

CLIENT ALERT

CFTC Settles “Insider Trading” Action Against Houston Energy Trader, Separately Settles Spoofing Action Against Sunoco

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On September 30, 2020, the CFTC issued two speaking orders settling charges related to two separate investigations. The first settlement was against an energy trader, Marcus Schultz, who misappropriated his employer’s natural gas trading information for his own personal benefit.¹ The Schultz settlement highlights the CFTC’s continued pursuit of misappropriation cases along with its insistence on borrowing concepts from the securities markets, such as “Inside Information,” that historically were used only in very limited circumstances in the commodities markets.

In a separate and unrelated speaking order, the CFTC settled charges against Sunoco related to a trader’s spoofing activity in crude oil, gasoline, and heating oil futures markets.² The Sunoco settlement follows the CFTC’s end-of-fiscal-year announcement of several other spoofing settlements obtained by the CFTC Division of Enforcement’s spoofing task force. Below are brief summaries of the Schultz and Sunoco settlements. Please contact us if you have any questions or concerns about your organization’s compliance with the Commodity Exchange Act (the “Act”) and the CFTC regulations discussed herein.

¹ See *In re Schultz*, CFTC No. 20-76 (Sep. 30, 2020) (speaking order), [here](#).

² See *In re Sunoco LP*, CFTC No. 20-75 (Sep. 30, 2020) (speaking order), [here](#).

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Schultz Settlement: CFTC Misappropriation Settlement Refers to Trading on the Basis of “Inside Information”

The CFTC settled charges against former energy trader Marcus Schultz, requiring him to pay a civil monetary penalty of nearly \$670,000 and disgorge nearly \$430,000 of ill-gotten gains. The CFTC found that Schultz “engaged in a fraudulent scheme to *misappropriate* material, nonpublic information . . . belonging to his employer . . . and to deceive [his employer] by entering into fictitious trades at prices that were not bona fide prices.”³ Furthermore, the CFTC described Schultz’s misappropriation of his employer’s material, nonpublic information as the misappropriation of “Inside Information.” Although the employer’s trading activity does constitute inside information, the crux of this settlement is about the misuse or misappropriation of the employer’s information for the employee’s own personal benefit. Importantly, the settlement does not address or otherwise suggest a prohibition on trading in the derivatives markets on the basis of a participant’s own inside information.

Schultz was a natural gas trader who became head of his company’s Southeast/Gulf Coast trading desk. His role as a trader provided him with access to his employer’s futures trading activity such as the prices, quantity, volume, thresholds or limits of impending company trading activity (referred to in the settlement as “Inside Information”). The agreements, policies, and procedures governing his employment created a duty to keep that information confidential. In violation of this duty, the Commission found that Schultz misappropriated his employer’s material, nonpublic information in two ways, as prohibited by Section 6(c)(1) of the Act and CFTC Rule 180.1.

First, Schultz disclosed material, nonpublic information about his company’s trading activity to a broker “under the guise of seeking [the broker’s] assistance in locating a counterparty for [Schultz’s company].”⁴ Instead, Schultz provided the broker with “information about the prices, quantity, volume, thresholds or limits of impending trades by [his employer] in natural gas futures contracts.”⁵ Thereafter, Schultz executed block trades on behalf of his company at non-competitive prices against the broker’s own trading account in order to allow the broker to profit by executing offsetting transactions at competitive prices. The arrangement also involved Schultz executing transactions against two of the broker’s customers at non-competitive prices, so that those customers could earn a profit through executing offsetting transactions.⁶ In all of these instances, Schultz received a share of any profits that the broker or the two market participants realized through their trading on the basis of Schultz’s information. The CFTC found that Schultz’s trades were not executed at bona fide prices, did not maximize the profit for his company, and were not arm’s-length transactions. He thus breached his duty to his company and misappropriated material, nonpublic information for his own personal gain. The CFTC found that Schultz’s “fictitious sales” violated Section 4c(a)(1) and (2) of the Act.

³ *In re Schultz* at 2 (emphasis added).

⁴ *Id.* at 3.

⁵ *Id.* at 2.

⁶ *Id.*

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Second, Schultz provided the broker with confidential information about changes in natural gas storage levels. Schultz’s company analyzed a weekly storage report published by the U.S. Energy Information Administration. Schultz disclosed material, nonpublic related to the analysis of this report, expecting that he would receive a share of any profits the broker realized using this information.

Schultz took a number of affirmative steps to conceal his unlawful actions. He received his shares of the profit through checks issued by investment companies owned by the broker, the brokerage firm, or the trading firm of one of the implicated market participants. Those persons paid Schultz directly or made the checks out to a real estate company owned by one of Schultz’s family members in order to make the payments appear to relate to legitimate investments. Schultz also made false statements to ICE and the CFTC by denying or failing to disclose key aspects of the fraudulent scheme.

Sunoco Settlement: Pursuing Spoofing Remains a Priority

The CFTC settled spoofing charges against Sunoco LP, requiring the company to pay a \$450,000 civil monetary penalty. The penalty was orders of magnitude lower than the recent spoofing penalties imposed on the Bank of Nova Scotia and JPMorgan Chase, perhaps reflecting that the Sunoco charges involved fewer, less severe incidents over a shorter time period. The CFTC found that Sunoco, by and through one of its former traders, engaged in multiple instances of spoofing involving futures contracts, including crude oil, RBOB, and heating oil futures contracts traded on the New York Mercantile Exchange (“NYMEX”).

Sunoco maintains a Refined Products desk staffed by traders who transact in oil and gasoline futures, both for hedging and discretionary purposes. From February 2014 through January 2015, one such trader (“Trader A”) placed bids and offers in Sunoco’s trading account that he intended to cancel before execution. The CFTC found that Trader A’s trading pattern exhibited the hallmarks of spoofing. Trader A would first place an iceberg order with a small visible quantity that he wanted to get filled (a “Genuine Order”). Then, on the opposite side of the market, he would place one or more larger orders—often for 50 or 100 lots—that he intended to cancel before execution (a “Spoof Order”). The CFTC found that generally, “Trader A canceled the Spoof Order(s) shortly after placing them, and often after his Genuine Order(s) were filled.”⁷ Trader A’s conduct violated Section 4c(a)(5)(C) of the Act, for which Sunoco was held liable through Section 2(a)(1)(B) of the Act and CFTC Rule 1.2.

In the speaking order, the CFTC recognized Sunoco’s remediation of the misconduct and its cooperation with the Division of Enforcement’s investigation. Upon becoming aware of Trader A’s misconduct, Sunoco promptly suspended him from trading futures contracts, conducted an internal investigation, and undertook proactive remedial measures to improve its compliance processes. These measures included upgrading Sunoco’s monitoring capabilities to allow for intraday trade

⁷ *In re Sunoco LP* at 2.

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monitoring, as well as enhancing its training program. It appears that these remediation efforts factored into the determination of the civil monetary penalty. The CFTC has recently made clear that it will take remediation into account when assessing corporate compliance programs in connection with enforcement matters.⁸

If you have any questions regarding this client alert, please contact one of the authors, any member of our CFTC team listed below, or the Willkie attorney with whom you regularly work.

⁸ For a discussion of the Division of Enforcement’s guidance on corporate compliance programs in connection with enforcement matters, see Willkie’s summary [here](#).

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Willkie has a dedicated team of attorneys with extensive knowledge and experience in all aspects of the Commodity Exchange Act and the CFTC regulatory regime. We would be pleased to assist on your matters.

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