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CFTC Targets Forex Industry Compliance

Barry R. Temkin, *Mound Cotton Wollan & Greengrass*
Felix Shipkevich

GUEST COLUMN

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On Oct. 18, 2010, the **Commodity Futures Trading Commission** implemented new regulations under the Dodd-Frank Act requiring, among other things, registration of retail foreign exchange dealers. The new rules carve out a new registration category for retail foreign exchange dealers (RFEDs) to be registered with the Commission and become members of the **National Futures Association**. These rules substantially increase the minimum net capital requirements, to $20 million, for those who act as counterparties to retail forex transactions. Smaller firms that could not afford the new net capital requirement have tended to leave the U.S. market. The CFTC has not wasted any time in enforcing the new regulations, and has unleashed a spate of new enforcement actions targeting the forex industry.

Who Has To Register?

The CFTC's new forex regulations apply to off-exchange foreign currency transactions with retail customers and the entities that offer, solicit, provide advice about or operate pools involving these transactions. The CFTC regulations, at 17 C.F.R. Sections 5.3(a)(5)(1) and 5.3(1)(6)(1), require, among other things, registration of certain parties engaging in retail forex business. In accordance with the new regulations, any firm acting as a counterparty to certain retail off-exchange forex transactions is required to register either as a RFED or as a futures commission merchant. Additionally, an individual who solicits orders, customers or customer funds in connection with retail forex transactions at a RFED or FCM is required to register with the CFTC as an introducing broker or associated person, depending on the specific conduct involved.

Recent Enforcement Actions

The CFTC has launched its new forex regulations with a barrage of enforcement actions targeting firms and individuals who allegedly engaged in retail forex transactions without properly registering with the agency.

In January, the CFTC simultaneously filed 13 enforcement actions in U.S. district courts accusing 14 defendants of illegally soliciting orders from non-eligible contract participants in connection with forex transactions without registering with the CFTC. In all but two of the complaints, the CFTC alleges that the defendants offered to take the opposite side of a retail customer's forex transaction without being registered as an RFED. In two other complaints, the defendants allegedly solicited retail customers to place forex trades without being registered as introducing brokers.

In each complaint, the CFTC has moved for a preliminary injunction preventing these defendants from operating without being registered. The CFTC is also seeking civil monetary remedies and remedial ancillary relief, including, but not limited to, trading and registration bans, disgorgement, rescission and interest.

The CFTC's Division of Enforcement recently filed a civil enforcement action against a retail forex firm alleging that the firm, while acting as a de facto RFED, solicited retail forex orders without registering, in violation of CFTC regulations. According to the complaint, the firm held itself out as an electronic communication network broker that provided online forex trading accounts and platforms to customers through its Web site. Customers opened a forex trading account through the Web site by accepting a "public offer agreement," which listed the firm's terms of service, and then completing an online account opening form, the agency alleged. The Division of Enforcement also sued a related firm that it alleged was acting as an unregistered introducing broker and soliciting retail customers who were non-ECPs on behalf of unregistered forex dealers. Another recent enforcement action alleged that the respondent firm told its clients that it was acting as a straight through processing party, yet was nonetheless functioning as a counterparty to its customers.

The Significance Of The Enforcement Actions

Based on the new regulations, firms and individuals conducting retail forex transactions with non-eligible contract participants must be registered with the CFTC. While these cases are in their early stages, it is clear that the CFTC is serious about seeking both monetary and remedial penalties against those firms and individuals that it believes are in violation of the new registration requirements.

Barry Temkin

Barry Temkin is a partner at Mound Cotton Wollan & Greengrass. Felix Shipkevich is the principal of Shipkevich Law Firm. Both are based in New York.

Felix Shipkevich