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CPO/CTA ISSUES
CFTC Finally Issues CPO/CTA Rulemaking on Exemptions

On February 9, 2012 the CFTC issued its final rule amending registration and compliance obligations for CPOs and CTAs. In a rulemaking that is likely to have a significant and broad impact, the amendments to Part 4 of the CFTC's rules: 1) rescind the exemption from registration provided in Rule 4.13(a)(4); 2) rescind relief from the certification requirement for annual reports provided to CPOs offered only to qualified eligible persons ("QEPs") under Rule 4.7(b)(3); 3) modify the criteria for claiming relief under Rule 4.5; 4) require the annual filing of notices claiming exemptive relief under several sections of the CFTC's rules; and 5) include new risk disclosure requirements for CPOs and CTAs regarding swap transactions.

Additionally, new CPO and CTA reporting requirements under Rule 4.27 will require CPOs and CTAs to file reports regarding their direction of commodity pool assets. These reports must include a description of certain information, such as the amount of assets under manage-

ment, use of leverage, counterparty credit risk exposure, and trading and investment positions for each pool. The new rule will take effect on July 2, 2012.

Finally, the CFTC has proposed—but not yet adopted—to amend Rule 4.12(c) such that the CPO of any pool whose units of participation will be offered and sold pursuant to an effective registration statement under the Securities Act of 1933 may claim the relief from the delivery and acknowledgement requirements under Rule 4.21, certain periodic financial reporting obligations under Rule 4.22, and the requirement that records be maintained at the CPO's main office under Rule 4.23 with respect to that pool. The proposed amendment seeks to respond to concerns by sponsors of investment companies registered with the SEC, which would also be required to register as CPOs under Rule 4.5, that they may be subject to duplicative, inconsistent, and possibly conflicting, disclosure and reporting requirements.

DODD-FRANK RULEMAKINGS
Whistleblower Rules

On October 24, 2011, the CFTC's whistleblower provisions under the Dodd-Frank Act took effect. New Section 23 of the CEA directs that the CFTC pay awards to whistleblowers who voluntarily provide the CFTC with original information about violations of the commodities laws that lead to a successful enforcement action resulting in monetary sanctions exceeding \$1 million. Awards may range from 10-30% of collected sanctions in an action.

The CFTC's whistleblower provisions provide incentives for both external and internal

reporting of violations of the commodities laws. When originally proposed, the CFTC's whistleblower provisions were criticized for providing awards only when information was given directly to the CFTC. These criticisms were addressed by including incentives for internal reporting in the final rule. Under the final rule, when determining the amount of an award, the CFTC will consider whether an individual utilized internal compliance programs and assisted with the pursuing investigation. Similarly, whistleblowers who report internally

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will be credited with information arising from the resultant internal investigation.

More information about the CFTC's whistleblowing provisions can be found [here](#).

Registration of Foreign Boards of Trade

Under the CFTC's current rules, an FBOT that wants to give U.S. market participants (including FCMs, CPOs and CTAs) direct access to its electronic trading system must first request and receive no-action relief from the CFTC's Division of Market Oversight.

Under the CFTC's new rules, which become effective on Feb. 21, 2012, any FBOT that desires to provide direct market access to U.S. customers will need to apply for an Order of Registration from the CFTC. The eligibility requirements and the CFTC's standards for review of applications under the new rules will be similar to the requirements and

standards used under the current no-action system (and FBOTs that had previously obtained no-action relief face only a limited application process). FBOTs that successfully register will need to maintain certain levels of organization and oversight, and report certain information to the CFTC on a quarterly basis. The CFTC intends the new registration system to result in more standardization and legal certainty, and more transparency among both applicants and the general public.

More information about the CFTC's new registration requirements for FBOTs can be found by clicking [here](#).

Volcker Rule

On January 11, 2012, the CFTC issued its proposed rules regarding the Volcker Rule. The CFTC's proposed rules substantially follow the form of rules proposed jointly by the Federal Reserve, the Office of the Comptroller of the Currency, the FDIC, and the SEC in November 2011.

The Volcker Rule generally prohibits banking entities from engaging in proprietary trading or from acquiring or retaining an ownership interest in, sponsoring, or having certain relationships with a hedge fund or private equity fund, subject to certain exemptions. It also provides for nonbank financial companies supervised by the Fed that engage in such activities or have such interests or relationships to be subject to additional capital requirements, quantitative limits or other restrictions.

