

I. Introduction

A. The CFTC and Its Evolving Powers

The commodity futures, options, and swaps markets are primarily regulated by the Commodity Futures Trading Commission (CFTC or Commission), in conjunction with a broad array of self-regulatory organizations (SROs). Traditionally, the CFTC has been relegated to the shadows of its more powerful and well-known regulatory counterpart in the securities market, the Securities and Exchange Commission (SEC). In consequence, practitioners are often less familiar with the practices, procedures, and powers of the CFTC and the vast network of self-regulatory organizations under its purview. Such knowledge gaps are becoming more harmful to attorneys in this space, as the Commission is increasingly asserting the reach of its enforcement arm—and is establishing itself as a true sister agency to the SEC. This Portfolio is intended to prepare practitioners for a new era of heightened enforcement.

The CFTC's mission is to "protect market users and the public from fraud, manipulation, abusive practice and systemic risks."¹ The Commission was established in 1974 through amendment of the Commodity Exchange Act (CEA),² which granted the CFTC exclusive jurisdiction over futures trading in all commodities.³ At the time, the majority of futures trading took place in the agricultural sector. Over the past 40 years, as

the futures industry has evolved to encompass complex financial and other derivative products, the CEA has been amended several times to expand the scope of the agency's authority—most recently in 2010 by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank).⁴

In passing Dodd-Frank, Congress heeded the message reflected in public conversation as well as government studies following the 2008 financial crisis—the need to focus greater attention on systemic risk in the marketplace, and to extend the reach and expand the resources of regulatory agencies tasked with oversight of individual markets and institutions. As a result, in the years since, the Commission's enforcement program has been substantially strengthened.

The CFTC's enforcement activities—and its resulting recoveries—have vastly expanded since the passage of Dodd-Frank. In fiscal years 2011 and 2012, the Commission filed 201 enforcement actions—almost as many as the previous five years (2006-2010) combined—and recovered over \$1.8 billion in civil monetary penalties, restitution, and disgorgement.⁵ In fiscal year 2013, the agency filed 82 enforcement actions and collected over \$1.7 billion in sanctions.⁶ For fiscal years 2014 and 2015, the CFTC obtained monetary sanctions in excess of \$3 billion.⁷ These recoveries far outstrip the \$280 million collected in 2009, the last year before Dodd-Frank.⁸

There is no indication that the CFTC's enforcement momentum is slowing—particularly in light of the fact that Dodd-Frank gave the CFTC authority over certain aspects of the previously unregulated swaps market. The Commission is

¹ COMMODITY FUTURES TRADING COMM'N (CFTC), CFTC STRATEGIC PLAN FY 2011-2015, at 2 (2011).

² 7 U.S.C. §§ 1–27f. This amendment was affected by the Commodity Futures Trading Commission Act of 1974, Pub. L. No. 93-463, 83 Stat. 1389 (1974).

³ The CFTC, like most government agencies, must be periodically reauthorized by Congress to update its authority and recommended spending levels. However, reauthorization is not required for the CFTC to function, and the Commission can continue to operate by relying on unauthorized appropriations from Congress, as it did from fiscal year 2006 to fiscal year 2008. John Kemp, *Reauthorization Fight Looms for CFTC 2013*, INSIDE DEBT 7 (Oct. 16, 2012). The CFTC reauthorization process is under the control of Congressional agriculture committees. The most recent CFTC Reauthorization Act was approved in 2008 as part of the Food, Conservation and Energy Act, Pub. L. 110-246, 122 Stat. 1651 (2008), and expired on September 30, 2013. On July 17, 2013, the Senate Committee on Agriculture, Nutrition and Forestry convened its first official hearing in connection with the next reauthorization vote. See Press Release, U.S. Senate Comm. on Agric., Nutrition and Forestry, Chairwoman Stabenow Says Committee Must 'Examine Lessons from the Past' Throughout CFTC Reauthorization Process (July 17, 2013). In June 2015, Congress passed legislation to reauthorize funding for the CFTC through 2019. Christina Marcos, *House passes CFTC reauthorization*, THEHILL.COM (June 9, 2015). The U.S. Senate Agriculture Committee approved reauthorization in April 2016, paving the way for a full Senate vote on authorization. Lisa Lambert, *Senate committee approves au-*

thorization for U.S. commodities regulator, REUTERS.COM (April 14, 2016).

⁴ Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), Pub. L. 111-203, 124 Stat. 1376 (2010). The Commission's mandate has been renewed and/or expanded under the Futures Trading Acts of 1978, 1982, and 1986; the Futures Trading Practices Act of 1992; the CFTC Reauthorization Act of 1995; the Commodity Futures Modernization Act of 2000; and the Dodd-Frank Act.

⁵ John H. Sturc & Jeffrey L. Steiner, *Expanded Authority, Increasing Numbers & Record Fines: The Changing Landscape of the CFTC's Enforcement Actions*, GIBSONDUNN.COM (Apr. 22, 2013).

