

**Statement of Chairman Gary Gensler  
Investment of Customer Funds and  
Funds Held in an Account for Foreign  
Futures and Foreign Options  
Transactions**

October 26, 2010

I support today's Commission vote on the proposed rulemaking regarding the investment of customer segregated and secured amount funds. This rulemaking fulfills part of the Dodd-Frank Act's requirement that the Commission remove all reliance on credit ratings from its regulations. In addition, the rule enhances protections regarding where derivatives clearing organizations (DCOs) and futures commission merchants (FCMs) can invest customer funds. The market events of the last two years have underscored the importance of prudent investment standards to ensure the financial integrity of DCOs and FCMs and of maximizing protection of customer funds.

[FR Doc. 2010-27657 Filed 11-2-10; 8:45 am]

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**COMMODITY FUTURES TRADING  
COMMISSION**

**17 CFR Part 180**

**RIN Number 3038-AD27**

**Prohibition of Market Manipulation**

**AGENCY:** Commodity Futures Trading Commission.

**ACTION:** Notice of proposed rulemaking.

**SUMMARY:** The Commodity Futures Trading Commission is proposing rules to implement new anti-manipulation authority in section 753 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. The proposed rules expand and codify the Commission's authority to prohibit manipulation.

**DATES:** Comments must be received on or before January 3, 2011.

**ADDRESSES:** You may submit comments, identified by RIN number AD27, by any of the following methods:

- *Agency Web Site, via its Comments Online process:* Comments may be submitted to: <http://comments.cftc.gov>. Follow the instructions for submitting comments on the Web site.

- *Mail:* David A. Stawick, Secretary of the Commission, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW., Washington, DC 20581.

- *Hand Delivery/Courier:* Same as mail above.

- *Federal eRulemaking Portal:* <http://www.regulations.gov>. Follow the instructions for submitting comments.

All comments must be submitted in English, or if not, accompanied by an English translation. Comments will be posted as received to <http://www.cftc.gov>. You should submit only information that you wish to make available publicly. If you wish the Commission to consider information that is exempt from disclosure under the Freedom of Information Act, a petition for confidential treatment of the exempt information may be submitted according to the established procedures in CFTC Regulation 145.9.<sup>1</sup>

The Commission reserves the right, but shall have no obligation, to review, pre-screen, filter, redact, refuse or remove any or all of your submission from [www.cftc.gov](http://www.cftc.gov) that it may deem to be inappropriate for publication, such as obscene language. All submissions that have been redacted or removed that contain comments on the merits of the rulemaking will be retained in the public comment file and will be considered as required under the Administrative Procedure Act and other applicable laws, and may be accessible under the Freedom of Information Act.

**FOR FURTHER INFORMATION CONTACT:** Robert Pease, Counsel to the Director of Enforcement, 202-418-5863, [rpease@cftc.gov](mailto:rpease@cftc.gov) or Mark D. Higgins, Counsel to the Director of Enforcement, 202-418-5864, [mhiggins@cftc.gov](mailto:mhiggins@cftc.gov), Division of Enforcement, Commodity Futures Trading Commission, Three Lafayette Centre, 1151 21st Street, NW., Washington, DC 20581.

**I. Background**

On July 21, 2010, President Obama signed the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act").<sup>2</sup> Title VII of the Dodd-Frank Act<sup>3</sup> amended the Commodity Exchange Act ("CEA")<sup>4</sup> to establish a comprehensive new regulatory framework for swaps and security-based swaps. The legislation was enacted to reduce risk, increase transparency, and promote market integrity within the financial system by, among other things: (1) Providing for the registration and comprehensive regulation of swap dealers and major swap participants; (2) imposing clearing and trade execution requirements on standardized derivative products; (3)

<sup>1</sup> 17 CFR 145.9.

<sup>2</sup> See Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law 111-203, 124 Stat. 1376 (2010). The text of the Dodd-Frank Act may be accessed at <http://www.cftc.gov/LawRegulation/OTCDERIVATIVES/index.htm>.

<sup>3</sup> Pursuant to Section 701 of the Dodd-Frank Act, Title VII may be cited as the "Wall Street Transparency and Accountability Act of 2010."

<sup>4</sup> 7 U.S.C. 1 *et seq.* (2006).

creating robust recordkeeping and real-time reporting regimes; and (4) enhancing the Commission's rulemaking and enforcement authorities with respect to, among others, all registered entities and intermediaries subject to the Commission's oversight.

In addition, Title VII of the Dodd-Frank Act contains expanded and clarified authority to prohibit manipulative behavior.

Section 753 of the Dodd-Frank Act amends section 6(c) of the CEA to expand the authority of the Commission to prohibit fraudulent and manipulative behavior. New CEA section 6(c)(1), which prohibits the use or employment of any manipulative or deceptive device or contrivance, requires the Commission to promulgate implementing rules within one year of enactment of the Dodd-Frank Act. The Commission also proposes to implement regulations pursuant to section 6(c)(3) of the CEA under its general rulemaking authority in section 8(a)(5) of the CEA.<sup>5</sup>

Accordingly, the Commission is proposing rules to address manipulative behavior. The Commission requests comment on all aspects of the proposed rules, as well as comment on the specific provisions and issues highlighted in the discussion below.

