**UNITED STATES OF AMERICA**
**BEFORE THE**
**COMMODITY FUTURES TRADING COMMISSION**

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| In the Matter of | CFTC Docket No. 01-05 |
| Scott N. Szach<br>10 South 042 Clarendon Hills Road<br>Hinsdale, Illinois 60521 | ORDER INSTITUTING PROCEEDINGS PURSUANT TO SECTIONS 6(c) AND 6(d) OF THE COMMODITY EXCHANGE ACT, AS AMENDED, MAKING FINDINGS AND IMPOSING REMEDIAL SANCTIONS |
| Respondent. | |

I.

The Commodity Futures Trading Commission ("Commission") has reason to believe that Scott N. Szach ("Szach") has violated Sections 4d(2), 4g(a) and 6(c) of the Commodity Exchange Act, as amended ("the Act"), 7 U.S.C. §§ 6d(2), 6g(a) and 9 (1994), and Commission Regulations 1.10(d), 1.12(h), 1.18(a), 1.20 and 166.3, 17 C.F.R. §§ 1.10(d), 1.12(h), 1.18(a), 1.20 and 166.3 (2000). Therefore, the Commission deems it appropriate and in the public interest that a public administrative proceeding be, and hereby is, instituted to determine whether Szach has engaged in the violations as set forth herein and to determine whether any order should be issued imposing remedial sanctions.

II.

In anticipation of the institution of this administrative proceeding, Szach has submitted an Offer of Settlement ("Offer") that the Commission has determined to accept. Without admitting or denying the findings herein, Szach acknowledges service of this Order Instituting Proceedings Pursuant to Sections 6(c) and 6(d) of the Commodity Exchange Act, As Amended, Making Findings and Imposing Remedial Sanctions ("Order"). Szach consents to the use of the findings herein in this proceeding and in any other proceeding brought by the Commission or to which the Commission is a party.[1]

[1] Szach does not consent to the use of the Offer or the findings in this Order as the sole basis for any other proceeding brought by the Commission, other than a proceeding brought to enforce the terms of this Order. Szach also does not consent to the use of the Offer or the findings in the Order by any other person or entity in this or any other proceeding. The findings made in the Order are not binding on any other person or entity named as a defendant or respondent in this or any other proceeding.

## III.

The Commission finds that:

### A. SUMMARY

From August 1997 until the end of December 1998, while acting as the Chief Financial Officer ("CFO") of Griffin Trading Company ("GTC"), a registered futures commission merchant ("FCM"), Szach engaged in unauthorized securities trading with the money of GTC and its customers. Szach attempted to conceal his activity by omitting and misclassifying his trading losses on GTC's books and records. As a result, GTC's books and records contained overstated and misclassified assets and were therefore not current and correct as required by Commission regulation. Szach also incorporated the overstatements and misclassifications into the Forms 1-FR-FCM ("1-FR") and Net Capital Computations which he signed and filed with the Commission on GTC's behalf.[2] To fund his unauthorized trading, Szach transferred or caused transfers to be made from GTC's customer segregated funds account ("the Seg Account"). Some of these transfers caused GTC to have less than the total amount of funds required to be on deposit in customer segregated accounts. Szach failed to report these instances of under-segregation to the Commission.

On December 30, 1998, GTC filed a voluntary petition under Chapter 7 of the United States Bankruptcy Code.[3] GTC's demise was caused by the trading of John Ho Park ("Park"), a customer in GTC's London branch office ("the London office") who, on December 21 and 22, 1998, sustained huge trading losses that neither he nor GTC was able to cover.

Szach was responsible for supervising all activity conducted in the London office. He did not, however, adequately supervise risk management activity there. He did not know relevant policies and procedures and took no steps to learn them; he did not insure that customer trading was monitored and permitted trading to occur that could not be monitored; he failed to institute written policies and procedures relating to risk management; and he failed to adequately supervise relevant personnel in the London office. As a result, Szach failed to identify Park as a customer who habitually breached his trading limits and whose trading ultimately forced GTC into bankruptcy.

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2 A Form 1-FR contains several sections, one of which is a Net Capital Computation. In some cases, GTC appropriately filed only the Net Capital Computation portion. For convenience, all relevant filings submitted by GTC to the Commission will be referred to as 1-FRs for the balance of this Order.

3 GTC actually ceased operations on December 23, 1998, after it fell below the applicable regulatory minimum net capital requirements.

B. RESPONDENT

Szach resides at 10 South 042 Clarendon Hills Road, Hinsdale, Illinois 60521. Szach was GTC's CFO during all relevant times. He has never been registered with the Commission in any capacity.

C. FACTS

1. SZACH'S UNAUTHORIZED SECURITIES TRADING.

a. Szach Lost More Than $2 million In Unauthorized Trading.

As GTC's CFO, Szach had access to and control over GTC's bank accounts, including its House and Seg Account. He was also responsible for the accuracy of GTC's books and records and for its regulatory accounting compliance. He alone prepared and filed GTC's 1-FRs.

In August 1997, Szach began to trade securities in a proprietary account owned by GTC. Szach funded his trading with money from GTC's Seg Account. Szach's trading in the proprietary account ("Unauthorized Trading Account") was neither known to nor approved by GTC's Owners and Directors and Szach took deliberate action to conceal his activity. On the whole, Szach's trading was very unprofitable and by December 23, 1998, when he confessed his activity, his losses amounted to more than $2 million.

b. Szach Falsified GTC's Books, Records And Filing To Hide His Trading.

Szach manipulated GTC's books and records in an attempt to hide his unauthorized trading. Szach intentionally omitted trading losses in the Unauthorized Trading Account from GTC's books and records, resulting in an overstatement of GTC's assets. On several occasions when Szach did adjust GTC's books to reflect his trading losses from the Unauthorized Trading Account, he improperly classified them on GTC's books.

