

CFTC ENFORCEMENT AND REGULATORY REPORT—OUTLOOK FOR 2018

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I. Introduction

Over the last year the U.S. Commodity Futures Trading Commission (the “CFTC” or the “Commission”) has been very active in shaping and defining the regulatory priorities of the agency under the leadership of Chairman J. Christopher Giancarlo. This has taken place, in part, through recent enforcement actions by the Division of Enforcement (“CFTC Enforcement”), which have shed light on the CFTC’s enforcement priorities under Chairman Giancarlo and CFTC Enforcement Director James McDonald. The CFTC has also undertaken a number of regulatory initiatives that underscore Chairman Giancarlo’s commitment to transforming the CFTC into a more efficient, forward-thinking regulator. This report describes recent activity by CFTC Enforcement and provides an update on the CFTC’s regulatory activity and agenda.

II. CFTC Enforcement Themes: Increased Actions, Real-Time Enforcement and Self-Reporting

Consistent with Chairman Giancarlo’s stated priority to “oversee robust enforcement of our rules,”¹ CFTC Enforcement has remained consistently active since January 20, 2017, when Chairman Giancarlo first assumed the role of acting Chairman. In March 2017, when announc-

ing the appointment of James McDonald as Director of CFTC Enforcement, Chairman Giancarlo warned that “there will be no pause, no let up and no relaxation in the CFTC’s mission to enforce the law.”² From the end of January through May 2017, CFTC Enforcement announced approximately three enforcement actions (i.e., consent orders and complaints) per month, and then in June and July 2017, enforcement activity began to rise, with the number of enforcement actions matching the total from the previous five months. This trend continued into the latter half of 2017, with nine enforcement actions in September 2017 alone, and into the beginning of 2018, when on a single day in January 2018, the CFTC filed eight enforcement actions. The CFTC is on track to far exceed in the first half of Fiscal Year 2018 (which runs from October 2017 through September 2018) the number of cases brought during the same period for Fiscal Year 2017. A report in the *Wall Street Journal* (“WSJ”) on February 27, 2018 indicated that the CFTC will file more than 10 fraud and manipulation enforcement actions over the next few weeks.³ If true, the agency will have brought 31 cases in the first six months of FY 2018 compared to 18 in FY 2017.

This active enforcement environment may be enhanced by the transfer of the market surveillance function of the CFTC from the Division of Market Oversight (“DMO”) into CFTC Enforcement in mid-2017. This transfer put the power of real-time market information into the hands of CFTC Enforcement, allowing the division to proactively look for market-disrupting behavior in the futures and derivatives markets, as well as the underlying commodity markets. Further, the transfer centralized *all* investigative authority, including special call authority, with CFTC

Enforcement.⁴ CFTC Enforcement now has significant authority to collect information from market participants without issuing a subpoena, though it is unclear under what conditions the division intends to utilize this power.

The enforcement activity over the past year demonstrates that CFTC Enforcement will maintain its focus on conduct that affects the integrity of the market. This is exhibited by the division’s aggressive policing of fraud, manipulation, and other market abuse, which includes the formation of specialized task forces focused on particular types of cases and a willingness to litigate matters, especially against individuals. It also includes policing less culpable conduct that nevertheless may have an impact on market integrity, such as failures to properly report swap data, and failure to properly secure data. The CFTC’s enforcement actions indicate that it will hold companies responsible for failures to supervise by applying the rule to a broad variety of conduct. Finally, through statements accompanying recent enforcement actions, market participants are starting to see the practical impacts of the recent CFTC Enforcement initiatives to encourage self-reporting and cooperation. The following sections explore some of these recent cases as well as CFTC Enforcement’s application of its cooperation and self-reporting guidelines in its settlements.

A. Manipulation and Spoofing: Precedent Continues to Grow

The CFTC continues to be proactive and aggressive in pursuing wrongdoing that involves trading misconduct, such as manipulation, spoofing, and wash trading. CFTC Enforcement proactively uses information gleaned from market surveillance, swaps data reporting, and whistle-

blower complaints to develop investigations in these areas. These cases can result in significant monetary penalties, particularly with a charge of manipulation which carries \$1 million per violation penalty. Recently, the CFTC has shown a particular emphasis on one particular form of manipulation: spoofing. Spoofing is defined as bidding or offering with the intent to cancel the bid or offer before execution.”⁵ It is market behavior that is intended to overload the quotation system of an exchange or trading platform, to delay another’s execution of trades, or to create an appearance of false market depth, thus undermining the integrity of the markets. CFTC Enforcement has actively policed spoofing since bringing the first spoofing action in 2013,⁶ but in January 2018 it became abundantly clear that spoofing was a particular target of CFTC Enforcement. On January 29, 2018, the CFTC announced the filing of eight spoofing actions, including settlements with three banks and the filing of actions in federal court against six individuals.⁷ In each of the press releases accompanying these enforcement actions, the CFTC noted that they were brought “in connection with the CFTC Division of Enforcement’s Spoofing Task Force.” The creation of the Spoofing Task Force is yet another indication of how focused the CFTC is on this particular form of manipulation. The cases filed against the individuals signals that CFTC Enforcement is as focused on individual behavior as institutional behavior, and that the agency will litigate matters to ensure individual compliance.

