

What Energy Cos. Can Expect From Cooperation With CFTC

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The [U.S. Commodity Futures Trading Commission](#) engaged in robust enforcement last year — filing 83 enforcement actions in fiscal year 2018, obtaining \$947 million in civil monetary penalties, restitution and disgorgement[1] — and the trend is likely to continue this year. In regard to energy, the CFTC has brought a variety of cases in recent years, including:



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- **EOX Holdings (Sept. 2018):** The CFTC brought a complaint against an introducing broker and its employee, claiming that the employee allegedly disclosed material, nonpublic information about block trading of energy contracts of the broker’s customers. The CFTC brought charges of manipulation and anti-disclosure against both the broker and the employee, as well as charges of inadequate record-keeping and failure to supervise against the broker.[2]
- **Geneva Trading (Sept. 2018):** The CFTC issued an order against an unregistered proprietary trading firm for the alleged spoofing by three of its traders in futures contracts, including heating oil, RBOB gasoline and light sweet crude oil. The CFTC settled charges of manipulation against the company, resulting in a \$1.5 million penalty.[3]
- **[Statoil ASA](#) (Nov. 2017):** The CFTC issued an order against an energy company for allegedly attempting to manipulate the Argus Far East Index, a propane benchmark, to benefit the company’s NYMEX-cleared swaps position, resulting in a \$4 million penalty.[4]
- **Simon Posen (July 2017):** The CFTC issued an order against a trader for allegedly spoofing futures contracts on NYMEX in commodities, including crude oil futures, resulting in a \$635,000 penalty.[5]
- **Total Gas & Power (Dec. 2015):** The CFTC issued an order against a natural gas trading firm, and its employee, for allegedly attempting to manipulate natural gas monthly index settlement prices, resulting in a \$3.6 million civil penalty.[6]

As seen by these examples, the CFTC’s energy enforcement regime has been largely focused on manipulation, including spoofing, but also includes other violations such as disclosure of material nonpublic information.

How Committed Has CFTC Enforcement Been to its 2017 Cooperation Policy?

The CFTC has demonstrated considerable commitment to its 2017 revised cooperation guideline for companies.[7] In its guideline, the CFTC notes that it defines “cooperation” as “more than ordinary cooperation or mere compliance with the requirements of law.”[8]

The guideline further explains that the CFTC “looks to what a company voluntarily does, beyond what it is required to do,” which would be considered “sincere, robustly cooperative, and indicative of a willingness to accept responsibility for the misconduct, where appropriate.”[9] The guideline notes that the reward for cooperation ranges from reduced charges to no enforcement action at all.[10]

The CFTC has fleshed out this written policy through multiple enforcement actions. As seen across these cases, there is a range of behaviors that the CFTC consistently defines as cooperative, including:

- Providing information about violative conduct that the CFTC would not have obtained otherwise;[11]
- Being “candid” in their proffer of information;[12]
- Spending “hundreds of hours” identifying documents and information;[13]
- Beginning their cooperation “early” or “immediately”;[14]
- Providing cooperation that is “substantial” or “material”;[15]
- Identifying alleged co-conspirators;[16]
- Promptly suspending the alleged perpetrator upon being made aware of the alleged conduct;[17]
- Engaging in an internal review;[18] and
- Enhancing its compliance program to better detect the violative behavior at issue.[19]

Consistent with its guideline, the CFTC declined to bring an enforcement action against a financial institution in a matter involving an alleged rogue employee because of the firm’s robust cooperation.[20]

What Should Energy Companies Do if They Suspect CFTC Violations Have Occurred?

What has emerged from the guidance, enforcement matters and declination letter is that whether a company decides to cooperate with the CFTC depends upon the specific facts and circumstances. Importantly, as noted, cooperation in this context is not the company meeting its legal obligations to respond to information requests, but the company going “beyond what it is required to do.”[21]

Initially, if a company becomes aware of a potential violation, the first decision is whether to self-report. Self-reporting has its advantages from a cooperation perspective, in that it puts the company on the best footing with the CFTC. The best example of a positive outcome from self-reporting is the aforementioned declination letter.[22]

However, declination may be harder to achieve where the violations involve more than the activities of a rogue employee, which was the case in the declination.[23] Moreover, several cases have shown that self-reporting is not a prerequisite for a company to be considered cooperative.[24]

Regardless of whether it self-reported, a company pursuing cooperation credit must meet a very high threshold since it must convince the CFTC that its level of cooperation is sufficiently “sincere” and “robust[.]”[25] Companies therefore must continually assess the benefit of pursuing potential cooperation credit against the loss from a strategy perspective of its voluntary actions. This is particularly the case since, though the CFTC notes in several cases that penalties are “substantially reduced” because of cooperation,[26] the specific dollar value of such cooperation in any particular instance, is unclear.

And even if the CFTC acknowledges that a company provided valuable cooperation, companies would similarly have to be thoughtful about the process of negotiating with the CFTC to receive meaningful discounts on penalties as reward for that cooperation. Therefore, clearly, if faced with conduct that the CFTC may consider violative, companies have complex decisions to make throughout about cooperation — from detection to final negotiation.

What Impact Could Swap Dealer Regulation Have on Energy Companies That Trade Derivatives?

