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CFTC Division of Enforcement Releases Enforcement Advisory on Penalties, Monitors, and Admissions

Advisory Signals Potential Increase in CFTC Penalties, Imposition of Monitors, and Required Admissions in Resolutions

SUMMARY

On October 17, the Commodity Futures Trading Commission's ("CFTC") Director of Enforcement, Ian McGinley, announced the release of a new Enforcement Advisory on Penalties, Monitors, and Admissions ("Advisory"). Director McGinley noted in his remarks that one of the goals of the Advisory is to "dispel th[e] myth" that the CFTC is "'friendly' when it comes to enforcement," and he emphasized the Enforcement Division's (the "Division") focus on increasing penalties to enhance deterrence. The Advisory, which supplements the CFTC's Enforcement Manual (first released in 2020), provides guidance on three key aspects of CFTC enforcement actions: (i) how civil monetary penalties will be calibrated, particularly for recidivists; (ii) when corporate compliance Monitors or Consultants will be imposed; and (iii) when requiring admissions will be appropriate.

A. Civil Monetary Penalties

In his remarks announcing the new policy, Director McGinley emphasized that, when assessing penalties, Division Staff will be guided by the overarching goal of achieving both general and specific deterrence. To this end, he signaled that penalties will be higher, particularly in instances of repeat violations—and not only where a single respondent has committed a violation more than once, but where violations were committed by different respondents and general deterrence will warrant a higher penalty. Director McGinley highlighted two situations in particular in which the Division will look to increase penalties.

First, to better achieve general deterrence, the Division will seek to increase penalties in matters involving specific areas or market sectors in which it believes violations are recurring. Director McGinley noted as an

example that the Dodd-Frank Wall Street Reform and Consumer Protection Act included provisions aimed at increasing transparency into the global swaps market by requiring data collection and reporting. More than 13 years later, the CFTC is still seeing issues in the data it receives from swap dealers. Director McGinley emphasized in his remarks that increasing deterrence through higher penalties is "particularly important" when multiple parties have violated the same law.

Second, with the respect to specific deterrence, the Division will seek to increase penalties where it believes a respondent is a repeat offender. The Advisory identifies five factors that the Division will consider in determining whether a respondent is a recidivist:

1. Overlap with prior enforcement actions. The Division will consider the overlapping nature of the prior and current Commission actions (for example, do they involve the same or similar kinds or categories of violations) and will look to whether the violations resulted from the same root cause or involved the same general subject matter.
2. Time between offenses. More recent conduct is likely to be given more weight in determining whether an entity is a recidivist.
3. Overlapping management. The Division will consider whether a case involves the same management as a prior enforcement action.
4. Pervasiveness of the new misconduct. New misconduct that is *de minimis* and quickly identified and remediated is less likely to result in a recidivism finding than pervasive new misconduct that persists over time.
5. Remediation. In evaluating recidivism, the Division also will consider the robustness and effectiveness of remediation, if any, that the respondent undertook and maintained since the prior resolution. Inadequate remediation reflects an insufficient commitment to addressing prior misconduct and minimizing the risk of recurrence.

Under current Division policies, recidivism is an aggravating factor that can increase the penalty amount in a resolution. Director McGinley announced that the Division plans to prioritize recidivism as an aggravating factor and will "heavily factor recidivism" in determining appropriate penalties for resolutions going forward.

B. Monitors and Consultants

Director McGinley said the Division also will seek to enhance remediation in connection with its enforcement actions through increased use of Monitors or Consultants, and he emphasized that a Monitor or Consultant may be appropriate, in particular, where the respondent is a recidivist. Under the Advisory, a "Monitor" is defined as a third party engaged by the Division to make and test recommendations for remediation. Where a Monitor is required, the Division will approve the selection of the specific Monitor and require regular reports from the Monitor detailing the remediation plan and the entity's implementation progress. Director McGinley said the Division will impose a Monitor when it "lack[s] the confidence that the entity will remediate itself, without Division oversight."

By contrast, under the Advisory, a "Consultant" is defined as a third party engaged by the respondent entity to "advise" on compliance enhancements. Respondents typically will be permitted to select their own

Consultant, without a need for Division approval, but Consultants will be required to provide periodic reports to the Division on the entity's implementation progress.

The Advisory also indicates that whenever a Consultant or Monitor is required, CFTC resolutions will require that appropriate personnel from the respondent entity, such as a Chief Compliance Offer, certify the completion of a remediation plan.

