

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 a vibrant blue color, matching the background. The hourglass is made of clear glass, and the sand is in the process of falling from the top bulb to the bottom bulb. The lighting is soft, highlighting the texture of the sand and the transparency of the glass.

This webinar will begin shortly.

FIA



CFTC Enforcement of Environmental Fraud

—
12 October 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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Presentation prepared by **SIDLEY**



Agenda

- CFTC Voluntary Carbon and Environmental Market Fraud Initiative
- CFTC Jurisdiction over Voluntary Carbon and other Environmental Markets
- Market Manipulation under the Commodity Exchange Act
- Illustrative Examples of Environmental Market Enforcement
- Trading Compliance Considerations for Environmental Markets
- New California Developments
 - California Climate Legislation
 - California Anti-Price Gouging Legislation



CFTC Voluntary Carbon Market and Environmental Fraud Initiative



CFTC Voluntary Carbon and Environmental Markets Initiative – First Convening

- On June 9, 2022, CFTC Chairman Rostin Benham hosted a [forum](#) to discuss Voluntary Carbon Markets to address concerns surrounding the quality of traded carbon offset credits, and the foundational items (e.g., registration, data integrity) necessary to ensure sound market structures.
- *“Our goal is to foster innovation in crafting solutions to the climate crisis while ensuring integrity and customer protection.” – Chairman Benham*
- After this meeting the CFTC published a [Request for Information](#) in the *Federal Register* seeking understanding regarding: types of data to evaluate climate-related financial risk, forecast scenario analysis and stress testing, risk management practices, information disclosure, voluntary carbon market structure, derivative product innovation, among other things.



CFTC Voluntary Carbon and Environmental Markets Initiative – Whistleblower Alert

On June 20, 2023, the CFTC’s Whistleblower Office in the Division of Enforcement [issued](#) an [alert](#) to make the public aware of how to identify potential fraud or manipulation of the carbon markets. Focusing on:

- *Fraud in the underlying spot markets*
- *Double counting related to carbon credits*
- *Fraudulent statements related to material terms: quality, quantity, methodology, environmental benefits, permanence, etc.*
- *Wash trading*
- *Market manipulation*



CFTC Voluntary Carbon and Environmental Markets Initiative – Environmental Fraud Task Force

On June 29, 2023, the CFTC’s Division of Enforcement [announced](#) the creation of a task force to “address fraud and other misconduct not only in regulated derivatives markets, but also in relevant spot markets (such as voluntary carbon credit markets), relating to purported efforts to address climate change and other environmental risks.”



CFTC Voluntary Carbon and Environmental Markets Initiative – Second Convening

- On July 19, 2023, CFTC Chairman Rostin Benham hosted a second Voluntary Carbon Markets [forum](#), this time highlighting what the Commission learned from its request for information. The Chairman explained:
- “Two main takeaways from the input we received are: 1) the Commission should use our anti-fraud and anti-manipulation enforcement authority to the fullest extent possible; and 2) the Commission should support the development of standards to promote the growth of high integrity carbon offsets.”



CFTC and Environmental Regulatory Coordination

On July 12, 2023, the Environmental Protection Agency (EPA) [promulgated](#) its Renewable Fuel Standard (RFS) for 2023-2025 and reiterated its memorandum of understanding that “allows EPA to share RIN transaction data with CFTC to advise EPA on the techniques used to minimize market manipulation, to increase CFTC’s understanding of the RIN market, and to conduct oversight for this market.”

The California Air Resources Board (CARB) also [coordinates](#) with the CFTC and the Federal Energy Regulatory Commission (FERC) “to strengthen carbon and related energy market monitoring, oversight, and enforcement.”



