



# FIA Forum: Commodities 2024

## CFTC Enforcement

September 17, 2024

Moderator: Neal Kumar, Wilkie Farr & Gallagher

Panelists: Elizabeth Davis, Davis Wright Tremaine

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# Self-Reporting and Cooperation Credit

- CFTC Enforcement Advisory Regarding Penalties, Monitors and Consultants, and Omissions (Oct. 17, 2023)
  - Advisory notes that enforcement staff will seek admissions in lieu of the prior “no admit or deny” default in certain settlements, harsher penalties especially for recidivists, and imposition of independent third-party monitors when circumstances warrant.
- Prior enforcement advisories focused on the benefits of self-reporting and cooperation.
  - See, e.g., CFTC Updated Advisory on Self Reporting and Full Cooperation (September 2017).
  - If a company or individual self-reports, fully cooperates, and remediates, the Division will recommend that the Commission consider a substantial reduction from the otherwise applicable civil monetary penalty. A reduced civil monetary penalty may be recommended where wrongdoing was not self-reported but otherwise fully cooperated and remediated deficiencies. The most substantial reductions will be when the misconduct was self-reported, full cooperation, and remediation.



# Self-Reporting and Cooperation Credit (cont'd)

- CFTC Updated Advisory on Self Reporting and Full Cooperation (September 2017) sets forth the requirements for full self-reporting and cooperation credit:
  - Voluntary disclosure to the Division-disclosure must be made prior to an imminent threat of exposure of the misconduct; made to the Division within a reasonably prompt time after becoming aware of the misconduct; and include all relevant facts known at the time of disclosure including all relevant facts about the individuals involved in the misconduct.
  - Full cooperation-fully adhere to the terms of the Division's January 2017 Advisories.
  - Timely and appropriate remediation of flaws in compliance and control programs.
- Cooperation, Self-Reporting and Remediation Recognition Staff Guidance (Oct. 29, 2020)
  - Intended to provide transparency and clarity regarding when and how the Division's self-reporting and cooperation assessments will be reflected and recognized in Commission enforcement orders.



# Self-Reporting and Cooperation Credit (cont'd)

- *In re Raizen Energia SA*, CFTC Dkt. No. 24-15 (Aug. 19, 2024)
  - Energy company and sugar merchant found to have engaged in wash sales and noncompetitive transactions by executing exchange for physical (EFPs) transactions involving sugar futures contracts traded on ICE Futures.
  - Respondents' EFPs were illegal wash sales and noncompetitive transactions because they were not independently controlled in violation of CEA Section 4c(a)(1) and (2)(A) and Reg. 1.38(a).
  - Respondents admitted the facts in the speaking order and acknowledged that their conduct violated the CEA and Regulations.
  - Respondents implemented remedial measures including ceasing the execution of EFPs between the Raizen entities, formulating a written compliance manual, training, retaining additional compliance personnel, and creating an email compliance hotline.
- *See also* Settlement of Charges Against Raizen Trading SA, ICE Disciplinary Notice, Case No. 2023-012 (April 19, 2024).



# Self-Reporting and Cooperation Credit (cont'd)

- Statement of Commissioner Caroline D. Pham on Self-Reporting and Cooperation Credit in Enforcement Actions to *In re Raizen Energia SA*, CFTC Dkt. No. 24-15 (Aug. 19, 2024)
  - Raised concerns regarding CFTC’s “contradictory” approach to self-reporting by market participants of potential violations and the standard applied for prompt self-reporting for purposes of cooperation credit.
    - Speaking order does not acknowledge cooperation credit, but Commissioner Pham believed that Respondents promptly self-reported the violations to the Division after an internal investigation.
    - Notes recent CFTC matters where reporting 6 months after the initial discovery of a potential non-compliance issue where an internal review is conducted was *not* considered “prompt” self-reporting. Pham stated “[b]ut it is more appropriate to consider whether the self-report was made promptly after a firm makes a determination in good faith that a material non-compliance issued has occurred, not from when the potential issue was discovered,” and that 6 months *is* a reasonable time.



# Self-Reporting and Cooperation Credit (cont'd)

- Statement of Commissioner Caroline D. Pham on Self-Reporting and Cooperation Credit in Enforcement Actions to *In re Raizen Energia SA*, CFTC Dkt. No. 24-15 (Aug. 19, 2024)
  - Commissioner Pham also noted the inherent conflict and “untenable” legal risk associated with self-reporting before the completion of an internal review or investigation.
  - Commissioner Pham stated that the CFTC has sought to bring fraud charges against market participants for allegedly making false statements to the CFTC when a market participant later discovers that the information in the initial self-report was not entirely accurate, which discourages prompt self-reporting because market participants will need to take additional time to ensure accuracy and mitigate the risk of being charged with making fraudulent false statements.
  - Statement recommends including a safe harbor from false statement charges if self-reported information later supplemented or corrected.
- Statement also proposed enhancements to CFTC internal governance and procedures.