Under the CFTC's proposed rules, banking entities would be required to establish an internal compliance program designed to ensure compliance with the Volcker Rule and regulations. This program would be overseen by each entity's board of directors and the appropriate federal agency. The proposed rules also would require firms with significant trading operations to report to the appropriate federal agency certain metrics designed to assist the agency and banking entities in

distinguishing prohibited proprietary trading from permitted activities. Certain transactions would be exempt.

The Commissioners approved the proposed rules by a 3-2 vote, with naysaying Republican Commissioners Scott O'Malia and Jill Sommers citing the proposed rules' complexity, enforcement challenges and unintended impact on liquidity in the swaps markets.

Private interests had expressed concern to the CFTC over the scope of the definitions of "hedge fund" and "private equity fund," as well as the ability of funds to raise capital from non-U.S. banks, insurance companies and other investors.

Under the Dodd-Frank Act, the Volcker Rule prohibitions are due to become effective on July 21, 2012. However, the CFTC's release requests comment on whether banking entities will need more time to prepare for and implement those prohibitions.

Public comment extends for 60 days after the February 14, 2012, publication of the CFTC's proposed rules in the Federal Register. Public comment on the rules proposed by the other four federal agencies ended February 13, 2012.

➔ **Fast Fact:** The North American Derivatives Exchange (NADEX) filed a proposal with the CFTC seeking to allow investors to bet on the outcome of the 2012 presidential election and party control of the U.S. House of Representatives and Senate. The CFTC rejected NADEX's plans to begin offering election-related contracts on January 4, 2012, and placed the proposal under a 90 day review period, which will end on April 2, 2012.

Positions Limits – and ISDA and SIFMA’s Subsequent Legal Challenges

The Final Rules

On Oct. 18, 2011, after several years of fits and starts, the CFTC finally adopted new rules implementing speculative position limits for 28 different commodity futures and options contracts. The CFTC’s final rules establish position limits for trading done both during and outside of the spot month. The spot-month limits will generally be set at 25% of the estimated deliverable supply of a particular commodity (with physically deliverable and cash-settled contracts for each commodity counted separately). The non-spot month limits for each contract will be set and reset every two years (based on updated open interest data) at 10% of the open interest for each contract up to 25,000 in open interest, and 2.5% of the open interest for volume in excess of 25,000.

The CFTC will aggregate the following positions for each trader for purposes of determining whether the trader has violated the new position limits: (1) positions in accounts for which the trader has control over trading; (2) positions held by the trader and others if all are acting pursuant to an agreement as though the positions are held by a single trader; (3) positions in accounts in which the trader owns a 10% or more interest; and (4) positions in multiple accounts or pools using identical trading strategies.

The new rules incorporate a bona fide hedging exemption similar to the exemption that existed prior to the Dodd-Frank Act, and establish a reporting requirement for traders relying on the exemption who exceed the position limits.

The compliance date for all spot-month limits and the non-spot-month limits for Legacy Referenced Contracts is 60 days after the term “swap” is defined by the CFTC. However, the non-spot-month levels for Legacy Referenced Contracts will be effective 60 days after publication of the CFTC’s position limit rules, and persons that hold positions in these contracts will be subject to the CFTC’s existing position limit rules.

For non-spot-month positions in non-Legacy Referenced Contracts, the compliance date will be established by CFTC order after the CFTC has received swap position data for 12 months. Subsequent non-spot-month limits for non-Legacy Referenced Contracts will be updated and published every two years, commencing two years after the CFTC’s initial determination. These position limits will be based on the higher of the most recent 12-month or 24-month average aggregate open interest.

More information about the CFTC’s new position limit rules can be found by clicking [here](#).

ISDA and SIFMA Challenge Rules

On December 2, 2011, ISDA and SIFMA filed challenges to the CFTC’s final rules in both the federal district and appellate courts in Washington, D.C. (The appellate court dismissed ISDA and SIFMA’s petition for lack of jurisdiction on January 20, 2012, stating that the rule must first be challenged in the district court.) ISDA and SIFMA raise several objections to the propriety of the CFTC’s rules.

First, they assert that the CFTC failed to find the rules “necessary and appropriate” to prevent excessive speculation, as is required under the CEA.