CFTC Jurisdiction Over Environmental Markets

Environmental Markets Examples – Cash, Derivatives, and Jurisdiction

Cash Markets	Cash Jurisdiction	Derivatives Markets	Derivatives Jurisdiction
Low Carbon Fuel Standards (LCFS) Credits	CARB	ICE LCFS (Opis) Futures – Cash Settled	CFTC
California Carbon Allowances (CCA)	CARB	ICE CARB CCA Futures and Options – Physical Delivery by Vintage	CFTC
Renewable Fuel Standard (RFS) Renewable Identification Numbers (RIN) – Ethanol, Biodiesel, Biofuels	EPA	ICE Biofuel Outright – D6 RINs (OPIS) Futures – Cash Settled	CFTC
Voluntary Carbon Offset Credits – Xpansiv – CBL Global Emissions Offset	??? CARB – CA?	CME GEO CBL Carbon Offset Futures	CFTC



CFTC Voluntary Carbon and Environmental Markets Initiative – Jurisdiction Over Environmental Commodities

The CFTC has clarified that “an emission allowance created by the EPA is a nonfinancial commodity and that agreements, contracts and transactions in such allowances may fall within the forward exclusion from the swap definition.” *Further Definition of Swap*, 77 Fed. Reg. 48,208 at 48,235 (Aug. 13, 2012).

CFTC provided “an interpretation that an intangible commodity ... which can be physically delivered qualifies as a nonfinancial commodity if ownership of the commodity can be conveyed in some manner and the commodity can be consumed. One example of an intangible nonfinancial commodity that qualifies under this interpretation ... is an environmental commodity, such as an emission allowance, that can be physically delivered and consumed (e.g., by emitting the amount of pollutant specified in the allowance). The interpretation provided herein recognizes that transactions in intangible commodities can, in appropriate circumstances, qualify as forwards, while setting forth certain conditions to assure that the forward exclusion may not be abused with respect to intangible commodities.” *Id.*



CFTC Anti-Manipulation Authority



CFTC Anti-Manipulation Authority

- **Price Manipulation 180.2** – It shall be unlawful for any person, directly or indirectly, to manipulate or attempt to manipulate the price of any swap, or of any commodity in interstate commerce, or for future delivery on or subject to the rules of any registered entity.
- **Fraud-Based Manipulation 180.1** – It shall be unlawful for any person, directly or indirectly, in connection with any swap, or contract of sale of any commodity in interstate commerce, or contract for future delivery on or subject to the rules of any registered entity, to *intentionally or recklessly*:
 - (1) Use or employ, or attempt to use or employ, any manipulative device, scheme, or artifice to defraud;
 - (2) Make, or attempt to make, any untrue or misleading statement of a material fact or to omit to state a material fact necessary in order to make the statements made not untrue or misleading;
 - (3) Engage, or attempt to engage, in any act, practice, or course of business, which operates or would operate as a fraud or deceit upon any person; or,
 - (4) Deliver or cause to be delivered, or attempt to deliver or cause to be delivered, for transmission through the mails or interstate commerce, by any means of communication whatsoever, a false or misleading or inaccurate report concerning crop or market information or conditions that affect or tend to affect the price of any commodity in interstate commerce, knowing, or acting in reckless disregard of the fact that such report is false, misleading or inaccurate. Notwithstanding the foregoing, no violation of this subsection shall exist where the person mistakenly transmits, in good faith, false or misleading or inaccurate information to a price reporting service.



CFTC Anti-Manipulation Authority - Environmental Fraud Task Force Focus

- Fraudulent statements related to material terms: quality, quantity, methodology, environmental benefits, permanence, etc.
- Fraud in the underlying spot markets
- Double counting related to carbon credits
- Wash trading
 - Offsetting transactions without economic risk to give the illusion of liquidity
- Market Manipulation
 - Corners, Squeezes, Cross Market Manipulation



Illustrative Examples of Environmental Market Enforcement



CARB LCFS – Misrepresentation of Actual Carbon Intensity of Fuel Produced

Itumbiara Bioenergia S.A. and Itumbiara Bioenergia Ltda.

