



WHITE PAPER

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The DOJ and the CFTC Are Focused on Commodities Fraud Enforcement—Are You?

Suggestions for Preparing Your Organization

The Department of Justice (“DOJ”) and the Commodity Futures Trading Commission (“CFTC”) in recent years have worked closely together to target companies and individuals for violations of the Commodity Exchange Act and other laws. As former senior officials at the DOJ and the CFTC, we expect the agencies to double down on this joint initiative in the years ahead, continuing to pursue commodities fraud cases with even greater focus and intensity. Accordingly, companies active in the commodities and derivatives markets should understand how these agencies work together and their enforcement priorities.

This *White Paper* addresses these issues and offers practical tips for companies to take stock of their compliance programs. Armed with this information, companies can ensure that they are prepared to deal with the potential for robust civil and criminal commodities fraud enforcement by the DOJ and the CFTC in the years ahead.

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INTRODUCTION

The DOJ and the CFTC in recent years have worked closely together to target companies and individuals for violations of the Commodity Exchange Act (“CEA”) and other laws. Between 2017 and 2020, for example, they brought 46 cases in parallel, racking up record penalties for commodities fraud¹ and breaking new ground by charging violations of the CEA together with other laws, such as the Foreign Corrupt Practices Act (“FCPA”) and Bank Secrecy Act (“BSA”), on the same sets of facts.

As former senior officials² at the DOJ and the CFTC, we expect the agencies to double down on this joint initiative in the years ahead, continuing to pursue commodities fraud cases with even greater focus and intensity. Accordingly, companies active in the commodities and derivatives markets should understand how these agencies work together and their enforcement priorities. Below, we address these issues and then offer practical tips for companies to take stock of their compliance programs. Armed with this information, companies can ensure that they are prepared to deal with the potential for robust civil and criminal commodities fraud enforcement by the DOJ and the CFTC in the years ahead.

HOW THE DOJ AND THE CFTC INVESTIGATE COMPANIES TOGETHER

In recent years, the DOJ and the CFTC have built a strong, collaborative, and enduring partnership for pursuing parallel commodities-related investigations and enforcement actions. At the DOJ, the Criminal Division’s Market Integrity and Major Frauds Unit (“MIMF”), which has seen a surge in resources in recent years, remains closely focused on commodities fraud. Leadership of MIMF and the CFTC’s Division of Enforcement meet regularly to review ongoing inquiries and investigations, to assess case status, and to coordinate resolutions. This partnership has led to a notable string of individual prosecutions and ever-larger corporate resolutions involving commodities-related misconduct.

Despite the change in administrations, the Criminal Division’s new leadership has signaled that it largely expects to continue many of the enforcement initiatives of recent years. There is thus every reason to expect that the DOJ and the CFTC will continue building on this collaborative process and bring even

more commodities-related cases in the years ahead. Based on our experience, we anticipate that four principal factors will drive joint enforcement efforts by the DOJ and the CFTC to newer heights:

- **Data Analytics.** In October 2020, the CFTC concluded a major reorganization that launched a new Division of Data. This Division will rely on the CFTC’s existing reporting, market intelligence, and surveillance infrastructure and build tools to better serve core Division of Enforcement program priorities. For an agency awash in market data, better analytical tools that convert big data into actionable intelligence will undoubtedly lead to more enforcement actions. For its part, DOJ’s Criminal Division has been vocal in recent years about its ability to leverage data analytics to detect, investigate, and prosecute wrongdoing across multiple areas of enforcement—including commodities fraud. Sophisticated data analytics has become industry standard in DOJ and CFTC investigations. Expect reliance on these tools to figure prominently in enforcement efforts at both agencies in the years ahead.
- **Internal and External CFTC Referrals.** In late 2019, the CFTC’s Market Participants Division (“MPD”) implemented the first-ever formal referral program with Enforcement. In its first full year, that program contributed nearly 10% of Enforcement’s 2020 docket. MPD has oversight responsibility for the 3,300 entities registered with the CFTC, so it is a source of additional charges—such as failure to supervise traders or maintain adequate internal controls—that can be brought against registered firms in commodities fraud cases. At the same time, the strong partnership that has developed in recent years between the CFTC and the DOJ means that the agencies are in close contact about cases with the potential for criminal charges. This kind of collaboration—both within the CFTC and between the agency and DOJ—will likely lead to more cases and additional charges against registered firms in the years ahead.
- **Whistleblowers.** The CFTC’s Division of Enforcement estimates that 30%-40% of its cases involve tips from whistleblowers. And in certain cases, whistleblower tips submitted to the CFTC result in referrals to the DOJ. Although there have been reports suggesting the CFTC’s whistleblower program may soon suffer a funding shortfall, we do not