Second, ISDA and SIFMA allege that the CFTC was mistaken in believing it was required by law to adopt position limits. Rather, they argue that the CEA directed the CFTC to exercise its discretion in determining whether position limits were appropriate.

Third, ISDA and SIFMA assert that the CFTC failed to conduct the cost-benefit analysis required by the CEA before new rules are issued. In particular, they claim that the CFTC did not consider the adverse effects the rules would have on markets and consumers.

Fourth, they allege that the CFTC failed to articulate a rational connection between the facts it found and its decisions to set position limits at the levels it did, to not exempt traders from the aggregation rules in certain instances, and to restrict legitimate hedging activity.

Finally, ISDA and SIFMA argue that the CFTC did not give interested persons a sufficient opportunity to participate in the rulemaking because it did not fairly inform the public of the empirical data and reasoning on which it planned to rely. ISDA and SIFMA seek to have the CFTC’s position limits rules declared unlawful and vacated.

On December 12, 2011, ISDA and SIFMA also filed a motion with the CFTC seeking a stay of the effective date of the rules pending a resolution of their legal challenges. The CFTC denied this motion on January 3, 2012. Thus, the CFTC’s position limits rules will proceed toward their effective compliance dates absent a decision to the contrary from the district court.

SWAPS

Swaps Rulemaking Continues

The CFTC and the SEC continue to create a regulatory framework for the OTC swaps markets.

After the CFMA prohibited the CFTC and SEC from regulating the OTC swaps markets, Dodd-Frank reversed course. Dodd-Frank now requires the SEC to oversee all security-based swaps (generally, swaps based on a single security or loan, a narrow-based group or index of securities, or events relating to a single issuer or issuers of securities in a narrow-based security index), while the CFTC oversees all other swaps (such as energy and agricultural swaps). The two agencies share authority over mixed swaps. Dodd-Frank requires the agencies to coordinate rulemaking efforts. Below is a summary of recent rulemaking efforts.

Registration of Swap Dealers and Major Swap Participants

The CFTC adopted [final rules](#) regarding registration of swap dealers and major swap participants on January 19, 2012. The final rules establish a registration process, including requiring swap dealers and major swap participants to become members of the NFA. The rules also prohibit swap dealers and major swap participants from permitting associated persons subject to a statutory disqualification to effectuate swaps transactions, with limited exceptions. These final rules become effective March 19, 2012, although registration will not be mandatory until after other Dodd-Frank rules have been finalized.

The SEC issued [proposed rules](#) on October 12, 2011 that would require security-based swap dealers and major security-based swap participants to register with the agency through new Form SBSE, similar to the Form BD used by broker-dealers. Participants registered with the CFTC or registered as broker-dealers would be eligible to submit shorter forms. Registrants would be required to update forms promptly, certify financial, operational and compliance capabilities, and retain certain information regarding their associated persons. Foreign registrants would be required to identify a U.S.-based agent for service of process, and submit a legal opinion that the registrant may permit access to books, records and on-site inspections by the SEC.

Real-Time Public Reporting of Swap Transaction and Pricing Data

On January 9, 2012, the CFTC adopted [final rules](#) regarding public reporting of swaps data. Dodd-Frank requires the

reporting of swaps data, including price and volume, as soon as technologically possible after execution, while protecting the anonymity of the transaction participants. The final rules establish a means of determining the party to report the transaction, recordkeeping and time-delay requirements, the means and timing of public dissemination by SDRs, and special accommodations for block trades. These final rules become effective March 9, 2012, although reporting will not be mandatory until after other Dodd-Frank rules have been finalized.

Swap Data Recordkeeping and Reporting Requirements

The CFTC adopted [final rules](#) on reporting and recordkeeping on January 13, 2012. The final rules require electronic reporting of swap data to an SDR at the creation and through to termination of the swap, including all primary economic terms, changes to these terms, and valuation data. The entity with the easiest, fastest and cheapest access to the data will be required to handle the reporting. All data for a swap must be reported to a single SDR, which is the SDR receiving the first data report. An SDR must maintain all swap data in a format acceptable to the CFTC, and must transmit all swap data to the CFTC upon request. These final rules become effective March 13, 2012, although reporting will not be mandatory until after other Dodd-Frank rules have been finalized.

