Commodity Futures Trading Commission
CEA CASES

NAME: EDWARD A. COX JR. AND GEORGE F. FREY JR.

CITATION: Comm. Fut. L. Rep. (CCH) P23,786; [1986-1987 TRANSFER BINDER]

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[P 23,786] In the Matter of Cox, et al.

Commodity Futures Trading Commission. No. 75-16. July 15, 1987. Opinion and Order in full text.

Previous opinions located at P 22,130; P 21,809; and P 21,767, 1982 -- 1984 Tr. Binder.

Manipulation -- Evidence -- Insufficient Proof. -- The Division of Enforcement failed to sustain a charge of complete manipulation, since the proof was insufficient as to whether the accused had the ability to influence market prices; whether artificial prices existed; and whether the accused caused the artificial prices. Although the Commodity Futures Trading Commission did not necessarily agree with an administrative law judge's holding that the accused had the specific intent to manipulate, the CFTC did not find it necessary to examine the accused's intent at any length, given the failure of proof as to all the other elements of the manipulation charge. The accused lacked the ability to influence market prices because the deliverable supply of wheat was adequate. Also, the closing futures price per bushel was not shown to be artifically high. The price rise was found to be the result of several competing factors on both the long and short sides of the futures market.

See P 10,025, "Liabilities -- Prohibitions" division, Volume 1.

The complaint in this proceeding charges the respondents with attempting to manipulate and manipulating the market price of May wheat futures contracts on the Chicago Board of Trade, in violation of Sections 6(b), 6(c), and 9 of the Commodity Exchange Act ("Act"), 7 U.S.C. §§ 9, 13, and 13b. An Administrative Law Judge ("ALJ") concluded that a violation had occurred and he imposed various sanctions. *In re Cox and Frey,* [1982-1984 Transfer Binder] COMM. FUT. L. REP. (CCH) P 21,767. Respondents have appealed, and the Commission's Division of Enforcement has replied in opposition. After reviewing the record, the appellate pleadings and the judicial and regulatory precedent, we have decided to grant the appeals, reverse the initial decision, and dismiss the complaint.

Statement of Facts

The complaint focuses on respondents' behavior during the last day of trading in an expiring futures contract. The Division of Enforcement does not contend that respondents acted in concert before the last trading day or that respondents manipulated the futures price on any day but the last day. As background for our analysis of the issues raised on appeal, we begin by summarizing the relevant events. The ALJ accurately stated the procedural history of the case in the initial decision and we see no need to repeat that statement here. The Judge also made extensive findings of fact. Unless modified or supplemented below, we adopt his factual findings as our own.

General Background. Cox and Frey are registered floor brokers and members of the Chicago Board of Trade, a designated contract market for wheat under the Act. Wheat futures are traded for five delivery months: July, September, December, March and May. Each futures contract represents 5,000 bushels of wheat. At the relevant time, the terms of the contract limited price fluctuations during one day's trading (including the last trading day) to ten cents per bushel above or below the previous day's settlement price; and federal regulations limited speculators to positions of two million bushels net long or net short in any one wheat futures contract or in all futures combined.

The month of May is a transitional period in the Chicago cash wheat market. The old crop wheat supply is nearly depleted, and the harvest of new crop wheat is imminent. Millers need to have enough old crop wheat to allow their milling operations to continue without interruption. But millers also try to keep their old crop stocks as low as possible. As a result, commercial demand for and cash sales of old crop wheat are normally slight in May. The May futures contract is the last contract that discovers prices of old crop wheat; the July futures contract is the first contract that discovers prices of new crop wheat.

Five months before trading expired, Cox began to establish a long position in the May contract. By January 25, Cox held long May contracts representing 1,995,000 bushels of wheat, one contract less than the speculative limit set by regulation. Cox maintained this position until May 7, the first day on which a long could express his intent to take delivery by stopping delivery notices issued on the May contract. By the opening on May 19, the last trading day, Cox had reduced his futures position by stopping delivery notices on 555,000 bushels of wheat. Cox had no agreements providing for the sale of this wheat to commercial users in the cash market. Nor was he a commercial user of wheat himself. He did, however, have an equal and opposite (*i.e.,* short) position in the July wheat futures contract. Cox began the final day of trading with a long position in the May futures contract of 1,440,000 bushels, or 30 percent of the long open interest.

In April, Frey assumed a long position in the May contract. By May 19, he held long contracts representing 760,000 bushels, or 16 percent of the long open interest. Unlike Cox, however, Frey did not control any cash wheat prior to May 19. If Cox's position and Frey's position are considered together (as the Division of Enforcement says they should be), the respondents began the final day of trading with long positions in the May future totaling 2.2 million bushels, or 46 percent of the long open interest. In the weeks before May 19, May wheat had been trading quietly, in a narrow range, with little price volatility. Its settlement price on May 18 was $ 1.60 3/4 per bushel.

The Final Day of Trading. Before the opening of trading on May 19, exchange officials were sufficiently concerned about the prospect for a disruptive market to deliver verbal messages to the two respondents. The record is unclear as to the exact wording of those messages. Cox was contacted through his clearing broker by the Board of Trade's Business Conduct Committee, and he was requested to make his position available on the futures market during the day's trading. Timing and price were apparently not mentioned, and Cox believes that he complied with the request. Similarly, Frey was contacted by the Business Conduct Committee and was reminded of his open position and the necessity that an orderly market be maintained. Again, the specific terms of this request are not of record. Both respondents were also "reportable traders," *i.e.,* they periodically advised the federal government of their large speculative positions, as required by regulation.

On the final day of trading, the May contract opened at prices of $ 1.61 1/2 to $ 1 62 per bushel. At 10:30 a.m. when the market for May wheat was at $ 1.65 per bushel and July wheat was at $ 1.49 per bushel, Cox and Frey met on the exchange floor, and Cox asked Frey to act as his broker. Cox placed a verbal order with Frey to sell 1,495,000 bushels of May wheat futures at $ 1.70 per bushel or at 20 cents over the July future. It is now clear that this order would not only liquidate Cox's entire long position, but would also establish a short position. At the time, however, Frey did not know whether the execution of this order would close out Cox's position, leave him long, or put him short. Before Cox gave his order to Frey, Cox did not know Frey's position. After placing the order, Cox learned that Frey was long, but Cox did not learn the extent of Frey's long position, nor Frey's price objectives. Cox did state that he "hoped" Frey's position was "quite a bit" long. Frey accepted the non-discretionary order and Cox then left the area.

Frey assertedly based his own pricing goal for the day ("limit up" or $ 1.70 3/4 per bushel) on his appraisal that cash wheat prices at Gulf ports had strengthened, that Chicago wheat prices were low in relation to Kansas City, and on his belief that "every pound" of wheat in Chicago would be needed for delivery on the contract. As a result of Cox's order and the ensuing conversation, one broker, Frey, held in hand long positions totalling 2.2 million bushels. Cox's pricing objectives were virtually identical to Frey's. Respondents maintain that their actions were wholly independent, noting that Cox often relied on Frey's superior skill as a floor broker and that, in the years prior to this incident, Frey had executed more than half of Cox's trades. Nevertheless, in these circumstances, the ALJ held that the separate positions of Cox and Frey were jointly controlled by prior agreement or understanding and should be aggregated, or treated as one, for purposes of this proceeding. The ALJ also concluded that Cox and Frey both "knew" that deliverable supplies of wheat in Chicago were insufficient to cover the obligations of those holding open short interests in the May contract. Respondents dispute these conclusions in their appeal briefs.

After Cox gave Frey his order, he returned to the pit twice to talk to Frey. By 10:41 a.m., Frey had not yet sold any of the contracts, because the market had not yet reached the price specified by Cox, nor that at which he was willing to sell his own contracts. Respondents' combined holdings were 61 percent of the long open interest.

At 11:31 a.m. Frey still held in hand long positions of more than 2.1 million bushels, which at that time constituted 97 percent of the long open interest. The bulk of the positions held by Frey were liquidated during the last ten seconds of trading at $ 1.70 per bushel. Frey executed all of Cox's order before the closing bell, but he was unable to liquidate 225,000 bushels of his own contracts. The closing price of $ 1.70 was more than nine cents above the previous day's settlement and slightly less than the daily trading limit. Over the life of the contract, trading prices had ranged as high as $ 1.78 per bushel.

Events After the Close of Trading. At the expiration of the May contract, Cox was short 85,000 bushels and he had accepted delivery of 585,000 bushels of wheat. Cox used 85,000 bushels of his cash wheat to deliver on his short May position. He sold another 405,000 bushels of his holdings on the cash market between June 3 and July 9, at prices at or below $ 1.63 per bushel. Cox eventually used his remaining 95,000 bushels to deliver against his short position in the July contract.

Frey took delivery of 225,000 bushels of wheat on his closing long position. He sold 130,000 bushels of that amount in the cash market between May 26 and June 21, at prices at or below $ 1.66 per bushel, and eventually delivered the remaining 95,000 bushels against his short position in the July contract.

Judicial and Commission Precedent

The essential elements of the offense of unlawful price manipulation have been described in a series of federal appellate court decisions, reviewing administrative determinations by the Secretary of Agriculture. n1 In addition, this Commission has once adjudicated a charge of attempted price manipulation and once adjudicated a claim of completed price manipulation. n2 To sustain the charge of completed manipulation under this precedent, the Division of Enforcement must establish each of several factors by a preponderance of the evidence:

(1) that the accused had the ability to influence market prices;

(2) that they specifically intended to do so;

(3) that artificial prices existed; and

(4) that the accused caused the artificial prices.

n1 *See General Foods Corp. v. Brannan,* 170 F.2d 220 (7th Cir. 1948); *Great Western Food Distributors, Inc. v. Brannan,* 201 F.2d 476 (7th Cir.), *cert. denied,* 345 U.S. 997 (1953); *G.H. Miller & Co. v. United States,* 260 F.2d 286 (7th Cir. 1958), *cert. denied,* 359 U.S. 907 (1959); *Volkart Brothers, Inc. v. Freeman,* 311 F.2d 52 (5th Cir. 1962); *Cargill, Inc. v. Hardin,* 452 F.2d 1154 (8th Cir. 1971), *cert. denied,* 406 U.S. 932 (1972).

n2 *See In re Hohenberg Brothers,* [1975-1977 Transfer Binder] COMM. FUT. L. REP. (CCH) P 20,271 (Feb. 18, 1977) (attempted manipulation); *In re Indiana Farm Bureau Cooperative Assn., Inc.,* [1982-1984 Transfer Binder] COMM. (Dec. 17, 1982) (manipulation). *See also* II Johnson, *Commodities Regulation,* §§ 5.00-5.35 (1982) and I Russo, *Regulation of Commodities Futures and Options Markets,* §§ 12.01-12.29 (1985 ed.).