anticipate that the program will be dormant for long (if at all) given its importance to the CFTC's enforcement mission. Nor do we expect that the flow of tips will fall off while this issue is resolved, given the financial incentives available to whistleblowers. To the contrary, whistleblower tips are likely to be a major driver of commodities fraud enforcement matters in the coming years.

- **Charging Different Offenses on the Same Facts.** The DOJ and the CFTC are increasingly looking at the same set of allegations and pursuing separate but related charging theories. In one recent action, the CFTC brought CEA charges against a firm on the same allegations that the DOJ charged under the FCPA. Although the CFTC does not have authority to enforce the FCPA, the case shows that the DOJ and the CFTC are looking at an established enforcement area in new ways, with an eye to bringing different but related charges. We expect these kinds of cases to continue, despite potentially enhanced litigation risk for the government around novel case theories—after all, the vast majority of cases against companies end in resolutions rather than trial.

WHAT THE DOJ AND THE CFTC ARE LOOKING FOR—PRIORITY ENFORCEMENT AREAS

These dynamics are likely to drive continued collaboration between the DOJ and the CFTC in the years ahead. But what types of cases will the two agencies partner to bring? Based on our experience and the agencies' recent track records, several areas appear ripe for intensified focus going forward.

- **Foreign Corruption.** As noted above, in December 2020, the DOJ and the CFTC announced their first-ever joint foreign corruption resolution in the commodities space. The case followed the CFTC's 2019 announcement that it would focus on foreign corrupt practices—an area that historically had been the province of the DOJ and Securities and Exchange Commission. While the CFTC's approach is novel, the agency takes the view that the same conduct underlying a traditional FCPA violation—i.e., bribery—can also violate the CEA by distorting the markets for physical commodities as well as futures and derivatives. DOJ anticorruption enforcement hit

a high-water mark last year, with the agency bringing several of the largest FCPA resolutions in history. A number of firms have disclosed ongoing investigations in this area. All of this provides good reason to expect that the CFTC and the DOJ will continue collaborating to bring foreign corruption cases in the commodities fraud space in the years ahead.

- **Spoofing and Market Manipulation.** In recent years, DOJ's MIMF and the CFTC have focused on ensuring market integrity by policing manipulative trading in the commodities markets. Best known are the agencies' joint efforts to use data analytics to detect and prosecute the practice known as "spoofing," which generally involves traders placing and then quickly cancelling orders to move markets in their favor. While the DOJ has had a somewhat mixed record prosecuting individuals for spoofing, the agencies have together secured steadily larger resolutions against financial institutions, culminating in a \$920 million joint resolution with a major U.S. bank in late 2020. Given the extensive trading data available to the agencies and their increasingly sophisticated analytics capabilities, it is not hard to see how a CFTC whistleblower tip or examination that uncovers suspicious trading patterns could quickly escalate into referrals to the Enforcement Division and, in appropriate cases, the DOJ. Going forward, look for the CFTC and the DOJ to continue pursuing these and other larger and more complex manipulative trading schemes.
- **Physical Commodities and Benchmark Manipulation.** In March of this year, the DOJ and the CFTC announced parallel cases against an oil trader who allegedly submitted false bids to manipulate related benchmark prices for fuel oil, which in turn benefitted related trading positions. Similarly, part of the agencies' joint anticorruption resolution in December 2020 involved allegations that traders manipulated physical commodity pricing benchmarks. Unlike futures and derivatives trading, manipulative activity in the more opaque markets for physical commodities—especially over-the-counter markets—can be harder to detect using data analytics, but both agencies have powerful tools at their disposal that allow them to obtain relevant information. If this recent activity is any guide, the DOJ and the CFTC appear intent on policing fraud in the physical commodities markets—particularly where such conduct has impacts on pricing benchmarks.

