

CFTC Interpretation Addresses Retail Ponzi Schemes

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On December 2, 2011, the Commodity Futures Trading Commission (CFTC or the Commission) issued its interpretation of the meaning of the term "actual delivery" for purposes of Section 742(a) of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the Dodd-Frank Act), and guidance on how the Commission will determine if the actual delivery exception applies to any given retail commodity transaction (the Interpretation).

Section 742(a) of Dodd-Frank Act, which creates new Section 2c(2)(D) of the Commodity Exchange Act (the "CEA"), provides the CFTC with jurisdiction over transactions in commodities that are entered into with or offered to non-eligible contract participants or non-eligible commercial entities on a leveraged or margined basis (retail commodity transactions), and subjects such transactions to both the anti-fraud provisions of Section 4b of the CEA and the on-exchange trading requirement of Section 4a thereof, as if such transactions were futures contracts. Section 742(a) excepts contracts of sale that "[result] in actual delivery within 28 days or such other longer period as the Commission may determine... based upon the typical commercial practice in cash or spot markets for the commodity involved."

Section 742(a) extends to retail transactions in *all* commodities the authority previously granted by Congress to the CFTC with respect to retail foreign currency transactions, following the 2004 decision of the seventh circuit in *CFTC v. Zelener*. In *Zelener*, the court held that retail transactions in foreign currency that were characterized as spot sales in contract documents were not futures contracts (and thus not subject to CFTC jurisdiction) notwithstanding that, in practice, the customers never took delivery of the foreign currency. Having regard to this history, the Interpretation makes clear that the CFTC will look beyond the four corners of contract documents in determining whether retail contracts that purport to provide for delivery of the underlying commodity properly qualify for the actual delivery exception. The Commission will employ a functional approach and examine, without limitation, the ownership, possession, title and physical location of the commodity, both before and after execution of the contract; the nature of the relationship between the buyer, seller and possessor of the commodity purchased or sold; and the manner in which the purchase or sale is recorded and completed.

In connection with release of the Interpretation, the CFTC's Director of Enforcement noted that the CFTC will use the added authority granted to it under the Dodd-Frank Act to prosecute ponzi schemes and other frauds in the retail commodities markets, such as scams by people acting as legitimate providers of investments in precious metals like gold and silver.

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