTI, contained false statements regarding Emerald’s registration status and affiliation with entities that were legitimately registered with the Commission. The complaint also alleged that, rather than trade the customers’ funds as promised, Emerald and CTI transferred the funds to various bank accounts in the United States, Japan, China, and Hong Kong in the names of Emerald, CTI, and others. Additionally, on March 15, 2005, Judge Matz issued an order requiring relief defendant ACE Emerald W. Holding, Inc. (ACE Emerald), of Las Vegas, Nevada, to disgorge

its ill-gotten gains. ACE Emerald, as a relief defendant, was charged with receiving customer funds to which it was not entitled, but was not charged with participation in any violation of law. The lawsuit is still pending as to defendants Emerald, Jian Zhuang and Hao Jan Lu, and relief defendants ACE Capital Advisory Group Inc., Lynwood Jen, and Esther Pranolo.

- *CFTC v. DBS Capital, Inc., et al.*, No. 03 *CFTC v. DBS Capital, Inc., et al.*, No. 03-1379 VRW, Consent Order Of Permanent Injunction (N.D.Cal. entered June 17, 2005). On June 17, 2005, the court entered a consent order of permanent injunction and other equitable relief against defendants DBS Capital, Inc., and Douglas Stevens, the founder and president of DBS. The order stems from an enforcement action filed on March 31, 2003. Without admitting or denying the findings, the defendants consented to entry of the order that found the defendants have been offering and selling illegal, off-exchange futures contracts to the retail public; and they fraudulently solicited approximately \$14 million from approximately 200 retail customers. In addition to being permanently enjoined from further violations as charged, the defendants were ordered to make restitution to customers of \$11,505,025, plus post-judgment interest, and to pay a \$3,191,597 civil monetary penalty.
- *CFTC v. World Market Advisors, Inc., et al.*, No. 05-60928-CIV-ALTONGA/TURNOFF (S.D.Fla. filed July 21, 2005). On July 21, 2005, the Commission filed an action against five Florida foreign currency firms, World Market Advisors, Inc. (WMA), U.S. Capital Management, Inc. (U.S. Capital), United Equity Group, Inc. (United Equity), Liberty One Advisors, LLC (Liberty One), Lighthouse Capital Management, LLC (Lighthouse), and five individuals, Jason T. Dean of Pompano Beach, Florida, Steven D. Knowles and Paul F. Plunkett of Deerfield Beach, Florida, Joseph D. Valko of Coconut Creek, Florida and Jeffrey Paul Jedlicki of Boca Raton, Florida, charging that defendants defrauded customers they solicited to trade foreign currency options contracts. The complaint also charges three Florida-based foreign currency dealers, Universal Options, Inc. (Universal Options), Qualified Leverage Providers, Inc. (QLP) and Safeguard FX, LLC (Safeguard), with liability as



principals for the acts of the five foreign currency firms. Specifically, the Commission's complaint alleges that since October 2002, WMA and a series of short-lived affiliates and successors, including the other corporate defendants, through their brokers, including Jedlicki, fraudulently solicited customers over the telephone throughout the U.S., Canada, and the U.K., using high-pressure "boiler room" sales tactics, to open accounts to trade foreign currency options contracts. The complaint further alleges that defendants solicited at least 924 customers, who collectively invested at least \$17.1 million to trade foreign currency options contracts. The customers paid defendants at least \$8.6 million in commissions, and lost approximately \$13.6 million in their trading accounts, according to the complaint. Over 96 percent of the customers lost money, and most customers lost all of their investments. On the day the action was filed, the court entered a restraining order that, among other things, freezes the assets of all defendants except Universal Options, QLP and Safeguard. The Commission received cooperation in their investigation and prosecution of this matter from the Florida Attorney General's Office of Statewide Prosecution, the Florida Office of Agricultural Law Enforcement, the Office of Financial Regulation and the Broward County Sheriff's Office, among others. The Commission also received assistance from the National Futures Association.