CFTC Enforcement also continues to apply aggressive interpretations of trader communications and other evidence in bringing manipulation charges, often reading an intent to manipulate in statements that reference the market impact of

potential trading strategies. For example, if a company has derivatives positions that could benefit from taking particular actions in the cash market, and the company takes those actions, CFTC Enforcement appears likely to deem any communications in which employees of the company acknowledge the relationship between the actions in the market and a potential benefit to the company’s derivatives position as evidence of an intent to manipulate.⁸

B. Fraud and Manipulation in Digital Currency Markets: New Product, Historical Approach

The CFTC remains active in policing fraud, both in the derivatives markets and in the underlying spot markets. A significant development over the past year has been the CFTC’s continued assertion of its jurisdiction over digital currencies and other digital assets, especially by bringing enforcement actions to deter fraud and manipulation. The CFTC first asserted authority over digital currencies in 2015, when the agency declared, in a pair of enforcement actions, that digital currencies are commodities under the Commodity Exchange Act (“CEA”).⁹ Since then, the CFTC has asserted its authority to police fraud and manipulation in digital currency spot markets. Most cases filed to date have focused on clear fraud against investors. For example, on September 21, 2017, the CFTC filed a complaint against Nicholas Gelfman, and Gelfman Blueprint, Inc., alleging that Gelfman operated a bitcoin Ponzi scheme, fraudulently soliciting funds from customers with assurances that their funds were being used to trade bitcoin pursuant to a trading program employing an algorithmic trading strategy.¹⁰ Although the defendants issued statements to customers purporting to show sig-

nificant trading profits, little trading occurred and the funds of later customers were used to pay off earlier customers.¹¹

Then, over the course of three days in January 2018, the CFTC filed three separate lawsuits related to digital assets.¹² Each of the lawsuits involves similar facts: the defendants fraudulently solicited funds from customers and purported to invest the funds, but instead misappropriated customer funds. These facts are typical for commodity fraud cases brought by the CFTC. However these cases affirm the CFTC's jurisdiction in the digital currency markets. In the press releases announcing these cases, the CFTC notes that the cases are being brought in connection with CFTC Enforcement's "Virtual Currency Task Force." Similar to the specialized unit on spoofing, this task force exemplifies the CFTC's focus on bringing enforcement actions related to digital currencies, particularly to protect unwitting investors.¹³ In a WSJ joint op-ed with the Securities and Exchange Commission ("SEC") Chairman Jay Clayton, written shortly after these cases were filed, Chairman Giancarlo emphasized that the CFTC and SEC will "continue to work together to bring transparency and integrity to these markets and, importantly, to deter and prosecute fraud and abuse."¹⁴ As discussed below, the attention of the CFTC to digital currency markets will continue, particularly because major futures exchanges, Chicago Mercantile Exchange, Inc. and Cboe Futures Exchange, LLC, launched Bitcoin futures contracts in late 2017. The CFTC's surveillance and enforcement focus increases where the underlying market—the spot digital currency market—relates or is used to price a fully regulated futures market. Market participants should, therefore, anticipate more

enforcement inquiries and actions in the digital currency area.¹⁵

C. Reporting and Recordkeeping Violations: Enforcement Mainstays

Many registrants are subject to expansive reporting and recordkeeping requirements. Chairman Giancarlo has stated several times that timely and accurate data reporting is absolutely critical to the agency's mission of ensuring the integrity of the futures and derivatives markets.¹⁶ The CFTC has brought numerous cases where registrants have failed to comply with these requirements. These are easy cases for the CFTC to bring as they are *per se* violations and do not require proof of intent. Often, the failures found are due to issues with the firm's systems and controls or internal policies and procedures. For example, in one recent case the CFTC brought an enforcement action against a swap dealer for failing to properly report Legal Entity Identifiers when reporting swap data.¹⁷ This was allegedly a result of a deficient design of its swap data reporting systems.¹⁸ In addition to a civil money penalty of \$550,000 (that was significantly reduced given the level of cooperation provided by the swap dealer), the swap dealer was required to enhance its systems to ensure proper reporting of Legal Entity Identifiers. While these cases typically do not involve malicious intent, market participants can expect that the CFTC will continue to bring these cases regularly as reporting failures can undermine the integrity of the markets and interfere with the CFTC's oversight functions.¹⁹ Early identification of problems and early communication with the agency, particularly with CFTC Enforcement, will aid institutions in staving off costly investigations, large fines and the imposition of onerous undertakings.

D. Cybersecurity Focus: A New Enforcement Priority

On February 12, 2018, the CFTC imposed a \$100,000 civil monetary penalty on a futures commission merchant (“FCM”) whose third party IT services provider failed to properly implement the company’s written information securities program, resulting in the exposure and compromise of customer data.²⁰ While the penalty amount is relatively small, again reflecting the significant cooperation provided to CFTC Enforcement in its investigation, this case should be seen as a clear warning to market participants that the CFTC expects robust and effective cybersecurity programs. This is an area of increasing concern and scrutiny for the CFTC as it goes directly to the core principles of a registered entity, namely to have adequate system safeguards. CFTC Chairman Giancarlo, in a recent hearing before the Senate Committee on Agriculture, Nutrition and Forestry, testified that he has long considered cyber-security to be the number one challenge facing markets the agency oversees.²¹ He noted that the agency itself faces 10,000 attempted cyber-attacks per month, that he meets once a month with his chief cyber-security officer, and that the CFTC regularly conducts cyber-attack drills. The Chairman stated very clearly that the agency expects its regulated entities to adopt and implement similar protocols as the agency itself uses. As part of the agency’s annual budget request, the Chairman requested additional funding so the CFTC can conduct greater oversight of cyber-security within the entities it regulates. One way the agency will ensure registrants are meeting its expectations may be through an Enforcement sweep of the industry, which is a coordinated program of investigations and potential actions for those

