UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

In the Matter of:	:	CFTC Docket No. 01-23
ANTHONY J. DIPLACIDO	:	OPINION AND ORDER

INTRODUCTION

This appeal arises from a ten-count Complaint issued by the Commission on August 21, 2001, charging that Anthony J. DiPlacido ("DiPlacido"), the sole remaining respondent in this case, manipulated and attempted to manipulate the settlement prices of electricity futures contracts on five occasions in 1998. The contracts in question were the Palo Verde ("PV") and California Oregon Border ("COB") contracts traded on the New York Mercantile Exchange ("NYMEX").[1] The case presents issues of first impression: the Commission has never considered a manipulation case based on allegedly manipulative trading floor practices in an adjudicated decision.

The Complaint also charged DiPlacido with aiding and abetting Robert S. Kristufek ("Kristufek"), an energy trader at Avista Energy Incorporated ("Avista"), and William H. Taylor ("Taylor"), an Avista Vice President, both of whom were named as respondents with DiPlacido,[2]

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[1] *In re DiPlacido, et al.*, [2000-2002 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 28,625 (CFTC Aug. 21, 2001). DiPlacido had been registered since 1979 as a NYMEX floor broker, whose NYMEX trading badge is "JADE." He also owned and was President of Energex, Ltd., a NYMEX registered floor broker association.

[2] The Commission entered into settlements with Kristufek and Taylor, on September 12, 2002, and September 30, 2003, respectively. *See In re DiPlacido*, et al., [2002-2003 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 29,153 (CFTC Sept. 12, 2002) and *In re William H. Taylor*, [2003-2004 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 29,594 (CFTC Sept. 30, 2003). The Commission found that both Kristufek and Taylor manipulated the settlement prices of NYMEX PV and COB electricity futures contracts on the dates at issue. Kristufek agreed to pay a $155,000 civil money penalty and to accept a 24-month trading ban, and Taylor agreed to pay a $155,000 civil money penalty and to accept a 30-month trading ban.

in manipulating and attempting to manipulate the PV and COB settlement prices.[3] In addition, DiPlacido was charged with non-competitive trading in furtherance of the alleged instance of manipulation that took place on July 27, 1998; and with recording and reporting the noncompetitively determined price as bona fide. Finally, DiPlacido was charged with failure to promptly produce documents during the Division of Enforcement's ("Division") investigation.

The manipulative misconduct in which DiPlacido was alleged to have engaged involved uneconomic trades executed on the NYMEX trading floor purportedly made with the specific intent to create artificial prices.[4] After conducting an oral hearing and reviewing the record created by the parties, an Administrative Law Judge ("ALJ") found DiPlacido liable for all counts of the Complaint. The ALJ imposed sanctions including a cease and desist order, a 20-year trading ban, a registration revocation, and a $500,000 civil money penalty.

DiPlacido raises both procedural and substantive challenges to the ALJ's decision. Procedurally, DiPlacido contends that the Commission was collaterally estopped from filing a complaint against him because NYMEX Compliance brought an action against him for the same conduct. In addition, DiPlacido argues that the ALJ denied him minimal due process, that the ALJ was biased, and that the ALJ improperly admitted certain tapes of telephone conversations into evidence.

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[3] At the same time this Complaint was filed, the Commission filed and simultaneously settled administrative proceedings against Avista, Former Avista Vice President of Trading Thomas Johns, and former Avista trader Michael T. Griswold, alleging the same manipulative scheme as in the DiPlacido Complaint. *See In re Avista Energy, Inc. and Michael T. Griswold*, 2001 WL 951736 (CFTC Aug. 21, 2001) and *In re Thomas A. Johns*, 2001 WL 951733 (CFTC Aug. 21, 2001). The Commission found that on the occasions at issue, Avista manipulated the settlement prices of the PV and COB electricity futures contracts. Avista agreed to a cease and desist order and a $2.1 million civil money penalty, Griswold agreed to an 18-month trading ban and a $110,000 civil money penalty and Johns agreed to a 12-month trading ban and a $50,000 civil money penalty.

[4] It should be noted that the NYMEX Floor Committee, which has responsibility for punishing trading violations on the NYMEX trading floor, *see* NYMEX Rule 3.20, took no action against DiPlacido for his conduct on the settlement dates at issue. DiPlacido later was charged with attempted manipulation by NYMEX Compliance for one of the settlement dates, and for the non-competitive trade and false reporting. Although NYMEX dismissed the attempted manipulation charge, it fined DiPlacido $50,000 and suspended him for 2 months for the non-competitive trade and false reporting charges.