Other FY 2005 Commission Enforcement Actions Alleging Illegal Forex Activity. During FY 2005, in addition to one enforcement action it filed under seal, the Commission also filed the following actions in this program area: *CFTC v. Foreign Fund, et al.*, No. 0 04 098 (M.D.Ten. filed Oct. 5, 2004); *In re Bentley Rothchild Group, Inc., et al.*, CFTC Docket No. 05-04 (CFTC filed Nov. 23, 2004) (simultaneous file and settle; forex fraud; sanctions including cease and desist order and \$10,000 civil monetary penalty); *CFTC v. Richmond Global Associates, LLC, et al.*, No. 05 CV 2181 (S.D.N.Y. filed Feb. 16, 2005); *CFTC v. Premium Income Corp., et al.*, NO. 3-05 CV 0416M (N.D.Tex. filed March 2, 2005); *CFTC v. Mercury Partners, Inc., et al.*, No. 05-60328 (S.D.Fla. filed Mar. 7, 2005); *CFTC v. G7 Advisory Services, LLC, et al.*, No. 05-80313 (S.D.Fla. filed April 12, 2005); *CFTC v. Presidential FX, Inc.,*

et al., No. 1:05CV492 (E.D.Va. filed April 29, 2005); *CFTC v. Webman, et al.*, No. 05 CV 4819 (S.D.N.Y. filed May 19, 2005); *CFTC v. Windsor Forex Trading Corp., et al.*, No. CV 05 2547 (E.D.N.Y. filed May 26, 2005); *CFTC v. National Investment Consultants, et al.*, No. C 05 2641 (N.D.Cal. filed June 29, 2005); *CFTC v. de Wet, No. 05 CV 8401* (S.D.N.Y. filed Sept. 30, 2005); *CFTC v. Efrogman, et al.*, No. 05 CV 8422 (S.D.N.Y. filed Sept. 30, 2005) (violation of prior Commission order in addition to forex fraud); and *CFTC v. Yanev*, No. C2 05 900 (S.D. Ohio filed Sept. 29, 2005).

Precious Metals And Other Illegal Off-Exchange Cases. During FY 2005, the Commission's Enforcement program prosecuted the following two actions that alleged non-forex, illegal off-exchange trading.

- *CFTC v. E-Metal Merchants, Inc., et al.*, No. 05-21574 (S.D.Fla. filed June 13, 2005). On June 13, 2005, the Commission filed an action against E-Metal Merchants, Inc., and two of its corporate officers, Benji Dayan and Andrew Stern, both of Miami, Florida, charging them with purchasing and selling illegal, off-exchange metals options. Specifically, the Commission's complaint charges that, since at least May 2004, E-Metal Merchants accepted over \$6.9 million from more than 200 customers for the purpose of engaging in the purchase and sale of illegal off-exchange metals option contracts. According to the complaint, E-Metal Merchants transferred more than \$5.4 million from its customers' account to the firm's operating account, \$575,000 to the firm's off-shore account in New Zealand, and \$509,000 to Universal Financial Holding Company, a firm owned by the secretary of E-Metal Merchants, Andrew Stern. As further alleged, that firm paid the president of E-Metal Merchants, Benji Dayan, and the secretary, Stern, over \$1 million from customer funds. Dayan and Stern are controlling persons of E-Metal Merchants and, therefore, are liable for the firm's violations of the CEA, the complaint alleges. On the same day the action was filed, the court entered a restraining order that, among other things, freezes defendants assets.



- *In re Trade Exchange Network*, CFTC Docket No. 05-14 (CFTC filed Sept. 29, 2005). On September 29, 2005, the Commission simultaneously commenced and settled an action against Trade Exchange Network Limited (TEN), a limited liability company based in Dublin, Ireland, alleging that TEN solicited and accepted orders from U.S. residents for commodity option contracts that were not excepted or exempted from the Commission's ban on options. TEN owns and operates an Internet-based trading platform that facilitates trading through its Web sites *www.Tradesports.com*, *www.Intrade.com*, and *www.TradebetX.com*. According to the findings in the order, TEN actively solicited U.S. residents to trade such contracts by retaining an individual in the U.S. to market TEN's products throughout the country, and TEN ultimately developed a U.S. customer base that was roughly 33 to 40 percent of its total customer base. The order further finds that the commodity option contracts offered on TEN's Web sites were not excepted or exempted from the Commission's regulation banning options trading, and therefore violated the CEA. TEN's high level of cooperation during the underlying investigation resulted in a reduction of the civil monetary penalty to \$150,000, which TEN agreed to pay. The order also calls for TEN to cease and desist from further violations of the CEA and comply with specific undertakings. In consenting to the entry of the Commission's order, TEN neither admitted nor denied the findings made in the order.