We focus our attention on three issues which we consider to be dispositive of the manipulation count here: the ability to influence market prices, the attainment of artificial prices, and the cause of the price rise at issue. We conclude that the proof is insufficient as to all three elements of that offense. Although we do not necessarily agree with the ALJ's holding that Cox and Frey had the specific intent to manipulate (*see* note 5, *infra*), we do not find it necessary to examine Cox's and Frey's intent at any length given a failure of proof as to all the other elements of the manipulation charge. Finally, the parties have tried this case and briefed their appeals solely on the completed manipulation offense. They have not specifically addressed the charge of attempted manipulation, and we have no occasion to do so on our own motion. n3

n3 Where a finding of criminal liability is reversed on appeal for insufficient evidence as to some element of a greater offense, federal appellate courts may reduce the liability to a lesser-included offense or to an attempted offense in certain limited circumstances. *Cf.* Fed. R. Crim. Pro. 31(c); 8A Moore's Federal Practice P 31.03[5] (2d Ed., 1985 Supp.); *Allison v. U.S.,* 409 F.2d 445, 450-51 (D.C. Cir. 1969).

In this case, the parties' appellate pleadings do not address the offense of attempted price manipulation, as discussed in the Commission's *Hohenberg* opinion. In view of the case's age, a remand to develop the record on this issue would be inappropriate. We thus treat the question of attempted manipulation as waived under 17 C.F.R. § 10.104(a). Nothing in this opinion expresses any view on that offense.

Cox and Frey Lacked the Ability to Influence Market Prices Because the Deliverable Supply of Wheat Was Adequate

When analyzing the ability of the accused to influence market prices, we must recognize that there are two ways to satisfy futures obligations: offset in the futures market or delivery of the underlying commodity. The accused lacks the ability to influence prices if other market participants can bypass his demands and extinguish their obligations elsewhere. Here, as in *Indiana Farm Bureau,* we are confronted with an arguably congested market and the claim that respondents either were responsible for the congestion or unlawfully exacerbated it. But as we recognized in *Indiana Farm Bureau,* P 21,796 at 27,285:

squeezes in general and manipulative squeezes in particular are possible only when the delivery option disappears and its tempering effect is lost. Thus, the adequacy of "deliverable supply," as distinguished from supply generally, and the role of market participants in the supply scenario is of great significance in any analysis . . . . The acquisition of market dominance is the hallmark of a long manipulative squeeze. For without the ability to force shorts to deal with him either in the cash or futures market, the (long) manipulator is not able successfully to dictate prices because a short may buy grain from other sources and deliver against his commitments.

See also Cargill, 452 F.2d at 1164-65; Johnson, § 5.12.

The ALJ calculated the deliverable supply of wheat on May 19 at 222,000 bushels -- far less than respondents' aggregate n4 long futures position of 2.2 million bushels. The ALJ also concluded that Cox and Frey were well aware of these supply conditions (Initial Decision, P s30-49). On appeal, respondents challenge the ALJ's deliverable supply calculations as unreasonably narrow, while the Division embraces them as essentially correct. We disagree with the ALJ's exclusionary approach in certain respects, and conclude that the deliverable supply was adequate. We need not here examine the limits of the disappearing delivery option language (quoted above) from *Indiana Farm Bureau* because, in this case, the record shows an abundance of deliverable wheat.

n4 Respondents claim that the ALJ erred in concluding that they had an arrangement or understanding between themselves as to how their long positions should be handled and in holding that Frey "controlled" their joint positions. They observe that Frey had no price discretion about executing Cox's order. In these circumstances, they argue that it was reversible error to aggregate their separate futures positions. While we do not necessarily agree with the ALJ's resolution of this issue, we find it unnecessary to discuss the matter at any length. We hold that the deliverable supply was adequate, even assuming that the decision to aggregate was correct.

"Committed" Wheat In Chicago. The ALJ determined that there were over 2.5 million

bushels of wheat in the Chicago warehouses as of May 19, but he excluded from his deliverable supply calculations approximately 2.3 million bushels of this wheat on the grounds that it was "committed." The ALJ reasoned that, because this wheat was already earmarked to satisfy milling needs and other commercial commitments, it was not available to the shorts to satisfy their delivery obligations (Initial Decision, P s38, 39). We agree with the ALJ that the commitments in this case were "irrevocable." The record does not show that the commitments at issue were to come due far off into the future. A sufficient time interval between the due dates on these prior commitments and the futures delivery date could allow the commercial holders of wheat an opportunity to make that wheat available for delivery on the May contract and subsequently to replenish existing stocks with other wheat, thereby honoring their prior commitments as well. We thus agree with the ALJ's decision to exclude this so-called "committed" wheat from the available supply. *Indiana Farm Bureau,* P 21,796 at 27,287 (". . . the basic calculation of deliverable supply may be accomplished without regard to what is known by the accused . . .") n5

n5 In contrast, "it is the deliverable supply known to the accused which must be looked to in determining whether respondent's purchase of contracts is susceptible to an inference of manipulative intent." *Id.* The record does not show that Cox and Frey then knew, or that any local traders then could have known, how much of the wheat in the Chicago warehouses was irrevocably

> committed to other uses (Tr. 1119-26). The publicly-available information did not permit a trader to determine the actual ownership or commitment of wheat stocks. As experienced market participants, Cox and Frey (and, we presume, the dominant short) knew that wheat supplies in the Chicago warehouses were generally at their lowest at the end of the crop year, and that supplies in this particular crop year were at their lowest in several years. Beyond this general information, however, the record does not show that Cox and Frey had the sort of "knowledge" of committed wheat supplies from which manipulative intent may properly be inferred. A trader's "estimates" or "assumptions" or "inferences" about the commitments of other persons do not show manipulative intent. To the extent that the ALJ held otherwise, he relied on the same flawed methodology that we rejected in *Indiana Farm Bureau. See also Cargill,* 452 F.2d at 1160 n.6 (wheat that Cargill had committed to its own export sales program was obviously known to Cargill itself).

Barge Wheat Controlled By The Dominant Short. The ALJ also excluded from deliverable supply approximately 2.0 million bushels of wheat, controlled by the dominant short, and loaded on some 50 barges for transit on the Missouri and Mississippi Rivers during April and May (Initial Decision, P s43-45). The dominant short, Cook Industries, moved this wheat from Kansas City to New Orleans, reasoning that the cash market price at New Orleans ($ 1.79 per bushel) was substantially higher than that available to it in Chicago (Tr. 793-804; 1049-50). Respondents argue on appeal that this wheat could have been delivered at Chicago and should be considered as available for delivery against Cook's short futures positions; the Division supports the ALJ's decision to exclude it.

Again, the holdings of *Volkart,* 311 F.2d at 59-60, and *Indiana Farm Bureau,* P 21,796 at 27,286, are instructive. As those decisions established, it is irresponsible market behavior for shorts to enter the delivery month, especially where low cash supplies are evident at the delivery point, without makeing adequate delivery preparations. The ultimate decision to deliver or offset in the trading pit is one of time, price, distance, and convenience. But the fact that the local supply of a commodity is scarce does not release the shorts from their obligation to honor their contractual commitments to deliver. That is particularly true when the short is an experienced futures market participant, sufficiently skilled to locate out-of-town wheat supplies for delivery on relatively short notice. We do not believe that a valid analysis of deliverable supply can be made in the context of the last trading day. The better approach, which we follow here, is to analyze the deliverable supply picture as it emerged throughout the delivery month.

Here, the evidence shows that the dominant short controlled a large supply of out-of-town wheat, had already loaded it on barges for shipment, could have sent those barges to Chicago, but made a business judgment not to do so. The ALJ erred in assuming that the shorts only had to start thinking about their delivery obligations on the last trading day, and in concluding that there was insufficient time to deliver wheat by barge between the last trading day (May 19) and the last delivery day (May 28). With prudent planning early in the delivery month, barge transit times of eight or more days would not have impeded timely delivery of this wheat in Chicago. The Division notes that there are gaps in the record as to the precise location and quantity of Cook's barge wheat at the relevant times (Answering Brief, at 48). But if the Division wanted to establish that some or all of these barges were too far away to be included in the deliverable supply, then it should have come forward with evidence from Cook, the asserted victim of the manipulation (Tr. 1116-17). In these circumstances, we conclude that the ALJ erred in excluding from deliverable supply barge wheat controlled by the dominant short.

Premium Grades Of Wheat in Kansas City. Finally, the ALJ excluded from deliverable supply approximately 24 million bushels of wheat stored afloat and at warehouses in Kansas City. The ALJ reasoned that this origin was outside the "normal" supply area for Chicago and that barge or rail transit times from Kansas City to Chicago were too long to be of much help to shorts between the close of trading on May 19 and the last delivery date, May 28 (Initial Decision, P s 35,40). n6 Again, respondents challenge this exclusion on appeal, while the Division embraces it. In addition, the Division notes that most of the wheat at Kansas City was hard wheat (a premium grade), and it cites judicial precedent for the notion that premium grades of wheat at out-of-town locations should not be considered deliverable (see Answering Brief, at 50-51 and cases cited therein).

n6 The ALJ did not analyze rail and barge transportation costs in any detail when he excluded out-of-town wheat from deliverable supply. The Division makes only passing reference to such costs in its answering brief. On the record before us, we hold that such transportation costs were not shown to impede the movement of grain between the points in question.

