

A close-up photograph of an hourglass with blue sand, set against a solid blue background. The hourglass is positioned vertically, with the top bulb containing a small amount of sand. The sand is falling through the narrow neck into the bottom bulb. The lighting is soft, highlighting the texture of the sand and the glass.

This webinar will begin shortly.

FIA



Getting Candid About Candor

—
19 April 2023



Reminders

- The webinar will be recorded and posted to the FIA website within 24 hours of the live webinar.
- Please use the “question” function on your webinar control panel to ask a question to the moderator or speakers.



Presenters

Host:

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Panelists:

John Byron, Partner, Financial Services Group, Steptoe

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Presentation prepared by **Steptoe**



Overview

- Government agencies have differing authority to prosecute false statements
 - Authority and recent developments of federal agencies and departments:
 - Commodity Futures Trading Commission (CFTC)
 - Securities and Exchange Commission (SEC)
 - Department of Justice (DOJ)
 - Federal Energy Regulatory Commission (FERC)
 - FERC's new proposed duty of candor, incl. as compares to authority of other federal agencies
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CFTC's Expanded Authority Over False Statements

- CEA has long prohibited false statements in certain contexts as part of its anti-fraud provisions
 - For example, CFTC could pursue charges for false statements “willfully” made in “any registration application or any report filed with the Commission.” CEA § 6(c)(2), 7 U.S.C. § 9(2) (2000)
- Dodd-Frank Act significantly expanded CFTC’s false statement of authority
 - Unlawful to “make *any* false or misleading statement of a material fact to the Commission . . . or to omit to state in any such statement any material fact that is necessary to make any statement of a material fact made not misleading in any material respect, if the person knew, or reasonably should have known, the statement to be false or misleading.” CEA § 6(c)(2), 7 U.S.C. § 9(2) (2010)

CFTC's Expanded Authority Over False Statements

- Key elements of Section 6(c)(2) of CEA
 - False statements to CFTC *in any context* are actionable (e.g., statements in interviews or attorney responses)
 - False statements are actionable through Commission enforcement action (*i.e.*, not solely criminal referral to DOJ)
 - CFTC burden = “preponderance of evidence”
 - False statements actionable when speaker “knew, or reasonably should have known,” statement false rather than higher standard that statement was made “knowingly and willfully”

CFTC's Expanded Authority Over False Statements

- CFTC has actively enforced its false statement authority
 - More than a dozen enforcement actions brought by CFTC that included charges under Section 6(c)(2)

"Witnesses in CFTC investigations must tell the truth. If they do not, the CFTC will not hesitate to take action to enforce [] Dodd-Frank's prohibition against providing false or misleading information and impose sanctions."

- Former CFTC Division of Enforcement Acting Director Gretchen Lowe

Recent Cases Under CFTC's Expanded False Statement Authority

- Key Facts
 - CFTC investigated bank and traders on precious metals trading desk for potential “spoofing” and compliance issues as to swap dealer business
 - Charged bank with making false and misleading statements and omitting facts in written submissions and testimony during investigation
 - Charged bank with making false statements to COMEX and NFA
 - Asserted violations under Section 6(c)(2) and Section 9(a)(4) of CEA
- Outcome
 - Bank settled and agreed to penalty of \$17 million

Recent Cases Under CFTC's Expanded False Statement Authority

- Key Facts
 - Complaint alleges that digital asset platform, directly and through others, made false and misleading statements of material fact to CFTC and omitted material facts in connection with self-certification of bitcoin futures product
 - Statements were made during in-person meetings with CFTC staff and in presentation materials, data, and documents provided to CFTC
 - CFTC charges platform with misleading Commission about fees it was charging, whether transactions had to be fully prefunded, and if the exchange was effectively preventing self-trading
 - CFTC brought claims under Section 6(c)(2) of CEA and seeks civil monetary penalties and disgorgement
- Litigation is ongoing

Recent Cases Under CFTC's Expanded False Statement Authority

- Key Facts

- Alleged that individual and two entities engaged in fraudulent scheme to solicit and misappropriate money given to them for purpose of trading futures in commodity pools
- CFTC issued subpoena to defendants, and CFTC alleged that defendants, through counsel, made false and misleading statements about number of clients

