

CLIENT ALERT

The CFTC and The CME Group Impose \$6.55 Million in Penalties on Commodity Trading Firm for Manipulative Schemes in the Agricultural Markets

July 17, 2018

AUTHORS

Athena Eastwood | Paul J. Pantano, Jr. | Neal E. Kumar | Sohair A. Aguirre

On July 12, 2018, the Commodity Futures Trading Commission issued an order accepting the settlement offer of, and imposing sanctions against, Lansing Trade Group, LLC for two separate and distinct manipulative schemes: (1) attempted manipulation of Chicago Board of Trade wheat futures and options on futures; and (2) aiding and abetting attempted manipulation of physical corn prices.¹ The CFTC's wheat manipulation investigation was conducted in conjunction with The CME Group, Inc. CME separately issued a Notice of Disciplinary Action, in which Lansing agreed to pay \$3.15 million (in addition to the CFTC penalty) for attempted manipulation of wheat futures.²

The CFTC found that Lansing purchased and subsequently cancelled (*i.e.*, redeemed) for load-out and delivery certain shipping certificates for wheat, with the intent to signal to the market a false increase in demand and thereby manipulate the price of wheat futures to benefit Lansing's futures spread positions. In a separate scheme, the CFTC found that Lansing worked with a commodity broker to execute two transactions (one to buy and one to resell physical corn) with a grain company at prices below the market price in order to create a downward effect on the price of corn. Unlike the

¹ *In re Lansing Trade Group, LLC*, CFTC Docket No. 18-16, 2018 WL 3387517 (July 12, 2018) ("Order").

² The CME Group, *Notice of Disciplinary Action*, File No. CBOT 15-0160-BC (July 12, 2018).

The CFTC and The CME Group Impose \$6.55 Million in Penalties on Commodity Trading Firm for Manipulative Schemes in the Agricultural Markets

CFTC's findings in the wheat portion of the settlement order, there is no allegation that the two physical corn transactions affected or were intended to benefit either company's OTC or exchange-traded corn derivatives positions.

The CFTC Order imposed a \$3.4 million civil monetary penalty against Lansing, ordered Lansing to undertake remedial measures to bolster its internal anti-manipulation controls, including amending its compliance policies and procedures, supplementing its training program, and adopting measures to deter and detect improper communications, and ordered Lansing to cease and desist from violating Sections 9(a)(2), 6(c)(1), and 6(c)(3) of the Commodity Exchange Act, as well as CFTC Regulations 180.1(a) and 180.2.

Attempted Manipulation of Wheat Futures Contracts

Lansing's scheme to influence the value of its Chicago Board of Trade ("CBOT") wheat spread and options positions began on March 3, 2015, when certain Lansing traders learned that a market participant was planning to register and tender for delivery a large number of shipping certificates with 3 ppm vomitoxin wheat ("Wheat Certificates"). The CFTC found that the market perceived a lack of demand for this below-milling-grade wheat.

According to the CFTC's July 12, 2018, Order, the Lansing traders understood this market perception and thus began a strategy to: (1) increase their long May-July, July-September, and September-December wheat spread positions ("Long Wheat Spread Positions"); (2) increase their May and July wheat call option positions; (3) purchase the Wheat Certificates; and then (4) cancel (*i.e.*, redeem) the Wheat Certificates for load-out and delivery. The CFTC found that Lansing's activities were designed to signal to the market that demand for 3 ppm vomitoxin wheat had increased in order to influence the price of CBOT wheat futures contracts and options on futures contracts, and to increase the value of Lansing's Long Wheat Spread Positions and wheat call option positions.

Recorded telephone communications of the Lansing traders demonstrated that they understood that the market did not expect the Wheat Certificates to be cancelled for load-out and delivery. During a discussion with a CBOT market participant about the impact of the plan on the price curve, one Lansing trader asked about cancelling the shipping certificates: "What do you think it does to the curve [the price of the spread] if it gets cancelled?" The market participant replied: "I think it has big ramifications . . ."