**II. Manipulation Under Section 753**

*A. Section 753's Amendments to the CEA*

Section 753 of the Dodd-Frank Act gives the Commission enhanced "anti-manipulation authority" as part of its expanded enforcement powers. It does so by amending section 6(c) of the CEA in a number of respects.

First, section 753 adds a new subsection (c)(1). Subsection (c)(1) broadly prohibits fraud-based manipulative schemes as follows:

It shall be unlawful for any person, directly or indirectly, to use or employ, or attempt to use or employ, in connection with any swap, or a contract of sale of any commodity in interstate commerce, or for future delivery on or subject to the rules of any registered entity, any manipulative or deceptive device or contrivance, in contravention of such rules and regulations as the Commission shall promulgate by not later than 1 year after the date of enactment of the Dodd-Frank Act, provided no rule or regulation promulgated by the Commission shall require any person to disclose to another person nonpublic information that may be material to the market price, rate, or level of the commodity transaction, except as necessary to make any statement made to the other person in or in connection with the transaction not misleading in any material respect.

<sup>5</sup> 7 U.S.C. 12a(5).

In addition, section 753 adds subsections (c)(1)(A), (B), and (C). Subsection (c)(1)(A) is a “Special Provision for Manipulation by False Reporting.” This subsection provides that:

Unlawful manipulation for purposes of this paragraph shall include, but not be limited to, delivering, or causing 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.

Section 6(c)(1)(C) provides that “Good Faith Mistakes” in the transmission of “false or misleading or inaccurate information to a price reporting service would not be sufficient to violate subsection (c)(1)(A).”

Subsection (c)(1)(B), captioned: “Effect on Other Law,” provides that nothing in Dodd-Frank shall affect, or be construed to affect, the applicability of CEA section 9(a)(2). Section 9(a)(2) is a provision in the CEA prohibiting, among other things, market manipulation and false reporting.<sup>6</sup>

Dodd-Frank Act section 753 also adds a new CEA section 6(c)(2), which is a “Prohibition Regarding False Information.” A prohibition regarding false information was previously in section 6(c) of the CEA,<sup>7</sup> but Dodd-Frank Act section 753 revises it to include not only false statements made in registration applications or reports filed with the Commission but now also any statement of material fact made to the Commission in any context. New section 6(c)(2) reads as follows:

It shall be unlawful for any person to make any false or misleading statement of a material fact to the Commission, including in any registration application or any report filed with the Commission under this Act, or

<sup>6</sup> 7 U.S.C. 13(a)(2) states that it shall be a felony punishable by a fine of not more than \$1,000,000 or imprisonment for not more than 10 years, or both, together with the costs of prosecution, for [a]ny person to manipulate or attempt to manipulate the price of any commodity in interstate commerce, or for future delivery on or subject to the rules of any registered entity, or to corner or attempt to corner any such commodity or knowingly to deliver or cause to be delivered for transmission through the mails or interstate commerce by telegraph, telephone, wireless, or other means of communication false or misleading or knowingly inaccurate reports concerning crop or market information or conditions that affect or tend to affect the price of any commodity in interstate commerce, or knowingly to violate the provisions of section 4, section 4b, subsections (a) through (e) of subsection 4c, section 4h, section 4o(1) or section 19.

<sup>7</sup> 7 U.S.C. 9, 15; *see also* Section 9(a) of the CEA, 7 U.S.C. 13(a)(2).

any other information relating to a swap, or a contract of sale of a commodity, in interstate commerce, or for future delivery on or subject to the rules of any registered entity, 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.

Finally, section 753 creates a new CEA section 6(c)(3), entitled “other manipulation.”<sup>8</sup> This provision provides that “[i]n addition to” the prohibition in section 6(c)(1):

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.

#### *B. Overview of the Commission's Proposed Rules Under Section 753*

The Commission proposes two rules under section 753. The first rule would be promulgated pursuant to new CEA section 6(c)(1), under which rulemaking is mandatory and must be completed within one year after the date of enactment of the Dodd-Frank Act (July 21, 2010). The second rule would be promulgated pursuant to new section 6(c)(3), and is proposed pursuant to the Commission's general rulemaking authority under section 8(a)(5) of the CEA.

The remaining provisions of section 753, including provisions prohibiting false reporting and information, are self-actuating; no rulemakings are needed to implement them. These new provisions will be automatically effective one year from the date of enactment of the Dodd-Frank Act. The Commission's authority under CEA section 9(a)(2) is not affected by new sections 6(c)(1) or (3).

#### 1. Section 6(c)(1)

The text of CEA section (c)(1) is patterned after section 10(b) of the Securities Exchange Act of 1934 (“Exchange Act”).<sup>9</sup> Exchange Act section 10(b) has been interpreted as a broad, “catch-all” prohibition on fraud and manipulation.<sup>10</sup> Likewise, the Commission proposes to interpret CEA section 6(c)(1) as a broad, catch-all provision reaching fraud in all its forms—that is, intentional or reckless conduct that deceives or defrauds market participants. Subsection (c)(1) is

<sup>8</sup> While this is a new statutory provision, the conduct prohibited is generally prohibited by CEA section 9(a)(2).

<sup>9</sup> 15 U.S.C. 78j(b).

