

Client Alert

Special Matters & Government Investigations Practice Group

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New CFTC Director of Enforcement Incentivizes Self-Reporting, Counts on “Buy-in” From Market Participants

In prepared remarks at New York University’s School of Law on September 25, 2017, the newly minted Director of Enforcement at the U.S. Commodity Futures Trading Commission passionately outlined the contours of the CFTC’s new “self-reporting and cooperation” enforcement program.¹

In his first major speech since taking the helm of the Enforcement Division in March of this year, James McDonald reflected at the outset that an enforcement approach driven by reactive charging decisions was wholly incapable of fulfilling the CFTC’s stated mission of fostering open, transparent, competitive, and financially sound markets. McDonald suggested that the CFTC needed the “buy-in” of futures and options market participants in order to prevent wrongdoing and achieve “optimal deterrence.”

To obtain this “buy-in,” McDonald acknowledged that the CFTC will need to provide incentives. With this acknowledgement, he unveiled the CFTC’s ambitious new program—designed to entice cooperation through rewards—contemplating a multistep process of 1) self-reporting; 2) cooperation; and, 3) remediation.

Self-reporting. To self-report, a company must *voluntarily disclose* wrongdoing to the Division of Enforcement. Under the program, a disclosure is voluntary only if it predates an imminent threat of enforcement and is independent of any other legal duty. Moreover, a disclosure is one that is made with the intent to notify the Division of Enforcement of the wrongdoing; *i.e.*, it must be purposeful. This self-disclosure must first occur within a reasonably prompt timeframe after learning of misconduct and must include all relevant facts known *at that time*. Presumably to incentivize self-reporting and ease the time pressure of immediate disclosure, McDonald stressed that the communications can be made on a rolling basis as the company learns of additional facts.

Although regulated companies may be in regular contact with non-Enforcement CFTC divisions, such as the Division of Swap Dealer and Intermediary Oversight or the Division of Market Oversight, as well as self-regulatory organizations like the National Futures Agency, McDonald

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made it clear that the Division of Enforcement must be contacted in the “first set of calls” for a company to have a colorable claim of having self-reported.

Cooperation. In seeking full cooperation credit, a company must disclose all known facts, including facts known about individuals at all levels of seniority. According to McDonald, the CFTC sees cooperation as necessarily proactive, not merely reactive; it is not enough for a market participant to merely respond to staff requests. Analogizing to the RICO context, McDonald suggested that he expected companies and individuals to “cooperate up,” by sharing information on supervisors and senior executives. McDonald indicated that proper, credit-worthy cooperation will last the duration of the investigation and provide the Enforcement Division with “particular facts . . . attributed to particular people.”

Remediation. Finally, a company must timely and appropriately employ remedial measures to ensure that the wrongdoing does not occur again.

As was thematically apparent from McDonald’s speech, the CFTC is determined to provide incentives to ensure “buy-in” to the CFTC’s enforcement approach, and more specifically, this new program. Thus, in exchange for a company’s appropriate process of self-reporting, cooperating, and remediating, McDonald said the CFTC will: 1) clearly communicate its expectations at the outset; 2) work with the company on remediation; and, 3) provide concrete benefits in the form of significantly reduced corporate fines. When pressed during a question and answer session after his remarks, McDonald suggested a self-reporting company could see a “significant reduction” in fines by approximately 75%, and possibly even be rewarded with the elusive and valuable full declination. McDonald also made very clear that the credit (*i.e.*, fine reduction) for companies that only cooperated—as opposed to self-reported and cooperated—would be significantly less. McDonald has clearly designed the program with the hopes that these incentives will tip the scales in favor of self-disclosure and full cooperation when a company is facing that decision—one he stated often comes down to a “dollars and cents” evaluation.

In articulating the details, McDonald made clear that the program did not offer a “get out of jail free card” to market participants, but rather sought to borrow methods that have been successful in prosecuting other misconduct, including organized crime. Indeed, McDonald acknowledged that the new program was derived in part from his experience as a federal prosecutor with the U.S. Attorney’s Office for the Southern District of New York and his overall familiarity with RICO murder prosecutions.

Takeaways

The well-versed CFTC practitioner may ask what, exactly, about this heralded program is new, as the CFTC is no stranger to cooperation credit.ⁱⁱ Under the new program, however, self-reporting is no longer folded into cooperation but is treated distinctly, with separate credit considerations. Moreover, under the new program, self-reporting could lead to a much more substantial reduction in penalty compared with mere cooperation.

Given this new approach, in CFTC investigations going forward, companies must be prepared to answer two questions. First, did we self-report? Second, did we cooperate? If the company can only answer the second question affirmatively, it should not expect a significant reduction in corporate penalties.

The CFTC’s promise of that reduction for self-reporting and cooperation presupposes that a company’s maximum liability is easily discernible at the time a company is faced with the decision of whether or not to self-report. But, under the CFTC’s current practice of charging each and every alleged occurrence of prohibited conduct as a separate and distinct violation of the Commodity Exchange Act or the CFTC’s Regulations, that is by no means the

case. On this point, McDonald agreed that the CFTC needs to be transparent regarding potential liability before a contemplated reduction can serve as a meaningful incentive for companies.

Ultimately, market participants still have a difficult decision as to whether they should proactively approach the CFTC when misconduct is discovered. But McDonald's lucrative rewards for full compliance with the CFTC's new program are intriguing.

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ⁱ Remarks of CFTC Director of Enforcement James McDonald to the Program on Corporate Compliance and Enforcement and the Institute for Corporate Governance and Finance at New York University's School of Law, September 25, 2017, *available at* <http://www.cftc.gov/PressRoom/SpeechesTestimony/opamcdonald092517>

ⁱⁱ *See, e.g.*, CFTC Enforcement Advisory: Cooperation Factors in Enforcement Division Sanction Recommendations for Companies, January 19, 2017, *available at* <http://www.cftc.gov/idc/groups/public/@lrenforcementactions/documents/legalpleading/enfadvisorycompanies011917.pdf>; CFTC Enforcement Advisory: Cooperation Factors in Enforcement Division Sanction Recommendations for Individuals, January 19, 2017, *available at* <http://www.cftc.gov/idc/groups/public/@lrenforcementactions/documents/legalpleading/enfadvisoryindividuals011917.pdf>