- Outcome

- Defendants consented to violations of CEA for, among other things, misappropriation and issuing false account statements, fraud, failing to register, and making false statements to Commission
- Defendants ordered to pay restitution and disgorge proceeds and to pay civil monetary penalties of more than \$13 million

CFTC's Authority Over False Statements to Futures Associations and Registered Entities

- Section 6(c)(2) – covers false statements made to the CFTC
- Section 9(a)(4) – covers false statements made to CFTC registered entities, boards of trade, swap data repositories, or futures associations acting in furtherance of their duties under the CEA

Recent Case Under CFTC's Section 9(a)(4) Authority

- Key Facts
 - Cattle feed yard submitted fraudulent invoices to its agribusiness partner for the costs of buying and feeding hundreds of thousands of “ghost cattle” and using the proceeds to cover margin calls on futures positions
 - Charged with submitting false and misleading information to CME concerning its cattle inventory, purchases, and sales in at least two hedge exemption applications seeking permission to exceed the exchange's position limits
 - CFTC did not allege that false statements misled anyone with respect to the futures contracts traded, induced others to trade, or injected false information into the physical or futures markets
- Outcome
 - Consent decree obligated trader to pay restitution and \$30M civil penalty

Section 9(a)(4) Authority Not Limited to Statements to Regulators

- Key Facts
 - No charges pertaining to any statements to regulators (e.g., CFTC, NFA, or an exchange)
 - Statements also did not concern the options and futures that he traded, did not mislead market participants, and did not insert false information into the market
 - Statements were, instead, to FCMs to induce them to open trading accounts
 - CFTC found that FCMs were unable to appropriately assess the risk
- Outcome
 - Trader settled and agreed to pay \$160,000 civil monetary penalty

Evolving Scope of CFTC False Statement Authority

- CFTC has used false statement authority in Section 6(c)(2) for false statements in variety of contexts
 - Interviews and formal testimony by CFTC
 - Written submissions to CFTC
 - Subpoena responses
 - Meetings with and presentations to CFTC
- CFTC has used authority in Section 9(a)(4) to pursue false statements to FCMs and exchanges even when false statements did not mislead anyone or influence any behavior in the market



Overview of SEC False Statement Authority

- Securities laws and regulations provide SEC authority to pursue false statements in a number of contexts
 - Examples → False statements in connection with purchase and sale of securities and in documents filed with SEC
- But securities laws do not have an analogue to Section 6(c)(2) of the CEA

"Frankly, I wish [the SEC] had the power the CFTC does."

- Former SEC Director of Enforcement Robert Khuzami



Overview of SEC False Statement Authority

- SEC must refer wrongdoers to DOJ for prosecution under 18 U.S.C. § 1001 and other federal statutes for false statements made during course of investigation

"Interviews with witnesses are typically conducted with a court reporter present and a verbatim transcript is usually produced. Although the staff cannot administer oaths or affirmations in a preliminary investigation, if a witness is willing to testify on the record, the Staff, after obtaining the witnesses's consent, will have the court reporter administer an oath. A criminal statute, which prohibits the making of false statements to government officials, 18 U.S.C. § 1001, applies even if the witness is not under oath. If the witness is placed under oath, then false testimony may be subject to punishment under federal perjury laws as well."

- Linda Chatman Thomsen, former Deputy Director of SEC Division of Enforcement

Notable Examples of Lack of Candor During SEC Investigation



Bernie Madoff



Martha Stewart



Niket Jain

DOJ Authority to Prosecute False Statements

False Statements in Government Matters (18 U.S.C § 1001)	Prohibits knowing and willful material false, fictitious, or fraudulent statements or representations “in any matter within the jurisdiction of the executive, legislative, or judicial branch of the Government of the United States”
Perjury (18 U.S.C. § 1621)	Prohibits any person under oath willfully from making statements that he or she does not believe to be true
Obstruction of Justice (18 U.S.C. § 1505)	Prohibits any person from “corruptly,” through threats of force or threatening letter or communication, influencing, obstructing, or impeding any proceeding before any department or agency of the United States

