

Cabinet News and Views

Informed analysis for the financial services industry



CFTC's Enforcement of Fraudulent and Manipulative Pump-and-Dump Scheme in Crypto Commodities



By **Peter Y. Malyshev**
Partner | Financial Services

The Commodity Futures Trading Commission (“CFTC”) has two levels of jurisdiction under the Commodity Exchange Act (“CEA”).

First, there is an exclusive (or regulatory) jurisdiction over “derivatives” on “commodities,” where the CFTC can regulate how, where, by whom and when derivatives trade. Derivatives traditionally include swaps, options and futures on commodities.

In addition, CFTC also has the non-exclusive jurisdiction to prosecute fraud and manipulation relating to a contract of sale of any “commodity” in interstate commerce. This is also referred to as enforcement jurisdiction, which may be concurrent with enforcement or regulatory jurisdiction of other regulators, such as the Securities and Exchange Commission (“SEC”). The CFTC rarely exercises this jurisdiction because it is so immensely broad and is only limited by the subject matter – the fraud and manipulation needs to occur with respect to a “commodity.” Most fungible things that are traded in interstate commerce are recognized as “commodities,” even if they are not specifically defined as such in the [CEA § 1a\(9\)](#). Virtual currencies, such as Bitcoin, ether, verge, dogecoin, and reddcoin, have been recognized as “commodities” by the CFTC and several courts.

On July 14, the U.S. District Court for the Southern District of New York entered a [consent order](#) in *CFTC v. McAfee and Watson* for violations of the CEA and CFTC regulations. McAfee and Watson on several occasions through mass media aggressively “pumped up” the market in specific cryptocurrencies, issuing recommendations to buy without disclosing that they had built up their own inventory of the cryptocurrencies before the commencement of the advertisement campaign. Then, when the price had significantly increased, they “dumped” the crypto, realizing a significant profit.

Even though no derivatives were involved, the CFTC alleged that this scheme constituted a fraud on the market and manipulation of commodity prices in violation of § 6(c)(1), § 6(c)(3) and § 9(a)(2) of the CEA, and § 180.1 and § 180.2 of the CFTC Regulations.

This case is significant as one of very few cases where the CFTC was successfully able to assert its enforcement jurisdiction over commodity transactions, as opposed to its traditional jurisdiction over commodity derivatives. Considering several Congressional proposals ([here](#) and [here](#)) to expand CFTC's exclusive (regulatory) jurisdiction over cash commodity markets in cryptocurrencies, this case demonstrates that the CFTC is ready and able to take on this additional role. To that end, the Chairman of the CFTC has [announced](#) on July 26 the formation of the CFTC Office of Technology Innovation to spearhead its FinTech and digital assets regulatory focus.