# Misappropriation of Material Non-Public Information (MNPI)

- *In re Trafigura Trading LLC*, CFTC 24-08 (June 17, 2024)
  - Company alleged to have obtained MNPI from an employee of a Mexican trading entity which included the Mexican trading entity's pricing formulas and information related to the total expected import volume, type, and anticipated destination of gasoline. Company found to be reckless in not knowing that the information had been transmitted to them in violation of the Mexican trading entity's duties to his employer in violation of CEA Section 6(c)(1) and Reg. 180.1(a)(1).
  - Company also violated CEA Section 6(c)(1) and Reg. 180.1(a)(1) and (3) for allegedly creating an artificially high value of the USGC HSFC benchmark by engaging in heavy bidding and buying of physical fuel oil in the Platts MOC trading window against its physical position which tended to increase prices paid in the MOC window and benefitting the company's long derivatives position.
  - First time that the CFTC has charged a violation of Reg. 165.19(b) for a company's failure to include whistleblower carve-out language in its employment agreements.



# CFTC's Whistleblower Program

- The CFTC's Whistleblower Program provides monetary incentives to individuals who report possible violations of the Commodity Exchange Act that leads to a successful enforcement action, as well as privacy, confidentiality, and anti-retaliation protections for whistleblowers. See [www.whistleblower.gov](http://www.whistleblower.gov).
- The program was created by Dodd-Frank, which amended the Commodity Exchange Act by adding Section 23, "Commodity Whistleblower Incentives and Protection."
- To be eligible for an award, a whistleblower must voluntarily provide the CFTC with original information about a potential violation of the Commodity Exchange Act that leads to a successful enforcement action brought by the CFTC that results in monetary sanctions exceeding \$1,000,000. See 17 C.F.R. § 165.5.
- A whistleblower may also be eligible for an award based on the amount collected in a Related Action, which is a judicial or administrative action brought by DOJ, an appropriate federal or state government agency acting within the scope of its jurisdiction, a registered entity, or foreign futures authority. See 17 C.F.R. § 165.11.





## CFTC's Whistleblower Program (cont'd)

- A person may not take any action to impede an individual from communicating directly with CFTC staff about a possible violation of the Commodity Exchange Act, including by enforcing, or threatening to enforce a confidentiality agreement or pre-dispute arbitration agreement with respect to such communications. See 17 C.F.R. §§ 165.19, 165.20; App. A to Part 165.
- The CFTC has authority to bring an action against an employer who retaliates against a whistleblower irrespective of whether the whistleblower qualifies for an award. See 17 C.F.R. § 165.20.
- No immunity from prosecution is given to individuals who provide information to the CFTC, so the CFTC is not precluded from bringing an action against the whistleblower in connection with the whistleblower's own conduct with the violation. See 17 C.F.R. § 165.16.
- Whistleblowers who meet all of the program's eligibility criteria may be paid a total award amount equal to between 10% and 30% of the amount of the monetary sanctions collected in the enforcement action. In cases involving multiple whistleblowers, the total award amount will not exceed 30%. See 17 C.F.R. § 165.8.



# Supervision - CME

- CME Market Regulation Advisory on Supervisory Responsibilities for Employees and Agents, Advisory No. CME Group RA2403-5 (July 1, 2024)
  - Provides additional guidance on how parties must discharge their supervisory duties.
  - Duty of diligent supervision (including the duty to develop and diligently enforce supervisory programs that are reasonably designed to detect and deter violations of exchange rules) belongs to members and any person within the jurisdiction of the exchange.
- Includes FAQs related to supervisory responsibilities, which includes the factors Market Reg will consider when assessing a potential violation of Rule 432.W.
  - CME Rule 432.W.: it is an offense for any party to fail to diligently supervise its employees and agents in the conduct of the business relating to the exchange.
  - Lists a litany of Market Reg disciplinary actions on supervisory failures.
  - Describes reasonable supervisory measures to prevent and detect rule violations and reasonable corrective actions to address noncompliance.



## Supervision - CME (cont'd)

- CME Rule 433: Parties are strictly liable for the acts, omissions, or failures of any officials, agents or employees acting for the party within the scope of their employment or office.
  - Agents include any automated trading system, outside counsel, and third-party vendors.
  - Advisory notes the additional supervisory responsibilities of parties operating ATSs to prevent and mitigate the risk the ATS or strategy may cause a market disruption or disrupt the systems of the Exchange or other market participants.
- Intermediaries expected to take appropriate action consistent with notices suspending or barring parties from CME Group markets and ensure those parties are not permitted to access CME Group markets.