C. Admissions

Director McGinley signaled that respondents should also be prepared for resolutions to include admissions, which he described as "the civil equivalent of a guilty plea." Under the new Advisory, "respondents should no longer assume that no-admit, no-deny resolutions are the default." Rather, the Division will discuss whether admissions are appropriate in each individual resolution.

The Advisory includes a "non-exhaustive" list of factors that counsel in favor of admissions, including: (i) if the respondent is entering into a parallel criminal resolution where the respondent admits to the underlying misconduct; (ii) if the evidence uncovered during the investigation "conclusively establishes" the misconduct; (iii) if and to what extent a respondent seeks cooperation credit; and (iv) if the offense is a strict liability offense in "clear violation of the law." In addition, both the Advisory and Director McGinley's remarks highlighted the potential deterrent effect of admissions, signaling that admissions may be more likely for recidivist respondents.

The Advisory also acknowledged that there may be factors that counsel against requiring admissions and identified examples: (i) if there is a "realistic risk of criminal exposure" arising from admitting the misconduct at issue, and (ii) if there is a "legitimate factual dispute" where the Division believes it faces "significant litigation risk establishing the fact at trial."

IMPLICATIONS

The Advisory and Director McGinley's accompanying remarks indicate one main theme—respondents, particularly recidivists, should be prepared for increased penalties and remediation requirements, including Monitors, and, potentially, admissions. In this vein, the CFTC's guidance is in line with recent announcements from both the Department of Justice ("DOJ") and the Securities and Exchange Commission ("SEC").

Any effort to increase clarity as to the important areas of penalties, Monitors, and admissions should be welcomed. The Advisory, however, leaves open a number of questions, which will be addressed through its application to particular cases. These questions are worth watching closely as the Division implements these policies.

To take one example, the Advisory focuses on regulated markets, and Director McGinley's accompanying remarks tied the policies closely to regulated nature of the markets at issue. But the Advisory on its face

does not distinguish between registrants and non-registrants, or between conduct in CFTC-regulated derivatives markets and the unregulated spot markets.

As another example, while the Advisory provides helpful guidance on the circumstances in which Monitors will be required and the core responsibilities Monitors will undertake, it leaves open some questions around how CFTC monitorships will work in practice. For example, the Advisory indicates that the Monitor will report to the Division on the respondent's remediation plan, suggesting that the contours of the remediation plan will define the scope of the monitorship. Because a clear scope and framework is essential for prompt and efficient conclusion of a monitorship, this will be an important point to confirm in connection with any specific monitorship and additional guidance in this area would be welcome. When and how will the plan of remediation will be approved, and by whom? Similarly, although the Advisory indicates that the Monitor and a relevant executive will be required to certify completion of the entity's remediation plan, it does not specify the standard against which remediation will be assessed.

In addition, Director McGinley, in his remarks, referenced Deputy Attorney General Lisa Monaco's previous statements on the DOJ's guidance on recidivism, which noted that special considerations are necessary when a defendant is in a highly-regulated industry with more touch points with regulators. One of those special considerations is that highly-regulated market participants are often subject to rules that can be enforced on a strict liability standard. Many CFTC rules applicable to registrants (*e.g.*, recordkeeping, data reporting and others) as well as rules applicable to non-registrants (*e.g.*, position limits) fall within this category. It has thus typically been understood that these sorts of regulatory violations would be treated differently from other, scienter-based violations in evaluating recidivism. It is unclear whether this Advisory intends to alter that understanding.

It is not always clear, moreover, how the Commission determines when these strict-liability, regulatory violations will be handled through informal discussions and remediation through the CFTC's policy divisions and when they will result in enforcement. This determination takes on even more significance if enforcement in these areas contributes to a recidivism analysis.

Another important consideration will be how the Division considers the timing of the offenses at issue in a recidivism analysis. Because enforcement investigations take time, it is not uncommon for the same entity to be subject to two actions, the filing of which is separated in time, but the underlying conduct as to each may be overlapping, often resulting from the same root cause that has since been remediated. These might appear to be a "repeat" offense from the perspective of the timing of the enforcement action, but not from the perspective of the timing (and cause) of the underlying conduct, which may be the more appropriate metric. We will thus be watching how the Division considers timing in its recidivism as well.

Director McGinley closed by noting the continued importance of "self-reporting and cooperation" in achieving a more favorable resolution. Director McGinley did not, however, offer much additional clarity regarding how self-reporting will be rewarded, and suggested that cooperation could come with a price, *i.e.*,

admitting to the violations. Particularly in light of Advisory's policies that seem to enhance penalties on respondents subject to enforcement actions, entities will be looking for as much clarity as possible regarding how they will be treated were they to self report. This is another recurring question that will be important to follow going forward.

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