registrants who do not meet the agency’s expectations.²²

E. Failure to Supervise: A Broadened Approach

CFTC rules impose a duty on registrants to “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.”²³ In several recent enforcement actions the CFTC has been interpreting this provision increasingly broadly, such that almost any breakdown in a company’s systems and controls can result in a charge of failure to supervise either as a standalone charge or as part of other violations. For example, the sole charge in the cyber-security case noted above was that the FCM failed to adequately supervise its third party IT services provider’s implementation of its written information securities program. The variety and extent of these cases indicate this type of violation will be frequently brought CFTC Enforcement. As such, market participants should review current systems and processes to ensure they have the ability to prevent and detect violations, as well as the ability to promptly remediate violations that occur. Otherwise, going forward, market participants can expect that failures to supervise, which lead to serious and repeated misconduct, may result in large fines.²⁴

F. Cooperation and Self-Reporting: Assessing the Impact

One of the clearest developments from CFTC

Enforcement under the new Director has been an emphasis on, and an expectation of, cooperation from institutions and individuals who are the focus of an enforcement investigation. As Director McDonald stated last year, CFTC Enforcement is focused on “giving companies and individuals the incentive, the right incentives to comply with the law while holding the people who violated the law accountable.”²⁵ To achieve that end, in 2017, CFTC Enforcement has provided much clearer guidance on what cooperation means and how to obtain credit for such cooperation.²⁶ Moreover, in a September 2017 speech Director McDonald announced updated guidelines on self-reporting and cooperation.²⁷ According to Director McDonald, the purpose of the updated guidelines is to shift the “analysis in favor of self-reporting” by offering companies “a significantly reduced penalty” for companies that choose to self-report. The key takeaway from these guidelines is that cooperation is measured both by how it assists CFTC Enforcement in a particular investigation, as well as how it assists CFTC Enforcement in achieving its investigatory goals. A finding of cooperation by the Division is now demonstrated in a well-defined link between the level of the charge being brought and the level of sanctions being imposed.

That guidance has begun manifesting itself in enforcement actions. In several of the recent spoofing enforcement actions, the CFTC specifically noted that the companies involved received credit for substantial cooperation and self-reporting, resulting in reduced penalties. Inclusion of these statements is a clear signal to market participants that cooperation has been, and will continue to be rewarded, while non-cooperation will result in stiffer penalties. Similarly, in the order in the cyber-security case

mentioned above, the CFTC included an entire section detailing the FCM’s “significant cooperation” provided to CFTC Enforcement, including “expeditiously providing relevant records including a detailed event timeline, internal communications, and technical documents, along with the results of the penetration test of its network,” as well as the FCM’s efforts to remediate the issue.²⁸

As the articulation of these principles under Director McDonald is fairly new, it is difficult to accurately assess the precise financial impact cooperation and especially self-reporting may have on a CFTC Enforcement action.²⁹ Cooperation can potentially result in much lower civil monetary penalties, and may also be the difference between a permanent ban from the derivatives industry, a temporary ban, or no ban at all. Each reported case provides some clue as to the how the cooperation factor may have been applied, but until some self-assessment is provided by CFTC Enforcement, the benefits of cooperation and self-reporting can only be inferred from a case-by-case analysis. When issues arise that may result in an enforcement investigation, market participants who proactively make remediation and implement changes, such as with policies and procedures and training of employees, may see a “substantial” reduction in the penalty recommended by CFTC Enforcement.

III. Regulatory Update: On Approach to a Full Commission and Agenda

On August 3, 2017, just before their summer recess, the Senate unanimously confirmed Giancarlo as Chairman—previously he had been serving in an Acting capacity. On that same day, Brian Quintenz, a Republican, and Rostin Behnam, a Democrat, were confirmed as Commissioners,

and have since been sworn in, bringing the Commission quotient up to three. While this is an improvement over the two member Commission that existed during the first half of 2017, the CFTC remains two seats short of a full commission. Dawn DeBerry Stump, a Republican, has been nominated as a Commissioner, and was unanimously passed out of the Senate Agricultural Committee, along with Mr. Quintenz and Mr. Behnam. Ms. Stump's confirmation vote before the full Senate will likely take place in conjunction with whomever is nominated to fill Commissioner Bowen's Democratic vacated seat. It has recently been reported that Dan M. Berkovitz, who served as general counsel of the CFTC from 2009-2013, is likely to be named the next Democratic commissioner, pending a review by President Trump's administration.³⁰ Prior to his tenure at the CFTC, Mr. Berkovitz was a senior staff lawyer for the Senate Permanent Subcommittee on Investigations, where he led investigations into the energy markets. He is currently a partner at a Washington law firm. Given his tenure on Capitol Hill and at the CFTC, Mr. Berkovitz's views on certain issues will be known, and thus his nomination is likely to be reported out of the Senate Agricultural Committee expeditiously, perhaps within three months. However, given other legislative priorities, his nomination (and that of Ms. Stump's) is unlikely to come before the full Senate for a confirmation vote before late Summer 2018.