Szach alone prepared and filed GTC's 1-FRs. He carried the overstatements and misclassifications related to his unauthorized trading into GTC's 1-FRs that he prepared, signed and caused to be filed with the Commission. The excess and adjusted net capital reported in these submissions were overstated as of each of the following month-ends and by the following amounts:

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| August 1997 | $ 10,759 |
| September 1997 | $ 1,715 |
| October 1997 | $ 40,180 |
| November 1997 | $ 63,292 |
| December 1997 | $ 94,000 |
| January 1998 | $ 100,099 |
| February 1998 | $ 121,039 |

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| March 1998 | $ 173,422 |
| April 1998 | $ 225,678 |
| July 1998 | $ 480,059 |
| August 1998 | $1,186,925 |
| September 1998 | $1,599,669 |
| October 1998 | $1,764,465 |

Szach adjusted GTC's books to reflect his trading losses for December 1997 and March, May and June 1998. These correspond to the times when GTC was audited, first by its outside auditor and then by its Designated Self Regulatory Organization ("DSRO").

GTC retained a certified public accountant to conduct an audit of its financial statements as of December 31, 1997. Part of that audit included confirmation of certain balances on GTC's General Ledger with independent third parties. If Szach had failed to account for the trading losses, as he had done in the past, and the accountants had attempted to confirm the balance in the Unauthorized Trading Account with third parties, the accountants could have found that the General Ledger was overstated by $108,000. By reclassifying the amount shown in the General Ledger as a current receivable, Szach concealed an overstatement that would have raised questions from the accountants about the Unauthorized Trading Account.

The same holds true for March, May and June 1998. As of the end of the month for these three months, Szach adjusted the General Ledger to reflect trading losses in the Unauthorized Trading Account. GTC's DSRO conducted an audit as of May 31, 1998. If Szach had not adjusted the Unauthorized Trading Account for the trading losses and the DSRO auditors sought to confirm the balance on the General Ledger, they would found that it was overstated by more than $153,397. The reclassification concealed an overstatement that would have otherwise raised questions about the Unauthorized Trading Account from the DSRO auditors.

c. <u>Szach's Transfers To Fund His Trading Caused GTC To Be Under-Segregated</u>.

But for the first transfer on August 12, 1997, that came out of GTC's House Account, almost all of the other transfers into the Unauthorized Trading Account came from GTC's Seg account. In its Seg Account, GTC typically maintained excess segregated funds, i.e., more money on deposit than was owed to customers. In most instances, the transfers to the Unauthorized Trading Account did not deplete the excess segregated funds and GTC, therefore, remained properly segregated.

On four occasions, however, between November 18, and December 22, 1998, GTC was under-segregated. On these occasions, funds were transferred from GTC's Seg Account to the Unauthorized Trading Account and another transfer was made from GTC's House Account into its Seg Account. The transfer from the House Account to the Seg Account was booked 'as of' the day of the transfer to the Unauthorized Trading

Account but did not actually occur until the next day. Neither Szach nor anyone else at GTC ever reported any of the instances of under-segregation to the Commission.

2. SZACH WAS A CONTROLLING PERSON OF GTC.

Szach exercised broad powers for GTC. All GTC accounting staff, both in its Chicago and London offices, reported to Szach and he was responsible for hiring, firing and preparing performance appraisals for those employees. Szach had access to and control over GTC's bank accounts and expenditures. Szach was ultimately responsible for all regulatory and compliance accounting matters in both the Chicago and London offices. He personally prepared, signed and filed GTC's 1-FRs. He negotiated and executed contracts. As a member of upper management, he attended monthly meetings with GTC Directors where all manner of business was discussed, policies were established and strategic planning was conducted. At these meetings, Szach participated in the decision to accept new customers including the Trading Group (identified below) and Park.

In addition to his responsibilities as CFO, in January 1997, Szach was placed in charge of GTC's London office. In that capacity, he was responsible for supervising all aspects of GTC's London operations, including risk management. After he became CFO, Szach estimated that 90-95% of his time was spent dealing with issues relating to GTC's London office. All London staff ultimately reported to Szach. He had authority to hire and fire personnel in that office and was responsible for preparing performance evaluations for high level personnel there.

On February 21, 1997, Szach became registered with the Securities and Futures Authority ("SFA") as GTC's Senior Executive Officer ("SEO").[4] As such, Szach was responsible for the effective management and control of GTC's London Branch, including risk management, and for compliance with SFA rules and regulations. In his capacity as SEO, Szach was responsible to the SFA for, among other things insuring that: GTC's London branch established relevant internal controls, including the effective management of risk; warning signals of problems were followed up and appropriate action taken; and an annual review was conducted to determine the effectiveness of the firm's compliance and monitoring procedures with the conclusions reported to the SFA.

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4 The SFA is the regulatory body responsible for overseeing the securities and futures sectors of the United Kingdom's financial services industry. The SFA operates under the oversight of the Financial Services Authority ("FSA"), which, until October 1997, was known as the Securities and Investments Board ("SIB"). The SFA requires firms to appoint an individual as the firm's SEO. This individual assumes the "[p]rimary responsibility for the effective management and control of a firm and for compliance with SFA's rules and regulations and all other regulatory requirements applicable to the business…"

3. SZACH FAILED TO SUPERVISE.

a. Background.

In September 1997, GTC accepted a trading group as a new customer (the "Trading Group"). GTC reserved the right to refuse to accept any new trader a group wished to add and this rule applied to the Trading Group. In March 1998, with GTC's permission, Park became a member of the Trading Group. Park lived in London and was registered with the SFA. Park traded for his own account and, as with other members of the Trading Group, GTC maintained an account for him designated as a Trading Group sub-account. Park opened his account with GTC on March 6, 1998 and initially traded on LIFFE.