<sup>10</sup> *Chiarella v. United States*, 445 U.S. 222, 226 (1980) (“Section 10(b) was designed as a catch-all clause to prevent fraudulent practices”).

also similar to the anti-manipulation authority granted to the Federal Energy Regulatory Commission (“FERC”) in sections 315 and 1283 of the Energy Policy Act of 2005, amending the Natural Gas Act and the Federal Power Act, respectively,<sup>11</sup> and the Federal Trade Commission (“FTC”) in sections 811 and 812 of the Energy Independence and Security Act of 2007.<sup>12</sup>

The SEC promulgated Rule 10b-5 to implement section 10(b) of the Exchange Act.<sup>13</sup> The FERC and the FTC have promulgated rules based on SEC Rule 10b-5 to implement their respective statutory anti-manipulation authority, but have modified SEC Rule 10b-5 as appropriate to reflect their distinct regulatory missions and responsibilities.<sup>14</sup>

Guided by section 6(c)(1)'s similarity to Exchange Act section 10(b), the Commission proposes an implementing rule that is also modeled on SEC Rule 10b-5, with modification to reflect the CFTC's distinct regulatory mission and responsibilities.

#### 2. Section 6(c)(3)

Before enactment of the Dodd-Frank Act, the Commission charged manipulation and attempted manipulation under CEA sections 6(c), 6(d), and 9(a)(2).<sup>15</sup> In Dodd-Frank, Congress provided a direct statutory prohibition on manipulation of prices of swaps, futures contracts, and commodities. The Commission proposes a rule under its general rulemaking authority, section 8(a)(5) of the CEA that mirrors the text of new CEA section 6(c)(3). The Commission proposes to continue interpreting the prohibition on price manipulation and attempted price manipulation to encompass every effort to improperly influence the price of a swap, commodity, or commodity futures contract.

#### *C. The Proposed Rule Under CEA Section 6(c)(1)*

Pursuant to section 6(c)(1) of the CEA, as added by section 753(a) of Dodd-Frank, the Commission proposes to add a new Part 180.

<sup>11</sup> Energy Policy Act of 2005, Public Law 109-58, §§ 315, 1283, 119 Stat. 594 (2005) (amending 15 U.S.C. 717c-1; 16 U.S.C. 824v).

<sup>12</sup> Energy Independence and Security Act of 2007, Public Law 110-140, §§ 811, 812, 121 Stat. 1492 (2007) (amending 42 U.S.C. 17301, 17302).

<sup>13</sup> 17 CFR 240.10b-5.

<sup>14</sup> 18 CFR Part 1c (FERC Rules prohibiting energy market manipulation); 16 CFR Part 317 (FTC Rule prohibiting energy market manipulation).

<sup>15</sup> As stated above, the amendments to CEA section 6 do not affect the Commission's authority under section 9(a)(2).

As stated in proposed § 180.1 (as set forth in the regulatory text of this proposed rule), the proposed rule is modeled, in part, on SEC Rule 10b-5, with modification to account for the unique regulatory mission of the CFTC. The discussion below is intended to give notice of how the Commission intends to interpret the elements of the Commission's proposed rule.

### 1. Manipulative or Deceptive Device or Contrivance

One purpose of the Commodity Exchange Act is to "deter and prevent price manipulation or any other disruptions to market integrity."<sup>16</sup> The Commission has historically relied upon multiple provisions of the CEA, including section 9(a)(2) and old section 6(c), to prevent and deter price manipulation of commodities in interstate commerce or for future delivery through administrative and civil enforcement actions.<sup>17</sup> Section 9(a)(2) makes it unlawful for any person "to manipulate or attempt to manipulate the price of any commodity in interstate commerce, or for future delivery \* \* \*" <sup>18</sup> The Dodd-Frank Act preserves this purpose and the Commission's authority to pursue instances of price manipulation and attempted price manipulation by making clear in new section 6(c)(1)(B) that nothing in section 6(c)(1) affects the applicability of section 9(a)(2), and by adding new section 6(c)(3), both of which are classified as anti-manipulation provisions.

The scope of new section 6(c)(1) differs from that of sections 9(a)(2) and 6(c)(3) in that it prohibits the use or employment of "any manipulative or deceptive device or contrivance" in connection with any swap, or a contract of sale of any commodity in interstate commerce, or for future delivery. For example, this provision has been interpreted in the SEC Rule 10b-5 context as prohibiting all practices "that are intended to mislead investors by artificially affecting market activity."<sup>19</sup> Consistent with judicial interpretations of the scope of SEC Rule 10b-5, the Commission proposes that subsection (c)(1) be given a broad, remedial

reading, embracing the use or employment, or attempted use or employment, of any manipulative or deceptive contrivance for the purpose of impairing, obstructing, or defeating the integrity of the markets subject to the jurisdiction of the Commission.<sup>20</sup>

### 2. Scienter

The Commission proposes that, consistent with the Supreme Court's interpretation of Exchange Act section 10(b) and SEC Rule 10b-5, a person must act with "scienter" in order to violate subsection 6(c)(1) of the CEA and the Commission's implementing rule.<sup>21</sup> "Scienter" in this context refers to a mental state embracing intent to deceive, manipulate or defraud, and it includes recklessness.<sup>22</sup> Just as