There are several major proposed rules that have yet to be finalized by the CFTC, including rules on automated trading, capital requirements for swap dealers, and position limits. Although the CFTC can finalize these rules with only three Commissioners, it may await a full Commission to take up the issues. Indeed, in his testimony

before the Senate Agricultural Committee, Chairman Giancarlo indicated that, in order to ensure position limits was a lasting rulemaking, it needed to be voted on by a full five member commission.³¹ Nevertheless, while the CFTC has not finalized any major rule in the past year, it has been active in shaping itself to reflect Chairman Giancarlo's priorities, particularly on regulatory efficiency, FinTech innovation, rethinking swaps market trading, and cross-border harmonization.

A. Project KISS Leads to First Rule Change

In March 2017, Acting Chairman Giancarlo announced Project KISS, which stands for "Keep it Simple, Stupid." The objective of the initiative is to conduct a review of CFTC rules, regulations, and practices, and identify areas that the Commission can simplify and make less burdensome. In May 2017, the CFTC entered into the second phase of the project and requested public input for modernizing and simplifying the CFTC's rules. Comment letters have been submitted and are being reviewed by the CFTC.³² On February 15, 2018, the CFTC announced the first result of this effort, the passage of an interim final rule that replaces the "the complex and confusing lettering for defined terms" in CFTC Regulation 1.3 "with a simple alphabetical list."³³ Prior to this change, definitions were added to CFTC Regulation 1.3 by simply adding a new numbered paragraph to the end of the list, without regard for alphabetical order, while definitions that were removed were replaced by a numbered paragraph reading "reserved."³⁴ This could make finding definitions unnecessarily difficult; the new alphabetical list should make finding the definition of a particular defined term more efficient.

B. The Regulatory Approach to FinTech Innovation and Digital Currency Markets

Chairman Giancarlo has long argued that regulators should foster, not unduly burden, financial innovation. This was the motivation behind the creation of LabCFTC, the CFTC's FinTech initiative which aims to accelerate the CFTC's engagement with the FinTech community and inform the CFTC's understanding of new technologies. In particular, Chairman Giancarlo has consistently emphasized the potential benefits of distributed ledger technology - the technology that underlies bitcoin and other digital currencies.³⁵ As noted above, the CFTC first asserted its jurisdiction over digital currency derivatives in 2015, in two different enforcement actions,³⁶ and has recently demonstrated its authority to police fraud and manipulation in the spot markets. However, its activity has not been limited to enforcement actions. Over the past year, as digital currencies have increasingly entered the mainstream (and regulatory) consciousness, the CFTC has been proactive in this space in a number of areas:

- **Public Outreach:** The CFTC has issued a number of documents intended to educate the public on digital currencies and the CFTC's role, including a customer advisory on the risks of digital currency trading,³⁷ and (through LabCFTC) a primer on virtual currencies.³⁸
- **Proposed Retail Commodity Guidance:** The CFTC has jurisdiction over retail commodity transactions entered into on a margined, leveraged, or financed basis, unless "actual delivery" of the commodity is made to the customer within 28 days.³⁹ In 2013

the CFTC issued guidance on what would be considered for "actual delivery," but at the time this guidance was released the focus was on traditional, physical commodities such as gold.⁴⁰ Recognizing that this guidance might not be applicable to digital currencies, in which there are no physical assets, but rather a digital representation of value stored in a virtual "wallet," the CFTC proposed additional guidance specifically addressed to "actual delivery" of a digital currencies.⁴¹ The CFTC's ultimate definition of "actual delivery" will be critical for market participants to determine which kinds of digital currency products over which the CFTC will assert regulatory authority. However, there is an expectation that the CFTC's definition will be broad and provide the CFTC with discretion, in order to reserve its enforcement and regulatory jurisdiction. Further, it has implications for companies operating in the cash markets. If a company offers a product subject to the CFTC's regulatory jurisdiction, that company would have to register with the CFTC (potentially as a designated contract market, a futures commission merchant, commodity pool operator, commodity trading advisor, or introducing broker, depending on its services), and would be subject to extensive CFTC oversight of its activities. Comments on the proposed guidance are due by March 20, 2018.

- **Bitcoin Futures Contracts:** In December 2017, Chicago Mercantile Exchange ("CME") and Cboe Futures Exchange, LLC ("Cboe") each self-certified a bitcoin futures contract with the CFTC. These prod-

ucts are cash-settled, based on bitcoin prices from several cryptocurrency exchanges.⁴² Although CME and Cboe went through the self-certification process, which does not allow for public comment or specific CFTC approval prior to listing, each interfaced extensively with the CFTC prior to offering the contract. As Chairman Giancarlo notes, the offering of these contracts by regulated designated contract markets will give the CFTC deeper insight into the bitcoin spot markets. Because the CME and Cboe products use data from certain spot markets, the CFTC will have access to that underlying data, and will thus be able to detect fraud and manipulation in those markets more easily. These futures contracts also further increase the jurisdictional basis for CFTC enforcement (based in fraud and manipulation) in the spot commodity markets in order to protect integrity of futures market.

Digital currency markets and the related technology have also been the focus of two recent commission meetings, a Market Risk Advisory Committee Meeting on January 31, 2018, and a Technology Advisory Committee Meeting on February 14, 2018. Beyond the CFTC, there has been increased focus on digital currencies throughout the government, including on Capitol Hill. To that end, SEC Chairman Clayton and CFTC Chairman Giancarlo were called to testify about digital currencies before the Senate Banking Committee on February 6, 2018. In his testimony, Chairman Giancarlo reiterated that his “do no harm” approach applies to digital currencies, while emphasizing that the CFTC would continue to police fraud in digital currency markets. He also indicated that the CFTC, in conjunction with other financial regulators, is working to deter-

mine and address regulatory gaps that may exist as it attempts to grapple with this emerging market.