In May 1998, GTC moved to new offices in London and Park was given an office within these new offices. In May 1998, GTC became a non-clearing member of Eurex.[5] On June 10, 1998, Park began to trade German Bund futures contracts ("bunds") on DTB (and later on Eurex). GTC's customers trading on Eurex could execute trades via computer or they could use an execution broker. Park, for example, frequently used an execution broker to execute many of his Eurex trades. Szach was contemporaneously aware of and permitted Park to use an execution broker.

A trader using an execution broker would call the broker to place the trade rather than key-punching the trade himself/herself. The execution broker would execute the trade and then advise the trader of the result. Once the trade was filled by the execution broker, the trade would be "given-up" to the clearing firm of which the trader ordering the trade was a customer. After the trades were given-up to the clearing firm, that firm had to accept those trades - a process often referred to as "taking them up." Unlike other exchanges, Eurex does not impose a time limit within which trades must be given-up by the executing broker.

b. Szach Failed To Account For Eurex's System

During all relevant times (and to this day) trading on Eurex ends for the day at 6:00 p.m. and the system shuts down completely at 6:30 p.m.[6] Any trades not accepted on the trading day in which they were executed must be given-up again the next day. Therefore, an unlimited number of trades could remain on the system overnight creating a risk to the clearing firm that would not be apparent until the next day. When the system slowed down, as often happened at the end of the day, trades could not be taken-up before the system shut down for the day.

[5] In September 1998, DTB merged with the Swiss Options and Financial Futures Exchange ("SOFFEX") to create the electronic trading platform and clearing house Eurex Deutschland ("Eurex"). As discussed in greater detail below, Park's trading on December 21 and 22, 1998, was conducted on Eurex.

[6] All times are given in GMT unless otherwise stated.

Szach was contemporaneously aware of these circumstances. Szach was aware that trades were being left on the system overnight more frequently between October and December 1998, and was specifically aware that this was happening with respect to Park's trades. He did not take steps to ascertain why this condition was occurring or what, if any, impact it had on GTC's ability to monitor customer trading. He failed to institute any procedures, written or otherwise, to address this condition, such as procedures to eliminate its occurrence or to ascertain and mitigate GTC's risk if it did occur.

c. Szach Failed To Implement Relevant Policies and Procedures.

Szach also failed to implement other relevant policies and procedures prescribed by GTC. At all relevant times, GTC had policies and procedures relating to risk management in place in its Chicago office that were intended to be implemented and enforced in the London office as well. Those policies and procedures included: obtaining give-up agreements, setting and documenting customer intra-day and overnight trading limits and monitoring customer trading. Szach was aware of these policies and procedures and was responsible for implementing and enforcing them in the London office.

i) Szach failed to implement "Give-up" policies.

One of GTC's policies in effect in both its Chicago and London offices was to execute a written give-up agreement with every execution broker that set forth the terms of their relationship. Szach did not insure that give-up agreements were obtained for traders in the London office. Despite the fact that Park was using an execution broker and Szach was so aware, no give-up agreement was executed between GTC and the execution broker that covered Park's Eurex trading.

ii) Szach failed to implement customer limit policies.

It was GTC's policy to set position limits, both intra-day and overnight, for its new customers, including those trading on Eurex. It was also GTC's policy to document the trader's limits in the account opening documents.

Park, like other GTC Eurex traders, was given an intra-day limit that was tied to the amount of money in his account. Thus, he could trade 1 contract for every £1,000 he maintained in his account at GTC. GTC did not permit Park to carry any position overnight - although, consistent with its custom and practice, it would consider a request to do so if made by Park in advance. The trading limits set by GTC for Park were not documented in any fashion.

As GTC's representative responsible for supervising risk management in the London office, Szach was responsible for implementing GTC's policy of imposing an intra-day and overnight limit on new customers. Szach, however, did not know what trading limits had been set for traders in the London office, including Park. He did not know how or when they had been set and simply assumed that they were in place. He took no steps to insure that Park was advised of his limits or to insure that Park's limits, or those of any other London customer, had been documented. Szach failed to implement customer monitoring policies.

It was GTC's policy to monitor the intra-day trading of its customers to supervise compliance with the limits it had imposed. It was also GTC's policy to confirm its customers' overnight position, if any. Yet, between May 1998 and September 26, 1998, GTC was unable to electronically monitor the trading by its Eurex customers effectively. During this time period, GTC did not compensate for this deficiency by performing the labor-intensive manual calculations that would have been necessary to monitor the trading. Even with electronic monitoring, GTC could not effectively monitor Park. For customers, like Park, who used an execution broker, GTC would not be aware of trades until they had been given-up by the execution broker.

If Eurex shut down for the day before all Park's trades could be taken up, the trades would have to be given-up again by the execution broker the next day. This happened on more than one occasion and happened more frequently between October and December 1998, and Szach was so aware. On these occasions, GTC staff did no more than ask Park about his position. Szach was aware that this was insufficient to comply with the GTC's policy of definitively ascertaining a trader's overnight position. He did not, however, insure that GTC staff took other independent steps to confirm Park's position.

At the time Park placed an order, GTC required that he complete an order ticket and give the ticket to GTC's back office staff so that they could claim trades given up by the execution broker. GTC staff testified that they also used these tickets to monitor Park's position but GTC did not require Park to time and date stamp the tickets. Moreover, there were numerous instances where Park did not provide his tickets to GTC staff in a timely manner. In the most extreme cases, Park locked his office door and refused to allow GTC back office staff access to obtain his tickets.