In addition to Kansas City, the ALJ also excluded from deliverable supply smaller quantities of wheat stored at St. Louis and Milwaukee. Although the inclusion of these stocks would not markedly alter the overall supply picture here, our reasoning as to Kansas City is equally applicable to wheat at those locations, too.

Based on our review of the record, we think the weight of the evidence does not warrant the exclusion of Kansas City as a "normal" supply area for Chicago. To the extent that distance between markets is a factor, New Orleans and Buffalo are more distant from Kansas City than is Chicago, and yet the record shows that Kansas City wheat was regularly delivered to New Orleans and Buffalo during the period in question. n7

n7 Distance becomes less of a factor as the nature of the underlying commodity shifts from the perishable (eggs in the *Great Western Food* and *G.M. Miller* cases) to domestic agricultural (wheat, here and in the *Cargill* case) to world commodities, such as oil, gold, or the like.

Respondents also challenge the ALJ's calculation of transit times from Kansas City to Chicago as unreasonably lengthy. But even if we were to accept the ALJ's figures as correct (8-14 days), we would reject his underlying premise: that market participants who began the delivery month with large short positions and who were still holding short futures positions on the last trading day had no duty to prepare for delivery prior to the last trading day. Had these shorts prepared to deliver Kansas City wheat to Chicago at the beginning of the delivery month, transit times of 8-14 days would not have impaired delivery by May 28.

We reject the Division's suggestion that premium grades of a commodity at out-of-town locations must routinely be excluded from deliverable supply calculations. It is our firm belief that the terms of the underlying futures contract should not be lightly ignored when calculating deliverable supply. If the terms of the contract permit delivery of premium grades of the commodity, then premium grades must be counted as part of the relevant supply, if otherwise available. The Board of Trade's contract stands in sharp contrast to the contracts traded at Kansas City and Minneapolis exchanges, which permit delivery of only a narrow class of wheat (*see* DX 2; Tr. 422,935). In general, the terms of the underlying futures contract are for the contract market to set and for market participants to honor. *In re Murphy and Rudman,* [1984-1986 Transfer Binder] COMM. FUT. L. REP. (CCH) P 22,798 at 31,354 (CFTC Sept. 25, 1985). Market participants who are dissatisfied with the terms of a futures contract (including delivery terms) are free either to petition the exchange to alter those terms or to refrain from trading an instrument they deem to be unsatisfactory. Similarly, for purposes of this adjudication, we take the contract as we find it, and will not listen to complaints that the deliverable supply classes or grades are "really" narrower than the terms of the contract permit. *Cf.* Section 5a(10) of the Act, 7 U.S.C. § 7a(10); Russo, § 12.14.

Prior appeals court opinions have upheld Agriculture Department decisions to exclude such premium grades when they were not subject to a premium price, *i.e.,* when they were deliverable only at par price. *See, e.g., Great Western Food v. Brannan,* 201 F.2d at 480-81; *Cargill,* 452 F.2d at 1165-66 n.9 (". . . .many of the problems in this case might well be eliminated if Board of Trade rules were changed to allow a premium for delivery of hard wheat."). In the present case, of course, premium price differentials were available in certain circumstances and the judicial precedent is thus distinguishable. We will not use this adjudication to "second guess" the exchange's judgment about the sufficiency of such price differentials.

On this record, we calculate the available wheat supply at approximately 26.2 million bushels. To be sure, some small portion of this wheat may not have been of deliverable quality and should be excluded from a final tally. But the present record does not permit us to state that figure with any precision. We hold only that the long futures positions held by Cox and Frey on May 19 (some 2.2 million bushels) were not shown by a preponderance of the evidence to exceed the supply of wheat that the shorts could have delivered to Chicago warehouses by the close of the delivery period on May 28 with prudent planning.

In these circumstances, Cox and Frey could not foreclose the shorts' delivery option and thus lacked the ability to influence market prices. Their conduct in the futures market (*i.e.,* evidence

suggesting that their trading activity created or exploited market congestion) is not dispositive, because market congestion cannot exist when deliverable supplies are adequate. *Indiana Farm Bureau,* P 21,796 at 21,283-86.

The Closing Futures Price of $ 1.70 Per Bushel Was Not Shown To Be Artificially High

The ALJ concluded that the price of May wheat futures contracts was artificially high once it reached and then exceeded $ 1.67 per bushel, *i.e.,* approximately during the last hour and fifteen minutes of trading on the last trading day (Initial Decision, P 105) (DX 8). The ALJ pointed to historical and contemporaneous market price comparisons to support his analysis (Initial Decision, P s 50-113).

On appeal, respondents argue that May wheat never reached an artificially high level on the last trading day. They contend that the historical price comparisons in the initial decision are incomplete and lack probative value. They criticize the ALJ's cash market comparisons as unreasonably narrow, and they cite opinion testimony and other data in the record which support their position. In its answering brief, the Division of Enforcement embraces the reasoning of the ALJ.

Measuring Artificial Prices. An artificial price is one that does not reflect the market or economic forces of supply and demand. Price artificiality traditionally has been studied by relating the price in question to other relevant economic data. Proof of artificiality generally has focused on significant deviations from normal historical futures market patterns and from related contemporaneous markets. *See Great Western Food Distributors,* 201 F.2d at 482-83; and *Cargill,* 452 F.2d at 1167-70. In recognition of a new and unique fact situation, we expanded the artificial price analysis in *Indiana Farm Bureau,* P 21,796 at 27,288 n.2 and 27,289 n.16 and expressed the view that historical price comparisons were (in that case) of less probative value than data from related contemporaneous markets, including the cash market for the underlying commodity. As we there stated (emphasis in original):

As the delivery time draws near, not only do the cash and futures prices converge, but the *markets* converge by virtue of the delivery mechanism. Depending on what else is going on in other segments of the aggregate market, the futures market may well define the aggregate market. If trading in the physical market is thin, in terms of quantity, quality, or volume, the futures market may be *the market.* The traders in the pit are buying and selling the commodity.

. . . to determine whether an artificial price has occurred one must look at the aggregate forces of supply and demand and search for those factors which are extraneous to the pricing system, are not a legitimate part of the economic pricing system, are not a legitimate part of the economic pricing of the commodity, or are extrinsic to that commodity market. When the aggregate forces of supply and demand bearing on a particular market are all legitimate, it follows that the price will not be artificial. On the other hand, when a price is affected by a factor which is not legitimate, the resulting price is necessarily artificial. Thus, the focus should not be as much on the ultimate price, as on the nature of the factors causing it.

We apply these principles here, noting that all of the above considerations are relevant to determining price artificiality, and the weight to be given these factors varies according to the circumstances of each case.

Historical Market Comparisons. The ALJ compared: (1) May futures prices in Chicago on May 19 to July futures prices in Chicago on the same day; and (2) May futures prices in Chicago on May 19 to the futures prices reached on the Kansas City Board of Trade and the Minneapolis Grain Exchange on the same day. He concluded that these price differences on May 19 were "abnormally wide" when measured against the corresponding data from the same markets in prior years (Initial Decision, P s 74-89). We disagree. First, the ALJ failed to take account of our *Indiana Farm Bureau* opinion, P 21,796 at 27,289 and n.16, which found that historical price comparisons may be of little value to the analysis of artificial futures prices, depending upon the situation. We reach the same conclusion here, recognizing that the prospective behavior of a "normal" market is not necessarily bounded by the market's historical experiences. While historical and spread data may be used in future cases, it is incumbent on the parties to explain or justify the relevance of such evidence.

Second, the ALJ's historical price comparisons go against the weight of the record evidence and are otherwise unpersuasive. Respondents argue that the ALJ ignored evidence which undercut the validity of his comparisons, *e.g.,* the fact that Kansas City May wheat rose more than 5 cents per bushel between May 5 and May 18, while Chicago May wheat prices remained stagnant and the fact that July futures contracts advance sharply (by more than 19 cents per bushel at Chicago and 15 cents per bushel at Kansas City) from May 19 to June 10. They suggest that these price movements confirmed the reasonableness of the $ 1.70 close. We agree. And absent evidence that the variances in the initial decision were statistically or economically significant, we regard the ALJ's data as distinctions without differences. *Cf. Great Western Food,* 201 F.2d at 482; Russo, §§ 12.26, 12.27.

For example, the ALJ expressed the view that a spread of 20 cents per bushel between May futures and July futures at the Board of Trade was "abnormally wide" (Initial Decision, P s 81-84, Tr. 923-27, DX 21). But he did not enter any findings about the "normal" May-July price spread or about the maximum permissible spread between these two contracts on the day in question. This gap in the record is significant, because respondent Cox held a spread position (long May-short July) and the absolute level of May wheat prices was less important to him than the size of the May-July spread. Indeed, his short July position gave him an assured means of disposing of any deliveries taken on the May contract. Finally, the ALJ was inconsistent in looking to futures prices at other contract markets such as Kansas City to determine artificiality in Chicago while, at the same time, he was defining the relevant cash market narrowly. Although we reject his narrow cash market definition (*see infra*), the underlying inconsistency detracts from the weight to be accorded his analysis here.

Cash Market Price Comparisons. The ALJ found that there was little commercial demand for wheat in Chicago during the month of May. In determining that $ 1.67 per bushel was the maximum reasonable futures price, the ALJ analyzed only those cash market transactions occurring (1) during the delivery month and (2) in the classes of wheat that were in his view "likely to be delivered" in satisfaction of the futures contract. In so holding, he excluded cash market transactions occurring after the delivery month and in other classes of wheat (Initial Decision, P s 50-73, 90-113).

