

UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

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1:52 pm, Jun 09, 2020

In the Matter of:

Aaron Klein,

Respondent.

CFTC Docket No. 12-08

OPINION AND ORDER

Aaron Klein petitions the Commission to modify a February 22, 2012 Order Instituting Proceedings Pursuant to Sections 6(c) and 6(d) of the Commodity Exchange Act, as Amended, Making Findings and Imposing Remedial Sanctions (“2012 Order”). The 2012 Order settled charges that Klein violated Sections 6(c) and 9(a)(3) of the Commodity Exchange Act (“CEA”), 7 U.S.C. §§ 9 and 13(a)(3) (2006), and Commission Regulation 3.10, 17 C.F.R. § 3.10 (2011), as a controlling person of a Commodity Trading Advisor that failed to disclose that Klein was a principal. In the 2012 Order, Klein agreed to never apply for registration with the Commission or claim exemption from registration, or act as a principal, agent, officer, or employee of any person registered, required to be registered, or exempted from registration with the Commission (collectively, the “registration bar”). Klein seeks to modify the 2012 Order to remove the registration bar.

For the reasons below, the Commission finds that Klein has failed to meet the standard for modifying a Commission order, and denies Klein’s petition.

BACKGROUND

From November 2006 through September 2008, Klein acted as an undisclosed controlling person of a Commodity Trading Advisor (“CTA”). *In re Aaron Klein*, CFTC No. 12-08, 2012 WL 601212, at *1 (CFTC Feb. 22, 2012). The CTA had one main client – a pool comprised of Klein’s family and a friend. *Id.* The CTA had trading authority over that client’s managed forex trading accounts. *Id.* Klein exercised general control over the CTA and its day-to-day functions through another principal of the CTA. *Id.* Klein was present at the CTA’s offices for a 2008 audit by the National Futures Association (“NFA”). *Id.* Klein drafted responses to the NFA’s audit questions and instructed the other principal to provide these responses to the NFA. *Id.* The CTA applied for registration with the Commission on November 6, 2006, and did not disclose that Klein was a principal, but instead disclosed the other principal as the sole principal. *Id.* at *2. The registration application was approved in February 2007. *Id.* The CTA sought renewal of its registration with the CFTC in 2008, and again did not disclose that Klein was a principal. *Id.*

The Commission found that in failing to disclose that Klein was a principal, the CTA violated CEA Sections 6(c) and 9(a)(3) and Commission Regulation 3.10 by knowingly omitting a material fact required to be stated in its regulatory filings. *Id.* The Commission held Klein liable for these violations as a controlling person of the CTA pursuant to CEA Section 13(b), 7 U.S.C. § 13(b). *Id.* at *3. Klein consented to and the Commission imposed the registration bar, among other sanctions, in the 2012 Order. *Id.* at *4-5.

In 2013, the Securities and Exchange Commission (“SEC”) adopted so-called “Bad Actor” rules disqualifying certain persons from offerings and sales of securities that are exempt from registration under Rule 506 of SEC Regulation D, 17 C.F.R. § 230.506. Rule 506(d)(1)(iii)

provides, in pertinent part, that securities issuers are barred from Regulation D offerings if the issuer or any of its directors, officers, general partners or managing members are subject to a CFTC order that, at the time of the securities sale, bars them from associating with an entity regulated by the Commission. 17 C.F.R. § 230.506(d)(1)(iii)(A)(1). Although Rule 506(d)(2) does not apply to CFTC orders issued before September 23, 2013, *id.* § 230.506(d)(2)(i), SEC Rule 506(e) requires that a securities issuer subject to such an order provide prospective purchasers with “a description in writing of any matters that would have triggered disqualification” had they occurred on or after September 23, 2013 (the “disclosure requirement”), *id.* § 230.506(e). Because the 2012 Order’s registration bar prohibits Klein from associating with an entity regulated by the Commission, it would have triggered the Rule 506(d) disqualification provision if it had been issued on or after September 23, 2013. Thus, the Rule 506(e) disclosure requirement applies to Klein. Klein seeks the removal of the registration bar from the 2012 Order so that he is no longer subject to the Rule 506(e) disclosure requirement.