Additionally, there were numerous instances when trades had been given up by Park's execution broker but GTC back office staff had no tickets from Park and vice versa. In fact, Park had instructed the execution broker not to give-up trades to GTC until he had confirmed them and it appears that the execution broker complied with Park's request. This created delays in trades being given-up to GTC and corresponding delays in monitoring Park's net position. However, GTC staff, including Szach, were aware or should have been aware that there were unexplained delays because they could see trades for which they had no tickets from Park and see tickets for which there were no trades. Neither Szach nor any other GTC staff insured that the problem was corrected.

When Park began to trade through an execution broker, GTC was unable to electronically limit that portion of his trading. Nevertheless, GTC did not inform the execution broker of Park's limit or seek to obtain its agreement to enforce the limit GTC imposed or inform GTC when Park was near, at or over his limit.

d. Szach Was Not Aware Of Monitoring Procedures.

Szach knew little about what risk management procedures were in place in the London office. He assumed that a previous manager of the London office had instituted procedures but he did not know what they were. He did not attempt to learn them despite the fact that GTC was entering a new marketplace with unfamiliar technology.

e. Szach Failed To Institute Written Policies And Procedures.

Szach failed to insure that written policies and procedures relating to risk management were in place in the London office. No written policies or procedures existed relating to: execution of written give up agreements, documentation of customer limits, monitoring customers on a real-time intra-day basis, independent confirmation of a trader's overnight position, or creation of emergency procedures for mitigating large open positions.

f. Szach Failed To Supervise The Managing Director.

In supervising the London office, Szach worked closely with the Managing Director of the London office (the "Managing Director"). The Managing Director was the highest on-site authority in the London office and was responsible for managing all day-to-day operations there, including risk management. He reported on all issues directly to Szach and all London staff reported through him to Szach.

Szach failed to adequately supervise the Managing Director. Szach testified that he believed the Managing Director was inexperienced in monitoring risk and he admitted that he did not know what his "capacity was to monitor the risk or his ability to interpret the data that came across his desk." Szach also knew that the Managing Director came from "an administrative not a trading background."

Szach was also aware that with the rapid growth of the London office, "it was very difficult for [the Managing Director] to concentrate fully on everything that was under his grasp." In a June 1997 performance appraisal, Szach stated that the Managing Director needed to "develop a process for analyzing and monitoring risk on the London books, customer and house trading." Despite this knowledge, Szach relied exclusively on the Managing Director to bring problems to his attention, and took virtually no independent steps to insure that the Managing Director was identifying potential problems or issues.

g. Park's Breaches.

GTC's procedures for monitoring Park were inadequate. On at least five days before December 21st, Park breached his intra-day trading limit by substantial amounts and for substantial periods. For example, with limits ranging between 200 and 540 contracts, Park had positions from 1,088 to 5,775 contracts. In addition, on these days Park's volume spiked dramatically. For example, on one occasion, Park traded 15,000 contracts. His previous average volume had been 1,542 contracts. There were similar spikes on other days.

On December 21 and 22, 1998, Park placed the trades that ruined GTC. On December 21, 1998, Park had £978,000 (approx. $1,564,880) in his trading account at GTC. His intra-day position limit was therefore 978 contracts. Park's largest position on this date was 10,176 contracts. Park first breached his limit on this date at 10:49 when he accumulated a long position of 1,015 contracts. He steadily built his long position throughout the day.[7]

When Park stopped trading on December 21st, he had a long position of 10,128 contracts.[8] GTC's limit mandated that Park was not to carry any position overnight and the overnight limit imposed by the Trading Group was 50 contracts. By about 18:30, based on Park's order tickets and trades sought to be allocated to GTC by the execution broker, London back office staff calculated that Park had an overnight position of 950 contracts. At the time the Eurex system shutdown for the day, 2,750 contracts had been given up to GTC by the execution broker but had not yet been accepted by GTC as Park had not provided the underlying trading tickets.[9] GTC was or should have been aware that Park had an overnight position of at least 3,700 contracts. GTC's staff did not confirm Park's overnight position with the execution broker.

Park returned to his office at GTC on December 22nd already long 10,128 contracts and traded from the opening until approximately 10:20 a.m. when GTC staff instructed him to liquidate his position. During that time, he added almost 3,000 more contracts to his long position. At some point in the morning of December 22nd, London office staff realized there was a problem with Park's trading. They contacted the Managing Director who in turn contacted the Chicago office. At that point the damage had been done. GTC received margin calls of DM 5 million (approx. £1.78 million /

[7] Park built his position throughout December 21st as follows:

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|---|---|---|---|
| 10:49 | 1,015 | 16:46 | 8,037 |
| 13:33 | 2,109 | 17:10 | 9,006 |
| 13:56 | 4,036 | 17:57 | 10,047 |
| 16:19 | 5,076 | 17:59 | 10,176 |
| 16:30 | 6,315 | close | 10,128 |
| 16:37 | 7,145 | | |

[8] Park's overnight exposure to market movements was approximately DM 250,000 (approx. £89,000 or $142,400) per tick.

[9] There were a further 8,050 contracts that had yet to be given up by the execution broker to GTC.

$2.85 million) and DM 13.5 million (approximately £4.8 million / $7.68 million). Neither Park, the Trading Group nor GTC was ultimately able to satisfy the second margin call and GTC filed for bankruptcy protection on December 30, 1998.

## D. VIOLATIONS OF THE ACT AND COMMISSION REGULATIONS

### 1. Szach Filed False Reports (1-FRs)With The Commission And Aided And Abetted GTC's Filing Of Those False Reports.

Liability attaches pursuant to Section 6(c) of the Act for one who willfully makes any false or misleading statement of material fact in any report filed with the Commission or willfully omits to state any material fact required to be included. Willfulness is defined as acting intentionally or with reckless disregard of regulatory obligations. *In re Squadrito*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,262 at 38,828 (CFTC March 27, 1992).