In prior manipulation cases, cash market prices for the underlying commodity have often been cited to measure the artifical nature of futures prices. Of course, such prices have general relevance to the inquiry. At the same time, they are not dispositive in and of themselves. The cash market has several characteristics which limit its reliability for comparative purposes: it may not be standardized as to quantities, qualities, or delivery points; it often involves negotiations between parties of different bargaining strength; prices for the same class and quantity of a commodity may vary widely on the same day; sales may be infrequent or sporadic (particularly at the end of a crop year, as here); all the relevant terms of a transaction may not be publicly known; and sales may on occasion reflect non-price factors, such as longstanding business relationships or convenience factors. As a result, cash market prices offer only a crude measuring tool -- a broad range of prices or "zone of reasonableness" -- against which to compare the artificial nature of futures prices. *Cf. Cargill,* 452 F.2d at 1168; Johnson, § 5.17; Russo, § 12.23. To compensate for these flaws, we generally prefer to examine the broadest possible range of relevant cash market transactions. Here, the initial decision did just the opposite.

We agree with respondents that it was error to ignore cash sales of hard red winter wheat on the theory that such wheat was not likely to be delivered in satisfaction of the futures contract (Initial Decision, P s 34, 107-08). Such wheat was clearly deliverable under the terms of the Board of Trade's contract, at a premium price in certain circumstances. In fact, 95,000 bushels of hard red winter wheat were delivered to satisfy an expiring short position on the May contract. If the underlying contract does not distinguish among grades or classes of wheat on the basis of protein content (and the Chicago Board of Trade's contract does not), then such distinctions may not be offered (as they were here) as a basis for excluding high protein wheat from the relevant cash market comparisons. To the extent that the ALJ held otherwise, he was in error (Initial Decision, P s 93, 95-96). Earlier in this opinion, we have rejected the notion that premium grades of a commodity must routinely be excluded from deliverable supply calculations just because they are premium grades. The same reasoning applies with equal force to artificial price measurements: if the underlying futures contract permits delivery of premium grades of the commodity, then cash sales of the premium grade are relevant to the artificial price analysis. *Cf. In re Murphy and Rudman,* P 22,798 at 31,354.

We also agree with respondents that it was error to ignore cash market transactions occurring in June and early July (Initial Decision, P 109). In so ruling, the ALJ looked only at cash transactions within the delivery month. But his ruling in that regard is internally inconsistent: if it is legitimate for the Division to show that respondents "buried the corpse" of their manipulation in June and July (sold wheat at prices below $ 1.70 per bushel), then it is equally legitimate for respondents to analyze other June-July cash market transactions at prices above $ 1.70 per bushel. The ALJ acknowledged that cash market prices for wheat rose in June, but he attributed this to changed circumstances (subsequent reports of corn blight). We read the record differently, concerns about corn blight influenced wheat futures prices as early as May 4 (DX Id, at 6; Tr. 1234). In a prior price manipulation case, calls to exclude cash market prices outside the delivery month have been rejected. *Cf. In re Indiana Farm Bureau Cooperative Association, Inc.,* [1977-1980 Transfer Binder] COMM. FUT. L. REP. (CCH) P 20,964 at 23,859 (Initial Decision, Dec. 12, 1979). We reach the same result here. Such prices may contribute to an understanding of the market equilibrium price. They are not necessarily dispositive. But the challenge to the parties is to identify the relevant factors which determine the market price and clues may be sought broadly.

The Division argues that respondents' evidence of cash wheat sales at prices above $ 1.70 per bushel is isolated and sporadic. But this is inconsistent with the Division's claim that there was a thin cash market, occurring at the end of the crop year. If the market was indeed thin, then respondents should not be faulted for citing few examples. In any event, the data relied upon by respondents find support from several trade witnesses, who expressed the view that $ 1.70 was a realistic price at the time (Tr. 434, 485-87, 612-14, 668). In addition, we cannot ignore the behavior of the dominant short in the futures market. Had Cook Industries made any effort to acquire cash wheat in Chicago during April or May (as an alternative to delivering out-of-town stocks), that might well have caused cash prices to strengthen.

The Futures Market. Given an inactive cash market for wheat in Chicago at the end of the crop year, we are again presented with a record suggesting that the futures market become *the market.* We find no abnormality in that market. We think it very significant that the Pillsbury Company (an independent hedger which was not named as a respondent and which had no ties to Cox or Frey) made a determination prior to the start of trading on May 19 to sell 130,000 bushels of its long wheat futures at $ 1.68 1/2 (DX 7, Cox Ex. 30, Tr. 1108, 1118). It later filled its order at that price -- thereby establishing that such a price was not artificially high in the estimation of other market participants. The ALJ's findings about the volatility of futures prices at the close of trading are also significant. The Judge determined that May wheat futures "retreated" from or "dropped" from or "showed same opposition to" respondents' offering price of $ 1.70 during the last half hour of trading (Initial Decision, P 7). In our judgment, this is evidence of a competitive marketplace, not one in which the longs had the shorts at their mercy and were free to name their own price. These factors undercut the ALJ's conclusion that the futures price was artificial at and above $ 1.67. Finally, the ALJ virtually ignored the fact that the Board of Trade had in place a self-regulatory device to block excessive price volatility -- the daily trading limit of plus or minus ten cents from the prior day's settlement. *Cf.* Johnson, § 2.20. In a case of this sort, where the allegations of misconduct are limited to events on a single trading day, proof that futures prices showed active resistance to an increase less than regular limit levels during the last half hour of trading is additional evidence that the prices in question were not excessive.

Stripped to its essentials, the initial decision stands for the proposition that there was a price aberration at the close of trading in May wheat futures, but that it was of small magnitude and short duration. At best, this is a lukewarm basis for sustaining the complaint. After reviewing the record, however, we conclude that even a limited finding of this nature is unsupported by the record. We hold that artificial futures prices were not shown to exist on May 19. This holding embraces (1) the closing price of $ 1.70 per bushel; (2) Cox's alternative price goal of May wheat at 20 cents over July wheat; and (3) Frey's price goal of "limit up" or $ 1.70 3/4 per bushel.

Without Resolving the Issue of Causation in this Case, a Discussion of the Elements of Causation is Warranted. Those Who Remain in the Futures Market Late in the Delivery Month Must be Prepared to Make or Take Delivery of the Underlying Commodity.

Once the Division of Enforcement shows that the respondents had the ability to influence prices and that the prices in question were artificial, it must then show that the respondents caused the artificial prices. *Volkart,* 311 F.2d at 58 and 60 (conduct must "produce" a price distortion; respondents must "create" prices not responsive to the forces of supply and demand); *Cargill,* 452 F.2d at 1163, 1169-70 (conduct must have "resulted in" a price which does not reflect the basic forces of supply and demand; the question is whether the artificially high price was "caused by" Cargill; the answer was held to be that "the only reason the price advanced so rapidly" was the conduct of Cargill); *Indiana Farm Bureau,* P 21,796 at 27,286 (no evidence that longs were "responsible for" market congestion, while irresponsible market behavior of shorts was a "serious contributing factor" to market congestion).

These decisions recognize that there can be multiple causes of an artificial price. Where these causes can be sorted out, and respondents are a "proximate" n8 cause of the artificial price, a charge of manipulation can be sustained. n9 If the multiple causes cannot be sorted out, or if the respondents are not one of the proximate causes, then the charge of manipulation cannot be sustained.

n8 It is our view that an artificial price is proximately caused by an act, or a failure to act, whenever it appears from the evidence in the case, that the act or omission played a substantial part in bringing about or actually causing the artificial price; and that the artificial price was either a direct result or a reasonably probable consequence of the act or omission. *Cf.* Black's Law Dictionary, 5th Ed., 1979, at 1103.

n9 Of course, the other elements of manipulation discussed at page 7 also would need to be met.

There would ordinarily be no need for us to analyze the element of causation, absent proof that the respondents had the ability to influence prices and absent proof that artificial prices existed. Here, however, it is clear that considerable confusion still surrounds the element of causation, in the wake of *Indiana Farm Bureau.* We thus examine the appropriate legal standard for causation and then apply that standard to the facts of record (assuming, purely for discussion purposes, that the other elements of the completed offense have been established). n10

n10 This approach is consistent with *Indiana Farm Bureau,* which discussed causation in some detail, notwithstanding the determination that deliverable supply was adequate and prices were not artificial.

Proving Causation. As noted, in order to establish a *prima facie* case of price manipulation, the Division of Enforcement must show that the respondents' conduct "resulted in" artificial prices. *Great Western Food,* 201 F.2d at 483. As with each of the other elements of this violation, it must do so under the preponderance-of-the-evidence standard. If the respondents argue that other factors, apart from their own behavior, materially contributed to the artificial prices, we will treat such claims as an affirmative defense. In order to be absolved of liability under such a defense, the respondents must rebut the evidence that they were a proximate cause of the artificial price. With these general principles in mind, we turn to the facts of record.

The Present Record. Respondents claim that the dominant short, Cook Industries, was the sole cause of the nine-cent surge in wheat futures prices on the last trading day. n11 Among other things, respondents assert that Cook: (1) depressed the price of Chicago wheat futures in April and May by maintaining a large short position; (2) was really a speculator and not a hedger; (3) could have and should have liquidated its short futures positions earlier and more gradually than it did; (4) failed to made adequate delivery preparations on the short futures positions it held until the last trading day; and (5) has a well-deserved reputation within the grain industry for deception and recklessness. Respondents criticize the initial decision as one-sided, asserting that it focused on the obligations of those who held long positions and ignored the responsibilities of those who held short positions. The Division's answering brief takes issue with each of these points, portraying Cook as a victim of respondents' misconduct, not as an independent cause of market disruption.

n11 For the reasons discussed in note 4, *supra,* we have assumed (without deciding) that the ALJ was correct to aggregate the long futures positions held by Cox and Frey. For consistency of analysis, we also aggregate the short futures positions held by Cook Industries, Cook Grain Division, Cook

& Associates, COMCO, their officers and employees (Tr. 702-04, 717-18). Hereafter, the term "Cook" embraces all of these affilated traders.