Additional Rulemakings

In the first weeks of February 2012, the CFTC adopted final rules on the topics of Business Conduct Standards for Swap Dealers and Major Swap Participants with Counterparties, and Protection of Cleared Swaps Customer Contracts and Collateral; Conforming Amendments to the Commodity Broker Bankruptcy Provisions Regarding Rulemaking.

Additionally, during the first half of 2012, the SEC expects to adopt rules for clearing agencies for security-based swaps, registration and regulation of security-based SDRs, mandatory clearing of security-based swaps, and the end-user exemption to mandatory clearing.

The SEC and CFTC delivered a final report to Congress on a comparative study of swaps regulation in the United States, Asia and Europe on January 31, 2012, and released the report to the public on February 2, 2012.

NFA

NFA Amends Anti-Money Laundering Rules for FCMs and IBs

NFA has amended its anti-money laundering rules for FCMs and IBs ("AML rules"), which became effective on January 3, 2012. The Amendments reflect recent changes to the regulations of the Bank Secrecy Act ("BSA") made by the Financial Crimes Enforcement Network ("FinCEN"), as well as recent advisories issues by FinCEN.

Specifically, the amendments 1) clarify that, under the BSA's confidentiality provisions, FCMs and IBs are prohibited from disclosing any information that would reveal the existence of a

suspicious activity report ("SAR"); 2) provide guidance for sharing SARs and information that would reveal the existence of an SAR with affiliates; 3) specify various record-keeping and timing requirements; and 4) conform NFA's AML rules to BSA requirements concerning the disclosure of foreign financial accounts and the reporting of the international transportation of currency or other financial instruments.

More information, including the full text of the amended AML rules, can be accessed [here](#).

RETAIL COMMODITY TRANSACTIONS

Interpretation of "Actual Delivery"

Congress amended the CEA in 2008 to grant express authority to the CFTC to regulate retail forex transactions. The Dodd-Frank Act amended the CEA again to grant the CFTC regulatory authority over other types of retail commodity transactions. However, the CFTC's regulatory authority over retail commodity transactions does not include a contract of sale that "results in actual delivery [of the commodity] within 28 days."

The CFTC recently published an interpretation of the term "actual delivery" as used in this context. The CFTC's interpretation uses a functional approach and examines how the agreement, contract or transaction is marketed, managed and performed. Relevant factors in this determination include the following:

- ownership, possession, title and physical location of the commodity purchased or sold;
- 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 the Federal Register notice, the CFTC included examples of transactions where actual delivery did and did not occur. The CFTC also invited public comments on whether its interpretation accurately construes the statutory language. Public comment on the rule ended February 13, 2012.

FUTURES COMMISSION MERCHANTS

Investment of Customer Funds

The CFTC's new rule on the investment of customer funds will take effect on February 17, 2012. The new rule tightens restrictions on the use of customer segregated funds by FCMs and DCOs. While less restrictive than the rule originally proposed by the CFTC on November 3, 2010, the final adopted rule imposes additional qualifications on permitted investments and removes certain types of investments from the list of permitted investments.

Notably, under the new rule, FCMs and DCOs can invest no more than 50% of their segregated customer funds in non-

Treasury money market funds. The rule also prohibits investments in foreign sovereign debt without approval by the CFTC and forbids in-house transactions where cash or permitted instruments are exchanged for customer funds. These new restrictions apply equally to customer segregated funds and funds held in an account for foreign futures and foreign options transactions.

More information and a full description of the new rule can be found [here](#).

CFTC Reviews 70 FCMs' Segregation of Customer Funds

In late January, the CFTC released findings of limited reviews of FCMs to assess compliance with requirements to segregate customer funds pursuant to Section 4d of the Commodity Exchange Act. The limited reviews also covered the FCMs' obligation to set aside in secured accounts funds deposited by customers for trading on foreign boards of trade under Section 4(b) of the Act and Part 30 of the Commission's regulations.

The reviews of 70 FCMs found that, as of the review date, each firm maintained assets in Section 4d segregated accounts in excess of the net liquidating equities of each of its customers as required under Section 4d. The reviews further found that, as of the review date, each FCM maintained assets in Part 30 secured accounts in excess of the aggregate margin required on all customers' open futures positions, plus any unrealized gains and less any unrealized losses on the open positions, as required by CFTC Rule 30.7. In addition:

- The FCMs held a total of approximately \$166 billion in segregated accounts, which was approximately \$13 billion (or 9%) in excess of the \$153 billion owed to customers. The FCMs also held approximately \$48 billion in Part 30 secured accounts, which was approximately \$7

billion (or 17%) in excess of the Part 30 secured amount obligation.