DISCUSSION

I. Standard for Modification of a Commission Order

On a motion to modify forward-looking sanctions like a registration ban, the Commission applies the standards applicable in federal court under Federal Rule of Civil Procedure 60(b)(5). *In re ADM Inv’r Servs., Inc.*, CFTC No. SD 97-15, 2000 WL 33675727, at *3 (CFTC Sept. 13, 2000). Rule 60(b)(5) provides that a court “may relieve a party . . . from a final judgment, order or proceeding” where “applying it prospectively is no longer equitable.” Fed. R. Civ. P. 60(b)(5). To apply this standard, the Commission uses the two-part test established by the Supreme Court in *Rufo v. Inmates of Suffolk Cty. Jail*, 502 U.S. 367, 383-84 (1992). *In re Frank H. McGhee*, CFTC No. 83-4, 2013 WL 4499019, at *4 (CFTC Aug. 20, 2013). Under this test, the party seeking modification must first demonstrate that modification is warranted by a

significant change in factual conditions or in the law. *Id.* (citing *Rufo*, 502 U.S. at 384). If the party seeking modification meets this burden, then he must show that the proposed modification is suitably tailored to the changed circumstances. *Id.* (citing *Rufo*, 502 U.S. at 383).

As to the first question, modification of a consent order is appropriate where changed factual conditions make compliance with the order substantially more onerous, the order becomes unworkable because of unforeseen obstacles, or enforcement of the order without modification would be detrimental to the public interest. *Id.* Modification may also be warranted if a change in the law makes legal what the order was designed to prevent. *Id.* at *7 (citing *Rufo*, 502 U.S. at 388). In determining whether the prospective application of a sanction is equitable, the Commission can look at competing considerations. *ADM*, 2000 WL 33675727, at *3. The weight accorded to any particular consideration should depend on the circumstances of the case. *Id.*

Modification is extraordinary relief that is available only if the moving party demonstrates exceptional circumstances. *McGhee*, 2013 WL 4499019, at *4 (citing *Motorola Credit Corp. v. Uzan*, 561 F.3d 123, 126 (2d Cir. 2009)). Relief from a consent order should not be granted simply because “it is no longer convenient to live with the terms.” *Id.* (citing *Rufo*, 502 U.S. at 383). “[T]he interest of the public is paramount,” and in the registration context, a petitioner must “make[] a reliable showing that it no longer poses a substantial risk to the public.” *Id.* at *4-5; *ADM*, 2000 WL 33675727, at *3.

II. Klein’s Request for Modification

Klein’s request is largely based on the SEC’s implementation of the disclosure requirement after settlement was negotiated and the 2012 Order was entered. Klein argues that the implementation of the disclosure requirement constitutes a significant change in factual

conditions because it makes compliance with the 2012 Order “substantially more onerous and unworkable,” and it makes conducting business “unduly and inequitably burdensome.” (Petition at 5-6, 12-13); (Reply at 2, 4, 6-7). More specifically, Klein alleges that the disclosure requirement “has had a marked deleterious effect upon the capital-raising wherewithal of companies with which Mr. Klein is affiliated,” including CloudCheckr, Inc., a company Klein founded and for which he served as COO from 2011 until 2017, and as strategic advisor thereafter. (Petition at 4, 6). Klein cites a single example of the alleged “deleterious effect,” where, according to Klein, a June 2016 private placement with CloudCheckr failed when a potential investor decided not to participate in the private placement because of the disclosure of the 2012 Order. (Petition at 6).

Klein argues that other factors also weigh in favor of modification. He downplays the significance of the 2012 Order charges by stating that “there was no implication of serious wrongdoing,” he “did not misappropriate funds, or commingle the funds of others with his own,” and there were no allegations of poor trading decisions or substantial losses. (Petition at 7-8). Klein describes the CTA’s misrepresentations to the Commission as “simply a failure to disclose Mr. Klein.” (Petition at 8). Klein also asserts that he has fully complied with the 2012 Order and points out that his 6.5 years of full compliance is larger than the 2 years over which the charged conduct spanned. (Petition at 4, 9). Finally, Klein asserts that there is minimal risk that the conduct prohibited by the registration bar will recur because he does not intend to work in the futures and derivatives business or to register with the CFTC, and even if he attempted to register or claim exemption, the CFTC’s procedural safeguards would provide the CFTC with the opportunity to take appropriate measures at that time. (Petition at 9-10).

The Commission does not believe that any of these alleged changes or factors, considered separately or together, justify modification of the Consent Order, because they are not significant factual or legal changes in circumstances.