<sup>20</sup> See, e.g., *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 202-03 (1976) (holding section 10(b) of the Securities Exchange Act of 1934 [15 U.S.C. 78j(b)] and SEC Rule 10b-5 thereunder [17 CFR 240.10b-5], on which section 753(c)(1) and the proposed rule are modeled, contain "catch-all" clauses that prohibit all fraudulent securities trading schemes, whether typical or novel); *SEC v. Zandford*, 535 U.S. 813, 819 (2002) (stating section 10(b) of the Exchange Act, "should be construed not technically and restrictively, but flexibly to effectuate its remedial purposes") (internal citations and quotations omitted); *Superintendent of Ins. of N.Y. v. Bankers Life & Casualty Co.*, 404 U.S. 6, 12 (1971) (noting that section 10(b) of the Exchange Act "must be read flexibly, not technically and restrictively"); *Dennis v. United States*, 384 U.S. 855, 861 (1966) (noting that fraud within the meaning of a statute prohibiting conspiracy to defraud the United States, 18 U.S.C.A. § 371, need not be confined to the common law definition of fraud: Any false statement, misrepresentation or deceit. Instead, fraud "reaches any conspiracy for the purpose of impairing, obstructing or defeating the lawful function of any department of Government") (internal quotations and citations omitted); *United States v. Richter*, 610 F.Supp. 480 (N.D. Ill. 1985), *affirmed*, *United States v. Mangovski*, 785 F.2d 312 (7th Cir. 1986), *affirmed*, *United States v. Konstantinov*, 793 F.2d 1296 (7th Cir. 1986). See also FERC, Prohibition of Energy Market Manipulation, 71 FR 4244, 4253 (Jan. 26, 2006) ("[f]inal rule prohibits the use or employment of any device, scheme, or artifice to defraud. The Commission defines fraud generally, that is, to include any action, transaction, or conspiracy for the purpose of impairing, obstructing or defeating a well-functioning market") (citations omitted).

<sup>21</sup> *Ernst*, 425 U.S. at 192-93 (holding that scienter is required for private actions for damages under Section 10(b) and SEC Rule 10b-5); *Aaron v. SEC*, 446 U.S. 680, 691 (1980) (applying *Ernst* to SEC action for injunctive relief under same provisions, and holding that its rationale "ineluctably leads to the conclusion that scienter is an element of a violation of § 10(b) and SEC Rule 10b-5, regardless of the identity of the plaintiff or the nature of the relief sought"); See also *Drexel Burnham Lambert, Inc. v. CFTC*, 850 F.2d 742, 748 (DC Cir. 1988) (applying same requirement to the general fraud provision in section 4(b) of the CEA, 7 U.S.C. 6(b)).

<sup>22</sup> See, e.g., *Ernst*, 425 U.S. at 193; *Hoffman v. Estabrook & Co.*, 587 F.2d 509, 516-17 (1st Cir. 1978); *Grebel v. FTP Software, Inc.*, 194 F.3d 185 (1st Cir. 1999); *Novak v. Kasaks*, 216 F.3d 300, 308 (2d Cir. 2000); *In re Advanta*, 180 F.3d 525, 535 (3d Cir. 1999); *Ottman v. Hangar*, 353 F.3d 338, 343-44 (4th Cir. 2003); *Nathenson v. Zonagen Inc.*, 267 F.3d 400, 408 (5th Cir. 2001); *In re Comshare, Inc.*

negligent conduct, even gross negligence, will not satisfy the scienter requirement under Exchange Act section 10(b) and SEC Rule 10b-5 (nor under the anti-fraud provision in CEA section 4b),<sup>23</sup> the Commission similarly proposes that only intentional or reckless conduct may violate CEA subsection 6(c)(1) and the Commission's implementing rule. Moreover, the Commission proposes that judicial precedent interpreting and applying Exchange Act section 10(b) and SEC Rule 10b-5 in the context of the securities markets should guide, but not control, application of the scienter standard under subsection 6(c)(1) and the Commission's implementing rule. The Commission believes that sufficient leeway must be given to permit application of the scienter standard under subsection 6(c)(1) and the Commission's implementing rule in a manner that comports with the purposes of the CEA and the functioning of the markets regulated by the CFTC. Therefore, application of the proposed scienter standard under subsection 6(c)(1) and the Commission's implementing rule will be tailored to the facts and circumstances of each case.

### 3. In Connection With

Consistent with Supreme Court precedent interpreting the words "in connection with" in the context of section 10(b) of the Exchange Act and SEC Rule 10b-5, the Commission proposes that "in connection with" under (c)(1) be given the same meaning—that is, where the scheme to defraud and the transactions subject to the jurisdiction of the Commission "coincide."<sup>24</sup> Guided by securities law precedent, the Commission proposes this requirement would be satisfied whenever misstatements or other relevant conduct are made in a manner

*Securities Litig.*, 183 F.3d 543, 550 (6th Cir. 1999); *Sundstrand Corp. v. Sun Chemical Corp.*, 553 F.2d 1033, 1045 (7th Cir. 1977); *Fla. State Bd. of Admin. v. Green Tree Fin. Corp.*, 270 F.3d 645, 654 (8th Cir. 2001); *In Re Silicon Graphics Sec. Litig.*, 183 F.3d 970, 977 (9th Cir. 1999); *Howard v. Everex*, 228 F.3d 1057, 1064 (9th Cir. 2000); *City of Philadelphia v. Fleming Cos.*, 264 F.3d 1245, 1258, 1260 (10th Cir. 2001); *Bryant v. Avarado Brands, Inc.*, 187 F.3d 1271, 1282 (11th Cir. 1999); *Rockies Fund v. SEC*, 428 F.3d 1088, 1093 (DC Cir. 2005).