- \$137 billion of the total segregated funds of \$166 billion (or 82.5%) and \$42 billion of the total Part 30 secured funds of \$48 billion (or 87.5%) was concentrated in the 14 FCMs reviewed by the CFTC.
- The FCMs posted approximately \$74 billion of segregated funds with Commission-designated derivatives clearing organizations. This represents 45% of the total segregated balance of \$166 billion.
- The FCMs held approximately \$30 billion of Section 4d segregated funds (or 18% of the total segregated funds of \$166 billion) with affiliated banks and/or custodian entities.

To determine whether FCMs maintained sufficient assets in segregated accounts to meet their obligations to all futures customers, the CFTC directed the DSIO to conduct limited reviews of 14 of the largest FCMs and to coordinate with the CME and NFA the review of 56 other FCMs carrying customer funds.

CFTC CASES

2011 Enforcement Results

On October 6, 2011, the CFTC released enforcement results for the Fiscal Year 2011. Ninety-nine enforcement actions were filed—55 of these actions related to fraud, 23 related to new regulations under the Dodd-Frank Act requiring foreign exchange dealers and introducing brokers to register with the commission, and the remainder related to manipulation, false reporting and other regulatory matters.

The Enforcement Division obtained orders levying over \$290 million in civil monetary penalties and \$160 million in restitution and disgorgement obligations. Additionally, through cooperation with state and federal law enforcement authorities, convictions were obtained in more than 70 criminal cases related to CFTC enforcement actions.

Newedge USA, LLC to Pay \$700,000 for Inaccurate Large Trader Reports

On January 9, 2012, the CFTC announced a settlement in which Newedge USA ("Newedge"), without admitting or denying any wrongdoing, agreed to pay a \$700,000 civil monetary penalty for submitting inaccurate large trader reports to the CFTC and for violating a February 7, 2011 CFTC order directing Newedge to improve the accuracy and timeliness of its large trader reporting. Newedge is a New York-based FCM and a subsidiary of global financial services company Newedge Group, SA.

Large trader reports are part of the CFTC's market surveillance program used to assess traders' activities and market power and enforce speculative position limits. Traders must report both public data, such as trading volume, open contracts, futures delivery and price, and confidential data, such as aggregate positions and trading activity, for each of their clearing members. According to the CFTC, Newedge's large

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trader reports contained numerous errors, including overstating and understating large trader positions and open interest, misreporting gross positions as net positions, reporting

exchanges of futures for positions that do not exist, and failing to report required positions.

→ **Fast Fact:** The CFTC receives about 600,000 large trader reports each day!

Enforcing Position Limits

The CFTC brought and settled an enforcement action in the third quarter of 2011 charging Merrill Lynch Commodities, Inc. ("MLCI") with violations of existing speculative position limits.

results of ISDA and SIFMA's challenges – with respect to a total of 28 commodities), it can bring an enforcement action for violation of those limits.

According to the CFTC's order, MLCI exceeded the CFTC's position limits for the trading of Cotton No. 2 futures contracts on four consecutive days in January and February 2011 through its trading on the IntercontinentalExchange U.S. MLCI ended each of the days in question with positions between 300 and 1,100 contracts over the applicable limits. The CFTC's order found that the violations were unintentional and resulted from a deficiency in MLCI's position limit monitoring system, yet imposed a civil monetary penalty of \$350,000.

Second, because it is a violation of the CEA to exceed any position limit set by an exchange, the CFTC can bring an enforcement action whenever a market participant trades in excess of an exchange's limits.

The position limit cases brought in the past two years evidence all four ways in which speculative position limits are enforced in the futures industry.

Third, the CEA makes it a felony to willfully violate any provision of the CEA, and thus creates a basis for the U.S. Department of Justice to charge position limit violations as a criminal offense.

First, if the CFTC has set its own speculative position limits (as it has done in the past with respect to several agricultural commodities, and as it has attempted to do – pending the

Finally, the exchanges themselves can bring actions when their members violate exchange position limit rules.