A. Klein Has Not Demonstrated a Significant Factual Change.

As noted, modification would be appropriate where changed factual conditions make compliance with the 2012 Order substantially more onerous or unworkable. We find that Klein has failed to demonstrate that either the disclosure requirement or any other changed factual conditions has made the 2012 Order substantially more onerous or unworkable such that the 2012 Order should be modified.

1. The Bad Actor Rules

The disclosure requirement does not make the 2012 Order substantially more onerous. It imposes only the marginal burden on Klein's companies to affirmatively inform prospective purchasers of the substance of the 2012 Order – a publicly available document. This is precisely what the SEC intended when it issued the disclosure requirement, it applies to anyone in Klein's position, and we cannot say that the SEC's rule is *per se* inequitable. Nor does the disclosure requirement make it more burdensome for Klein to comply with the 2012 Order's undertakings themselves – to not register or apply for registration with the Commission or claim exemption from registration, or act as a principal, agent, officer, or employee of any person registered, required to be registered, or exempted from registration with the Commission. The Bad Actor rules do not make it more difficult for Klein to refrain from that conduct. For these reasons, we find that the implementation of the disclosure requirement does not make the 2012 Order substantially more onerous.

The disclosure requirement also does not make the 2012 Order unworkable. In *Rufo* the Supreme Court articulated this aspect of the Rule 60(b)(5) standard by reference to cases in which an undertaking could not actually be carried out due to unforeseen obstacles. *See Rufo*, 502 U.S. at 384 (citing *New York State Ass’n for Retarded Children, Inc. v. Carey*, 706 F.2d 956, 969 (2d Cir. 1983) (finding provision requiring State to reduce number of patients at particular facility from 5700 to 250 by transferring patients to facilities with 10-15 bed limitation unworkable because State could not find appropriate housing facilities for transfer patients, and allowing modification to increase bed limitation); and *Philadelphia Welfare Rights Org. v. Shapp*, 602 F.2d 1114, 1120-21 (3d Cir. 1979) (modification allowed where defendants could not find sufficient clients to meet decree target numbers for medical screenings due to circumstances beyond defendants’ control)). Klein’s situation is not analogous. As discussed, Klein can still carry out the 2012 Order’s undertakings as prescribed by the registration bar. For these reasons, we find that the disclosure requirement has not made the 2012 Order unworkable.

2. Other Factors

The remaining factors that Klein sets forth in favor of modification are not changed factual conditions that make compliance with the 2012 Order substantially more onerous, unworkable, or detrimental to the public interest. As to the seriousness of the Commission’s charges against him, while Klein may not regard the charges or violations as serious, his conduct provided sufficient grounds for the Commission to impose the lifetime registration bar in the first place—and Klein agreed to it rather than contest the charges. The passage of time and Klein’s alleged compliance with the 2012 Order are not extraordinary. “Compliance is just what the law expects.” *McGhee*, 2013 WL 4499019, at *5 (quoting *SEC v. Advance Growth Cap. Corp.*, 539 F.2d 649, 652 (7th Cir. 1976)). Moreover, to permit modification based on Klein’s compliance

with the 2012 Order would undermine the efficacy of the registration bar as a tool in furtherance of the public interest. *CFTC v. Kelly*, 736 F. Supp. 2d 801, 804 (S.D.N.Y. 2010). Finally, Klein's stated intent not to work in the futures and derivatives business, even when considered with his record of compliance and the passage of time, is insufficient to deem the prospective application of the registration bar inequitable, because it does not establish that compliance with the registration bar has become substantially more onerous, unworkable, or detrimental to the public interest. *See SEC v. Coldicutt*, 258 F.3d 939, 942 (9th Cir. 2001) (denying petition to terminate injunction prohibiting offering or selling securities where defendant changed professions, complied with injunction for 9 years, and stated she did not intend to re-enter securities industry or seek trading license).

Klein has not demonstrated that the implementation of the Bad Actor rules, or any other change in factual conditions, has made the 2012 Order substantially more onerous or unworkable, or that enforcement of the 2012 Order would be detrimental to the public interest. Accordingly, the Commission finds that modifying the 2012 Order is not warranted by a change in factual conditions.

B. Klein Has Not Demonstrated a Significant Change in the Law.

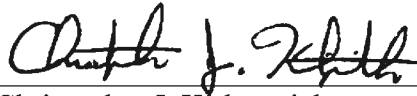
Under the *Rufo* standard, "modification of a consent decree may be warranted when the statutory or decisional law has changed to make legal what the decree was designed to prevent." *Rufo*, 502 U.S. at 388. Although the implementation of the Bad Actor rules is a change in law, it does not make legal what the 2012 Order was designed to prevent. Accordingly, we find that modification of the 2012 Order is not warranted by a change in law.