Enforcement Litigation for Goal 3

Litigation by Goal Three

Goal Three: Ensure market integrity to foster open, competitive, and financially sound markets.

Trade Practice. The legislative history of the CEA notes that one of the fundamental purposes of the Act is to ensure fair practices and honest dealing in the futures market and to control those forms of speculative activity that demoralize the market to the detriment of producers, consumers, and the markets. Consistent with Congress' mandate, the Commission brings trade practice cases to address a variety of unfair, abusive, or deceptive ploys by traders to avoid exposing their orders to market risk. Such actions can create non-competitive prices in the marketplace and have the potential to harm public customers, producers, and others. Improper trade practices include a variety of activities, including trading done in violation of exchange rules, such as trading ahead of a customer order, wash trading, accommodation trading, and fictitious trading. During FY 2005, the Commission filed six enforcement actions in this program area, and also achieved significant litigation results in one action filed in this practice area during previous fiscal years. An example of the Commission's success in this program area appears below:

United States v. Helffrich. With the assistance of the Commission's Enforcement program, the U.S. Attorney for the Northern District of Illinois obtained a criminal

conviction of Stuart Michael Helffrich for wire fraud and fraudulent conversion of his customers' commodity futures positions. Helffrich, while a registered floor broker at the CBOT, transferred winning trades from his customers' accounts into his own trading account and "parked" his own losing trades in their accounts, all to cover up mounting losses and to inflate the value of his own personal trading accounts. The scheme went on for approximately six weeks until it was discovered. Helffrich caused trading losses of over \$866,000 to two large grain dealers, and to Helffrich's employer, who ultimately repaid the customers. In addition, the scheme caused the customers to pay additional margin and exposed them to additional market risk. On May 10, 2005, U.S. District Court for the Northern District of Illinois issued the guilty verdict and on September 1, 2005, Helffrich was sentenced to 41 months' imprisonment, with 3 years' supervised release at the conclusion of the period of incarceration. In addition, Helffrich was ordered to repay his employer more than \$800,000. This criminal case was the result of a Division referral after the Chicago Board of Trade revoked Helffrich's membership and the Commission revoked his registration. *In the Matter of Stuart Michael Helffrich*, SD 04-08 (Sept. 3, 2004).

Other FY 2005 Enforcement Program Actions Alleging Trade Practice Violations. During FY 2005, the Commission's Enforcement program filed the following trade practice enforcement actions: *In re Hucko*, CFTC Docket



No. 05-01 (CFTC filed Oct. 26, 2004) (simultaneous file and settle; fraudulent trade allocation; sanctions including cease and desist order, permanent trading ban and \$50,000 civil monetary penalty); *In re Hencorp Becstone Futures LC, et al.*, CFTC Docket NO. 05-06 (CFTC filed Dec. 22, 2004) (simultaneous file and settle; wash sales and reporting of non-bona fide prices involving CSCE coffee futures; sanctions including cease and desist order and \$100,000 civil monetary penalty); *In re Maddox*, CFTC Docket No. 05-10 (CFTC filed June 9, 2005)(simultaneous file and settle; fraudulent trade allocation; sanctions including \$25,000 civil monetary penalty, \$31,000 restitution and one year personal trading ban); *In re Armajaro Trading Ltd., et al.*, CFTC Docket No. 05-11 (CFTC filed June 21, 2005) (simultaneous file and settle; fictitious and non-competitive trading in CSCE cocoa spread cross trades; sanctions including cease and desist order and total of \$60,000 civil monetary penalties); and *In re Credit Lyonnais Rouse Ltd.*, CFTC Docket No. 05-13 (CFTC filed Aug. 24, 2005) (simultaneous file and settle; fictitious and non-competitive trading in CSCE cocoa spread cross trades; sanctions including cease and desist order and \$85,000 civil monetary penalty).