In addition, to maximize the potential impact of cancelling the Wheat Certificates, a Lansing trader communicated with the writer of a market newsletter, who agreed to disseminate information about Lansing's intent to cancel and load-out the Wheat Certificates to the market. In a call with another trader later that day, the Lansing trader described his communication with the newsletter, saying: "Just a really good day man, and just this freaking market is just upside-down right now, and I've gotten so many calls about what in the f**k is going on in Chicago." He continued by saying: "it's just so lopsided, and I got [the newsletter writer], he's gonna give it the gas tonight, and it's gonna be good."

The CFTC and The CME Group Impose \$6.55 Million in Penalties on Commodity Trading Firm for Manipulative Schemes in the Agricultural Markets

The scheme culminated on March 10, 2018, when Lansing cancelled all 250 Wheat Certificates for load-out. The CFTC found that this sent a false or misleading signal to the market that there was demand for the Wheat Certificates, substantially increasing the value of Lansing's wheat spread and option positions.

In its Order, the CFTC concluded that Lansing's scheme demonstrated that it had (1) specific intent to affect the market price of CBOT's Wheat Futures and Wheat Options Contracts, and (2) took overt acts in furtherance of its attempt to manipulate those prices, thereby engaging in acts of attempted manipulation in violation of Sections 9(a)(2), 6(c)(1), and 6(c)(3) of the Commodity Exchange Act ("CEA") and CFTC Regulations 180.1(a) and 180.2.

Although the facts differ significantly, the CFTC's Order echoes allegations it expressed in its 2015 complaint against Kraft Foods Group ("Kraft") for attempted market manipulation.³ In Kraft, the company signaled its intent to take delivery on its futures contracts of \$90 million of wheat for which the CFTC alleged it had neither the intent nor the physical capacity to take delivery. The CFTC alleged that Kraft intended to take delivery in order to mislead the market into believing that Kraft was going to begin fulfilling its commercial needs via futures contracts, rather than via cash purchases (as Kraft routinely had done). According to the complaint, the scheme increased the price of CBOT futures contracts for wheat and decreased the cash price of wheat—the result that Kraft allegedly intended. Following this price change, Kraft took physical delivery of only approximately \$4 million worth of wheat, reselling the certificates of the remaining approximately \$86 million, a fact that the CFTC relied on to argue that Kraft lacked a *bona fide* commercial need for the wheat. In the Lansing Order, the CFTC similarly found that Lansing did not have a commercial need for wheat, but rather, made the decision to cancel the Wheat Certificates in order to send a misleading signal to the market in an attempt to manipulate wheat futures.

Aiding and Abetting Attempted Manipulation of the Cash Price of Corn

In a separate scheme from the attempted CBOT wheat manipulation, Lansing also settled with the CFTC for aiding and abetting an attempt to manipulate the cash price for yellow corn from Columbus, Ohio ("Columbus Corn").

According to the Order, on February 19, 2015, a third-party Commodity Broker ("Broker") contacted a trader at Lansing to request his assistance in helping a grain company ("Grain Company") attempt to lower the cash price for Columbus Corn. The cash price is the price for delivery of the actual cash or spot commodity via customary market channels. This price typically is based on the price of a futures contract plus or minus a basis, which generally reflects the cost of delivery to the market.

The request from the Broker was explicit. In a recorded telephone call, he stated: "So the goal of this whole project for [Grain Company] is, just so you know, and I know that you already know, is they want to drive Columbus basis down."

³ Complaint, *U.S. Commodity Futures Trading Comm'n v. Kraft Foods Group, Inc. and Mondelez Global LLC*, No. 15-2881 (N.D. Ill. Apr. 1, 2015).

The CFTC and The CME Group Impose \$6.55 Million in Penalties on Commodity Trading Firm for Manipulative Schemes in the Agricultural Markets

They want to be more liquid, they want the basis to come down.” In response, the Lansing trader stated: “Well, I like [the trader from Grain Company] and I like [Grain Company] so I don’t want to work against them, that’s for sure.” The Broker replied: “And . . . he speaks most highly of you guys . . . because you’re willing to do stuff like this.”