- In December 2021, CARB reached an approximately \$300,000 civil penalty settlement with two [Itumbiara Bioenergia](#) entities, for misrepresenting the transportation method of fuel produced in Brazil and imported to California. Subsequently, Itumbiara ***submitted quarterly fuel reports that deviated from the actual carbon intensity of the fuel reported.*** In 2022, CARB settled with [Diamond Green Diesel](#) for similar carbon intensity misrepresentations.
- Fuel reporting entities selling, supplying or offering for sale transportation fuel into California must report fuel to CARB as well its carbon intensity, which determines the number of credits or deficits the fuel will generate and ultimately demonstrate the fuel reporting entity met its annual compliance requirements.



Regulator Coordination – Artifice or Device to Defraud

Volkswagen

In 2017, Volkswagen pled guilty to defrauding the US, committing wire fraud, and violating US and California law with respect to vehicle emissions requirements. VW paid approximately \$2.8 billion settlement for [engaging](#) in a “long-running scheme to sell approximately 590,000 diesel vehicles in the U.S. by using a defeat device to cheat on emissions tests mandated by the [EPA] and the [CARB], and lying and obstructing justice to further the scheme.”

“[After](#) VW admitted to the presence of defeat devices in the affected vehicles, CARB, the U.S. Environmental Protection Agency, the California Department of Justice, and the U.S. Department of Justice took legal action against the company, resulting in billions of dollars in court judgements, and civil and criminal penalties.”



EPA RINS Fraud

Green Diesel, LLC

On March 7, 2016, Philip Joseph Rivkin, a/k/a Felipe Poitan Arriaga, CEO of Green Diesel, LLC was [sentenced](#) to more than 10 years in prison and ordered to pay \$87 million in restitution and ordered to forfeit \$51 million generating and selling fraudulent biodiesel RINs.

Rivkin claimed to produce millions of gallons of biodiesel and then generated and sold RINs based upon this claim. In reality, the indictment states, no biodiesel was ever produced.

The case involved EPA and DOJ enforcement coordination.



EPA RINS – Failure to Retire RINs

Chemoil Corporation

On September 29, 2016, EPA entered into a [settlement](#) with Chemoil Corporation that requires the company to retire 65 million renewable fuel credits to resolve alleged violations of the RFS program. “EPA alleged that Chemoil exported at least 48.5 million gallons of biodiesel from the United States in 2011, 2012, and 2013, without retiring the approximately 72.7 million biomass-based diesel RINs for that fuel.”

“The market value of the credits at the time of the settlement agreement -- along with an additional 7.7 million renewable identification numbers (RINs) already retired by Chemoil in the lead up to this settlement -- was more than \$71 million.”

A \$27 million civil penalty was assessed.



Trading Compliance and Investigation Considerations



Trading Compliance and Investigation Considerations

Compliance

- For non-registrant, principal traders there are no specific supervisory requirements.
- However, the CFTC has provided [guidance](#) on how to think about such compliance programs.
- Consider documentation of trading and hedging strategies.

Responding to an Investigation

- As the CFTC will likely be coordinating with other environmental regulators like the EPA , CARB, and perhaps the DOJ market participants subject to these multi-disciplinary investigations would need to consider legal advice pertaining to each of these disciplines.



New California Developments



California Climate Legislation

- On October 7, 2023, California Governor Gavin Newsom [signed](#) into law landmark climate disclosure and financial reporting legislation: the [Climate Corporate Data Accountability Act](#), (SB 253) and the [Climate-Related Financial Risk Act](#) (SB 261). Referred to as the Climate Accountability Package, these new California laws impose unprecedented reporting requirements on large U.S. public and private companies doing business in California including:
 - Disclosure of Scope 1 and Scope 2 greenhouse gas (GHG) emissions beginning in 2026 and Scope 3 GHG emissions in 2027; and
 - Submission of biennial climate-related financial risk reports to the California Air Resources Board (CARB) beginning in 2026.