Financial, Supervision, Compliance and Record-keeping. During FY 2005, the Commission filed one enforcement action in this program area during FY 2005, and also achieved significant litigation results in two actions filed in this practice area during previous fiscal years. An example of the Commission's success in this program area is provided below:

- *In the Matter of G. Victor Johnson and Altschuler, Melvoin and Glasser, LLP*, CFTC Docket No. 04-29 (CFTC filed June 13, 2005). On June 13, 2005, the Commission issued an order accepting settlements of accounting firm (Altschuler, Melvoin & Glasser, LLP (AMG)) and engagement partner (G. Victor Johnson) arising from audits performed of a commodity pool that failed to detect a fraud perpetrated on investors by the pool's operator. Under the terms of the settlements, Johnson and AMG will pay \$200,000 to the defrauded pool investors, will repay all audit fees earned from the audit engagements (which will go to victims of the fraud) and will pay a civil monetary penalty of \$150,000. Additionally, Johnson

will not participate in any audit of any commodity pool or Commission registrant in certain capacities until after December 31, 2005, and AMG will provide training in fraud examination and detection to staff, as well as review portions of its audit programs that were implicated in the alleged audit failures and report to the Commission on its review.

Statutory Disqualifications. During FY 2005, the Commission filed five enforcement actions in this program area. An example of the Commission's success in this program area is provided below:

- *In re McKenna*, CFTC Docket No. SD 05-03 (CFTC filed May 20, 2005). On May 20, 2005, the Commission simultaneously filed and settled an action against Brion Scott McKenna, a former gas trader for Williams, a subsidiary of The Williams Companies, Inc., a publicly-traded company, revoking his registration as an associated person for three years and ordering him to cooperate fully with the Commission and other Federal authorities in connection with this proceeding and any related inquiry. The Commission's action was the result of McKenna's guilty plea in the U.S. District Court for the Northern District of California to a felony violation involving manipulation while employed as a natural gas trader at Williams. Previously, on July 29, 2003, the Commission simultaneously filed and settled an action against Williams for false reporting of natural gas trading information, with Williams agreeing to pay a \$20 million civil monetary penalty.

Other Commission Actions Filed In This Program Area. During FY 2005, the Commission instituted the following additional statutory disqualification actions: *In re Wnukowski*, CFTC Docket No. SD-5-01 (CFTC filed Dec. 30, 2004); *In re Beacon Hill Asset Mgt. LLC*, CFTC Docket No. SD 05-02 (CFTC filed May 3, 2005); *In re Palomino Capital Mgt.*, CFTC Docket No. SD 05-04 (CFTC filed July 14, 2005); and *In re Kaulentis*, CFTC Docket No. SD 05-05 (CFTC filed Aug. 1, 2005).



The CFTC Glossary

THE CFTC GLOSSARY

A GUIDE TO THE LANGUAGE OF THE FUTURES INDUSTRY

http://www.cftc.gov/opa/glossary/opaglossary_a.htm

Because the acronyms of many words and phrases used throughout the futures industry are not readily available in standard references, the Commission's Office of External Affairs compiled a glossary to assist members of the public.

This glossary is not inclusive, nor are general definitions intended to state or suggest the views of the Commission concerning the legal significance, or meaning of any word or term. Moreover, no definition is intended to state or suggest the Commission's views concerning any trading strategy or economic theory. If you cannot find the term you are looking for or have any other comment, please email us at glossary@cftc.gov. The glossary was last revised September 2005.