⁶ Press Release, CFTC, CFTC Releases Enforcement Division's Annual Results (Oct. 24, 2013). Of the \$1.7 billion that the CFTC collected in sanctions, \$1.5 billion constituted civil monetary penalties and \$200 million constituted restitution and disgorgement. The civil monetary penalties alone total more than seven times the Commission's operating budget for the fiscal year. *Id.*

⁷ Press Release, CFTC, CFTC Releases Annual Enforcement Results for Fiscal Year 2014 (Nov. 6, 2014); Press Release, CFTC, CFTC Releases Annual Enforcement Results for Fiscal Year 2015 (Nov. 6, 2015) (noting that the CFTC obtained \$3.27 billion in 2014 and \$3.14 billion in 2015).

⁸ *Commodity Futures Trading Commission Performance and Accountability Report Fiscal Year 2009*, at 4, (2009).

likely to focus its enforcement efforts on, among other things, violations relating to fraud and market manipulation; disruptive trade practices like spoofing and layering; manipulation of financial benchmarks such as exchange rates and interest rates; customer fund segregation requirements; and supervisory failures. Practitioners who engage in commodity futures work should expect and prepare for more aggressive enforcement in these and other areas in the years ahead.⁹

B. The CFTC's Partners in Enforcement

The vast network of SROs, which aid the CFTC in its market oversight responsibilities, is comprised of a variety of futures exchanges and the National Futures Association (NFA).¹⁰ SROs have the power to enforce industry regulations and standards with respect to their members; these include financial and sales requirements of the SROs' own making as well as those promulgated directly by the CFTC. The enforcement priorities of SROs are informed and influenced by those articulated by the CFTC, but do not necessarily overlap. In cases where a suspected violation infringes on both the Commission's rules and an SRO's rules, the two agencies will generally coordinate their enforcement efforts to ensure that resources are used efficiently. It is possible, however, for a company or individual to be subjected to parallel investigations regarding the same conduct.

C. Investigations and Enforcement Actions

The CFTC's Division of Enforcement, as well as its counterpart within each SRO, may initiate an investigation for a variety of reasons. For example, these enforcement agencies may open an inquiry as part of their regular market surveillance activities or in response to information provided by a wide variety of sources, including internal recommendations and publicly-available information such as news sources. Entities and individuals should expect to receive inquiry letters in the

⁹ Virtually all participants in the commodity futures market will be affected by the Commission's heightened vigilance: designated contract markets and swap execution facilities; swap data repositories; derivatives clearing organizations; swap dealers; registered futures associations; and others.

¹⁰ The SEC oversees several SROs that also provide futures and options contracts to their members. These include, for example, the Chicago Board Options Exchange, the Boston Options Exchange and the International Securities Exchange. A discussion of these organizations is beyond the scope of this Portfolio.

ordinary course of business. While these organizations may occasionally identify and request further information regarding a specific transaction that is deemed potentially problematic, they often issue inquiry letters as a matter of routine review into a particular area of market activity. As such, the issuance of an inquiry letter is not indicative of wrongdoing and will not necessarily give rise to a formal investigation or enforcement action. An inquiry may ultimately blossom into a formal investigation if the Commission or SRO has reason to suspect that a violation of the CEA, CFTC regulations promulgated thereunder, or applicable SRO rules has taken place. At this later stage, the respondent may be required to furnish information through documents or testimony.

Investigations may be concluded without any enforcement action. Should the CFTC determine that a violation has occurred, it may bring an enforcement proceeding before an administrative law judge, file an action in federal court, or, if criminal conduct is suspected, refer the case to the Department of Justice; in the case of an SRO, such actions typically are adjudicated by the entity's Business Conduct Committee or similar body. Usually, the respondent is offered an opportunity to submit a written offer of settlement that does not require an admission of guilt. The consequences of an enforcement action can be serious and include monetary penalties; censure; disgorgement; temporary or permanent bans from certain markets; and cease-and-desist orders.

D. Overview of Portfolio

The purpose of this Portfolio is to educate practitioners about the functions, operations, and procedures of the CFTC and the various SROs that, taken together, comprise the regulatory framework for the commodity futures markets in the United States. Chapter II provides an overview of the history of the commodity markets and the various products traded on such markets. Chapter III discusses the structure of the Commission as well as the SROs under its purview. Chapter IV provides an in-depth guide to navigating the enforcement mechanisms of the Commission. Chapter V sets forth the various enforcement regimes and priorities of prominent SROs with which practitioners can expect to interact, in the course of their market activities. Chapter VI discusses the likely enforcement priorities of the CFTC in the next several years. It is our hope that, by the end of the Portfolio, practitioners will have a comprehensive understanding of (i) regulatory exposure for their commodity futures clients; (ii) the various ways one can act to mitigate the risk of an enforcement action; and (iii) best practices in the event that an enforcement action is initiated.