

Monthly Futures Exchange Issuance Report - January 2015

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January's Highlight The exchanges are starting off 2015 with a continued focus on investigating and penalizing violations of disruptive trading practices, as well as pre-arranged trading and block trading. These three categories represented a large majority of the exchanges' enforcement efforts in 2014, and from what we saw in January, they will continue to remain a focus going forward. On this note, this month the ICE Futures Exchange will implement an amendment to Rule 4.02, adding section (I) to consolidate rules that prohibit disruptive trading practices. The new text of Rule 4.02(I) reads as follows: *In connection with the placement of any order or execution of any Transaction, it shall be a violation of the Rules for any Person to: (I) Engage in any other manipulative or disruptive trading practices prohibited by the Act or by the Commission pursuant to Commission regulation, including, but not limited to:*

(1) Entering an order or market message, or cause an order or market message to be entered, with:

(A) The intent to cancel the order before execution, or modify the order to avoid execution;

(B) The intent to overload, delay, or disrupt the systems of the Exchange or other market participants;

(C) The intent to disrupt the orderly conduct of trading, the fair execution of transactions or mislead other market participants, or

(D) Reckless disregard for the adverse impact of the order or market message.

(2) Knowingly entering any bid or offer for the purpose of making a market price which does not reflect the true state of the market, or knowingly entering, or causing to be entered, bids or offers other than in good faith for the purpose of executing bona fide Transactions.

The new rule is effective as of January 14, 2015. The FAQ on the new Rule 4.02(I) can be found here:

https://www.theice.com/publicdocs/futures_us/Futures_US_Disruptive_Practice_FAQ.pdf

Rule Changes CME Group- Rule 853- Transfer of Trades and Customer Accounts Pending all relevant regulatory review, effective February 4, 2015, all CME Group Exchanges will adopt a revision to Rule 853- Transfer of Trades and Customer Accounts. The revision will remove the requirement that a transfer of trades approved pursuant to the provisions of Rule 853.A.2 require that one or more entities becomes the successor in interest to one or more other entities. The revision is intended to address circumstances where an entity is exiting the trading of futures and options on futures, but is not going out of business. **CME Group- Rule**

562- Position Limit Violations Pending all relevant regulatory review, effective Feb 6, 2015, all CME Exchanges will adopt a revision to Rule 562-Position Limit Violations. The revisions will clarify that positions established intraday which exceed a position limit constitute a violation and eliminate the provision that making a bid or offer that, if accepted, would cause a person to exceed a position limit constitutes a violation. **CME Group- Rule 561-Daily Submission of Large Trader, Ownership/Control Reports, and Open Interest** Rule 561 is being amended to conform the requirements for Forms 102A and 102B to the requirements of the CFTC's OCR rule. The requirement to submit the new Form 102A will commence three months after the CFTC effective date for Form 102A, May 11, 2015. The requirement to submit the new Form 102B will commence on the same date as the CFTC effective date for Form 102B, March 11, 2015. The exchange acknowledges that certain members of the Futures Industry Association have requested no-action relief to the CFTC to delay the noted compliance dates currently set forth. The exchange will defer to any no-action relief granted by the CFTC. **Advisory Notices CBOT Rule 526- Block Trades** On January 6, 2015, CME and CBOT issued an advisory notice regarding revisions being made to CBOT Rule 526. Specifically, the revisions, which became effective January 21, 2015, codify the minimum size for swap block trades. The new minimums will be set based on Appendix F to Part 43 of the CFTC Regulations. **CME Rule 534- Wash Trades** CME Group has updated the FAQ section to Rule 534. The Rule itself remains unchanged. **CME Rule 534- Block Trades** Effective January 25, 2015, NYMEX begin allowing block trading in a two new products- Freight Route Liquid Petroleum Gas (Baltic) Futures and Gold Kilo Futures.

Disciplinary Actions ICE FUTURES Virginia Power Energy Marketing Inc. *Position Limits* Violation of Rule 6.20(b)- Position Limits. In two instances, Virginia Power allegedly exceeded the spot month spec position limit for Henry LD1 Fixed Price Futures. \$27,500 fine; cease and desist. **D.E. Shaw & Co** *Position Limits* Violation of Rule 6.20(C)-Position Limits. In one instance, D.E. Shaw established a position in the spot month CME/NYMEX Nat Gas Futures contract while simultaneously holding a position in excess of spot month spec position limits in Henry LD1 Fixed Price Futures. \$20,000 fine; cease and desist. **J&P (China) Capital Management** *Position Limits* Violation of Rule 6.13(A)- Enforcement of Position Limits and 6.19(a)- Position Limits for Cotton No. 2. J&P exceeded the 5,000 lot all months combined position limits for Cotton No. 2. \$15,000 fine; \$255,110 disgorgement; cease and desist. **J.P. Morgan Securities** *Misc.* Violation of Rule 18.05(d)- Open Interest in Energy Contracts. JP Morgan reported inaccurate open interest data which resulted in an overstatement in open interest. \$10,000 fine. **Heat Energy Group, Mercuria Energy, and Eagle Seven** *Pre-Arranged Trades* Violation of Rule 4.02(g)-Trade Practice Violations. Allegedly the three companies acted through a third party broker to coordinate a series of block trades in order to repay a previously sustained loss and unrelated customer error. Heat received a \$15,000 fine and cease and desist. Mercuria received a \$7,500 fine and cease and desist. Eagle Seven received a \$7,500 fine and cease and desist. **CME GROUP J.P Morgan Securities** *Block Trades* Violation of Rule 526- Block Trades & Rule 536- Recordkeeping Requirements and Market Regulation Advisory Notice RA1203-3 Block Trades. Allegedly JPMS reported inaccurate execution times for certain block trades; failed to report certain block trades within the allowable time; failed to maintain order tickets or other records of executed block trades; and, in one instance, reported an inter-commodity spread trade to the Exchange as a block trade when the transaction did not meet the minimum quantity

threshold for inter-commodity spread block trades. \$75,000 fine (CBOT), \$40,000 fine (CME).