- **Key Differences with CFTC Authority under Section 6(c)(2)**

- Intent standard higher → false statement must be “willful” or “knowing” rather than “knew, or reasonably should have known”
- Burden of proof → Beyond a reasonable doubt rather than by a preponderance of the evidence



Contours of Criminal False Statement Liability

- False Statements (18 U.S.C. § 1001)
 - Covers almost any affirmative statement or concealment of fact that is material
 - Statements can be written or oral, sworn or unsworn, and voluntary or required by law
 - Statements can be made indirectly
 - Courts are divided over whether “willfully” requires proof that the defendant knew his or her conduct was unlawful
- Perjury (18 U.S.C. § 1621)
 - Limited to statements made under oath
 - Literally true but unresponsive answer, even if the witness intends to mislead, cannot form the basis of a perjury charge
- Obstruction of Justice (18 U.S.C. § 1505)
 - § 1515(b) defines corruptly as “acting with an improper purpose, personally or by influencing another, including making a false or misleading statement . . .”
 - Proceeding can be an investigation

FERC's Existing Duties of Candor

- FERC does not currently have a broad prohibition on false statements
- FERC has adopted various regulations imposing a duty of candor for specific types of communications

Examples:

Submissions Required by FPA and NGA	Certain submissions must be under oath and subject to penalty of perjury.
Pipeline Certificates (18 CFR § 157.5)	FERC has interpreted provision to require applicants seeking pipeline certificates to disclose “fully and forthrightly . . . all information relevant to the application.” <i>See Black Marlin Pipeline Co.</i> , 4 FERC ¶ 61,039, at 61,088 (1978).
Anti-Market Manipulation (18 CFR § 1c.1(a)(2), 1c.2(a)(2))	Prohibits “untrue statements of material fact” in connection with natural gas or electric energy transactions.
Market Behavior Rule (18 CFR § 35.41(b))	Prohibits false statements made by entities who have sought or obtained electric market-based rate authority.



FERC's Proposed Duty of Candor

"Any entity must provide accurate and factual information and not submit false or misleading information, or omit material information, in any communication with the Commission [and various FERC-jurisdictional or approved entities], where such communication relates to a matter subject to the jurisdiction of the Commission, unless the entity exercises due diligence to prevent such occurrences."



Key Features of FERC's Proposal

- Covers all communications related to a matter subject to FERC's jurisdiction
- Covers not only communications with FERC and FERC staff itself but also with other entities that operate within FERC's regulatory scheme
- Intends to reach individuals employed by or acting on behalf of relevant entities, including agents and contractors (e.g., lawyers)
- No intent or willful misconduct standard
- No materiality element to differentiate between material misstatements and inadvertent errors
- Provides safe-harbor if entity can show that it exercised due diligence
 - But will add significant cost on regulated parties in communicating with Commission and related entities

Industry Reactions to FERC's Proposal

It's Bad Policy

a solution in search of a problem

scope is too broad

no requirement of intent

no materiality standard

It's Unlawful

arbitrary and capricious under APA

no statutory basis in FPA

first amendment concerns

Comparison Between CFTC's Authority and FERC's Proposal

	CFTC Authority	FERC Proposed Rule
Coverage	Any communication with CFTC and registered entities, boards of trade, swap data repositories, or futures associations	Any communication with FERC and various FERC-jurisdictional or approved entities
Materiality Standard	Must relate to material fact	No materiality standard
Intent	Knew or reasonably should have known statement was false	No intent required but protection if exercised due diligence



Thank you for joining us today!

Upcoming Webinar:



Event Contracts

10:00 – 11:00 AM ET



Energy Transition: Trends in Derivatives Transactions

10:00 – 11:00 AM ET



Additional questions?

FIA

The image features the letters 'FIA' in a bold, sans-serif font. The 'F' is a solid dark grey. The 'I' is a solid dark grey. The 'A' is composed of two overlapping shapes: a light green triangle pointing upwards and a light blue triangle pointing downwards, which together form the letter 'A'. The background consists of several overlapping, semi-transparent geometric shapes in shades of light green, light blue, and white, creating a layered, abstract effect.