# Supervision - CFTC

- CFTC Reg. 166.3 Duty to Supervise
  - Each Commission registrant, except an associated person who has no supervisory duties, must diligently supervise the handling by its partners, officers, employees and agents (or persons occupying a similar status or performing a similar function) of all commodity interest accounts carried, operated, advised or introduced by the registrant and all other activities of its partners, officers, employees and agents (or persons occupying a similar status or performing a similar function) relating to its business as a Commission registrant.
- Reg. 166.3 is an independent violation for which no violation of the CEA or regulations is needed.
- Violation shown by showing either that the registrant's supervisory system was generally inadequate or the registrant failed to perform its supervisory duties diligently.



## Supervision – CFTC (cont'd)

- *In re Advantage Futures LLC*, CFTC Dkt. No. 23-45 (Sep. 20, 2023)
  - FCM violated Reg. 166.3 by failing to ensure that the company followed its customer surveillance procedures and failing to ensure that its customers' order and execution data was processed for surveillance for disruptive trading over a four-year period.
  - Surveillance vendor had failed to process data for one exchange's futures contracts and not received data from another exchange. Company also failed to send certain order and trade data to its surveillance vendor and failed to switch data feed connections when the company switched to a new clearing broker.



# Position Limits

- *In re Vitol, Inc. and Vitol SA*, CFTC Dkt. No. 24-14 (Aug. 14, 2024)
  - First time CFTC enforced position limits on aggregate positions held on multiple exchanges.
  - Vitol held positions in the CME Live Cattle Futures and aggregate futures equivalent positions in the NYMEX WTI Options and IFED WTI Options in excess of the position limits and therefore violated CEA Section 4a(b) and Reg. 150.2.
    - Section 4a(b) makes it unlawful directly or indirectly to hold or control a net long or a net short position in any commodity for future delivery in excess of any position limit established by the CFTC.
    - Reg. 150.2 sets forth federal speculative position limits.
- No scienter required to be established to prove position limits violation.



## Position Limits (cont'd)

- Self-reporting credit given for the December 2022 trading that violated the CME exchange limits for live cattle, but not for the June 2021 trading activity related to WTI trading on ICE and CME.
  - CME imposed a fine on Vitol for the violating CME Rule 562 position limits for live cattle futures. *See In re Vitol, Inc.*, CME 22-1636-BC (Aug. 25, 2023).



# *Chevron* Deference and Reg. 180.1

- *Loper Bright Enterprises v. Raimondo*, 144 S.Ct. 2244 (2024)
  - Held that, under the Administrative Procedure Act, courts must exercise independent judgment in determining the meaning of statutory provisions, even ambiguous ones.
  - Abolished *Chevron* deference under which a reviewing court was required to defer to a federal agency's reasonable interpretation of ambiguity in a statute administered by the agency.
- Reg. 180.1 contains language mirroring the older SEC Rule 10b-5 that prohibits any “device, scheme or artifice to defraud.”





## *Chevron* Deference and Reg. 180.1 (cont'd)

- Impact on the scope of Reg. 180.1?
  - In its 2011 implementing release for Reg. 180.1, the CFTC stated that it would be “guided, but not controlled, by the substantial body of judicial precedent applying the comparable language of SEC Rule 10b-5.” 76 Fed. Reg. at 41,399.
  - The implementing release for Reg. 180.1 also stated that the CFTC could prove manipulation in violation of Reg. 180.1 based on a showing of “recklessness.” 76 Fed. Reg. 41398–99.
  - This departs from Rule 10b-5 precedents holding that intent, rather than recklessness, is necessary to prove manipulation. E.g., *Sullivan & Long Inc. v. Scattered Corp.*, 47 F.3d 857 (7th Cir. 1995).
  - Can CFTC avoid being “controlled” by judicial precedent interpreting Rule 10b-5 without *Chevron* deference?



# Attempted Benchmark Price Manipulation

- *In re TOTSA TotalEnergies Trading SA*, CFTC Dkt. No. 24-19 (Aug. 27, 2024)
  - TOTSA settled a charge of attempted price manipulation in violation of CEA Section 6(c)(1) and Reg. 180.1(a)(1), based on allegations that TOTSA sold physical EBOB gasoline at artificially low prices during the Argus price determination window to benefit a short EBOB futures position that priced to the Argus benchmark.
- Dissenting Statement of Commissioner Caroline D. Pham on Commercial End-User Enforcement Action to *In re TOTSA TotalEnergies Trading SA*, CFTC Dkt. No. 24-19 (Aug. 27, 2024)
  - Commissioner Pham dissented from the settlement order, characterizing the CFTC’s case as based on weak evidence and a “textbook example of policymakers with no industry experience second-guessing commercial business decisions in a bubble.”
  - Commissioner Pham also suggested that the Enforcement Division had engaged in “gamesmanship” by failing to disclose to the Commission a white paper and accompanying expert reports submitted by TOTSA.



# CFTC and Exchange Enforcement Programs At a Glance

- CME Enforcement Trends
  - CME's automated surveillance program
- CFTC Enforcement Program Trends and Priorities
  - Cases to see at the end of September?