J.P. Morgan Securities *Misc.* Violation of Rule 854-Concurrent Long and Short Positions. Allegedly, JPMS overstated open interest as a result of netting down contracts. The overstated open interest resulted from an internal account assignment error that placed futures positions in the wrong subaccount. JPMS overstated open interest at least two other times. \$75,000 (CBOT), \$20,000 fine (CME)

Sunil Arora *Pre-Arranged Trades* Violation of Rule 539.C.- Pre-Execution Communications Regarding Globex Trades. Arora allegedly engaged in pre-execution communications related to orders and subsequently crossed the opposing customer buy and sell orders on Globex without entering a RFQ and RFC. \$60,000 fine; 30 business day suspension.

Bradley Bauman *Disruptive Trading* Violation of Rule 432-General Offenses and Rule 527- Errors and Mishandling of Orders. Bauman allegedly recorded numerous trades opposite other market participants with whom a trade was not affected. Bauman then busted the resulting outrades the following morning, which Bauman then improperly resolved by placing it in his personal account rather than in an error account. \$15,000 fine; 10 business day suspension.

NYMEX Robert Leeds (2) *Spoofing* Violation of Rule 432- General Offenses. Leeds allegedly entered orders on the Globex platform that were not for the purpose of bona fide transactions. The entry and cancellation of the orders by Leeds led to fluctuations in the publicly displayed Indicative Opening Price. \$20,000 fine; 15 business day suspension. Violation of Rule 432- General Offenses. Same actions as above on a different occasion. \$40,000 fine; 15 business day suspension.

Itochu Corp *Lack of Documentation* Violation of Rule 538.H- Documentation. Allegedly Itochu entered into an EFRP transaction that did not contain documentation of the related swap transaction and therefore was not a bona fide EFRP. \$7,500 fine.

COMEX Michael Imperio *Spoofing* Violation of Rule 432- General Offenses. Imperio entered multiple large orders without the intent to trade, which he would subsequently cancel. \$60,000 fine; 4 week suspension.

Kaloti Jewellery International DMCC *Pre-Arranged Trades* Violation of Rule 432-General Offenses & Rule 534- Wash Trades Prohibited. Allegedly, Kaloti's co-CEO and trading desk supervisor entered orders in Gold futures and directed Kaloti traders to trade opposite him between accounts owned by Kaloti. The COMEX Panel found that these wash trades were used to close out Kaloti's position at one of its clearing firms. \$30,000 fine.

Tarek El-Mdaka *Pre-Arranged Trades* Violation of Rule 534- Wash Trades Prohibited. El-Mdaka is the Kaloti co-CEO, noted above, who ordered the improper wash trades. \$10,000 fine; 5 business day suspension.

CBOT Credit Suisse Securities *Misc.* Violation of Rule 432-General Offenses. Allegedly Credit Suisse operated an automated trading system that malfunctioned and caused excessive orders and cancel messages to be entered. Although Credit Suisse became aware of the malfunction, it allowed the system to continue to operate improperly for 90 minutes. After deactivating the system, Credit Suisse notified the Exchange of the issue. \$175,000 fine.

Stephen Gola *Spoofing* Violation of Rule 432-General Offenses. Gola allegedly entered large orders with no intent to trade and for the sole purpose of inducing other market participants to trade against the small orders resting on the other side of the order book. \$65,000 fine; 10 business day suspension.

Jonathan Brims *Spoofing* Violation of Rule 432-General Offenses. Brims allegedly entered large orders with no intent to trade and for the sole purpose of inducing other market participants to trade against the small orders resting on the other side of the order book. \$50,000 fine; 10 business day suspension.

Other Issues to Note:

- On January 20, 2015, the CFTC announced that it had settled charges against Olam International, Ltd. and Olam Americas, Inc. for violating position limits and unlawfully executing noncompetitive trades. According to the CFTC Order settling the charges, Olam International and Olam Americas did not disclose to the CFTC that they were not independently controlled and therefore their orders should have been aggregated for purposes of applicable position limits. Had the positions of Olam International and Olam Americas been aggregated, they would have violated relevant position limits on six different trading days. Further, the companies impermissibly entered into exchange for related physical transactions (EFPs) opposite each other- a prohibited noncompetitive transaction if done between companies that are not independently controlled. The settlement agreement requires the companies to pay a **\$3 million civil penalty** and prohibits them from committing future violations. The full release from the CFTC regarding this settlement can be found here:
<http://www.cftc.gov/PressRoom/PressReleases/pr7104-15>.
- Effective February 3, 2015, ICE Swap Trade LLC will begin using a new Rulebook. The new Rulebook has not yet received all relevant regulatory approvals.

If you have any questions about the information contained in this month's report, or questions about major exchange issuances that occurred in the second half of 2014, please contact: **David Perlman, Michael Brooks, Bob Pease, or Jennifer Lias**.