Pursuant to Section 4g(a) and Commission Regulation 1.10(d), GTC is also responsible for filing 1-FRS with the Commission. Pursuant to Section 13(a), Szach is liable for aiding and abetting GTC's filing of false reports.

Liablity as an aider and abettor requires proof that (1) the Act was violated, (2) the named respondent had knowledge of the wrongdoing underlying the violation, and (3) the named respondent intentionally assisted the primary wrongdoer. *In re Nikkhah*, [Current Transfer Binder] (CCH) ¶ 28,129 at 49,888 (CFTC May 12, 2000). Only knowing and conscious assistance will suffice and recklessness is not enough. *In re Richardson Securities*, [1980-82 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,145 at 24,646 (CFTC Jan. 27, 1981). Such knowledge, however, may be inferred. *In re Lincolnwood Commodities*, [1982-84 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21986, at 28,255 (CFTC January 31, 1984).

In addition, Section 4g(a) of the Act and Commission Regulation 1.10(d) together require that FCMs file 1-FRs with the Commission. This duty is imposed directly on FCMs but as a practical matter this task is delegated to employees. In this case, GTC delegated to Szach. Such delegation does not impose a direct regulatory obligation on the employee. It does, however, create an opportunity for the employee to aid and abet an FCM's failure to meet its regulatory responsibility. *Cf. In re Nikkhah*, ¶ 28,129 at 49,888 (discussing FCM's Section 4g(a) record-keeping responsibilities and delegation to employees.)

The same conduct that establishes Szach's willfulness for purposes of Section 6(c) confirms his liability for aiding and abetting GTC's violation. Szach prepared and signed multiple 1-FRs and then caused them to be filed with the Commission. For each, Szach affirmed that all information contained therein was "true, correct and complete." Each of the filings was false either because it reflected overstated assets or because assets were misclassified. Szach took money out of an FCM corporate account and used it for his own individual purposes. He attempted to conceal his unauthorized activity and GTC's false filings flow directly from that prohibited conduct. He controlled every step in the process that led to the filing of the false forms. He may therefore be deemed to have aided and abetted GTC's violations and to have acted willfully for purposes of Section 6(c) as well.

2. Szach Was A Controlling Person Of GTC And Is Therefore Responsible For The Following Violations Attributable To GTC.

a. GTC's Violations.

Pursuant to Commission Regulation 1.18(a), GTC was required to maintain current books and records. As a result of Szach's failure to account for and/or his improper classification of the trading losses in the Unauthorized Trading Account, it failed to do so.

Pursuant to Section 4d(2) of the Act and Commission Regulation 1.20, GTC was required to segregate all monies received by GTC from customers to margin, guarantee or secure futures trading or contracts. On at least four instances from November 18, 1998 up to and including December 22, 1998, as a result of Szach's transfers into the Unauthorized Trading Account, GTC failed to do so. From on and after September 28, 1998, pursuant to Commission Regulation 1.12(h), whenever an FCM is or should be aware of any instance of under-segregation, it is required to immediately report that deficiency to the Commission. GTC failed to report the four instances of under-segregation to the Commission as required.

Commission Regulation 166.3 imposes on registrants an affirmative duty to "diligently supervise the handling by its … employees and agents … of all commodity interest accounts carried, operated, advised or introduced by the registrant and all other activities of its … employees and agents … relating to its business as a Commission registrant." A violation under Regulation 166.3 is an independent violation for which no underlying violation is necessary. *In re Collins*, [1996-1998 Transfer Binder] Comm. Fut. L. Rep. ¶ 27,194 at 45,744 (CFTC Dec. 10, 1997). If an adequate supervisory system was in place, Regulation 166.3 can still be violated if the supervisory system was not diligently administered. *Id.* This is a fact intensive undertaking. *In re GNP Commodities, Inc.*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,360 at 39,219 (CFTC Aug. 11, 1992, *aff'd in part and rev'd in part sub nom. Monieson v. CFTC*, 996 F.2d 852 (7th Cir. 1993). GTC, as a Commission registrant, had a duty to diligently supervise. As discussed at length above, it failed to do so. Relevant polices and procedures were not implemented and enforced in the London office, existing procedures were inadequate to effectively monitor certain customer trading, no written risk management policies and procedures existed and relevant personnel in the London office were not properly supervised.

Szach was a Controlling Person of GTC.

Szach was a controlling person of GTC pursuant to Section 13(b) of the Act. As such, he may be held liable for the violations attributable to GTC set forth immediately above. Controlling person liability exists pursuant to Section 13(b) of the Act for one who directly or indirectly controls any person who has violated any provision of the Act (or regulations promulgated thereunder) and who either acted with a lack of good faith or knowingly induced the acts that constitute the violation. Szach is liable as a controlling person because he:

1. Exercised general control over GTC;

2. Possessed the power or ability to control the specific transaction or activity upon which the primary violation was predicated; and

3. Acted with a lack of good faith or knowingly induced, directly or indirectly, the acts constituting the violation.

*Monieson v. CFTC*, 996 F.2d 852, 859 (7th Cir. 1993).

i) Szach exercised general control over GTC.

Control is defined as the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract or otherwise. *Monieson v. CFTC*, 996 F.2d at 859. Szach was GTC's CFO. He was personally and ultimately responsible for all GTC's internal and regulatory accounting. All Chicago accounting staff and all London staff reported to him and he made hiring, firing, promotion and compensation decisions regarding this staff. He approved expenditures and had signatory authority over GTC's bank accounts. He negotiated and executed contracts on behalf of GTC and participated in setting policy. Subject only to GTC's Directors, he had ultimate supervisory authority for the London office.

ii) Szach controlled the specific activity in question.

