

CLIENT ALERT

# Fire at Will! The CFTC Continues Aggressive Stance on Misappropriation

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## AUTHORS

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On December 14, 2023, the CFTC issued a speaking order (the “**Order**”) imposing remedial sanctions against Freepoint Commodities LLC (“**Freepoint**”), a commodity merchant that trades physical and derivative oil products, for misappropriation of material non-public information.<sup>1</sup> The CFTC found that between 2012 and 2018, one or more Freepoint traders engaged in physical commodity trades knowingly using material nonpublic information (“**MNPI**”) obtained through fraudulent means from a South American state-owned enterprise (“**SOE A**”). According to the CFTC, by misappropriating MNPI, Freepoint enriched itself by about \$30.5 million. The CFTC ordered Freepoint to pay a total of \$91.5 million, comprised of a \$61 million civil monetary penalty and \$30.5 million in disgorgement.

Earlier this fall, the CFTC’s Division of Enforcement published an advisory explaining that “respondents should no longer assume that no-admit, no-deny resolutions are the default.”<sup>2</sup> Notwithstanding the advisory, Freepoint neither admitted nor denied the CFTC’s findings or conclusions in the Order. The absence of an admission presumably reflects the fact that the Commodity Exchange Act (“**CEA**”) provides parties injured by fraud or manipulation in connection with trading commodity interests a private right of action. The Order highlights a potential sticking point for the CFTC’s efforts to extract admissions in cases alleging fraud or manipulation.

The Order also highlights the CFTC’s continued pursuit of misappropriation cases, where a person knowingly uses misappropriated MNPI related to physical transactions to hedge its physical purchases on U.S. futures exchanges.

<sup>1</sup> Commodity Futures Trading Commission, *Order Instituting Proceedings Pursuant to Section 6(c) and (d) of the Commodity Exchange Act, Making Findings, and Imposing Remedial Sanctions* (December 14, 2023) (the “**Order**”), [available here](#).

<sup>2</sup> Willkie’s summary of the advisory is [available here](#).

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Market participants should take note that alleged problematic conduct was limited to physical commodity transactions with Freepoint using the derivatives markets to hedge certain physical commodity purchases. As a reminder, although the CFTC's regulatory authority is limited to derivatives (e.g., futures contracts and swaps), the agency retains anti-fraud and anti-manipulation authority over the underlying commodities markets. This means that the CFTC may, as was the case in the Order, pursue investigations regarding misappropriation that relate to primarily physical commodity trading.

### How Freepoint Fraudulently Obtained and Used Nonpublic Material Information

Beginning in or around June 2012, Freepoint engaged a consultant who used a portion of his consulting fees to pay bribes to SOE A employees in exchange for sensitive market information.<sup>3</sup> The information the consultant collected included "(1) advance notice of certain of SOE A's oil shipments, including details concerning the quality and quantity of fuel oil being shipped; (2) details of certain of SOE A's negotiations with Freepoint's competitors, including competing bids for cargoes and SOE A's negotiation strategy; and (3) general information regarding SOE A's commercial plans."<sup>4</sup> To avoid detection, the consultant "set up a series of consulting companies to receive the money to be used for bribes and his own fees."<sup>5</sup> To further conceal the fraud, the Freepoint traders:

- Submitted bids for all cargoes, even cargoes they did not want;
- Did not tell their SOE A counterparts that they had access to confidential information;
- Never mentioned the consultant's name to any SOE A employees; and
- Used code words, fake names, private emails, and encrypted messaging applications to communicate.

One or more Freepoint traders knowingly used this MNPI to enter into physical oil transactions with SOE A, purchase fuel oil for delivery in the United States, and hedge some of the fuel oil purchases on the U.S. futures exchanges.<sup>6</sup> Through this scheme, Freepoint made about \$30.5 million in profit between June 2012 and November 2018.<sup>7</sup>

### Violation of the Commodity Exchange Act and CFTC Rules

The Order provides that "[t]rading commodities in interstate [. . .] commerce in knowing possession of material non-public information obtained through corrupt payments and disclosed in breach of a pre-existing duty violates [CEA] Section

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<sup>3</sup> The Order at 2.

<sup>4</sup> *Id.* at 2-3.

<sup>5</sup> *Id.* at 3.

<sup>6</sup> *Id.*

<sup>7</sup> *Id.*

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6(c)(1) and [CFTC] Regulation 180.1(a).”<sup>8</sup> Here, the CFTC alleges that Freepoint violated CEA Section 6(c)(1) and CFTC Regulation 180.1(a)(1)-(3) by virtue of “intentionally or recklessly trading physical oil products in knowing possession of misappropriated and corruptly obtained material non-public information.”<sup>9</sup>

In addition to paying the civil penalty, the Order explained that Freepoint took measures to ensure it does not violate Section 6(c)(1) of the CEA and CFTC Regulation 180.1(a)(1)-(3) in the future. In particular, Freepoint:

1. Hired a third-party consultant to review and assess Freepoint’s anti-bribery and anti-corruption compliance programs;
2. Updated and implemented anti-bribery policies, procedures, and controls and enhanced due diligence procedures for agents of the company;
3. Hired new employees to undergo the updated anti-bribery and due diligence policies, procedures, and controls; and
4. Implemented anti-corruption training for anyone acting on behalf of Freepoint.<sup>10</sup>

Notably, the CFTC may have considered these steps in deciding not to impose a required third-party consultant or monitor in connection with the Order.

### Parallel Matter with the DOJ Fraud Section

Freepoint’s fraudulent behavior also attracted the attention of the Department of Justice (“**DOJ**”). On December 14, 2023, the DOJ’s Fraud Section announced that it entered into a deferred prosecution agreement with Freepoint that deferred “criminal prosecution on a charge of conspiracy to violate the Foreign Corrupt Practices Act.”<sup>11</sup> The CFTC recognizes the criminal penalty and forfeiture Freepoint must pay the DOJ and will allow Freepoint to offset it against the \$61 million civil monetary penalty. Note that in 2019, the CFTC released an enforcement advisory regarding violations of the CEA involving foreign corrupt practices. This policy, which closely mirrors the DOJ’s Foreign Corrupt Practices Act self-disclosure policy, gives parties that self-disclose a presumption of leniency absent aggravating factors.<sup>12</sup>

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<sup>8</sup> *Id.* at 4.

<sup>9</sup> *Id.* at 5.

<sup>10</sup> *Id.* at 7.

<sup>11</sup> Commodity Futures Trading Commission, “CFTC Orders Freepoint Commodities LLC to Pay \$91 million for Fraudulent Scheme to Misappropriate Material Non-Public Information” (December 14, 2023), [available here](#).

<sup>12</sup> Willkie’s summary of the advisory is [available here](#).

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