<sup>23</sup> See, e.g., *Ernst*, 425 U.S. at 214; see also, *Drexel Burnham Lambert, Inc. v. CFTC*, 850 F.2d at 742, 748 (DC Cir. 1988) ("mere negligence, mistake, or inadvertence fails to meet [CEA] section 4b's scienter requirement \* \* \* a degree of intent beyond carelessness or negligence" is necessary to violate CEA section 4b.) (citations omitted).

<sup>24</sup> *SEC v. Zandford*, 535 U.S. at 822 ("It is enough that the scheme to defraud and the sale of securities coincide.").

<sup>16</sup> 7 U.S.C. 5(b) (2006).

<sup>17</sup> In case law, "[t]he Commission has long recognized that the intent to create an artificial price is the *sine qua non* of manipulation." *In re Sumitomo Corporation*, [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,327 at 46,499 (CFTC May 11, 1998), citing *In re Indiana Farm Bureau Cooperative Assoc., Inc.*, [1982-1984 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,796 at 27,282 (CFTC Dec. 17, 1982).

<sup>18</sup> 7 U.S.C. 13(a)(2).

<sup>19</sup> *Santa Fe Industries, Inc. v. Green*, 430 U.S. 462, 494 (1977).

reasonably calculated to influence market participants.<sup>25</sup>

#### 4. Reliance, Loss Causation and Damages

Like precedent under both SEC Rule 10b-5 and CEA section 4b, the Commission proposes that the common law elements of fraud, reliance, loss causation, and damages, are not needed to establish a violation of subsection 6(c)(1) and the Commission's implementing rule in the context of an enforcement action.<sup>26</sup>

Reliance, loss causation and damages are elements of private claims, but not enforcement actions brought by the CFTC or SEC.<sup>27</sup> This is so because the government's duty is to enforce the remedial and preventative terms of the statute in the public interest, and not merely to police those whose plain violations have already caused demonstrable loss or injury.<sup>28</sup> However, reliance, loss causation, and damages may be relevant in any Commission determination of the appropriate penalty or remedy for a violation.

#### 5. Attempt

The Commission's proposed rule under (c)(1) explicitly prohibits attempted fraud. The Commission proposes that an "attempt" here, as elsewhere in the CEA, requires: (1) the requisite intent and (2) an overt act in furtherance of that intent.<sup>29</sup>

#### 6. Materiality

Sections (1)(b) and (2) of the Commission's proposed rule incorporate the concept of materiality. In the securities context, the Supreme Court has rejected the adoption of a bright-line rule to determine materiality.<sup>30</sup> Instead,

<sup>25</sup> See *United States SEC v. Pirate Investor LLC*, 580 F.3d 233, 249 (4th Cir. 2009) citing *SEC v. Rana Research, Inc.*, 8 F.3d 1358, 1362 (9th Cir. 1993) (affirming the Second Circuit's holding in *SEC v. Texas Gulf Sulphur Co.*, 401 F.2d 833, 862 (2d Cir. 1968) that SEC Rule 10b-5 is violated whenever assertions are made in a manner reasonably calculated to influence the investing public).

<sup>26</sup> *Berko v. SEC*, 316 F.2d 137, 143 (2d Cir. 1963) (reliance, loss causation and damages not relevant because "the Commission's duty is to enforce the remedial and preventive terms of the statute in the public interest, and not merely to police those whose plain violations have already caused demonstrable loss or injury"); accord *United States v. Davis*, 226 F.3d 346, 358 (5th Cir. 2000); *United States v. Haddy*, 134 F.3d 542 (3d Cir. 1998); *Slusser v. CFTC*, 210 F.3d 783, 785-87 (7th Cir. 2000).

<sup>27</sup> *Id.*

<sup>28</sup> *Berko*, 316 F.2d at 143.

<sup>29</sup> See, e.g., *In re Hohenberg Bros. Co.*, [1975-1977 Transfer Binder] No. 75-4, Comm. Fut. L. Rep. (CCH) ¶ 20,271 at 21,477. (CFTC Feb. 18, 1977).

<sup>30</sup> *Basic Inc. v. Levinson*, 485 U.S. 224, 236 & n.14 (1988) ("A bright-line rule indeed is easier to follow than a standard that requires the exercise of judgment in the light of all the circumstances. But

the Supreme Court directed lower courts to engage in a "fact-specific inquiry" in assessing materiality in securities cases.<sup>31</sup> The Commission proposes that the determination of whether a fact is "material" be fact and circumstance dependent.<sup>32</sup> The Commission proposes that the standard for materiality should be objective rather than subjective.<sup>33</sup> That is, the test is whether a reasonable person would have considered the fact material. Further, as a general proposition, statements of optimism alone (*i.e.*, "puffery") are not material.<sup>34</sup> Finally, with respect to omissions, the Commission proposes that an omission be considered material if there is a substantial likelihood that the omitted fact would have been viewed by a reasonable person as having significantly altered the total mix of information available.<sup>35</sup>

#### D. The Proposed Rule Under CEA Section 6(c)(3)

The Commission proposes a rule under new CEA section 6(c)(3) that mirrors the statute, making it:

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.