As to the second element set forth in *Monieson*, Szach possessed the power or ability to control the specific transactions and activity upon which the primary violations are predicated. Szach is charged as a controlling person for GTC's failure: (1) to maintain current books and records; (2) to segregate customer funds; (3) to report its under-segregated status to the Commission; and (4) to supervise. Respectively:
(1) Szach was ultimately responsible for the accuracy of GTC's books and records. In addition, he personally performed the accounting for the General Ledger. He personally recorded what he wanted to record when he wanted to record it with regard to his trading in the Unauthorized Trading Account. He was the only person with knowledge of his losses and failed to account for them accurately and honestly in GTC's journals. (2) Szach was personally responsible for the transfers that caused GTC to be under-

segregated. (3) As CFO, Szach was ultimately responsible for all GTC's regulatory compliance including compliance with GTC's reporting requirements. (4) Szach spent 90-95% of his time dealing with issues relating to the London office and personally supervised all aspects of activity there, including risk management.

iii) Szach knowingly induced GTC's failure to maintain current books and records and its failure to comply with its segregation requirements.

A controlling person knowingly induces the acts constituting a violation when, through a conscious act or omission, he causes, directly or indirectly, the controlled person to violate the Act or Commission Regulations. *In re Spiegel* [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,232 at 34,765 (CFTC August 21, 1986). The same evidence demonstrating his willfulness (with respect to GTC's false filings) also serves to confirm Szach's knowing inducement with respect to GTC's failure to maintain current books and records and its failure to comply with its segregation requirements.

These violations flow derivatively from Szach's unauthorized trading and his attempt to conceal it. He controlled all facets of that activity and did so alone. He engaged in unauthorized trading and failed to record and misclassified his losses on GTC's books. Szach caused the transfers that led GTC to be under-segregated. He was or should have been aware of the effect of those transfers. Constructive knowledge is sufficient. *Id.* at 34,767.

iv) Szach acted with a lack of good faith in failing to supervise GTC's London office.

A controlling person acts with a lack of good faith if he fails to maintain a reasonably adequate system of internal supervision and control or fails to enforce that system with reasonable diligence. *Monieson v. CFTC*, 996 F.2d at 860. As the individual responsible for supervising risk management in the London office, Szach was responsible for implementing GTC's policies and procedures in the London office. He was responsible for insuring that existing policies and procedures were adequate and, if not, for implementing and enforcing new ones.

Szach's lack of good faith is apparent from his lack of diligence in fulfilling his responsibility for critical activity in GTC's London office. Szach was aware of relevant policies but failed to insure that they were implemented and enforced in the London office. For example, Szach was aware that it was GTC's policy to: obtain an executed give-up agreement, set and document customer trading limits and monitor and enforce those limits. He failed to implement these policies. Key give-up agreements were not in place and trading limits were not documented. Szach insisted that procedures for monitoring Eurex risk were in place before he assumed responsibility for the London office but he did not know what they were and therefore could not have known whether they were adequate in light of the new technology. Szach was aware of instances in which Park's trades were not accepted by GTC on the day in which they were executed.

He did not investigate why this was occurring or institute procedures to insure that GTC was adequately advised of the attendant risk.

Furthermore, because he did not know - or try to learn - the trading limits set for GTC's London customers, he could not interpret relevant reports and did not follow up obvious warning signals relating to Park's trading. Had he done so, he would have known that Park had breached his limits by substantial amounts for substantial time periods on numerous occasions well in advance of his trading on December 21st and 22nd that destroyed GTC.

Szach relied on the Managing Director to monitor the intra-day trading of GTC's London customers and to bring any problems relating thereto to his attention. He took no steps or took inadequate steps to insure that the Managing Director was able to fulfill this responsibility and that he was doing so. He did this despite his knowledge that the Managing Director lacked relevant training and experience and that he was over-burdened.

Szach's lack of good faith is also evidenced by his failure to insure that written policies and procedures relating to risk management were in place in the London office. As set forth above, if such polices and procedures had been in place and enforced, Park may not have accumulated the large positions that ultimately bankrupted the firm, or at the least, would have mitigated the losses.

While Szach was involved in many activities relating to the London office, he exercised little if any supervision with respect to risk management. Policies and procedures that were in place and enforced in GTC's Chicago office did not receive similar treatment in the London office and Szach failed to insure that existing procedures were adequate. He failed to enforce GTC's system of supervision with reasonable diligence and this failure constitutes a lack of good faith.

IV.

## OFFER OF SETTLEMENT

Szach has submitted an Offer of Settlement in which he, subject to the foregoing: acknowledges service of this Order and admits the jurisdiction of the Commission with respect to the matters set forth in this Order; waives (1) the service and filing of a complaint and notice of hearing, (2) a hearing and all post-hearing procedures, (3) judicial review by any court, (4) any objection to the staff's participation in the Commission's consideration of the Offer, (5) all claims that he may possess under the Equal Access to Justice Act, 5 U.S.C. § 504 (1994) and 28 U.S.C. § 2412 (1994), as amended by Pub. L. No. 104-121, §§ 231-232, 110 Stat. 862-63, and part 148 of the Commission's Regulations, 17 C.F.R. §§ 148.1, et seq. (2000), relating to, or arising from this action, and (6) any claim of double jeopardy based upon the institution of this proceeding or the entry in this proceeding of any order imposing a civil monetary penalty or any other relief.