C. Rethinking Swap Market Size to Comport with Market Risk

Chairman Giancarlo has long been a proponent of restructuring the CFTC’s approach to regulating swaps.⁴³ While an overhaul of the swaps trading rule may not be finalized for some time, Chairman Giancarlo has begun laying the groundwork for rethinking the swaps market in a way that could influence any eventual reforms. On February 1, 2018, Chairman Giancarlo announced a new potential paradigm for measuring the size of the swap market, as put forth in a paper by CFTC Chief Economist Bruce Tuckman.⁴⁴ According to the paper, measuring the size of swap markets by notional value overstates the size of the market, in particular the “risk transfer between pairs of counterparties.”⁴⁵ Instead, the paper proposes a new measure of market size, “Entity Netted Notionals,” computed by converting “the long and short notional amounts of each entity to 5 year risk equivalents; net longs against shorts in a given currency within pairs of legal entities; and sum the resulting net longs (or net shorts) across entities.”⁴⁶ This new method of measuring swaps activity could have some effect on future regulatory treatment of certain entities, including potentially determining a *de minimis* exception for registration as a swap dealer.⁴⁷

D. Developments towards Re-Establishing Cross-Border Markets

Chairman Giancarlo has argued that that the CFTC’s current cross-border approach, which emphasizes “identical, rule-by-rule substituted compliance analysis,” is inconsistent with the ap-

proach agreed upon by the G-20, which urged a commitment to “consistent,” rather than “identical,” implementation.

1. Margin for Uncleared Swaps

In a step towards harmonization, on October 3, 2017, the CFTC and European Union entered into an agreement recognizing equivalence of rules related to margin requirements for swap dealers and major swap participants.⁴⁸

2. The Brexit Threat to Cross-Border Harmonization

However, in a potential hindrance to Chairman Giancarlo’s desire for greater harmonization, as part of the negotiations over Brexit, the European Commission (“EC”) is considering overhauling its regulatory framework for derivatives clearinghouses—a move that potentially threatens the prior agreement between the CFTC and the EC on clearinghouse oversight by giving the EC supervisory oversight of U.S. clearinghouses. Chairman Giancarlo has made clear that he would not support any proposal that would allow “European authorities [to] exercise direct oversight over U.S.” clearinghouses,⁴⁹ and recently reiterated that “American markets must continue to be regulated under American law by U.S. regulators overseen by the U.S. Congress.”⁵⁰ On January 8, 2018, Chairman Senator Pat Roberts (R-KS) and Ranking Member Senator Debbie Stabenow (D-MI) of the Senate Agricultural Committee, sent Chairman Giancarlo a letter indicating that if the EC moves to change its regulatory framework for clearinghouses, they would approve and encourage him to revisit any relief granted to foreign entities.⁵¹

3. Implementation of the “Common Approach” to Mutual Recognition of Swaps Trading Platforms

In a major development toward global harmonization of the swaps trading markets, on December 8, 2017, the CFTC issued an Order exempting certain multinational trading facilities (“MTFs”) and organized trading facilities (“OTFs”) authorized within the European Union (“EU”) to trade derivatives, from the requirement to register with the CFTC as swap execution facilities (“SEFs”) (the “CFTC Order”). The CFTC Order was made effective on January 3, 2018.⁵² The CFTC found EU-wide legal requirements—including requirements under the EU’s New Markets in Financial Instruments Regulation (“MiFIR”), the EU’s amended Markets in Financial Instruments Directive (“MiFID II”) and the EU’s Market Abuse Regulation—established regulatory frameworks for MTFs and OTFs which satisfied the CEA standard for granting an exemption from the SEF registration requirement.⁵³ Similar to the Dodd-Frank Act, and also as a response to the 2008 financial crisis, MiFID II and its companion regulations provide for a sweeping overhaul of financial product trading, which, ultimately, is intended to boost transparency and limit systemic risk across the EU.

The CFTC Order exempted 10 MTFs and 6 OTFs authorized within the EU from the SEF registration requirements.⁵⁴ Beginning on January 3, 2018, market participants, subject to the CFTC’s jurisdiction, were able to satisfy the CEA’s swaps trading mandate by transacting on the aforementioned 16 trading venues. Additionally, to the benefit of the trading venues, participation by a US person would not trigger the requirement that the MTFs or OTFs register as a

SEF with the CFTC. In a coordinated action, the European Commission (“EC”) adopted a decision on December 5, 2017, finding that the legal and supervisory frameworks of 14 DCMs and 23 SEFs were sufficient under MiFID II. The EC’s decision enabled EU counterparties to trade derivatives, subject to the EU trading obligation, on the approved DCMs and SEFs.

The CFTC’s Order and the EC decision follow the October 13, 2017 announcement of a common approach regarding the mutual recognition of certain CFTC-and EU-authorized derivative trading venues by CFTC Chairman Giancarlo and EC Vice President for Financial Stability Dombrovskis.⁵⁵ The CFTC is also looking to establish equivalence networks in Japan, Singapore, Hong Kong, and Australia.

Importantly, the CFTC Order granting exempt SEF status to EU-authorized MTFs and OTFs does not affect other requirements under the CEA and the CFTC’s regulations. The CFTC has particularly highlighted certain of these continuing requirements in the Order, which includes reporting requirements as they pertain to swap transactions (meaning U.S. counterparties will still have to report the swap to a swap data repository in the U.S.) and certain external business conduct obligations.