California Anti-Price Gouging Legislation

In March 2023, California Governor Gavin Newsom [signed](#) into law the California Gas Price Gouging and Transparency Law to regulate price gouging of retail oil liquids products, which:

- Authorizes the California Energy Commission (CEC) to set a maximum gross gasoline refining margin and a penalty for refiners that exceed it.
- Requires new data collection authority and creates an independent division to monitor petroleum markets and flag potential market manipulation.
- Requires an assessment of transportation fuel demand and discussion of methods to ensure an adequate, affordable, and reliable fuel supply as the state transitions away from petroleum fuels.



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Paul Tyrrell



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PAUL TYRRELL focuses his practice on securities and commodities compliance and enforcement matters affecting financial institutions, with an emphasis on sales practice and supervisory rules applicable to broker-dealers and their associated persons. He also advises clients on their compliance with the USA PATRIOT Act, Bank Secrecy Act and related anti-money laundering requirements. Paul's extensive regulatory and litigation experience informs his comprehensive approach to challenges that clients encounter throughout their various lines of business. He is a member of Sidley's global Securities Enforcement and Regulatory practice, which received the *2019 Chambers USA Award* for "Financial Services Regulation," and was named the "Law Firm of the Year" for Securities Regulation in 2020 and 2017 by *U.S. News – Best Lawyers*.

Paul was a senior special regional counsel at FINRA's (formerly NASD) Boston District Office. He managed investigations and filed disciplinary matters arising out of broker-dealer examinations. He also counseled Member Regulation staff and industry participants on FINRA and MSRB rules.

As a senior trial attorney with the CFTC in New York, Paul managed enforcement matters involving commodity futures and options. He also worked as a senior attorney with the FDIC and taught business law at the University of Massachusetts-Boston.

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MAUREEN GORSEN practices at the intersection of public policy, litigation, and regulatory advocacy with a keen sense of her clients' business objectives. She is a member of Sidley's Environment practice, focusing on enforcement defense and regulatory compliance. Maureen has defended clients in both federal and state enforcement matters, including hazardous waste, stormwater, air quality, AB 32, Prop 65, product labeling, food packaging, and business and tax regulation. She develops strategies for regulatory and permit compliance for environmental, financial, tax, consumer products, and supply chain regulation issues. Maureen also assists clients in developing corporate policies to reduce product liability risks and meet sustainability, supply chain, anti-slavery and human trafficking, and conflict minerals statutes.

She is the former director of the California Department of Toxic Substances Control (DTSC), where she directed regulation of waste, soil, and water cleanups under the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA), the Resource Conservation and Recovery Act, and brownfields laws. Maureen spearheaded the California Green Chemistry Initiative and resulting laws governing chemicals under the California Safer Consumer Products rules and other states' products programs and federal Toxic Substances Control Act (TSCA) reform.

Maureen is also the former general counsel of the California Environmental Protection Agency (CalEPA) and the California Natural Resources Agency.

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CASEY KHAN is a member of the Energy practice group, representing clients on a variety of regulatory, enforcement, compliance and transactional matters involving the U.S. energy and commodity markets. Casey has over 15 years of experience working directly on commodity and financial trading floors in risk management, legal, and compliance functions. His advisory experience includes trading and hedging operations, risk management controls, and the creation and implementation of robust compliance programs. Casey recognizes the complexity of operating in a fast-paced competitive market environment, and the need for high-integrity transaction analysis when advising clients and practicing before U.S. exchanges and regulatory commissions.

Additionally, Casey represents institutions in regulatory proceedings, inquiries, and investigations before the Commodity Futures Trading Commission (CFTC), Federal Energy Regulatory Commission (FERC), and various Commodity & Derivative Exchanges (CME, ICE).

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FIA

The image features the letters 'FIA' in a bold, sans-serif font. The 'F' is dark grey. The 'I' is dark grey with a green triangle overlapping its right side. The 'A' is blue with a green triangle overlapping its left side and another blue triangle overlapping its right side. The background consists of several overlapping geometric shapes: a light green triangle pointing down from the top left, a light blue triangle pointing up from the bottom left, a light green triangle pointing up from the bottom right, and a light blue triangle pointing down from the top right. The overall composition is clean and modern.