MarketWatch
November 15, 2011 9:48 AM EST

Nov. 14, 2011, 3:42 p.m. EST

Financial regulators face more work and less money

By Anjelica Tan of Medill News Service

WASHINGTON (MarketWatch) — Two federal agencies responsible for regulating Wall Street are facing budget constraints, limiting their ability to close accounting gaps and leaving uncertainty in the markets.

The Securities and Exchange Commission and the Commodity Futures Trading Commission, the top financial regulators in Washington, must find a way to carry out more duties with reduced budgets as they continue to implement the Dodd-Frank Act through the summer of 2012.

The SEC estimates it needs $109.0 million in new funding resources to perform its Dodd-Frank duties in 2012, according to a Government Accountability Office report. The CFTC estimates it needs $77.0 million for the same reason.

But the agencies will be funded at or below levels from last year.

The SEC requested $1.407 billion for fiscal year 2012, but the House denied the 19% budget increase and allocated $1.185 billion — the 2011 funding level.

The CFTC faces a similar situation. The agency requested a $308.0 million budget for fiscal year 2012, but the House approved $171.9 million — or 44% less than what the CFTC requested, and 15% below 2011 levels.

“The SEC already had inadequate resources to handle all of its responsibilities, and Dodd-Frank added to that significantly,” said Gregory Little, a lead defense attorney in SEC investigations involving insider trading allegations and inflated earnings disclosures.

“Now it’s being asked to do much more without adding more resources,” said Little, who is a partner at White & Case LLP in New York.

“There are many hard questions about financial regulation to answer,” added Jeffrey Frankel, professor at the Harvard Kennedy School of Government. “The question of funding the SEC is incredibly easy to answer.”

A ‘deficit neutral’ budget

One of the SEC’s additional duties mandated by Dodd-Frank is to set up five new offices: Investor Advocate, Credit Ratings, Municipal Securities, Whistleblower Protection, and Minority and Women Inclusion.

The SEC is hiring 331 new full-time employees in 2012 to staff the offices, according to a GAO report. The employees being hired for Dodd-Frank duties represent 56.3% of the SEC’s total agency-wide hiring increase of 588 employees in 2012.

“While the SEC budget by law is deficit neutral, we are committed to using precious resources as effectively as possible,” said SEC spokesman John Nester.

Unlike the CFTC, which is fully funded by Congress, the SEC’s resources come directly from offsetting Treasury collections. Under Dodd-Frank, the SEC is required to raise or lower the transaction fees Wall Street pays to match Congress’ budget appropriation.

Right now, Wall Street pays about $20 for every $1 million in securities transactions — so the industry benefits if spending is reduced.

Continuous debate on the Hill

Republicans have been pushing back against financial regulation.

“I don’t think the problem facing our financial regulators is a lack of money,” said Mark Calabria, director of financial regulation studies at the Cato Institute, a libertarian think tank based in Washington. “Right now, it’s misguided priorities.”

Rep. Scott Garrett, New Jersey Republican, proposed a bill in June that requires the SEC to perform a robust analysis to ensure the benefits of the agency’s rulemaking outweigh the costs.

“One of the points we made through last year’s hearings was that some of these agencies have failed in their duties,” said Garrett, chairman of the House Finance Subcommittee on Capital Markets and Government-Sponsored Entities and vice chairman of the House Budget Committee.

“The same federal agencies that missed the mark on the Bernie Madoff ponzi scheme are now being rewarded with increased funding and more power,” Garrett continued, referring to the SEC. “For the people who lost millions of dollars in that scandal, what would they think of that?”

Democrats including Rep. Barney Frank, who co-authored the Wall Street protection act, fire back, restating the need to adequately fund the SEC and CFTC.

“They’re trying to sabotage the situation by not giving money,” said Frank. “These are complicated subjects that involve very smart people, and we need technology and resources for these agencies.”

Red flags

While the SEC and CFTC are just two of eleven federal agencies responsible for carrying out Dodd-Frank, they arguably face the most scrutiny.

A recent case the SEC and CFTC took heat for is the Oct. 31 bankruptcy of MF Global, former New Jersey Gov. John Corzine’s broker-dealer that went under after losing more than $600 million in risky European bets.

The regulators dispute this.

“I think we should be clear, MF Global’s failure is a result of MF Global decisions, investment decisions, bad decisions and not the result of regulatory failure,” said Schapiro in a PBS interview one week after the bankruptcy.

Barbara Roper, director of investor protection at the Consumer Federation of America, said lack of funding may have played a role.

“We have a system of regulation that allows MF Global a good deal leeway in what it invested in. The SEC and CFTC were paying attention. They were using regulatory tools available in the case of MF Global.”

“No matter how well you fund the agencies, they will miss problems on occasion,” she said. “But a lack of funding does unquestionably contribute to these sorts of regulatory failures.”