The Commission proposes to continue interpreting the prohibition on price manipulation and attempted price manipulation to encompass every effort to influence the price of a swap, commodity, or commodity futures contract that is intended to interfere with the legitimate forces of supply and

ease of application alone is not an excuse for ignoring the purposes of the Securities Acts and Congress' policy decisions. Any approach that designates a single fact or occurrence as always determinative of an inherently fact-specific finding such as materiality, must necessarily be overinclusive or underinclusive").

<sup>31</sup> *Id.* at 240. See also *SEC v. Talbot*, 530 F.3d 1085, 1097 (9th Cir. 2008) (quoting *Arrington v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 651 F.2d 615, 619 (9th Cir. 1981) ("Questions of materiality [under the securities laws] \* \* \* involv[e] assessments peculiarly within the province of the trier of fact").

<sup>32</sup> Dodd-Frank section 6(c)(1) makes clear that "no rule or regulation promulgated by the Commission shall require any person to disclose to another person nonpublic information that may be material to the market price, rate, or level of the commodity transaction, except as necessary to make any statement made to the other person in or in connection with the transaction not misleading in any material respect."

<sup>33</sup> *Cf. TSC Indus., Inc. v. Northway, Inc.*, 426 U.S. 438, 445 (1976).

<sup>34</sup> *Cf. Raab v. General Physics Corp.*, 4 F.3d 286, 289-90 (4th Cir. 1993).

<sup>35</sup> *Cf. TSC Indus.*, 426 U.S. at 449; *Basic*, 485 U.S. at 231-32.

demand in the marketplace.<sup>36</sup> The Commission reaffirms this broad reading of the term "manipulation" with respect to new CEA section 6(c)(3), while also recognizing that manipulation cases are fact-intensive and that the law in this area will continue to evolve largely on a case-by-case basis.

Early manipulation cases involving "corners" and "squeezes" produced an analytical framework that has since been applied in a wide variety of other factual situations not involving "market power."<sup>37</sup> That framework requires that the Commission establish: "(1) That the accused had the ability to influence market prices; (2) that they specifically intended to do so; (3) that artificial prices existed; and (4) that the accused caused the artificial prices."<sup>38</sup> The Commission reaffirms this four-part test and, in the section to follow, discusses the element of artificial price.

#### 1. Price Affected by Factors Outside of the Forces of Supply and Demand

The traditional framework for price manipulation has required demonstrating the existence of an "artificial price." In various circumstances, extensive economic analysis may not be necessary to demonstrate that this element has been met. The conclusion that prices were affected by a factor not consistent with normal forces of supply and demand will often follow inescapably from proof of the actions of the alleged manipulator. For example, in one of the landmark manipulation cases,<sup>39</sup> the respondent placed an order well above the price he needed to pay for egg futures so that the closing price would influence the market to place a higher than expected value on futures contracts for November 1968 eggs. The

<sup>36</sup> See *Cargill, Inc. v. Hardin, Secretary of Agriculture*, 452 F.2d 1154, 1163 (8th Cir. 1971) ("The methods and techniques of manipulation are limited only by the ingenuity of man. The aim must be therefore to discover whether conduct has been intentionally engaged in which has resulted in a price that does not reflect basic forces of supply and demand").

<sup>37</sup> See, e.g., *In re DiPlacido*, 2008 WL 4831204 (CFTC 2008), *aff'd in pertinent part*, *DiPlacido v. Commodity Futures Trading Comm'n*, 364 Fed.Appx. 657, 2009 WL 3326624 (2d Cir. 2009), Comm. Fut. L. Rep. ¶ 31,434 (noting evolution of analytical framework and applying it to scheme affecting settlement price); *In re Henner*, 30 Agric. Dec. 1151 (1971) (applying traditional framework *sub silentio* to scheme involving uneconomic behavior); *In re Soybean Futures Litig.*, 892 F. Supp. 1025, 1047 (N.D. Ill. 1995) (While the traditional framework derived from "market power" cases such as corners and squeezes, market power is not a necessary element of manipulation cases.).

<sup>38</sup> *In re Cox*, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,786 at 34,061 (CFTC July 15, 1987).

<sup>39</sup> *In re Henner*, 30 Agric. Dec. 1151.

Commission's predecessor agency sustained the finding of the judicial officer that:

[t]he inference is inescapable that the respondent paid more than he had to \* \* \* for the purpose of causing the closing price to be at that high level. No further proof is needed to show that the settlement price was artificial.<sup>40</sup>

The Commission recently cited this "conclusive presumption" with approval in *In re DiPlacido*.<sup>41</sup> In that case, DiPlacido placed proportionately large orders, in an illiquid market, while ignoring more favorable bids and offers, so that closing prices for electricity futures would be inflated. These actions convinced the Commission and the Second Circuit Court of Appeals that the resulting closing prices were *de facto* illegitimate.<sup>42</sup> Cases of this nature, where distorted prices foreseeably follow from the device employed by the manipulator, do not require detailed economic analysis of the effect on prices.<sup>43</sup> As the Commission explained in *In re Hohenberg Bros.*:<sup>44</sup>

[T]o determine whether an artificial price has occurred one must look at the aggregate forces of supply and demand and search for those factors which are extraneous to the pricing system, are not a legitimate part of the economic pricing system, are not a legitimate part of the economic pricing of the commodity, or are extrinsic to that commodity market. When the aggregate forces of supply and demand bearing on a particular market are all legitimate, it follows that the price will not be artificial. On the other hand, when a price is affected by a factor which is not legitimate, the resulting price is necessarily artificial. Thus, the focus should not be as much on the ultimate price, as on the nature of the factors causing it. (emphasis added).