Substantively, DiPlacido contends that the ALJ failed to apply the correct legal standard for manipulation, that the Division failed to prove that DiPlacido manipulated the settlement prices as alleged, that he had no notice that his conduct was improper and that even if he could be found liable, the ALJ imposed excessive sanctions. The Division defends the ALJ's liability findings and choice of nonmonetary sanctions, but cross-appeals the $500,000 civil money penalty and urges the imposition of a $1.1 million penalty on DiPlacido.

As noted above, this is the first time that the Commission has considered a manipulation case based on trading floor practices in an adjudicated decision. Those manipulation cases the Commission has decided were based on allegations of manipulation involving traditional market "corners" or "squeezes," through which the alleged manipulator unlawfully creates artificial prices on the futures market through control of the cash market, or by obtaining futures contracts requiring delivery of commodities greater than available supply. The trade practice based manipulation at issue in this case is based on the manipulation theory adopted by the Judicial Officer of the U.S. Department of Agriculture in *In re Henner*, 30 Agric. Dec. 1151 (1971), a case brought by the Commission's predecessor agency, the Commodity Exchange Authority.

In that case, the Judicial Officer, whose decision was the final decision of the agency,[5] concluded that Henner, through his trading activity on the trading floor of the Chicago Mercantile Exchange, "paid more than he had to . . . for the purpose of causing the closing price to be at [a] high level," and on that basis found Henner liable for manipulation. *Id.* at 1194.[6]

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[5] *Henner*, 30 Agric. Dec. at 1157.

[6] *Henner* has been mentioned by the Commission on occasion, but never exhaustively discussed in an adjudicated decision. *See, e.g., In re Indiana Farm Bureau Cooperative Assoc.*, [1982-1984 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,796 at 27,282 (CFTC Dec. 17, 1982).

Based on our review of the record, we believe that DiPlacido's procedural challenges are unpersuasive, and that on the merits, the evidence supports a finding that DiPlacido manipulated the PV and COB futures contract settlement prices on four of the five occasions at issue. DiPlacido does not address the ALJ's liability finding that DiPlacido aided and abetted Kristufek and Taylor in manipulating PV and COB settlement prices, which may be deemed admitted pursuant to Commission Regulation 10.102(d)(3),[7] and we believe is supported by the weight of the evidence.

DiPlacido also does not address his liability for the non-competitive, after hours trade in his appeal brief or reply brief and likewise pursuant to Commission Regulation 10.102(d)(3), the violations based on that trade are deemed admitted. The evidence also supports a finding that DiPlacido failed to produce documents in a timely manner. Based on our independent assessment of the record, we affirm the ALJ's cease and desist order and registration revocation, modify the ALJ's trading prohibition, and impose a civil money penalty of $1 million.

BACKGROUND

A. Procedural Background

The first five counts of the ten-count Complaint issued by the Commission focused on DiPlacido's alleged manipulative misconduct, charging him with manipulating and attempting to manipulate the settlement price of the PV electricity contract for the nearby delivery month on April 24, May 22, July 27, and August 25, 1998, and the COB settlement price on July 27, 1998,

[7] Commission Regulation 10.102(d)(3) provides that "[a]ny matter not briefed shall be deemed waived, and may not be argued before the Commission." 17 C.F.R. § 10.201(d)(3).

in violation of Sections 6(c), 6(d) and 9(a)(2) of the Commodity Exchange Act ("CEA" or "Act").[8]

Counts VI through VIII of the Complaint all stemmed from a single allegedly noncompetitive trade executed in furtherance of the manipulation on July 27, 1998, in violation of Sections 4c(a)(A) and 4c(a)(B) of the Act and Commission Regulation 1.38(a). Count IX, based on the same trade, charged DiPlacido with violating Section 4g of the Act and Commission regulation 1.35(d) by falsely recording and reporting the noncompetitively determined price.

Count X charged DiPlacido with violating Section 4g of the Act and Commission Regulation 1.31(a) by failing to promptly produce trading documents as required in response to a Commission-issued subpoena.