Regarding the CFTC, one of the main concerns for energy users that use derivatives is that they may be defined as swap dealers, a registration category that carries relatively burdensome requirements.[27] In 2018, the CFTC determined that as long as a company keeps its swap dealing activity to \$8 billion or less in gross notional amount within the prior 12 months, it would not have to register.[28]

While the CFTC finalized the threshold, it did not, however, approve other aspects of the proposal which energy users supported, including providing an exemption for swaps that are exchange-traded or cleared, and using alternate measures of de minimis activity such as total number of counterparties or transactions.[29] Advocacy may continue in 2019 to get some of these exemptions added to CFTC regulation, including through the reauthorization process.

The CFTC also has yet to finalize a proposed capital rule for swap dealers. The proposal provides options for capital calculation for all dealers, but nonfinancial commercial entities can also avail themselves of a “tangible net worth” approach which is less burdensome.[30] If the proposal were approved, many energy companies that decide to register as dealers may be able to avail themselves of the tangible net worth safe harbor.

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[1] Staff of Commodity Futures Trading Commission, Annual Report on the Division of Enforcement (2018) available at https://www.cftc.gov/sites/default/files/2018-11/ENFAnnualReport111418_0.pdf (Annual Enforcement Report).

[2] See Complaint, CFTC v. EOX Holdings LLC et al. , Civ. No. 18-cv-8890 (September 28, 2018 SDNY), available at <https://www.cftc.gov/sites/default/files/2018-09/enfeoxholdingsllccomplaint092818.pdf>.

[3] See e.g., Order Instituting Proceedings, Geneva Trading USA LLC (Geneva), CFTC Dkt. No. 18-37 at 2, (Sept. 20, 2018), available at <https://www.cftc.gov/sites/default/files/2018-09/enfgenevaorder092018.pdf>.

[4] See e.g., Order Instituting Proceedings, Statoil ASA, CFTC Dkt. No. 18-04, (Nov. 14, 2017), available at <https://www.cftc.gov/sites/default/files/idc/groups/public/@lrenforcementactions/documents/legalpleading/enfstatoilorder111417.pdf>.

[5] See e.g., Order Instituting Proceedings, Simon Posen, CFTC Dkt. No. 17-20, (July 26, 2017), available at <https://www.cftc.gov/sites/default/files/idc/groups/public/@lrenforcementactions/documents/legalpleading/enfposenorder072617.pdf>.

[6] See e.g., Order Instituting Proceedings, Total Gas & Power North America Inc. and Therese Tran, CFTC Dkt. No. 16-03, (Dec. 7, 2015), available at <https://www.cftc.gov/sites/default/files/idc/groups/public/@lrenforcementactions/documents/legalpleading/enfnorthamerorder12715.pdf>.

[7] See CFTC, see “CFTC’s Enforcement Division Issues New Advisories on Cooperation” (Jan. 19, 2017), available at <https://www.cftc.gov/PressRoom/PressReleases/pr7518-17>.

[8] CFTC, “Cooperation Factors in Enforcement Division Sanction Recommendations for Companies,” at 1, available at <https://www.cftc.gov/sites/default/files/idc/groups/public/@lrenforcementactions/documents/legalpleading/enfadvisorycompanies011917.pdf>.

[9] Id.

[10] Id.

[11] See e.g., Order Instituting Proceedings, Grayson Brookshire (Brookshire), CFTC Dkt. No. 18-45, at 2, (Sept. 27, 2018), available at <https://www.cftc.gov/sites/default/files/2018-09/enfgraysonbrookshireorder092718.pdf>.

[12] See e.g., Order Instituting Proceedings, Justin Blake Barrett (Barrett), CFTC Dkt. No. 18-44, at 2, 5 (Sept. 27, 2018) available at <https://www.cftc.gov/sites/default/files/2018-09/enfjustinblakebarrettorder092718.pdf>.

[13] See e.g., Brookshire at 2, 5.

[14] See e.g., Travis Stephenson (Stephenson), CFTC Dkt. No. 18-48, at 2, 5 (Sept. 27, 2018) available at <https://www.cftc.gov/sites/default/files/2018-09/enfravisstephensonorder092718.pdf>.

[15] See e.g., Order Instituting Proceedings, William Earl Berry et al., (Berry), CFTC Dkt. No. 18-42, at 2, 5 (Sept. 27, 2018) available at <https://www.cftc.gov/sites/default/files/2018-09/enfberrymediaworksorder092718.pdf>.

[16] See e.g., Schranz at 2-3, 5.

[17] See e.g., Geneva at 3.

[18] See e.g., Geneva at 5.

[19] See e.g., Order Instituting Proceedings, [Mizuho Bank Ltd.](#) (Mizuho), CFTC Dkt. No. 18-38, at 3 (Sept. 21, 2018), available at <https://www.cftc.gov/sites/default/files/2018-09/enfmizuhobankorder092118.pdf>.

[20] See letter to [Deutsche Bank Securities Inc.](#) and Deutsche Bank AG (Nov. 8, 2018), available at https://www.cftc.gov/sites/default/files/2018-11/enf_DeutscheBankDeclinationLetter110818.pdf.

[21] See supra note 8.

[22] Id.

[23] Id.

[24] See e.g., Brookshire.

[25] See supra note 8.

[26] See e.g., supra note 19 at 3.

[27] See Part 23 of the CFTC rules.

[28] “De Minimis Exception to the Swap Dealer Definition,” 83 Fed. Reg. 56666 (Nov. 13, 2018).

[29] See “De Minimis Exception to the Swap Dealer Definition; Proposed Rule,” 83 Fed. Reg. 27444 (June 12, 2018).

[30] “Capital Requirements of Swap Dealers and Major Swap Participants; Proposed Rule,” 82 Fed. Reg. 13971 (March 16, 2017).