CONCLUSION

For the foregoing reasons, the Commission finds that Klein has not met the standard for modifying a Commission order, and his Petition to Modify Order is denied.

IT IS SO ORDERED.

By the Commission (Chairman TARBERT and Commissioners QUINTENZ, BEHNAM, STUMP, and BERKOVITZ) (Commissioner BERKOVITZ filed a concurring statement).



Christopher J. Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission

Dated: June 9, 2020

Concurring Statement of Commissioner Dan M. Berkovitz

In re: Aaron Klein

While I concur with the Commission's Opinion and Order denying Aaron Klein's petition to modify his 2012 settlement order ("2012 Order"), I would deny this petition on the grounds that what is in essence a plea for relief from the collateral consequences of a CFTC Order should be directed to the agency that has imposed those collateral consequences. Since Klein is seeking relief from the application of the Securities and Exchange Commission's ("SEC") "bad actor" rules, Klein should direct his petition for relief to the SEC.

Eight years after settling with the CFTC and agreeing never to apply for registration with the Commission or claim exemption from registration, Klein has petitioned the Commission to remove this registration bar. Klein claims that the bar is impeding his ability to raise funds through private securities offerings.

By his own admission, Klein is not seeking modification of the 2012 Order so that he may trade in the commodities markets or otherwise engage in any activities requiring CFTC registration or exemption from registration.¹ Nor is he challenging a sanction imposed by the CFTC relating to a matter over which the Commission has jurisdiction.² Rather, Klein's complaint is with a *collateral* consequence of a CFTC order—a consequence that is imposed directly by the SEC. The SEC's bad actor rules require Klein to disclose the 2012 Order to potential investors prior to a private placement of securities,³ and it is that disclosure obligation that he contends is having an "adverse effect on [his] ability to raise funds for his . . . companies."⁴

The CFTC should not be the forum for relief from collateral consequences that arise from the rules or orders of another federal or state agency; the individual should petition such other agency for relief. This approach ensures that the Commission is deferring to and respecting the authority and expertise of the agency with the direct interest in the relief being sought. It would also promote administrative efficiency and conserve the Commission's limited resources.

Here, the Commission should have denied Klein's petition on the basis that he must seek relief from the SEC. Whether Klein must disclose past conduct prior to offering securities is a decision in the exclusive purview of the SEC. The CFTC does not possess the expertise to determine the appropriate procedures for securities offerings or capital formation, nor does it have any regulatory responsibility over such matters. And the Commission should not agree to

¹ Petition at 10 ("Mr. Klein has no intention [of] seeking registration or otherwise re-entering the futures trading business.")

² Petition at 12 (explain that the circumstances giving rise to Klein's petition are "unrelated to the futures industry").

³ See 17 C.F.R. § 230.506(d).

⁴ Reply at 4.

modify its orders or rewrite history simply because a petitioner wants to escape the collateral consequences of his or her actions.

The Commission has a strong interest in expediency and finality of its settlement orders. Relitigating the terms of settlement orders subsequent to their entry due to the collateral consequences imposed by other agencies in areas outside the CFTC's jurisdiction compromises these interests.⁵ It needlessly ties up valuable Commission resources, hinders the Commission's interest in the finality of its enforcement actions, and potentially interferes with the ability of other federal and state regulators to protect the integrity of the markets under their jurisdiction.

It is not for the CFTC to decide which disclosure obligations apply to securities markets participants. Nor is it appropriate for the CFTC to determine which persons should be disqualified from certain securities offerings.⁶ These matters should be directed to the SEC.

⁵ *Cf. Miller v. SEC*, 998 F.2d 62, 65 (2d Cir. 1993) (denying a petition to vacate a six-year-old administrative order, the Second Circuit explained that “[i]f sanctioned parties easily are able to reopen consent decrees years later, [agencies] would have little incentive to enter into such agreements”).

⁶ *See* Dissenting Statement of Commissioner Dan M. Berkovitz: In re Tower Research Capital LLC: Waiver of SEC “Bad Actor” Disqualifications (Nov. 7, 2019), available at <https://www.cftc.gov/PressRoom/SpeechesTestimony/berkovitzstatement110719>.