In keeping with the fact-intensive nature of manipulation cases, the Commission recognizes that economic analysis may in some cases be appropriate to determine whether the conduct in question actually caused an artificial price. The Commission stresses, however, that an illegal effect on price can often be conclusively

presumed from the nature of the conduct in question and other factual circumstances not requiring expert economic analysis.

The Commission also emphasizes, consistent with the weight of existing precedent, that the conduct giving rise to a manipulation charge need not itself be fraudulent or otherwise illegal.<sup>45</sup> The actions of the respondents in *Zenith-Godley*,<sup>46</sup> *Henner*,<sup>47</sup> and *DiPlacido*,<sup>48</sup> for instance, were not intrinsically fraudulent or otherwise illegal apart from violating the CEA, and the manipulation charges were sustained in each of those cases.

## 2. Attempt

The Commission's proposed anti-manipulation rule under (c)(3) explicitly prohibits attempted price manipulation. The Commission proposes that attempt here, as elsewhere in the CEA, requires: (1) The requisite intent and (2) an overt act in furtherance of that intent.<sup>49</sup>

## III. Request for Comment

The Commission requests comment on all aspects of the proposed rules.

## IV. Administrative Compliance

### A. Cost-Benefit Analysis

Section 15(a) of the CEA<sup>50</sup> requires the Commission to consider the costs and benefits of its actions before promulgating a regulation under the CEA. By its terms, section 15(a) does not require the Commission to quantify the costs and benefits of a rule or to determine whether the benefits of the regulation outweigh its costs; rather, it requires that the Commission "consider" the costs and benefits of its actions. Section 15(a) further specifies that the costs and benefits shall be evaluated in light of five broad areas of market and public concern: (1) Protection of market participants and the public; (2) efficiency, competitiveness and financial integrity of futures markets; (3) price discovery; (4) sound risk management practices; and (5) other public interest considerations. The Commission may in its discretion give

greater weight to any one of the five enumerated areas and could in its discretion determine that, notwithstanding its costs, a particular rule is necessary or appropriate to protect the public interest or to effectuate any of the provisions or accomplish any of the purposes of the CEA.

With respect to benefits, the proposed rules would enhance the authority of the Commission to ensure fair and equitable markets. The Commission has determined that market participants and the public will benefit substantially from prevention and deterrence of manipulation. Markets that are free of market manipulation will function better as venues for price discovery and hedging.

With respect to costs, the Commission has determined that participants in the markets should already have mechanisms in place to ensure that their employees and agents will refrain from attempting to manipulate the markets.

The Commission invites public comment on its cost-benefit considerations. Commenters are also invited to submit any data or other information that they may have quantifying or qualifying the costs and benefits of the proposed rules with their comment letters.

### B. Anti-Trust Considerations

Section 15(b) of the CEA, 7 U.S.C. 19(b), requires the Commission to consider the public interests protected by the antitrust laws and to take actions involving the least anti-competitive means of achieving the objectives of the CEA. The Commission believes that the proposed rules will have a positive effect on competition by improving the fairness and efficiency of the markets through reducing the adverse effects of manipulation and disruptive practices.

### C. Paperwork Reduction Act

The provisions of the proposed Commission Regulation [17 CFR Part 180] would not result in new recordkeeping requirements within the meaning of the Paperwork Reduction Act of 1995 ("PRA").

### D. Regulatory Flexibility Act

The Regulatory Flexibility Act ("RFA")<sup>51</sup> requires that agencies consider whether the rules they propose will have a significant economic impact on a substantial number of small entities and, if so, provide a regulatory flexibility analysis respecting the impact.<sup>52</sup> The rules proposed by the

<sup>40</sup> 30 Agric. Dec. 1151, 1194.

<sup>41</sup> *In re DiPlacido*, 2008 WL 4831204 (CFTC 2008), *aff'd in pertinent part*, *DiPlacido v. Commodity Futures Trading Comm'n*, 364 Fed.Appx. 657, 2009 WL 3326624 (2d Cir. 2009), Comm. Fut. L. Rep. ¶ 31,434, *cert. denied*, 130 S. Ct. 1883 (2010).

<sup>42</sup> *Id.*

<sup>43</sup> See, e.g., *In re Eisler and First West Trading, Inc.*, [2003–2004 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 29,664 at 55,837, 2004 WL 77924 (CFTC Jan. 20, 2004) (involving direct falsification of data input to calculation of settlement prices).

<sup>44</sup> [1975–1977 Transfer Binder] No. 75–4, Comm. Fut. L. Rep. (CCH) ¶ 20,271 at 21,477 (emphasis added); see also, *United States v. Reliant Energy Services, Inc.*, 420 F. Supp. 2d 1043 (N.D. Cal. 2006).

<sup>45</sup> See, e.g., *Cargill, Inc. v. Hardin*, 452 F.2d 1154 (8th Cir. 1971); *G.H. Miller & Co. v. United States*, 260 F.2d 286 (7th Cir. 1958).

<sup>46</sup> *In re Zenith-Godley Co., Inc. and John McClay, Jr.*, 6 Agric. Dec. 900 (1947) (extravagant purchases of butter for the purpose of supporting milk prices).