ARMING YOUR COMPLIANCE PROGRAMS TO ADDRESS THESE CHALLENGES

No one can predict whether or when an investigation may arise, but it is possible to design an effective compliance program that positions your organization to reduce the likelihood of misconduct and, if necessary, respond effectively to an inquiry from the CFTC or the DOJ. In the best-case scenario, an effective compliance program can deter employee misconduct in the first place. If it does occur, a well-designed compliance program can help a company to quickly marshal the facts and implement a response. It can also increase the likelihood that misconduct is detected early, better positioning a company to consider self-disclosure and allowing it to take advantage of the benefits available for cooperation and remediation. And in the event of an enforcement action, the design and effectiveness of a compliance program are variables that can impact the form and size of any resolution.

In recent years, both the DOJ's Criminal Division and the CFTC's Division of Enforcement have published guidance—such as the Criminal Division's *Evaluation of Corporate Compliance Programs* (“DOJ ECCP”) guidance and CFTC Enforcement's *Guidance on Evaluating Compliance Programs in Connection with Enforcement Matters* (“CFTC Guidance”)—explaining how they look at compliance programs in enforcement matters. Based on our experience with these policies, we believe companies operating in the commodities space—whether financial institutions or other types of companies—will be well-served to ask themselves the following questions when evaluating their compliance programs to address the emphasis on commodities fraud.

1. **Does your compliance program look at your business the same way the DOJ and the CFTC do?** The very first question in the DOJ ECCP asks whether a company's compliance program is “well designed”—i.e., whether it is “adequately designed for maximum effectiveness in preventing and detecting wrongdoing” and whether it is “well-integrated into the company's operations and workforce.” In our experience, some organizations maintain separate compliance functions with responsibility for obligations under the FCPA, BSA, CEA, and other laws. Similarly, coverage of “U.S. law” issues can sometimes be less robust for companies or business units in foreign countries, even

though the long arm of the DOJ and the CFTC can reach extraterritorial conduct.

Every company is different, and the design of any compliance program will necessarily vary depending on a company's risk profile and business operations. But in evaluating compliance programs, companies should bear in mind that the DOJ and the CFTC do not take a “siloes” approach to commodities fraud. Companies should therefore ensure that they are taking an integrated approach to the design and structuring of their compliance programs. Companies should inventory key business lines in order to spot potential issues—both in the United States and abroad—that may trigger interest by the DOJ and the CFTC. A company's compliance program can be fine-tuned based on such a bottom-up approach, with an eye to identifying critical areas in which policies, procedures, training, and testing can be strengthened.

2. **How well do you integrate data analytics into your surveillance, monitoring, and internal audit functions?** As explained earlier, the DOJ and the CFTC are focused on using data analysis to spot commodities fraud. More importantly, both agencies have made clear that they expect corporate compliance departments to be doing the same. The DOJ ECCP asks: “Do compliance and control personnel have sufficient direct or indirect access to relevant sources of data to allow for timely and effective monitoring and/or testing of policies, controls, and transactions?”

In light of this focus, companies should evaluate their surveillance, monitoring, and internal audit functions to ensure that they are taking advantage of available data and analytical tools in reviewing business operations, such as trading activity. The CFTC and the DOJ do not make details of their own data analysis tools public, but their approach in charged cases can be instructive. In addition, many exchanges and trading associations offer helpful guidance and training programs. Forensic consulting firms can also help buttress internal efforts to analyze internal data and trading activity. In short, resources abound to upgrade how your organization uses data to identify, assess, and address potential instances of problematic trading. If a company uses data analytics to help drive its business—and many do—it is a safe bet the DOJ and the CFTC will expect it to do the same for its compliance function.