4. Cross-Border FinTech Collaboration

On February 19, 2018, the CFTC and the UK’s Financial Conduct Authority (“FCA”) signed an arrangement that commits the regulators to collaborating and supporting innovative firms through each other’s FinTech initiatives: LabCFTC and FCA Innovate.⁵⁶ The arrangement illustrates the continued forward looking regula-

tory stance of the CFTC. The FCA’s FinTech initiative has been in place for some time and the CFTC’s FinTech initiative has been a hallmark of Chairman Giancarlo’s agenda since the beginning of his term as Chairman. The approach here is important because the derivatives markets are global in nature and these cross-border initiatives are very important to enhance market structure and avoid fragmentation.

IV. Conclusion

As discussed in detail above, the CFTC has had a very active 2017, bringing significant enforcement matters and continuing to lay the groundwork for further regulatory changes. The development of digital currency markets and the increased public awareness and use of these markets has meant the CFTC has had to dedicate considerable resources to understand, police, and determine how it should approach these markets. However, CFTC Enforcement still maintained a highly proactive and aggressive enforcement program by bringing numerous actions across traditional markets. It has balanced this aggressive stance with a willingness to consider reduced penalties for market participants with robust systems and controls who provide full cooperation and self-reporting to CFTC Enforcement. The remainder of 2018 will see this pace of enforcement cases continue; while on the regulatory front, market participants should see the agency bring major rule proposals related to swaps trading and position limits, as well as further significant developments toward continued cross-border harmonization.

ENDNOTES:

¹Statement of J. Christopher Giancarlo, Act-

ing Chairman, CFTC, before the U.S. Senate Committee on Agriculture, Nutrition, and Forestry (June 22, 2017), *available at* <http://www.cftc.gov/PressRoom/SpeechesTestimony/opagiancarlo-25>.

²CFTC Press Release: CFTC Acting Chairman Giancarlo Appoints James McDonald as Enforcement Director (Mar. 30, 2017), *available at* <http://www.cftc.gov/PressRoom/PressRelease/s/pr7541-17>; *see also* Remarks of Acting Chairman J. Christopher Giancarlo before the 11th Annual Capital Market Summit: Financing American Business, US Chamber of Commerce (Mar. 30, 2017), *available at* <http://www.cftc.gov/PressRoom/SpeechesTestimony/opagiancarlo-21>.

³Gabriel T. Rubin, CFTC Steps Up Enforcement Against Fraud, Market Manipulation, Wall Street Journal (Feb. 27, 2018), *available at* <http://www.wsj.com/articles/cftc-steps-up-enforcement-against-fraud-market-manipulation-1519727401>.

⁴Commission Delegated Authority Provisions and Technical Amendments, 82 Fed. Reg. 28,763 (June 26, 2017).

⁵CEA § 4c(a)(5)(C); 7 U.S.C. § 6c(a)(5)(C).

⁶*In re Panther Energy Trading LLC*, CFTC Docket No. 13-26 (July 13, 2013).

⁷*See* CFTC Press Release: CFTC Files Eight Anti-Spoofing Enforcement Actions against Three Banks (Deutsche Bank, HSBC & UBS) & Six Individuals (Jan. 29, 2018), *available at* <http://www.cftc.gov/PressRoom/PressReleases/pr7681-18>.

⁸*See, e.g., In re Statoil ASA*, CFTC No. 18-04 (Nov. 14, 2017), *available at* <http://www.cftc.gov/idc/groups/public/@lrenforcementactions/documents/legalpleading/enfstatoilorder111417.pdf>.

⁹*See In re Coinflip, Inc., d/b/a/ Derivabit*, and Francis Riordan, CFTC No. 15-29 (Sept. 17, 2015) (finding that an operator of a bitcoin options trading platform failed to register as a designated contract market or as a swap execution facility), *available at* <http://www.cftc.gov/idc/groups/public/@lrenforcementactions/documents/legalpleading/enfcoinfliporder09172015.pdf>

; and *In re TeraExchange LLC*, CFTC No. 15-33 (Sept. 24, 2015) (finding that a swap execution facility facilitated the wash trading of two transactions in a bitcoin swap), *available at* <http://www.cftc.gov/idc/groups/public/@lrenforcementactions/documents/legalpleading/enfteraexchangeorder92415.pdf>.

¹⁰*CFTC v. Gelfman Blueprint, Inc., et al.*, Case No. 17-cv-7181 (S.D.N.Y.) (Sept. 21, 2017), *available at* <http://www.cftc.gov/idc/groups/public/@lrenforcementactions/documents/legalpleading/enfgelfmancomplaint09212017.pdf>.

¹¹*Id.*

¹²*CFTC v. Dean, et al.*, Case No. 18-cv-00345 (E.D.N.Y.) (Jan. 18, 2018); *CFTC v. McDonnell, et al.*, Case No. 18-cv-0361 (E.D.N.Y.) (Jan. 18, 2018); *CFTC v. My Big Coin Pay, Inc., et al.*, Case No. 18-cv-10077 (D. Mass.) (Jan. 16, 2018).

¹³*See, e.g.,* CFTC Press release, CFTC Charges Randall Crater, Mark Gillespie, and My Big Coin Pay, Inc. with Fraud and Misappropriation in Ongoing Virtual Currency Scam (Jan. 24, 2018), *available at* <http://www.cftc.gov/PressRoom/PressReleases/pr7678-18>.