The ALJ rejected respondents' claim that Cook unlawfully depressed the price of wheat futues in April and May (Initial Decision, P s 79-80). Absent evidence of specific intent to depress prices and evidence that the April and early May prices were artificially low, we must agree. In essence, this is an argument that the Cook interests were conducting (or attempting to conduct) a short side manipulation, and that the wrong respondents were named in the complaint. To prevail on such a defense, Cox and Frey would have to present a good deal more evidence than they did on this record. Respondents also argued at the hearing that Cook was not evenly hedged for minimum risk, had misrepresented its *bona fide* hedge status to the federal government, and was really maintaining a speculative spread position. But the initial decision did not address this claim in any detail and respondents do not pursue it with any particularity in their appeal briefs. We consider the issue as abandoned.

Respondents' other arguments are more meritorious. We agree that Cook was slow to liquidate its dominant short position in Chicago May wheat futures On April 1, Cook was short approximately 7.5 million bushels, or 30 percent of the short open interest. On May 3, Cook was short 4.7 million bushels. At the opening on the last trading day, May 19, Cook was still short some 2.8 million bushels, or 59 percent of the short open interest. At all times before the final trading day, the short positions held by the Cook interests were larger than the sum of Cox's long and Frey's long positions. During April and early May, Cook controlled approximately 235,000 bushels of cash wheat in Chicago warehouses, and it eventually delivered all of this wheat against its short futures positions or sold it in the cash market. But Cook did not move any additional wheat into Chicago from other locations during April or May.

The record shows that Cook had been short on the two prior Chicago wheat futures contracts (in December and March) and had made significant deliveries on those contracts. Cox and Frey showed that on May 19 there were rumors at the Chicago Board of Trade to the effect that Cook might again deliver significant quantities of additional wheat to satisfy its short May futures position. The ALJ gave no weight to these rumors because, in his view, no one believed them (Initial Decision, P s 43-45). We think this was in error. The record reflects that Cook had planted the Chicago delivery rumors and that they were false. n12 *See In re Kosuga,* 19 Agric. Dec. 603, 621 (19 A.D. 603, 621) (1960) (the possibility of delivery by a substantial short clearly constitutes a price-depressing factor); *In re Henner,* 30 Agric. Dec. 1151, 1234 (30 A.D. 1151, 1234) (1971) (spreading false intelligence is one of the most common methods of manipulating the market); *In re Hohenberg Brothers,* P 20,271 at 21,476 n.28 (where the holders of substantial long positions are ready to stop delivery notices, the price depressant effect of large deliveries will generally be muted).

n12 The record does not show that Cook ever planned to ship large quantities of wheat to Chicago during the delivery month. Nor is this a case in which Cook altered preexisting plans in reponse to subsequent price rises for wheat at Gulf ports. On the contrary, the record is clear that the price differential favoring Gulf ports existed at least as early as mid-April and continued during the delivery month. Tr. 528-29, 915, 1156, 1158, 1445-59. *Contrast* Tr. 508 (". . . Cook was advertising to all during that period that he had wheat in barges for delivery, so therefore you had to assume that the short . . . was able to deliver.") and Tr. 646 (". . . certainly in this particular case [Cook] blew all kinds of smoke . . . they were trying to talk their position into a correct position.") *with* Tr. 738 (Cook official could not recall any such rumors).

At the same time, Cook was selling over 12 million bushels of wheat for May and June shipment to the Gulf for export, thus consciously giving up its ability to deliver against its short position in Chicago May wheat. Respondents argue that Cook was spreading false rumors of delivery to extricate itself from its large short Chicago May futures position at the most advantageous price while, at the same time, taking advantage of higher prices at the Gulf for sale of its cash wheat. The weight of the evidence supports this view of events. Indeed, on cross-examination, the Division of Enforcement's chief economic witness virtually conceded that the shorts were a major cause of the price rise. He testified: "If the shorts had been able to deliver, the problem in May [wheat] would not have occurred" and ". . . the price rise which occurred would not have happened had the shorts had the capacity to deliver on their position." (Tr. 1021, 1022).

Respondents also argue that Cook had a well-deserved reputation for deception and recklessness within the grain industry. They point to the fact that Cook Industries and several of its employees (including Division witness McCaull) later pleaded no contest or guilty to criminal charges arising out of the short-weighing of export grain. We also note that the Board of Trade's staff reminded McCaull on May 19 of his obligation to assure an orderly liquidation of the May wheat contract (Frey Ex. 29, at p. 392; Tr. 1503-05). This, of course, was quite similar to the "jawboning" that the exchange's staff directed at Cox and Frey -- on which the ALJ placed a heavy emphasis. While we do not reverse the ALJ's favorable credibility determination as to witness McCaull (Initial Decision, P 45), we give far less weight to that testimony than did the ALJ. Nor do we embrace the Division efforts to portray Cook Industries as the wholly innocent victim of respondents' evil intrigues (Answering Brief, at 54 n.23). *In re Resenthal & Co.,* [1984-1986 Transfer Binder] COMM. FUT. L. REP. (CCH) P 22,221 at 29,173 n.26 (CFTC June 6, 1984) (standard governing review of credibility findings).

On balance we accept parts of respondents' arguments. We agree that the actions of the dominant short were a major cause (but not the sole cause) of the nine cent price rise on the last day of trading, when Cook had exhausted its delivery capacity and had to buy in its entire short position. On the record before us, we hold that the price rise was the result of several competing factors on both the long and short sides of the futures market. In these circumstances, it was not appropriate for the ALJ to sustain the charge of completed price manipulation without first sorting out the multiple causes. But because the other elements of the offense are also missing, we see nothing to be gained by a remand on this issue or by addressing the matter futher in this opinion.

We emphasize that futures market participants who remain in the market late into the delivery month must be prepared to perform all of their obligations in the delivery process, *i.e.,* making or taking delivery of the underlying commodity. Participants who are not so prepared cannot assume they will be able to offset in the futures market without experiencing the prospect of an adverse price movement. n13

n13 The respondent longs in *Indiana Farm Bureau,* unlike Cox and Frey, were hedgers with a pre-existing commercial need for the grain on which they took delivery. But Cox and Frey could have (and did, in part) use their May deliveries to satisfy their short July wheat futures positions. We see no basis for distinguishing *Indiana Farm Bureau* on the grounds that the persons taking delivery in this case were long speculators, instead of long hedges. The shorts' obligation to deliver (and the longs' obligation to take delivery) are identical in both situations.

The parties raise several other issues in their appellate pleadings, but we find it unnecessary to address these issues. Their resolution would not alter the outcome and could only delay this proceeding further.

* * *

After reviewing the record, the initial decision, and the appellate pleadings, IT IS ORDERED THAT:

Respondents' appeals are granted, the initial decision is reversed, and the complaint is dismissed. Respondents' motions for oral argument are denied.

By the Commission (Chairman PHILLIPS and Commissioners HINDMAN, SEALE, and DAVIS) (Commissioner WEST dissenting).

* * *

Commissioner WEST Dissenting.

Since at least 1868 when the Chicago Board of Trade adopted the first rule against "the practice of 'corners,' of making contracts for the purchase of a commodity, and then taking measures to render it impossible for the seller to fill his contract, for the purpose of extorting money from him," n1 a primary goal of both industry and later government regulation of futures trading has been the prevention of price manipulation. Over 65 years ago, the 1922 Grain Futures Act required each exchange to actively police against manipulation, and the 1936 Commodity Exchange Act gave federal regulators authority to prosecute manipulators. This priority has been remphasized in the law in every Congressional review since that time.

n1 Taylor, *History of the Board of Trade of the City of Chicago,* p. 371.

Most recently, the Commission, in its fiscal 1988 budget request to Congress, included an increase for its market surveillance program whose "primary objective" is "to detect and prevent manipulation, threats of corners, and other market disruptions." n2

n2 CFCT "Budget Explanatory Notes," fiscal year 1988.

Despite this long history, the Commission and federal courts still find themselves today struggling to define the legal boundaries between free competition and prohibited manipulation. Fortunately, the Commission and its predecessor agency have found it necessary to bring only a small number of manipulation cases over the decades. The result, however, is a dearth of settled caselaw. As recently as 1982, Commissioners considering the case of *Indiana Farm Bureau Cooperative Assn., Inc.,* [1982-1984 Transfer Binder] COMM. FUT. L. REP. (CCH). P 21,796 (Dec. 17, 1982), found it necessary to issue three separate opinions to explain their positions on disputed points involving fundamental concepts in "manipulation" law; the responsibilities of market shorts, the required *mens rea,* and the difference between price "artificiality" and true market price.

The case before us today is significant as a statement of our current framework for analyzing manipulation cases. I am concerned with several points regarding the structure of the Commission opinion's analysis as well as its conclusions. Therefore, I feel obliged to dissent.