→ **Fast Fact:** Counting this latest enforcement action, the CFTC has now brought five position limit enforcement actions in the past two years (six, counting the criminal indictment issued against Evan Dooley), compared to just three actions in the previous eight years.

CFTC Strong on Supervision

Following a recent trend, the CFTC has continued to initiate and settle enforcement actions charging market participants with failure to supervise, including four such cases since August 2011.

Enskilda—\$150,000 Fine

In the most recent case, the CFTC found that London-based FCM Enskilda Futures Ltd. ("EFL") had accepted and entered matching buy and sell orders on at least 35 occasions, giving the impression that it was engaged in wash or fictitious sales. EFL did not have its own compliance manual, and did not train its employees on the regulatory requirements in the U.S. commodities industry. Based on these deficiencies and the matching orders, the CFTC found that EFL (and its principal) had violated CFTC Rule 166.3. The CFTC imposed a civil monetary penalty of \$150,000.

Velocity—\$180,000 Fine

The CFTC imposed a \$180,000 monetary penalty on a Texas-based FCM, Velocity Futures, LLC ("Velocity"), for failing to develop and implement an adequate system to monitor trading in its customers' accounts. More specifically, the CFTC found that Velocity did not conduct a diligent background check on the principal of a foreign IB, despite knowledge of his possible criminal background. As it turns out, the principal was a fugitive from the Florida Department of Corrections. The CFTC found that after introducing accounts to Velocity, the principal proceeded to churn several of the accounts over a 20-month period – without any intervention from Velocity. The CFTC found that Velocity's lack of procedures for reviewing commission-to-equity ratios, together with the churning, established a Rule 166.3 violation. In agreeing to the settlement, Velocity neither admitted nor denied the CFTC's findings.

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Forex Capital Markets—\$14,200,000 Fine

On a much larger scale, the CFTC imposed a \$14.2 million fine on Forex Capital Markets LLC ("FXCM") in October 2011 for its failure to supervise its own personnel's handling of more than 57,000 customer accounts. In particular, the CFTC found that FXCM's customers had been deprived of the benefit of positive price slippage on their orders over a two-year period to the tune of \$8 million, while being forced to incur losses on negative price slippage. Because FXCM's employees failed to detect the firm's asymmetrical treatment of price slippage, the CFTC found that the firm had violated Rule 166.3. The CFTC also sanctioned the firm for failing to produce promptly certain

records in response to the CFTC's letter request, thereby forcing the CFTC to subpoena the records.

Tenco—\$140,000 Fine

The CFTC settled an enforcement action against a Chicago-based FCM, Tenco, Inc., arising out of Tenco's failure to prevent two of its telephone clerks from exercising trading authority over accounts without written trading authorizations. The CFTC imposed a civil monetary penalty of \$140,000, finding that the respondent had violated both CFTC Rule 166.3 (supervision) and CFTC Rule 166.2 (trading authorization).

CME CASES**Charles Martell**

Charles Martell was fined \$80,000 and barred for 18 months from applying for, owning or holding a membership of any exchange owned or controlled by the CME and access to any CME trading floor or electronic trading and clearing platforms for violation of CME 432.Q (acts detrimental to the exchange) and T (dishonorable or uncommercial conduct).

Pursuant to an offer of settlement in which Martell neither admitted nor denied any rule violation, a panel of the CME BCC found that Martell, a non-member proprietary trader working for a member firm, traded index futures including E-mini NASDAQ 100 Index futures contracts over the CME Globex electronic platform using a trading strategy that misled other market participants for the benefit of Martell.

Amarillo Brokerage Company

Amarillo Brokerage Company was fined \$75,000 for violations of CME 534 (wash trades prohibited) and 432.Q (acts detrimental to the exchange).

Pursuant to an offer of settlement in which Amarillo neither admitted nor denied any rule violations, a panel of the CME BCC found that on numerous dates between December 2008 and June 2010, two employees of Amarillo executed 541 transactions totaling 3,750 contracts in the expiring Live Cattle futures contracts where there was common beneficial ownership on both sides of the transactions. According to the findings, the opposing buy and sell orders were placed with the knowledge and intent that the orders would match opposite one another, and that Amarillo's purpose in doing

so was to freshen long futures position dates prior to the commencement of the respective delivery months.