¹⁴Jay Clayton and J. Christopher Giancarlo, Regulators Are Looking at Cryptocurrency: At the SEC and CFTC, We Take Our Responsibility Seriously, Wall Street Journal, January 24, 2018, *available at* <https://www.wsj.com/articles/regulators-are-looking-at-cryptocurrency-1516836363>.

¹⁵The SEC is also focused on this area, with a recent report stating that it has issued “dozens of subpoenas and information requests” to cryptocurrency companies. Jean Eaglesham and Paul Vigna, Cryptocurrency Firms Targeted in SEC Probe, Wall Street Journal (Feb. 28, 2018), *available at* <https://www.wsj.com/articles/sec-launches-cryptocurrency-probe-1519856266>.

¹⁶*See, e.g.,* Written Testimony of Chairman J. Christopher Giancarlo before the U.S. Senate Agriculture, Nutrition, and Forestry Committee, Washington, D.C. (Feb. 15, 2018) (noting that the lack of regulator access to accurate swaps data was at “the heart of the 2008 financial crisis”), *available at* <http://www.cftc.gov/PressR>

oom/SpeechesTestimony/opagiancarlo38.

¹⁷*In re Citibank, N.A., et al.*, CFTC No. 17-26 (Sept. 25, 2017), available at <http://www.cftc.gov/idc/groups/public/@lrenforcementactions/documents/legalpleading/enfcitibankorder092517.pdf>.

¹⁸*Id.*

¹⁹*Id.* at 5.

²⁰*In re AMP Global Clearing LLC*, CFTC No. 18-10 (Feb. 12, 2018), available at <http://www.cftc.gov/idc/groups/public/@lrenforcementaction/s/documents/legalpleading/enfamglobalorder021218.pdf>.

²¹See Testimony of Chairman J. Christopher Giancarlo before the U.S. Senate Agriculture, Nutrition, and Forestry Committee, Washington, D.C. (Feb. 15, 2018), available at

<https://www.agriculture.senate.gov/hearings/state-of-the-cftc-examining-pending-rules-cryptocurrency-regulation-and-cross-border-agreements>.

²²See FY 2019 Budget Request at 2, available at <http://www.cftc.gov/idc/groups/public/@newsroom/documents/file/cftcbudget2019.pdf>.

²³17 C.F.R. § 166.3.

²⁴*In re Cargill, Inc.*, CFTC No. 18-03 (Nov. 6, 2017), available at <http://www.cftc.gov/idc/groups/public/@lrenforcementactions/documents/legalpleading/cargillorder110617.pdf>.

²⁵*CFTC Talks*, EP005: CFTC Director of Enforcement James McDonald (Aug. 25, 2017), available at http://hwcdn.libsyn.com/p/2/2/1/221a3c555a7ecbd9/CFTC_Talks_Ep_5_Transcript.pdf?c_id=16566154&expiration=1503895103&hwt=d1c77e4c98f9dac2fe4b3e00abfd5839.

²⁶Enforcement Advisory: Cooperation Factors in Enforcement Division Sanction Recommendations for Companies and Individuals; available respectively at <http://www.cftc.gov/idc/groups/public/@lrenforcementactions/documents/legalpleading/enfadvisorycompanies011917.pdf> and <http://www.cftc.gov/idc/groups/public/@lrenforcementactions/documents/legalpleading/enfadvisoryindividuals011917.pdf>. CFTC Enforcement's emphasis on cooperation

was further highlighted in June 2017, when the CFTC entered into its first ever non-prosecution agreements (“NPA”) with individual traders. In announcing the NPAs, the CFTC emphasized the individuals’ “substantial cooperation, immediate willingness to accept responsibility for their misconduct, material assistance provided to the CFTC’s investigation of [the financial institution], and the absence of a history of prior misconduct.” CFTC Enforcement Director McDonald also noted that NPAs offer the CFTC “a powerful tool to reward extraordinary cooperation in the right cases.” CFTC Enters into Non-Prosecution Agreements with Former Citigroup Global Markets Inc. Traders Jeremy Lao, Daniel Liao, and Shlomo Salant (June 29, 2017), available at <http://www.cftc.gov/PressRoom/PressReleases/pr7581-17>. The CFTC has not yet entered into additional NPAs, and it is unclear whether NPAs will be extended to companies, making the issue ripe for consideration by the CFTC.

²⁷Speech of James McDonald, Director of the Division of Enforcement Commodity Futures Trading Commission Regarding Perspectives on Enforcement: Self-Reporting and Cooperation at the CFTC (Sept. 25, 2017), available at <http://www.cftc.gov/PressRoom/SpeechesTestimony/opamcdonald092517>.

²⁸*In re AMP Global Clearing LLC* at 5.

²⁹For example, it will be difficult to determine when cooperation and self-reporting result in the closure of an investigation and a declination to bring an enforcement action, as that information is normally not made public by the agency. However, it is possible that minor regulatory violations self-reported to CFTC Enforcement will be handled as compliance issues with remediation being overseen by another division.

³⁰Benjamin Bain, Ex-CFTC Counsel Is Likely Pick for Democratic Slot, Sources Say, Bloomberg (Feb. 20, 2018), available at <https://www.bloomberg.com/news/articles/2018-02-20/ex-cftc-counsel-is-said-to-be-pick-for-agency-s-democratic-slot>.