The factual situation in *Cox and Frey* presents a classic "squeeze" n3 scenario. By 11:31 am on May 19, 1971, the last trading day in May wheat futures, two traders held 97.1 percent of the long open interest representing a demand for 2.2 million bushels of wheat. Major short traders, meanwhile, apparently found themselves not having prepared for delivery. While 24 million bushels of technically delivery-grade wheat sat in Kansas City warehouses, it would have taken at least 8 to 10 days to transport the wheat to Chicago -- presumably too late for the contract's May 28 delivery deadline. Another 2 million bushels sat on barges in the Mississippi River owned by the largest short but also too far away to retrieved on time. As a result, the Administrative Law Judge correctly determined that only 222,000 bushels of wheat in Chicago were available for deliveries under the contract as of May 19.

n3 Senator Pope defined a "squeeze (congestion)" during Congressional debates leading to enactment of the Commodity Exchange Act as follows:

> "These are terms used to designate a condition in maturing futures where sellers (hedgers or speculators), having waited too long to close their trades, find there are no new sellers from whom they can buy, deliverable stocks are low, and it is too late to procure the actual commodity elsewhere to settle by delivery. Under such circumstances and though the market is not cornered in the ordinary sense, traders who are long hold out for an arbitrary price. 80 *Cong. Rec.* 8089 (1928)

Prices of May wheat futures that day opened at $ 1.61 1/2 per bushel and reached $ 1.65 by 10:00 am. Both Cox and Frey, who were speculators, each conceded that they planned to hold out for about $ 1.70, or, in the alternative for Cox, a 20 cent premium over the July futures. As a result, Frey, trading both positions on the floor and thus knowledgeable of Cox's position and plans, did not liquidate the bulk of their long contracts until the last 10 seconds of trading. Presumably, had short traders not bought from Frey at $ 1.70 at that point, they would have been forced to deliver 2.2 million bushels -- apparently a physical impossibility given that most wheat was out of reach -- and thus thrown into default. One witness, representing the Continental Grain Company, specifically testified that his firm could not locate wheat to deliver on its large short position that day and therefore also liquidated at the $ 1.70 price since "it did not wish to risk having to pay a higher price for deliverable wheat." (Initial Decision, P 61).

In analyzing these circumstances, the majority opinion has distilled from relevant case decisions four key ingredients of a completed manipulation:

-- That the accused had the ability to influence market prices; [Strictly speaking, of course, the Commission recognizes that an illegal manipulation can occur without this element, such as by floating false rumors to affect prices. *See In re Hohenberg Brothers,* [1975-1977 Transfer Binder] COM. FUT. L. REP. (CCH) P 20,271. (February 18, 1977).

-- That they specifically intended to do so;

-- That "artificial" prices existed; and

-- That the accused caused the artificial prices.

The Commission's opinion has determined that Mssrs. Cox and Frey's actions on May 19, did not amount to a manipulation because two of the above ingredients were not met: (i) an adequate deliverable supply of wheat existed -- shorts could have brought wheat in from out of town had they prepared better, and (ii) prices did not reach "artificial" levels. The Commission does not reach a conclusion as to whether Cox and Frey "proximately" caused any price effect, but it finds that Judge Duncan has not sufficiently "sorted out" various competing causes. The majority does not examine at any length the ALJ's finding of requisite intent.

The majority seems to imply that since short traders acted irresponsibly by not making adequate preparations for delivery -- a conclusion which I do not dispute -- the longs had no responsibility to show restraint. By making this responsibility test part of its deliverable supply analysis, the Commission has effectively precluded any consideration of subsequent foul play by the longs. As a result, the majority opinion appears to step far beyond the Commission's reasoning in *Indiana Farm Bureau* by creating an analytical framework under which failure by the shorts to adequately prepare for delivery becomes an absolute defense for the longs to use against charges of manipulation, even in extreme cases where an actual supply shortage, specific intent, artificial price, and causation are proven.

I. *Ability To Influence Market*

To demonstrate that Mssrs. Cox and Frey had the ability to influence prices under the Division of Enforcement's theory of the case, the Division had to demonstrate that an insufficient deliverable supply of the commodity existed

Without adequate deliverable supply, the shorts would not be able to deliver under their contracts without buying back futures contracts from the longs who held 97.1 percent of the long contracts. Otherwise, they would face default. Judge Duncan found that as of May 19 when Cox and Frey undertook their alleged market operation, 222,000 bushels of wheat were available for delivery under the contract -- far less than the 2.2 million bushels which Cox and Frey could demand under their long contracts. The Judge excluded from his calculation two other possible sources of wheat: 2 million bushels loaded onto barges in the Mississippi River plus another 24 million bushels stored in Kansas City, essentially because this wheat was economically impractical and physically impossible to deliver on time.

The Commission rejects the ALJ's finding on the theoretical ground that had the shorts prepared for delivery before the last day of trading, they *could have* moved the wheat to Chicago by May 28, the delivery deadline. "With prudent planning [before the last day], barge transit times of eight or more days would not have impeded" delivery, the Commission says. "Had the shorts prepared to deliver Kansas City wheat to Chicago at the beginning of the delivery month, transit time of 8-14 days would not have impaired delivery." n4

n4 Most commercial hedgers, of course, enter the market not as a means to take or make delivery but rather to reduce the risk of price volitility on their businesses. Only a tiny percentage of hedge or speculative positions result in actual delivery.

Certainly, in determining the ultimate liability of Mssrs. Cox and Frey, the Commission must consider whether the shorts contributed to the congested market situation of May 19. It may well be true, as the Commission suggests, that irresponsible, negligent actions by the shorts were as much to blame for the apparent shortage that day as any actions by the longs. I agree that we must not send a statement that shorts can walk away from their contractual commitments. However, to simply define the market congestion out of existence because the Commission felt the shorts were negligent amounts to establishing a "contributory negligence" standard which creates an absolute shield for the longs no matter how egregious their subsequent behavior. Manipulation, as a statutory offense directed at the wrongdoing of respondents, is simply not suitable to such an analysis.

The *only* precedent for tying the behavior of shorts to the calculation of deliverable supply is the 25 year old case of *Volkart Brothers Inc. v. Freeman,* 311 F.2d 52 (5th Cir., 1962), which was roundly criticized by the 8th circuit in *Cargill v. Hardin* 452 F2d 1154 (*cert. denied*) n5, is never cited by any other court for this proposition, and is arguably inconsistent with *Indiana Farm Bureau.* The Commission explicitly limited its *Indiana Farm Bureau* analysis to factual settings where "a long has not intentionally created *or exploited* a congested situation" (P 21,796 at p. 27,286, emphasis added). In fact, evidence exists in today's case that such exploitation did indeed occur. The majority's analysis, however, never reaches the issue since the congestion is defined out of existence at the beginning. Rather, in *Indiana Farm Bureau,* the Commission agreed that deliverable supply was an "objective fact" which could be determined "without regard to what is known by the accused," (p. 27,287) or, presumably, by what is known by the shorts.

n5 The *Cargill* court felt that *Volkart,* if read "at its broadest reach . . . holds that manipulative squeezes are not prohibited by the Commodity Exchange Act. . . . We think this approach disregards commercial reality and the economic functions of the futures market."

Even where delivery was physically possible, legal precedents over the past 35 years, with the possible exception of *Volkart,* have consistently excluded from the delivery pool commodity supplies so distant as to create economic hurdles to delivery. n6 The 7th Circuit explained the rationale in *Great Western Food Distributors v. Brannan* 201 F.2d 476 (1953) with respect to eggs: shorts would not normally deliver more expensive out-of-town eggs "unless control of the local supply is acquired by one who intentionally raises the price of Chicago refrigerator eggs to the level of out of towns. This, of itself, would constitute an arbitrary fixing of prices." The Division of Enforcement in its appeal brief argues sensibly against "[expanding] the concept of deliverable supply to include *all* wheat *anywhere* that can be delivered at *some* price, no matter how high it might be." They point out that

"under this view, the more successful the upward price manipulation, the larger the deliverable supply will be, since at artificially high prices parties can profit by disrupting the normal flow of the cash commodity and making delivery to the manipulator on the futures market. At some point, the manipulated futures price will be high enough to warrant shipments of wheat into Chicago from around the country, or even around the world." (Division's Answering brief, p. 49). n7

n6 Even in *Volkart,* the 5th circuit refused to exclude "bales of uncertified cotton stored at ports designated as delivery points" from the delivery pool under consideration -- quite a different situation from the Commission's decision today to include Kansas City wheat under a contract which specified the Chicago switching section as the *sole* delivery area. The Commission's *Indiana Farm Bureau* decision never reaches the question of whether to include non-economic or non-available supplies in a delivery pool. While castigating the shorts for possibly "irresponsible" market behavior, the Commission in that case upheld that ALJ's finding that "in fact there was an adequate supply of deliverable corn *in Chicago* at the time." (emphasis added)

n7 The majority opinion dismisses this argument in a footnote, saying that since "the ALJ did not analyze rail or barge transportation costs in any detail when he excluded out-of-town wheat from the deliverable supply" and the Division of Enforcement "makes only passing reference to such costs," therefore "we hold that such transportation costs were not shown to impede the movement of grain between the points in question." This issue of exclusion of non-economic sources from a contract's delivery pool for purposes of such a supply analysis, however, is addressed in P P 34, 35, and 107 of Judge Duncan's Initial Decision and pages 46-52 of the Division's Answering Brief.

The majority notes that the premium supplies rejected by the Courts in *Cargill* and *Great Western* were not subject to premium price differentials under exchange rules. In *Great Western,* though, a differential did exist for out-of-town supplies. In the present case, Chicago Board of Trade rules provided a 1 cent per bushel premium or discount for certain wheat classes based on quality but not location -- all deliveries were required to be made in the Chicago switching district. (I.D. P 33). As a result, the exchange-set premium would not necessarily offset the transportation expense cited by Judge Duncan in P 107 of his decision.

Under the circumstances, I see no reason to depart from Judge Duncan's reading of the evidence that as of May 19, the available deliverable supply for the May wheat contract was approximately 222,000 bushels, not the 26 + million which *could have been* present had the shorts acted differently. As a result of the lack of deliverable supply, I must conclude that Mssrs. Cox and Frey had the objective ability to influence market prices at that time. Bear in mind, however, that this conclusion represents only one of four elements set out by the Commission.

In countering this point, the majority opinion says that a "valid analysis" of the supply situation cannot be made "in the context of the last trading day," but rather must look at the "supply picture as it emerged throughout the month." (p. 11) This view, however, seems unduly inflexible in light of the fast-paced reality of exchange trading, particularly as modern advances in data processing and telecommunications technology have made commonplace instantaneous market reactions to subtle changes in the commercial environment worldwide. Traders routinely adjust their stategies several times a day to keep up with events. We have seen several examples during the past year of drastic price changes occurring in minutes. In future cases, we must be prepared to recognize the possibility that complex market supply situation can emerge, be analyzed, and improperly exploited in the context of a single hour, let alone a single trading day, where there is profit to be made.