Neil Brookes

Neil Brookes was fined \$50,000 and his trading privileges were suspended for 25 days for violations of NYMEX Rule 432.Q (acts detrimental to the exchange). Pursuant to an offer of settlement in which Brookes neither admitted nor denied any rule violations, a panel of the NYMEX BCC found that Brookes caused a malfunction in an ATS operated by Infinium Capital Management by live-testing an algorithmic strategy he developed.

Centaurus Advisors LLC

Centaurus Advisors LLC was fined \$75,000 for violations of NYMEX Rule 562 (position limits) and 432 (failure to comply with an order of the exchange). Pursuant to an offer of settlement in which Centaurus neither admitted nor denied any rule violations, a panel of the NYMEX BCC found that Centaurus violated an order by the CME Market Regulation Department ordering Centaurus not to increase its aggregate short May 2011 Henry Hub Natural Gas futures position by establishing an aggregate interday peak position exceeding the "do not increase" order by .11%. This was Centaurus' fourth position limit rule violation in a 24 month period and also a violation of a previous BCC order to cease and desist from violating exchange rules.

NFA CASES

Cogito Asset Management Corp.

A panel of the NFA BCC found Cogito Asset Management Corp., Todd Joseph Krejci, and Jacek Sroka violated NFA C.R.2-4 (failing to uphold high standards of commercial honor and just and equitable principles of trade); C.R.2-9(a) (failure to supervise); and C.R.2-29(a)(1) (misleading sales solicitations).

The panel found that that Cogito and Sroka developed and implemented a trading strategy that generated large commissions for Cogito and Sroka, but offered little, if any benefit to Cogito's customers and that Cogito and Sroka failed to supervise the firm's operations. Cogito and Krejci made deficient sales solicitations to customers.

Pursuant to offers of settlement in which Cogito, Krejci and Sroka neither admit nor deny any rule violations, Cogito was permanently barred from NFA membership and from acting as a principal of an NFA Member, a four-year membership bar was placed on Sroka, and a three-year membership bar was placed on Krejci. After the expiration of the membership bar, Sroka will have to pay a fine in the amount of \$35,000 to apply for membership or seek to become a principal and Krejci will have to pay a fine in the amount of \$25,000 to do the same.

ZuluTrade Inc.

ZuluTrade Inc. was fined \$10,000 for failure to maintain required books and records, failure to maintain required capital, and failure to give required notice. ZuluTrade neither admitted nor denied violation of any rule.

Mohr & Moore LLC

Mohr & Moore LLC and William Elmer Moore were ordered to withdraw from NFA membership and associate membership for violations of NFA C.R. 2-39 (soliciting, introducing or managing forex transactions or accounts); 2-36(c) (forex just and equitable principles of trade); 2-41(b) (forex trading advisors—disclosure); and 2-10 (recordkeeping requirements for FCMs/IBs). M&M is permanently barred from membership and Moore is barred for five years, with a fine of \$40,000 if he seeks membership after the bar.

Pursuant to an offer of settlement, a panel of the NFA BCC found that M&M and Moore opened and exercised discretion over 110 customer accounts without providing those customers with a disclosure document, failed to observe high standards of commercial honor and just and equitable principles of trade by entrusting a convicted felon with their customers' investments, and failed to maintain trading records to support performance claims in disclosure documents.

CME

CME Establishes \$100 Million Fund for Farmers and Ranchers

CME group has decided to create a \$100 million fund to protect agricultural customers in cases of brokerage insolvency. Although the fund will not be available to MF Global victims, the fund was created in response to MF Global's collapse and may be a means of restoring market faith and encouraging market participation. The new insurance-backed fund will

reimburse farmers and ranchers using CME contracts up to \$25,000 per account in cases of brokerage insolvency. Cooperative accounts will be eligible for up to \$100,000 in reimbursement. The fund will not cover hedge funds or other individual traders in the futures industry. The fund is expected to start on March 1, 2012.

MF GLOBAL

MF Global Claims Process

In November 2011, James W. Giddens, the court-appointed trustee for the liquidation of MF Global Inc. ("MF Global"), established separate, parallel claims processes for former commodity futures customers and securities customers of MF Global.