<sup>47</sup> *In re Henner*, 30 Agric. Dec. 1155.

<sup>48</sup> *In re DiPlacido*, 2008 WL 4831204 (CFTC 2008), *aff'd in pertinent part*, *DiPlacido v. Commodity Futures Trading Comm'n*, 364 Fed.Appx. 657, 2009 WL 3326624 (2d Cir. 2009), Comm. Fut. L. Rep. ¶ 31,434.

<sup>49</sup> See, e.g., *In re Hohenberg Bros.*, [1975–1977 Transfer Binder] No. 75–4, Comm. Fut. L. Rep. (CCH) ¶ 20,271 at 21,477.

<sup>50</sup> 7 U.S.C. 19(a).

<sup>51</sup> 5 U.S.C. 601.

<sup>52</sup> *Id.*

Commission will not have a significant economic impact on a substantial number of small entities. As explained above, legitimate market participants should already have procedures in place to prevent their employees and agents from manipulating the markets. Accordingly, the Chairman, on behalf of the Commission, hereby certifies, pursuant to 5 U.S.C. 605(b), that the proposed rules will not have a significant impact on a substantial number of small entities.

#### *E. Congressional Review Act*

The Congressional Review Act establishes certain procedures for major rules, defined as those rules that would result in an annual effect on the economy of \$100 million or more, or have other substantial impacts. These proposed rules are not subject to any of those requirements because they would not have any of these substantial impacts; rather, they should result in significant economic benefits.

#### **List of Subjects in 17 CFR Part 180**

Commodity futures.

For the reasons stated in the preamble, the Commodity Futures Trading Commission proposes to add a new 17 CFR Part 180 as set forth below:

### **PART 180—PROHIBITIONS AGAINST MANIPULATION**

Sec.

180.1 Prohibition against manipulation.

180.2 Other manipulation.

**Authority:** 7 U.S.C. 6c(a), 9, 12(a)(5) and 15, as amended by Title VII of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376 (June 16, 2010); 5 U.S.C. 552 and 552(b), unless otherwise noted.

#### **§ 180.1 Prohibition against manipulation.**

(a) 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 section shall exist where the person mistakenly transmits, in good faith, false or misleading information to a price reporting service.

(b) Nothing in this section shall be construed to require any person to disclose to another person nonpublic information that may be material to the market price, rate, or level of the commodity transaction, except as necessary to make any statement made to the other person in or in connection with the transaction not misleading in any material respect.

(c) Nothing in this section shall affect, or be construed to affect, the applicability of Commodity Exchange Act section 9(a)(2).

#### **§ 180.2 Other manipulation.**

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.

Issued in Washington, DC, on October 26, 2010 by the Commission.

**David A. Stawick,**

*Secretary of the Commission.*

#### **Statement of Chairman Gary Gensler**

##### *Prohibition of Market Manipulation*

October 26, 2010

I support the proposed rulemaking to enhance the Commission's ability to protect against manipulation. Today's rule builds upon important new authorities that Congress granted the Commission to protect market participants in the commodities, futures and swaps markets. Together with the authority granted by Congress to prohibit disruptive trading, this proposed rule gives the Commission the broad new ability to effectively combat fraud and manipulation. The proposed rulemaking promotes fair and efficient markets, for the first time allowing the Commission to protect against fraud-based manipulation. I thank Senator Cantwell for her leadership in bringing this important new authority to the Commission.

[FR Doc. 2010-27541 Filed 11-2-10; 8:45 am]

**BILLING CODE 6351-01-P**

## **DEPARTMENT OF LABOR**

### **Employment and Training Administration**

#### **20 CFR Part 655**

**RIN 1205-AB61**

#### **Wage Methodology for the Temporary Non-Agricultural Employment H-2B Program; Extension of the Comment Period**

**AGENCIES:** Employment and Training Administration.

**ACTION:** Proposed rule; extension of comment period.

**SUMMARY:** On October 5, 2010, the Employment and Training Administration (ETA) issued a Notice of Proposed Rulemaking (NPRM) to amend its regulations governing the certification of the employment of nonimmigrant workers in temporary or seasonal non-agricultural employment and the enforcement of the obligations applicable to employers of such nonimmigrant workers. The proposed rule provided a comment period for the regulatory text through November 4, 2010. The agency has received several requests to extend the comment period and has decided to extend the comment period for an additional 8 days, to November 12, 2010.

**DATES:** The comment period for the notice of proposed rulemaking published October 5, 2010, 75 FR 61578 is extended through November 12, 2010. Interested persons are invited to submit written comments on the proposed rule on or before November 12, 2010.

**ADDRESSES:** You may submit comments, identified by Regulatory Information Number (RIN) 1205-AB61, by any one of the following methods:

- **Federal e-Rulemaking Portal:** <http://www.regulations.gov>. Follow the Web site instructions for submitting comments.

- **Mail:** Please submit all written comments (including disk and CD-ROM submissions) to Thomas Dowd, Administrator, Office of Policy Development and Research, Employment and Training Administration, U.S. Department of Labor, 200 Constitution Avenue, NW., Room N-5641, Washington, DC 20210.

- **Hand Delivery/Courier:** Please submit all comments to Thomas Dowd, Administrator, Office of Policy Development and Research, Employment and Training Administration, U.S. Department of Labor, 200 Constitution Avenue, NW., Room N-5641, Washington, DC 20210.