II. *Causation*

I certainly endorse the policy underlying the Commission's holding in this case that short traders must honor their commitments to deliver on their futures contracts. I agree with its emphasis

"that futures market participants who remain in the market late into the delivery month must be prepared to perform all of their obligations in the delivery process, *i.e.,* making or taking delivery of the underlying commodity. Participants who are not so prepared cannot assume they will be able to offset in the futures market without experiencing the prospect of an adverse price movement." (p.28-29)

The *olkart* court voiced this same concern, quoting the NY Cotton Exchange's argument against giving a "license . . . to all traders holding short positions to disregard their obligations to deliver under futures contracts."

At the same time, longs also owe no less of a responsibility to the marketplace. When shorts choose to deliver, longs must be prepared to take delivery. Also, large long traders entering a shortage situation cannot flex their market muscle specifically intending to create "artificial" prices. Chairman Philip M. Johnson, in his concurring opinion in *Indiana Farm,* noted that, as a technical matter, the legal rights of long traders to exact high prices from shorts during innocent market congestions are not unlimited. Irresponsible action by longs can unquestionably create as much havoc with orderly trading as irresponsible action by shorts. True, the Commission is not in business to protect experienced short traders from the effects of their trading mistakes, nor should it protect long traders unable to take delivery. However, laws against market manipulation exist not only to protect traders in the pits, but also to protect the general public outside the exchange building which relies on the economic efficiencies achieved through the hedging and price discovery functions of regulated futures markets.

Chicago Board of Trade officials acted in a highly responsible manner when they contacted Mssrs. Cox and Frey, as well as the representative of Cook Industries, before trading opened on May 19 asking their cooperation in the contract liquidation. The Commission itself sometimes expresses concern through its market surveillance staff to traders holding large positions late in a delivery month to avoid manipulation or disruption. Chairman Johnson, in his *Indiana Farm Bureau* concurrence, explained that giving too much latitude to the longs could undermine these efforts.

"Natural supply shortages, accompanied by substantial long positions in the market, are not uncommon, and they have always warranted special vigilance. The exchanges frequently notify large traders of their overriding responsibility to the marketplace under these circumstances and, in the main, traders act to avoid a major market disturbance. . . . Under the majority's formulation, however, longs who do not intentionally create or exacerbate the market congestion might feel free to demand as high an offset price from shorts as possible" (p. 27,294)

-- perhaps even prices bordering on "artificial."

The facts in this case indicate that Cox and Frey did more than simply stand by and passively reap the rewards of a pre-existing supply shortage -- rather, they actively aggravated the problem both prior to and during the day on May 19.

Cox, for instance, maintained a large futures position (just below the speculative limit) for 3 1/2 months as open interest steadily declined. He made no real effort to offset this position in the pit until the last half hour of trading. He then offered to liquidate only through limit (rather than market) orders, n8 and further aggravated supply problems by stopping delivery notices at the earliest possible moment even though he had no commercial use for wheat himself and no firm commitments to sell wheat to others in the cash market. He held onto his cash wheat until the end of the delivery period before making delivery on his own closing short position (thereby effectively blocking any redeliveries of the wheat). Frey, meanwhile, increased his long position by 110,000 bushels on May 17 and 18 and failed to liquidate his own position before the close of trading even though he had no commercial use for wheat and no firm plans to sell wheat in the cash market. In the *Indiana Farm Bureau* decision, the Commission specifically criticized such tactics. "[Where], once the congested situation becomes known to him, the long exacerbates the situation by, for example, intentionally decreasing the cash supply or increasing his long position in the futures market," a manipulative intent could be inferred, it said. (P 21,796 at p. 27,289, fn. 12) Certainly, substantial evidence exists on this record for the Commission or Judge Duncan to find that Cox and Frey "exploited" or "exacerbated" the market situation in the manner contemplated by the *Indiana Farm Bureau* holding.

n8 "Limit orders" are orders to buy or sell only at a specified price rather than at the market's price.

The majority opinion states the "causation" prong of a market manipulation case now requires a showing of "proximate" cause, a concept drawn from tort law implying not only that the acts of the respondants resulted in the effect, but also that they "played a substantial part" in producing the outcome, and that the result was a "direct result" or "reasonably probable consequence" of these actions. As a result, the majority says, even if the price effect would not have occurred *but for* the actions of the respondents, it would not find causation where "multiple causes" exist which "cannot be sorted out."

Under this rationale, the Commission finds that actions of the major short in the market, Cook Industries, were also a "major cause" of the May 19 price rise, particularly Cook's failure to adequately prepare for delivery and its spreading of false rumors about its delivery plans. At this point, the majority concludes that Judge Duncan had erred in sustaining the charge of manipulation "without first sorting out the multiple causes."

In fact, however, Judge Duncan did consider the argument raised by Cox and Frey that, as a policy matter, shorts traders should not be protected from the adverse price impact which may occur when they hold large positions late in a contract delivery month without making adequate preparations to deliver. Even where the shorts have contributed to market congestion in this regard, he points out, "the Act mandates that the futures market price shall not be an intentionally manipulated price." (Initial Decision, p. 36) I agree with Judge Duncan. The large shorts may have created an opportunity for mischief by failing to prepare adequately for their delivery responsibilities, but this fact does not break the proximate causal link between the actions of Cox and Frey and the resulting price effect where the evidence suggests that they exploited and exacerbated that supply problem with the specific intent and ability to move the market at will.

At the bottom line, we are faced here with a situation where neither the longs nor the shorts come to us with clean hands. Still, our precedents mandate that if in fact Messrs. Cox and Frey took affirmative actions in the marketplace on May 19 specifically intending to raise prices to "artificial" levels and if such "artificial" prices resulted, then we must find them liable for a "manipulation," regardless of whether the shorts, through their own neglect, actually created the opportunity for the manipulation or worsened its effect.

If a bank leaves its vault open overnight and a burglar takes the money, the burglar cannot escape guilt based on the bank's negligence. If Cook was guilty of spreading false market rumors designed to depress prices, then perhaps Cook should have been named a respondent in a separate enforcement action. Its potential wrongdoing, however, does not excuse that of Cox and Frey. Two wrongs do not make a right.

History demonstrates that the legal standards for establishing a market manipulation case -- ability, specific intent, artificial price, causation -- are more than sufficient to prevent frivolous prosecutions from being brought against long traders who simply take innocent advantage of a lucky turn of events in the trading environment. However, the CEA makes clear that there are limits to acceptable market behavior. The regulated futures pit is not an insulated battleground between longs and shorts. Where any trader steps over the line and deliberately exploits or exacerbates an preexisting supply shortage to the extent of damaging the futures pricing mechanism, then the victims are not only the other traders in the pit but all producers, processers, retailers, and consumers across the country who depend on the market for its proper economic functioning.

III. *Artificial Prices*

The majority rejects Judge Duncan's finding that artificial prices existed during appromimately the final hour of trading on May 19, 1971, when short traders finally offered to pay Messrs. Cox and Frey's price of $ 1.70 per bushel for their wheat contracts. The Judge concluded based on his analysis that wheat futures prices that day "at $ 1.67 or above were abnormal or artificially high." (I.D. P 105) The majority says:

"Stripped to its essentials, the initial decision stands for the proposition that there was a price aberration at the close of trading in May wheat futures, but that it was of small magnitude and short duration." (p.22)

Section 9(b) of the Commodity Exchange Act, of course, does not outlaw only big manipulations -- all manipulations of any size are prohibited. n9 The fact that respondents may have used their firepower to push prices only a few cents per bushel beyond natural levels does not undo the illegality committed. In fact, I would not characterize the price movement in this case as being of "small magnitude." A tainted 3 cent advance on 2.2 million bushels of grain, as is alleged here, would yield profits of $ 66,000 -- no small amount.

n9 "It shall be a felony . . . for any person to manipulate or attempt to manipulate the price of any commodity in interstate commerce, or for future delivery on or subject to the rules of any contract market, or to corner or attempt to corner any such commodity . . . ." CEA Section 9(b).

More troubling to me, however, is the wide path which the majority cuts in rejecting Judge Duncan's holding. As precendent for future enforcement actions, the majority leaves few guideposts by which market participants and Commission staff will be able to evaluate future conduct.

In reaching his conclusion that prices were artificial, Judge Duncan compared the May 19 price movement in the Chicago May futures contract to prices in related futures and cash markets. Specifically, he found that:

-- Prices of the September, December, March, and July 1971 wheat futures contracts had traded in a consistent daily pattern with the May contract over a period of six months with the single exception of one day, May 19, the day of the alleged manipulation;

-- The price spread between the May and July delivery contracts had also followed a consistent pattern during delivery months over the prior 10 years with the sole exceptions of 1963 [found to have been a manipulated market in *Cargill v. Hardin, supra*] and May 19, the day of Messrs. Cox and Frey's alleged manipulation;

-- Prices of the comparable wheat contracts at the Kansas City Board of Trade and the Minneapolis Grain Exchange failed to display any upward movement on May 19 similar to the price move on the CBT contract;

-- Cash market prices throughout May, as supplemented by extensive testimony from commercial businessmen, also demonstrated the unusual nature of the futures price movement. With scant commercial demand, Judge Duncan found no cash transactions in either of the wheat classes normal to Chicago -- No.2 soft red winter and No.2 yellow hard winter wheat -- above $ 1.67 per bushel and only two between May 13 and 25 above $ 1.60. On May 19, the day of the alleged manipulation, both classes of wheat sold for $ 1.58 in the cash market -- far below the $ 1.70 futures price. Since May 19 was the last trading day on the May contract, when cash and futures prices normally *converge,* this disparity is particularly significant. Similarly, bids by five major commercial firms for Chicago wheat during May were substantially lower than the May 19 closing futures price. I attach two charts from Judge Duncan's opinion to this dissent which dramatize these comparisons.