The Broker then proposed prices to the Lansing trader, stating: “[The Grain Company trader] says he’ll do it at a penny if we can tell the market that we used 9 over Evansville and 8 over Columbus.” After checking in with a co-worker, the Lansing trader replied: “f**k it, let’s do it.”

That same day, Lansing entered into two transactions with the Grain Company at the exact lower prices discussed with the Broker. In one, Lansing sold to the Grain Company 315,000 bushels of yellow corn, FOB Evansville, priced at 3.94, which was comprised of a Futures Price of 3.85 (based on the March 2015 contract) and a Basis of +.09. In the other transaction, Lansing purchased from the Grain Company 315,000 bushels of yellow corn, FOB Columbus, priced at 3.93, which was comprised of a Futures Price of 3.85 (based on the March 2015 contract) and a Basis of +.08.

In its Order, the CFTC noted that Lansing understood that the Broker told Lansing that it was entering into a transaction for Columbus Corn below the market price and that the Broker told Lansing that this transaction with the Grain Company would be used by the Grain Company to spread false or misleading information about the price of Columbus Corn.

Section 13c(a) of the CEA, provides, in relevant part, that any person who commits or willfully aids, abets, counsels, commands, induces, or procures the commission of a violation of the CEA or Regulations, or who acts in combination or concert with any other person in any such violation, may be held responsible for such violation as a principal.⁴

In order to establish liability under Section 13c(a), the CFTC must prove that (1) the CEA was violated; (2) the defendant knew of the wrongdoing underlying the violation; and (3) the defendant intentionally assisted the principal wrongdoers.⁵ Although actual knowledge of the primary wrongdoer’s conduct is required, knowledge of the unlawfulness of that conduct need not be demonstrated.⁶ Knowing assistance may be inferred from the surrounding facts and circumstances.⁷

Accordingly, the CFTC found that Lansing’s conduct satisfied the three requisite elements of the aiding and abetting charge. First, the transaction with the Grain Company was an illegal attempt to manipulate the price of a commodity in interstate commerce. Second, the CFTC found that the Lansing trader knew of the wrongdoing because the Broker directly informed the trader that the price was below market and the purpose of the transaction was to drive the Columbus Corn basis down. Third, by executing the trade at the lower price, Lansing intentionally assisted the Grain Company. The

⁴ 7 U.S.C. § 13c(a) (2012).

⁵ *In re Nikkhah*, CFTC Docket No. 95-13, 2000 WL 622872, at *11 n.28 (May 12, 2000); *see also In re Richardson Sec., Inc.*, CFTC Docket No. 78-10, 1981 WL 26081, at *8 (Jan. 27, 1981).

⁶ *In re Lincolnwood Commodities, Inc.*, CFTC Docket No. 78-48, 1984 WL 48104, at *28 (Jan. 31, 1984).

⁷ *Id.*

The CFTC and The CME Group Impose \$6.55 Million in Penalties on Commodity Trading Firm for Manipulative Schemes in the Agricultural Markets

CFTC therefore concluded that Lansing willfully aided, abetted, counseled, and worked in combination and in concert with others to attempt to manipulate the price of Columbus Corn. It seems likely that the CFTC will also bring an action against the primary violator.

If you have any questions regarding this client alert, please contact the following attorneys or the attorney with whom you regularly work.

Athena Eastwood

202 303 1212

aeastwood@willkie.com

Paul J. Pantano, Jr.

202 303 1211

ppantano@willkie.com

Neal E. Kumar

202 303 1143

nkumar@willkie.com

Sohair A. Aguirre

202 303 1140

saguirre@willkie.com

Copyright © 2018 Willkie Farr & Gallagher LLP.

This alert is provided by Willkie Farr & Gallagher LLP and its affiliates for educational and informational purposes only and is not intended and should not be construed as legal advice. This alert may be considered advertising under applicable state laws.

Willkie Farr & Gallagher LLP is an international law firm with offices in New York, Washington, Houston, Paris, London, Frankfurt, Brussels, Milan and Rome. The firm is headquartered at 787 Seventh Avenue, New York, NY 10019-6099. Our telephone number is (212) 728-8000 and our fax number is (212) 728-8111. Our website is located at www.willkie.com.