Szach stipulates that the record basis on which the Order is entered consists of the Order and the findings in the Order consented to in the Offer. Szach consents to the Commission's issuance of this Order, which makes findings as set forth herein and orders that Szach: (1) cease and desist from violating the provisions of the Act and the Commission Regulations he has been found to have violated; (2) be prohibited from trading on or subject to the rules of any contract market for a period of ten years from the date of this Order and all contract markets shall refuse him trading privileges, beginning the third Monday after the date of this Order; (3) liquidate all futures and options on futures positions held by him or on his behalf, or in which he has any beneficial interest, before commencement of the denial of his trading privileges; (4) be permanently prohibited from appearing or practicing before the Commission; (5) pay a contingent civil monetary penalty of up to $220,000.00 pursuant to a ten year payment plan; and (6) comply with his undertakings as set forth in the Offer and incorporated in this Order.

V.

## FINDING OF VIOLATIONS

Solely on the basis of Szach's consent, as evidenced by the Offer, and prior to any adjudication on the merits, the Commission finds that Szach violated Sections 4d(2), 4g(a) and 6(c), 7 U.S.C. §§ 6d(2), 6g(a) and 9 (1994) of the Act and Commission Regulations 1.10(d), 1.12(h), 1.18(a), 1.20 and 166.3, 17 C.F.R. §§ 1.10(d), 1.12(h), 1.18(a), 1.20 and 166.3 (2000).

VI.

## ORDER

Accordingly, **IT IS HEREBY ORDERED THAT:**

A. Szach shall cease and desist from violating Sections 4d(2), 4g(a) and 6(c) of the Act and Commission Regulations 1.10(d), 1.12(h), 1.18(a), 1.20 and 166.3.

B. Szach shall be permanently prohibited from trading on or subject to the rules of any contract market for a period of ten years from the date of this Order, and all contract markets shall refuse him trading privileges, beginning on the third Monday after the date of this Order.

C. Szach shall liquidate all futures and options held by him or on his behalf, or in which he has any beneficial interest, before commencement of the denial of his trading privileges.

D. Szach shall be permanently prohibited from practicing before the Commission pursuant to Commission Regulation 14.8, 17 C.F.R. 14.8.

E. Szach shall pay a contingent civil monetary penalty in the amount of up to $220,000.00, pursuant to a payment plan. Szach shall make an annual civil monetary penalty payment ("Annual CMP Payment") as directed by a monitor designated by the Commission (the "Monitor") on or before July 31 of each calendar year, starting in calendar year 2001 and continuing for ten years (or until the civil monetary penalty is paid in full, if that happens first).[10] Szach shall make each such Annual CMP Payment by electronic funds transfer, U.S. postal money order, certified check, bank cashier's check, or bank money order, made payable to the Commodity Futures Trading Commission, and sent to Dennese Posey, or her successor, Division of Trading and Markets, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, N.W., Washington, D.C. 20581, under cover of a letter that identifies Szach and the name and docket number of this proceeding. Szach shall simultaneously transmit a copy of the cover letter and the form of payment to the Monitor and to the Director, Division of Enforcement, Commodity Futures Trading Commission, 1155 21st Street, N.W., Washington, D.C. 20581.[11]

The amount of Szach's Annual CMP Payment shall consist of a portion of: (1) the adjusted gross income (as defined by the Internal Revenue Code) earned or received by him during the course of the preceding calendar year;[12] plus (2) all other net cash receipts, net cash entitlements or net proceeds of non-cash assets received by him during

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[10] Szach's ten year CMP period shall run from January 1, 2001 through December 31, 2010. Annual CMP Payments for a calendar year shall take place by July 31 of the following year. Therefore, the final Annual CMP Payment for the year 2010 will occur on or before July 31, 2011.

[11] Szach agrees that the National Futures Association is hereby designated as the Monitor for a period of ten years commencing from January 1, 2001. Notice to the Monitor shall be made to Daniel A. Driscoll, Esq., Executive Vice President, Compliance, or his successor, at the following address: National Futures Association, 200 West Madison Street, Chicago, IL 60606. For ten years, based on the information contained in Szach's sworn financial statements, tax returns and the other financial statements and records provided to the Monitor, the Monitor shall calculate the total amount of the civil monetary penalty to be paid by Szach for the year. On or before June 30 of each year and starting in calendar year 2001, the Monitor shall also send written notice to Szach with instructions to pay by no later than July 31 of that year the amount of the civil monetary penalty pursuant to the payment instructions provided above.

[12] It is the intent of the parties hereto that the CMP agreed to in this matter be paid solely from Szach's personal income, assets or receipts. If, therefore, Szach marries while he is still obligated to make payments pursuant to this agreement, no income, assets or receipts of his spouse should be taken into consideration by the Monitor in determining the payment to be made for any calendar year.

the course of the preceding calendar year. The Annual CMP Payment will be determined as follows:

| Where Adjusted Gross Income Plus Net Cash Receipts Total: | Percent of Total to be Paid by Szach is: |
|---|---|
| Up to $25,000 | 0% |
| $25,000 - 50,000 | 20% of the amount above $25,000 |
| $50,000 - $100,000 | $5,000 (this represents 20% of the amount between $25,000 and $50,000) plus 30% of the amount above $50,000 |
| Above $100,000 | $20,000 (this represents 20% of the amount between $25,000 and $50,000, plus 30% of the amount between $50,000 and $100,000) plus 40% of the amount above $100,000. |

Szach shall receive a dollar for dollar credit towards his Annual CMP Payment for any sum paid in criminal restitution. In the event that the amount of criminal restitution paid in a twelve month period covered by the Annual CMP Payment exceeds the required Annual CMP Payment, the excess criminal restitution shall not be credited against any future Annual CMP Payment.