The inevitable conclusion I must draw from these data is that the 3 cent price movement of May 19 which Judge Duncan found to be artificial was a singular phenomenon occurring solely on the Chicago Board of Trade May wheat futures contract during the last hour of trading *and no place else* -- not the cash market, not other CBT futures contracts, and not futures contracts traded on other exchanges. I agree with Judge Duncan, the trier of fact, who personally presided at lengthy hearings on the subject, in concluding that "artificial" prices occurred.

The majority opinion disputes Judge Duncan's conclusion on the grounds that he looked at the wrong data. In explaining what data the Judge should have considered and why, however, the majority again raises more questions than it answers.

First, the majority uses *Indiana Farm Bureau* as authority to reject Judge Duncan's use of "historical price comparisons." On this basis it casts aside as irrelevant Judge Duncan's demonstration that on May 19, the CBT May wheat contract price deviated from a consistent decade-long price pattern for no discernible reason other than the actions of two long traders. The majority has stepped far beyond the *Indiana Farm Bureau* precedent in this regard. Specifically, the Commission's decision to look beyond historical price trends in *Indiana Farm Bureau* was based on an unusual set of factors, particularly actions by the federal government. As it explained in that case:

"[Historical] price comparisons of the type relied upon by the courts in *Cargill* and *G.H. Miller* are of limited probative value here because of the unique combination of circumstances which led to the price rise in the corn pit on July 20, 1973." (p. 27,286)

The Commission in that case felt obligated to justify at length its decision to look beyond the traditional price comparisons which courts have required for decades. The decision was hardly automatic. Unfortunately, the majority opinion today *states no specific reasons whatever* why the market for May 1971 wheat differed in any way from that of earlier years or months. n10 Rather, the majority reverses the clear presumption in *Indiana Farm Bureau* that such historical price evidence is relevant unless circumstances dictate otherwise. In its opinion, the Commission

"[recognizes] that the prospective behavior of a 'normal' market is not necessarily bounded by the market's historical experiences. While historical and spread data may be used in future cases, it is incumbent on the parties to explain or justify the relevance of such evidence." (p. 17)

In other words, the fact that prices are shown to be unusual, unprecedented, singular, or out of the mainstream is no longer presumed relevant or indicative to demonstrating whether they are "artificial." What, then, *is* relevant to this analysis?

n10 In fact, the majority points out that May is a "transition period" in Chicago when commercial wheat demand is low -- a factor which would support Judge Duncan's finding that the May 19 price jump was abnormal. (p. 2)

In *Indiana Farm Bureau,* the Commission wrestled with this question and concluded that the "legitimacy" of the market factors causing a particular price movement is as important as the unique nature of the price in demonstrating artificiality. Specifically, it said:

"When the aggregate forces of supply and demand bearing on a particular market are all legitimate, it follows that the price will not be artificial. On the other hand, when a price is affected by a factor which is not legitimate, the resulting price is necessarily artificial." [p. 27,288, fn.2]

Indiana Farm Bureau did not attempt to define what it meant by a "legitimate" economic force. The analysis, however, appears to envision that "legitimate" supply and demand factors could include any regular commercial activities or other price determinants beyond the control of respondents like Cox and Frey. Specifically in *Indiana Farm Bureau,* the Commission decided to include certain factors unique to the futures market as legitimate:

"The tight corn supply and Indiana Farm's standing for delivery were legitimate forces of supply and demand which caused futures prices to rise. The panic bidding of shorts who were totally unprepared to deliver caused the most dramatic spurt in prices." *Indiana Farm* p.27,286.

While I am troubled by the same questions about the Commission's reasoning in *Indiana Farm Bureau* on this point as was Chairman Johnson in his concurring opinion, n11 the case before us today differs substantially from *Indiana Farm Bureau* in this regard. Rather than the "legitimate" factors discussed there, the key ingredients of the May 19 price jump in CBT May wheat involved a trading abuse unique to that market. Cox and Frey were not commercial grain dealers as was the Indiana Farm Bureau Cooperative Association -- they were speculators. "Panic bidding" by shorts cannot be blamed for raising prices -- rather, Cox and Frey set goals of about $ 1.70 per bushel and then imposed it on the marketplace through "limit orders." Neither did the large long position held by Mr. Frey in the pit reflect normal "legitimate" speculation, but was the result of two speculators' combining their separate accounts into a single dominant market force. But for the deliberate actions of the longs, the price deviation would not have occurred.

n11 "The majority's decision poses an intellectual dilemma On the one hand, if *all* influences in the futures market are absorbed into the supply/demand equation, it would follow logically and almost automatically that no futures price could be considered artificial, even if it deviated dramatically from other prices for the same commodity," Johnson said, adding, however, that "if less than all futures market influences are to be included, we should provide clearer guidance to identifying what the majority classes as "illegitimate" factors, an arduous task that has not been undertaken here." Johnson concurrence, *Indiana Farm Bureau* p.27,295 fn.8.

Having rejected "historical data" from the Chicago market, the majority turns instead to historical data from the Kansas City market -- that wheat futures on the Kansas City Board of Trade rose more than 5 cents between May 5, and 18, somehow justifying a similar, sharper price rise later in Chicago. How? This is unclear. The majority also relies on after-the-fact data, arguing that the

Chicago July future rose substantially during the several weeks following May 19. From a sheer economic viewpoint, this comparison is faulty on two grounds. First, the May future was a "spot" contract experiencing its liquidation while the July contract in late May and early June was not yet even in its delivery month. As a result, different economic characteristics between the two could be expected. n12 Also, as the majority opinion itself points out, prices for the May and July contracts reflect different crop years. It says:

"The May futures contract is the last contract that discovers prices of old crop wheat; the July futures contract is the first contract that discovers prices of new crop wheat." (p.2)

More importantly, though, *Indiana Farm Bureau* emphasized that the essence of price artificiality is that the price "did not reflect the legitimate forces of supply and demand in the particular market *at the time of the alleged manipulative activity".* (p.27,283 emphasis added) Judge Duncan's "historical" analysis demonstrated how the CBT May contract deviated from the norm at the time of the Cox and Frey sales -- following the *Indiana Farm Bureau* standard. If price normalcy is to be an issue at all then Judge Duncan's analysis should prevail, and not the majority's analysis of data on prices in Kansas City two weeks beforehand or its analysis of prices in Chicago two weeks afterward.

n12 The basic behavioral difference to be expected would be "convergence," defined by the CFTC's "Glossary" as "The tendency of prices for physicals and futures to approach one another, usually during the delivery month." *See* "Glossary of Futures Trading Terms," *Commodity Futures Trading Commission Annual Report 1985.*

Finally, aside from pointing to certain other isolated transactions, the majority criticizes Judge Duncan for not including in his analysis a review of prices for more expensive premium out-of-town grades of wheat, specifically "hard red winter wheat" whose price touched $ 1.71 per bushel two days later on May 21. As the initial decision explains, however, inclusion of these prices would seriously distort the analysis. Prices for these premium wheat grades incorporate the very factors which have led Courts for at least the last 35 years to exclude these distant sources from their calculations of deliverable supply. n13 As Judge Duncan observed:

"The Chicago Board of Trade wheat futures contract discovers prices for the cheapest or least expensive wheat expected to be delivered." The out-of-town wheats "had a transportation expense added to their cost and also had milling characteristics and specified protein content making them more expensive." [I.D. P 107]

n13 *See* fn.7, *supra,* concerning how earlier decisions have treated the presence of exchange-set price premiums or discounts in analyzing out-of-town supplies.

By definition, these prices are abnormal and non-economical for Chicago. No one in Chicago would pay these prices unless forced by market irregularities. For the same reasons that I would exclude these wheat classes in calculating deliverable supply, I would exclude them from an artificial price formula as well.

The majority opinion leaves us with a very serious question. In a future case, what evidence must the Enforcement Division or private litigants present in order to demonstrate "artificial" prices? Will *any* set of data prove good enough? Under the majority's interpretation, historical prices are now presumed irrelevant. Local prices are deemed irrelevant. Contemporaneous futures and cash prices are deemed insufficient. The concept of price "artificiality" must have some context, a time and place. A price can only be "artificial" compared to some other contemporaneous price which we consider "natural" or "legitimate." Simple logic would tell us to begin the inquiry as Judge Duncan did, by looking to see whether the price of a suspect market is abnormal, suggesting the presence of some cause outside the usual supply and demand factors. A showing at this point that the aberration was caused by albeit-unusual but "legitimate" forces, as occurred in *Indiana Farm Bureau,* presumably would end the inquiry under that precedent.

If, however, it can be demonstrated that the unusual price effect can be traced to non-"legitimate" actions taken by the alleged manipulators which were specifically designed for that purpose, then, assuming the requisite showing of "intent," those prices should be viewed as "artificial" even under the most restrictive reading of *Indiana Farm Bureau.*

Based on the record before us, the market operation of Mssrs. Cox and Frey on May 19 was carefully targeted at a single futures expiration month in a single city on a single exchange. Within that modest context, it created a movement in prices which was abnormal and unexplainable. No "legitimate" commercial or economic factor is in evidence other than the concerted actions of two floor traders designed to fleece extra dollars from the market. The "artificial" price movement might have been only 3 cents and short-lived, but it existed and was a clear violation of the law.

Conclusion

Based on the above analysis, I see no reason to reverse Judge Duncan's decision in this case. Judge Duncan's opinion establishes each of the four elements stated by the majority as necessary for finding a market "manipulation": ability to influence prices, causation, artificial price, and intent (which the majority does not question in its opinion outside of a single footnote, fn. 5). For these reasons, I respectfully dissent. n14

n14 My dissent is limited to the question of liability of Messrs. Cox and Frey based on the majority's application of relevant law regarding the nature of market manipulations. I state no view on the discovery issues raised by respondents on appeal.

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