³¹Written Testimony of Chairman J. Christopher Giancarlo before the U.S. Senate Agricul-

ture, Nutrition, and Forestry Committee, Washington, D.C. (Feb. 15, 2018), available at <http://www.cftc.gov/PressRoom/SpeechesTestimony/opagiancarlo38>.

³²See CFTC Press Release, Remarks of CFTC Chief of Staff Michael Gill at the National Press Club, CFTC Kiss Policy Forum, Washington, D.C. (Feb. 12, 2018) (discussing the number and types of comment submissions received in response), available at <http://www.cftc.gov/PressRoom/SpeechesTestimony/opagill2>.

³³See CFTC Press Release, Giancarlo: We're Making Government Function More Efficiently for Taxpayers and Market Participants (Feb. 15, 2018), available at <http://www.cftc.gov/PressRoom/PressReleases/pr7696-18#PrRoWMBL>.

³⁴83 C.F.R. 7,979 (Feb. 23, 2018).

³⁵CFTC Press Release, CFTC Launches LabCFTC as Major FinTech Initiative (May 17, 2017), available at <http://www.cftc.gov/PressRoom/PressReleases/pr7558-17>.

³⁶See *In re Coinflip, Inc.* and *In re TeraExchange LLC*.

³⁷Customer Advisory: Understand the Risks of Virtual Currency Trading, available at http://www.cftc.gov/idc/groups/public/@customerprotection/documents/file/customeradvisory_urvct121517.pdf.

³⁸A CFTC Primer on Virtual Currencies, available at http://www.cftc.gov/idc/groups/public/documents/file/labcfctc_primercurrencies100417.pdf.

³⁹CEA 2(c)(2)(D)(iii).

⁴⁰Retail Commodity Transactions Under Commodity Exchange Act, 78 FR 52,426 (Aug. 23, 2013).

⁴¹Retail Commodity Transactions Involving Virtual Currency, 82 Fed. Reg. 60,355 (Dec. 20, 2017).

⁴²Several large bitcoin traders are calling for physical settlement instead of cash settlement, arguing that pricing based on spot market exchanges may “not reflect the most precise price of the coin.” Frank Chaparro, *The Top Cryptocurrency Traders are Asking For a Big Shake-up to*

Bitcoin Futures, Business Insider (Feb. 22, 2018), available at <http://www.businessinsider.com/the-top-cryptocurrency-traders-are-asking-for-a-big-shakeup-to-bitcoin-futures-2018-2>.

⁴³J. Christopher Giancarlo, Pro-Reform Reconsideration of the CFTC Swaps Trading Rules: Return to Dodd-Frank (Jan. 29, 2015).

⁴⁴Richard Haynes, John Roberts, Rajiv Sharma, and Bruce Tuckman, *Introducing ENNs: A Measure of the Size of Interest Rate Swap Markets* (Jan. 2018), available at http://www.cftc.gov/idc/groups/public/@economicanalysis/documents/file/oce_enns0118.pdf.

⁴⁵*Id.* at 1.

⁴⁶*Id.*

⁴⁷The current *de minimis* threshold for registration as a swap dealer is \$8 billion. Without further action from the CFTC, the *de minimis* threshold will drop to \$3 billion on December 31, 2019. Market participants are concerned that if the *de minimis* threshold drops, many smaller market participants and end-users will be required to register as swap dealers, but there will be little overall regulatory benefit.

⁴⁸Comparability Determination for the European Union: Margin Requirements for Uncleared Swaps for Swap Dealers and Major Swap Participants, 82 Fed. Reg. 48,394 (Oct. 18, 2017).

⁴⁹Remarks of CFTC Chairman J. Christopher Giancarlo before the Eurofi Financial Forum (Sept. 14, 2017), available at <http://www.cftc.gov/PressRoom/SpeechesTestimony/opagiancarlo28>.

⁵⁰Written Testimony of Chairman J. Christopher Giancarlo Before the U.S. Senate Agriculture, Nutrition, And Forestry Committee (Feb. 15, 2018), available at <http://www.cftc.gov/PressRoom/PressReleases/opagiancarlo38#PrRoWMBL>.

⁵¹Letter from Senator Pat Roberts and Senator Debbie Stabenow to CFTC Chairman J. Christopher Giancarlo (Jan. 8, 2018) available at <https://www.agriculture.senate.gov/imo/media/doc/01-08-18%20CFTC%20EUROPEAN%20CLEARING%20LETTER.pdf>.

⁵²CFTC Approves Exemption from SEF Registration Requirement for Multilateral Trading Facilities and Organised Trading Facilities Authorized Within the EU (Dec. 8, 2017) *available at* <http://www.cftc.gov/PressRoom/PressReleases/pr7656-17>.

⁵³In the Matter of the Exemption of Multilateral Trading Facilities and Organised Trading Facilities Authorized Within the European Union from the Requirement to Register with the Commodity Futures Trading Commission as Swap Execution Facilities - CFTC Order of Exemption

(Dec. 8, 2017) *available at* http://www.cftc.gov/idc/groups/public/@requestsandactions/documents/ifdocs/mtf_order12-08-17.pdf.

⁵⁴*See id.*

⁵⁵*See id.*

⁵⁶CFTC Press Release, US CFTC and UK FCA Sign Arrangement to Collaborate on Fin-Tech Innovation (Feb. 19, 2018), *available at* <http://www.cftc.gov/PressRoom/PressReleases/pr7698-18>.