Glossary of Acronyms

AE.....	The Actuarials Exchange, LLC
AEP.....	American Electric Power Company, Inc.
AEPES.....	AEP Energy Services, Inc.
ALJ.....	Administrative Law Judge
AMG.....	Altschuler, Melvoin & Glasser, LLP
AML.....	Anti-Money Laundering
AWB.....	Australian Wheat Board
BSE.....	Bovine Spongiform Encephalopathy
BTEX.....	BrokerTex Futures Exchange
CBOT.....	Chicago Board of Trade



CBFB.....	Cross-Border Futures Broker
CCORP.....	The Clearing Corporation
CEA.....	Commodity Exchange Act
CESR.....	Committee of European Securities Regulators
CFTC.....	Commodity Futures Trading Commission
CFMA.....	Commodity Futures Modernization Act of 2000
CME.....	Chicago Mercantile Exchange
COSRA.....	Council of Securities Commissions of the Americas
CPO.....	Commodity Pool Operator
CSRS.....	Civil Service Retirement System
CTA.....	Commodity Trading Advisor
CTI.....	City Trust and Investment Company Limited
DART.....	Designation and Rule Tracking System
DCIO.....	Division of Clearing and Intermediary Oversight (CFTC)
DCM.....	Direct Clearing Member
DCO.....	Derivatives Clearing Organization
DMO.....	Division of Market Oversight (CFTC)
DOJ.....	Department of Justice
DOL.....	Department of Labor
EHRI.....	Enterprise Human Resources Integration
ESC.....	Enterprise Services Center
EUREX US.....	U.S. Futures Exchange, LLC
FBI.....	Federal Bureau of Investigation
FCM.....	Futures Commission Merchant
FCOM.....	FutureCom
FECA.....	Federal Employees Compensation Act
FEGLI.....	Federal Employees Group Life Insurance Program
FEHBP.....	Federal Employees Health Benefits Program
FERC.....	Federal Energy Regulatory Commission
FERS.....	Federal Employees' Retirement System
FILAC.....	Filings System



FIRREA	Financial Institutions Reform, Recovery, and Enforcement Act of 1989
FISMA	Federal Information Security Management Act of 2002
FMFIA	Federal Managers' Financial Integrity Act of 1982
FTE	Full-time Equivalent
FWC	Future Workers Compensation
FY	Fiscal Year
GAAP	Generally Accepted Accounting Principles
GAO	Government Accountability Office
GCC	Guaranty Clearing Corporation
GMAC	Global Markets Advisory Committee
GPRC	Government Performance and Results Act of 1993
IB	Introducing Broker
ICC	Intermarket Clearing Corporation
IOSCO	International Organization of Securities Commissions
ISS	Integrated Surveillance System
JO	Judgment Officer
KCBT	Kansas City Board of Trade
LCH	London Clearing House
MDA	Management's Discussion and Analysis
MGE	Minneapolis Grain Exchange
MOU	Memorandum of Understanding
MMOU	Multilateral Memorandum of Understanding
NFA	National Futures Association
NYCC	New York Clearing Corporation
NYMEX	New York Mercantile Exchange
OCC	The Options Clearing Corporation
OGC	Office of the General Counsel (CFTC)
OIRM	Office of Information Resources Management (CFTC)
OMB	Office of Management and Budget
ONXCC	OnExchange Clearing Corporation
OPM	Office of Personnel Management



ORB.....	Other Retirement Benefits
PAAM.....	Philadelphia Alternative Asset Management Co., LLC
PART.....	Program Assessment Rating Tool
QLP.....	Qualified Leverage Providers, Inc.
RIC.....	Registered Investment Companies
RWG.....	Registration Working Group
SC4.....	Standing Committee 4
SC5.....	Standing Committee 5
SEC.....	Securities and Exchange Commission
SFE.....	Sydney Futures Exchange Limited
SFFAS.....	Statement of Federal Financial Accounting Standards
SFP.....	Security Futures Products
SRO.....	Self-Regulatory Organization
TAC.....	Technology Advisory Committee
TEN.....	Trade Exchange Network Limited
USA PATRIOT.....	Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism
USDA.....	United States Department of Agriculture
UK.....	United Kingdom
WMA.....	World Market Advisors, Inc.