F. In the event that Szach does not make payments as directed above, the Commission may bring a proceeding or an action to enforce compliance with this Order and at its option may seek payment of the unpaid Annual CMP Payment(s) or immediate payment of the entire amount of the civil monetary penalty required above. The only issues Szach may raise in defense of such enforcement action is whether he has made the Annual CMP Payment(s) as directed by the Monitor and/or whether the Monitor has correctly calculated the amount of the Annual CMP Payments in accordance with the terms of the Order. Any action or proceeding brought by the Commission compelling payment of the Annual CMP Payments, due and owing as set forth above, or any portion thereof, or any acceptance by the Commission of partial payment of the Annual CMP Payments made by Szach, shall not be deemed a waiver of Szach's obligation to make further payments pursuant to the payment plan, or a waiver of the Commission's right to seek to compel payments of the remaining balance of the civil monetary penalty assessed against him.

G. The Commission notes that an order requiring immediate payment of the civil monetary penalty against Szach would be appropriate in this case, but does not impose it based upon Szach's financial condition. Szach acknowledges that the Commission's acceptance of the Offer is conditioned upon the accuracy and completeness of the sworn Financial Statement dated August 1, 2000 and other evidence Szach has provided regarding his financial condition. Szach consents that if at any time following the entry of this Order, the Division of Enforcement ("Division") of the Commission obtains information indicating that Szach's representations concerning his financial condition were fraudulent, misleading, inaccurate or incomplete in any material respect at the time they were made, the Division may, at any time following the entry of this Order, petition the Commission to: (1) reopen this matter to consider whether Szach provided accurate and complete financial information at the time such representations were made; (2) require immediate payment of the full amount of the civil monetary penalty as set forth above; and (3) seek any additional remedies that the Commission would be authorized to impose in this proceeding if Szach's Offer had not been accepted. No other issues shall be considered in connection with this petition other than whether the financial information provided by Szach was fraudulent, misleading, inaccurate or incomplete in any material respect, and whether any additional remedies should be imposed. Szach may not, by way of defense to any such petition, contest the validity of, or the findings in, this Order, assert that payment of a civil monetary penalty should not be ordered, or contest the amount of the civil monetary penalty to be paid. If in such proceeding, the Division petitions for, and the Commission orders, payment of less than the full amount of the civil monetary penalty, such petition shall not be deemed a waiver of Szach's obligation to pay the remaining balance of the civil monetary penalty assessed against him, pursuant to the payment plan; and

H. Szach shall comply with the following undertakings, as set forth in the Offer:

1. <u>Reporting/Disclosure Requirements to be Reviewed by Monitor</u>. Szach shall provide his sworn financial statement to the Monitor on June 30 and December 31 of each calendar year, starting June 30, 2001, and continuing through and including December 31, 2010. The financial statement shall provide:

   a. a true and complete itemization of all of Szach's rights, title and interest in (or claimed in) any asset, wherever, however and by whomever held;

   b. an itemization, description and explanation of all transfers of assets with a value of $1,000 or more made by or on behalf of Szach over the preceding six-month interval; and

   c. a detailed description of the source and amount of all of Szach's income or earnings, however generated.

Szach shall also provide the Monitor with complete copies of his signed federal income tax return, including all schedules and attachments thereto (<u>e.g.,</u> IRS Forms W-2) and Forms 1099, as well as any filings he is required to submit to any state tax or revenue authority, on or before June 30 of each calendar year, or as soon thereafter, beginning in

2001 and ending in 2010. If Szach moves his residence at any time, he shall provide written notice of his new address to the Monitor and the Commission, through Phyllis J. Cela, Acting Director, Division of Enforcement, Commodity Futures Trading Commission, or her successor, at 1155 21st Street, N.W., Washington D.C. 20581, within ten calendar (10) days thereof.

2. Cooperation. Szach shall cooperate fully and expeditiously with the Monitor and the Commission in carrying out all aspects of his Annual CMP Payment. He shall cooperate fully with the Monitor and the Commission in explaining his financial income and earnings, status of assets, financial statements, asset transfers, tax returns, and shall provide any information concerning himself as may be required by the Commission. Furthermore, Szach shall provide such additional information and documents with respect thereto as may be requested by the Monitor or the Commission.

3. Fraudulent Transfers. Szach shall not transfer or cause others to transfer funds or other property to the custody, possession, or control of any member of his family or any other person for the purpose of concealing such funds or property from the Monitor or the Commission.

4. Registration With The Commission. Beginning on the date of this Order, Szach shall never: apply for registration or seek exemption from registration with the Commission in any capacity, and shall never engage in any activity requiring such registration or exemption from registration, except as provided for in Section 4.14(a)(9) of the Commission Regulations, 17 C.F.R. § 4.14(a)(9); act, directly or indirectly as a principal, officer or director of any person registered, exempted from registration or required to be registered with the Commission, unless such exemption is pursuant to Section 4.14(a)(9) of the Commission Regulations, 17 C.F.R. § 4.14(a)(9); act, directly or indirectly, in a supervisory capacity over any person employed by any person registered, required to be registered or exempted from registration, unless such exemption is pursuant to Section 4.14(a)(9) of the Commission's Regulations. In addition, for a period of ten years from the date of this Order, Szach shall be prohibited from being employed, directly or indirectly and in any capacity, with any person registered, required to be registered or exempted from registration, unless such exemption is pursuant to Section 4.14(a)(9) of the Commission's Regulations.

5. Practice Before The Commission. Szach shall never apply to the Commission for reinstatement pursuant to Commission Regulation 14.10, 17 C.F.R. § 14.10.

6. Public Statement. Neither Szach nor any of his agents or employees under his authority or control, shall take any action or make any public statements denying, directly or indirectly, any finding in this Order, or creating, or tending to create, the impression that this Order is without a factual basis;

provided, however, that nothing in this provision shall affect Szach’s (i) testimonial obligations; or (ii) right to take legal positions in other proceedings to which the Commission is not a party.

The provisions of this Order shall be effective on this date.

By the Commission:

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Jean A. Webb
Secretary to the Commission
Commodity Futures Trading Commission

Dated: January 8, 2001