Commodity futures customers owed cash or property from one or more commodity futures customer accounts must file separate commodity futures customer claims for each account. Customers who received open commodity positions and/or cash or cash equivalents through court-authorized bulk

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transfers may file commodity futures customer claims if cash or property remains due. The deadline for commodity futures customer claims was January 31, 2012. However, commodity futures customer claims received after January 31, 2012, but on or before June 2, 2012, may be afforded general creditor status.

Securities customers seeking maximum protection under the Securities Investor Protection Act of 1970 ("SIPA") were required to file their claims no later than January 31, 2012.

However, securities customers may file claims until June 2, 2012, but claims filed after January 31, 2012 may not be granted maximum SIPA protection.

General creditor claims must be filed by June 2, 2012.

The Trustee intends to review claims promptly and the Trustee's staff intends to work with claimants throughout the process to ensure a fair determination is made on each claim.

ENFORCEMENT OF SETTLEMENT AGREEMENTS

Judge Rakoff's Influence on Enforcement Actions Spreads to E.D. Wis.

While Judge Jed S. Rakoff's (S.D.N.Y.) proclivity for scrutinizing consent judgments in SEC enforcement actions is well known, it appears his influence is spreading, at least to one other U.S. District Court. Proliferation of Judge Rakoff's approach would affect profoundly the SEC's and respective defendants' ability and willingness to settle future enforcement actions.

The SEC filed a complaint and proposed settlement in U.S. District Court, Eastern District of Wisconsin against Milwaukee-based Koss Corporation and its CEO and former CFO, Michael J. Koss, on October 24, 2011. The underlying malfeasance was an accounting fraud perpetrated by Koss's former Principal Accounting Officer, who previously pleaded guilty in a related criminal matter to embezzling over \$30 million during a five-year period.

Claims against the settling defendants pertain to record-keeping violations and inadequate internal controls. The SEC seeks injunctive relief against both settling defendants, along with reimbursement by Mr. Koss of incentive bonuses over a three-year period.

On December 20, 2011, Judge Rudolph T. Randa requested the SEC provide "written factual predicate" substantiating why the court should find the proposed final judgments to be "fair, reasonable, adequate, and in the public interest." Specifically, Judge Randa found the previously offered consent documents inadequate with respect to both the specificity of the injunctive relief requested (timeframe, oversight, etc.) and the basis for the disgorgement figures for the individual settling defendant. Absent additional information, the court determined that it is incapable of approving the settlements as fair, reasonable, adequate, and in the public interest.

Judge Randa's request is notable as an endorsement of the higher scrutiny Judge Rakoff has applied to SEC settlements in recent years. In November, Judge Rakoff refused to approve a settlement between the SEC and defendant "because [the proposed consent judgment] does not provide the Court with a sufficient evidentiary basis to know whether the requested relief is justified under any of these standards" of fairness, reasonableness, adequacy or public interest. *S.E.C. v. Citigroup Global Mkts, Inc.*, No. 11 Civ. 7387, ___ F.Supp. 2d ___, 2011 WL 5903733, at *4 (S.D.N.Y. Nov. 28, 2011).

Judge Rakoff noted that the proposed consent judgment continued the SEC's longstanding practice of prohibiting the defendant from denying the allegations, while permitting the defendant not to admit the allegations, either. This language often conduces settlement by allowing defendants to sidestep the collateral estoppel effect an admission in the enforcement action would have on an ensuing private action concerning the same subject matter. Nonetheless, Judge Rakoff believes such an equivocal presentation of the defendant's actions precludes him from determining whether the settlement actually is fair, adequate, reasonable and in the public interest.

Judge Rakoff has ordered a trial date of July 16, 2012. Both the SEC and defendant have appealed the ruling, with the SEC seeking to stay the district court proceedings pending appeal.

Judge Randa's request in the *Koss* case does not challenge the SEC's settlement practices as directly as Judge Rakoff has in the *Citigroup* case, but it does cite two of Judge Rakoff's higher-profile opinions in refusing to approve the settlement.

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The question remains to what extent future courts will be compelled scrutinize SEC settlements in the manner of Judge Rakoff, either through an appellate court's endorsement of such scrutiny or simply following his reasoning. Whether Judge Rakoff's approach to SEC settlement will be expanded to CFTC settlements also remains to be seen.

Update: After 17 pages of additional briefing by the SEC, addressing the factual predicate that would allow a determination of the fairness of the settlement, Judge Randa indicated his approval of the settlement as proposed in *SEC v. Koss Corp.*



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