3. **Is your compliance program a two-way street, where the legal/compliance team and business units communicate regularly?** The DOJ ECCP explains that to be “truly effective,” a compliance program must include “appropriately tailored training and communications.” In our experience, the DOJ and the CFTC expect a company to regularly consider necessary updates and revisions to compliance policies, procedures, and controls, and to incorporate “lessons learned” from both its own experiences and those of other similarly situated companies. We have found that this is only possible where a company has a culture that encourages and supports open communication and collaboration between its compliance function and business units about risks the company and its peers face through their operations.

Of course, a compliance department must remain objective in carrying out its core functions, but that does not mean compliance can—or should—wall itself off from the business. Likewise, guidance makes clear that a compliance department should communicate important messages to the business units regularly and in terms they can understand, with an eye toward making those communications effective—think “ripped from the headlines” updates on recent cases and settlements, for example. Business units should also be encouraged to collaborate with compliance staff by bringing issues and concerns to their attention as they arise. There should be a shared culture of communication and problem-solving, rather than an atmosphere of “gotcha” and blame-shifting.

A spirit of open dialogue can have many other benefits, like encouraging potential whistleblowers to raise issues internally in the first instance, rather than directly with law enforcement and regulators. Both the DOJ and the CFTC place significant emphasis on the effectiveness of a company’s internal reporting procedures. While there can be significant financial incentives for tipping the government, in many cases whistleblowers are principally motivated to go outside the organization because they feel like the business culture has gone awry, management has turned a blind eye toward misconduct, and their concerns are not being taken seriously. If your organization maintains a strong culture of compliance, those issues are more likely to be handled in-house in the first instance.

4. **Do you have a robust playbook for responding to regulatory inquiries, with clear guidelines for spotting and escalating issues in priority areas for law enforcement?** Many significant enforcement matters brought by the DOJ and the CFTC began with an inquiry that a derivatives exchange made of a participant, or that a futures broker made of its customer. Accordingly, your organization will be well-served to treat those kinds of inquiries with the same degree of care as it does an inquiry from the DOJ, the CFTC, or other law enforcement. Your company’s answers to an exchange or broker may very well wind up in the hands of law enforcement.

Companies will be better positioned in responding to inquiries about their trading activities—regardless of the source—if their response procedures call for thorough fact gathering, analysis, and dialogue that involves all key internal stakeholders. Depending upon the circumstances, the surfacing of potentially problematic information at an early stage may help a company determine whether, in keeping with existing DOJ and CFTC guidelines, the initial response should be coupled with commitments to remediate shortcomings and cooperate fully throughout the ensuing investigation.

Of course, in preparing any response, a company should apply a modification of the old adage “measure twice, cut once”—namely, check the facts twice, and respond accurately and completely the first time. And the facts should come before any narrative that seeks to explain why things went wrong, even if the intention is to provide clarity to the regulators about the organization’s mindset. We have seen firsthand companies lose credibility when they attempt to offer explanations that are later contradicted by documents or testimony.

The DOJ and the CFTC are focused on working together to investigate and prosecute commodities-related misconduct. Going forward, we expect them to build on their already-significant track record in this area to bring more and larger cases. Companies should take stock of their compliance function and ensure that they are prepared to deal with the potential for active civil and criminal commodities fraud enforcement by the DOJ and the CFTC in the years ahead.

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ENDNOTES

- 1 We use “commodities fraud” broadly throughout this memorandum as a shorthand for fraud, market manipulation, spoofing, and other forms of unlawful commodities-related trading practices.
- 2 Joshua B. Sterling previously served as Director of the Market Participants Division at the CFTC, where he dealt regularly with commodities fraud enforcement matters. Brian C. Rabbitt most recently served as Acting Assistant Attorney General for the DOJ’s Criminal Division and, prior to that, as a senior enforcement official at the U.S. Securities & Exchange Commission.

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