Nature of the Manipulative Scheme. With regard to the manipulative scheme, the Complaint alleged that prior to September 1998, Avista entered into over-the-counter ("OTC") derivative contracts, whose value at expiration was based on the daily settlement price of the NYMEX PV or COB electricity futures contracts on the last day of options trading (the "Options Expiration Day"), which was also the penultimate day of futures trading. The April, May, July and August dates on which the Complaint alleged that the manipulations occurred were the Option Expiration Days. On each of these days, the Complaint alleged that the daily settlement price was calculated by determining the weighted average of the prices of all trades executed during the last two minutes of the trading day ("the Close"). The Complaint further alleged that in comparison to other NYMEX energy futures contracts, such as natural gas or crude oil, the market for NYMEX PV and COB futures contracts in 1998 was small and illiquid.

[8] Each of these counts also charged DiPlacido, pursuant to Section 13(a) of the Act, with aiding and abetting Kristufek and/or Taylor in attempting to manipulate or manipulating the settlement prices on these dates.

The manipulative scheme alleged in the Complaint involved a variety of practices, including:

- selling NYMEX PV electricity futures contracts at prices less than the prevailing price during the April and May 1998 Options Expiration Days;
- purchasing NYMEX PV electricity futures contracts at prices higher than the prevailing price during the July and August 1998 Options Expiration Days;
- purchasing NYMEX COB electricity futures contracts at prices higher than the prevailing price during the July 1998 Options Expiration Day;
- entering into a noncompetitive trade; and
- placing large orders for NYMEX Western U.S. electricity futures contracts on the Options Expiration Days in April, May, July, and August 1998 without legitimate, economic reasons or considerations.

These strategies were employed in order to increase the value of Avista's OTC positions.

DiPlacido filed an Answer on March 6, 2002, in which he denied every count of wrongdoing and moved for dismissal of the Complaint based on various grounds, including that the allegations of the Complaint, even if true, did not meet the standards of manipulation under the Act and that the Complaint was barred by collateral estoppel by the NYMEX enforcement action.[9]

The ALJ conducted an oral hearing on December 2-3, 2003, during which the Division presented its case, and January 12-13, 2004, when DiPlacido presented his case. The Division's

[9] The ALJ considered DiPlacido's motion for dismissal as a motion for summary disposition pursuant to Commission Regulation 10.91. On April 24, 2002, the Division filed an Answer and Cross-Motion for Summary Disposition on Counts VI through X of the Complaint. DiPlacido filed a memorandum in opposition to the Division's cross-motion on September 16, 2002. The ALJ denied both motions on January 8, 2003, and indicated that the matter would proceed to hearing.

case consisted of CDs of recorded telephone conversations that Avista recorded of its traders, which included conversations between DiPlacido, his confederates at Avista and other NYMEX floor personnel. The Division called four authentication witnesses who testified regarding how the tape recordings were made of all Avista traders' telephone conversations, how they were stored, how they were prepared in response to the Division's request and the chain of custody between the time the tapes were produced to the Division and the hearing. In addition, the Division submitted the Declaration of Robert Livingstone ("Livingstone Declaration"), DiPlacido's floor clerk, who also gave live testimony. The Division also called four NYMEX floor brokers, who testified regarding their observation of DiPlacido's alleged misconduct; Kristufek; and DiPlacido himself. Finally, the Division called Dr. Hendrik Bessembinder ("Bessembinder") as its expert witness.

DiPlacido called three witnesses, including himself; Sanford Goldfarb, a NYMEX floor trader; and his expert witness, Dr. Albert S. Kyle ("Kyle"). Each of the experts filed written reports with the parties' pre-hearing memoranda in accordance with a pre-hearing order issued by the ALJ, and these reports were admitted into evidence at the hearing. The parties also filed exhibits.[10]

B. Evidence

The evidence shows the following with regard to the five Closes at issue, the after-hours non-competitive trade and the failure to comply with the Commission's subpoena.

[10] At the hearing, DiPlacido filed a motion, described as an Offer of Proof, to place in the record a 16-page unsigned and undated document that purports to be a supplement to the direct written testimony of his expert witness, Kyle. On January 26, 2004, the ALJ rejected DiPlacido's Offer of Proof. By letter dated January 27, 2004, DiPlacido again requested that the Court admit the supplement to Kyle's testimony into evidence. The ALJ deemed the letter to be a motion to reopen the evidentiary record, and denied the Motion on February 4, 2004.

1. <u>April 24, 1998 PV Close</u>

Immediately prior to the beginning of the April 24, 1998 Close, Taylor, the Avista Vice President, spoke with DiPlacido and placed an order for him to sell 50 May PV futures contracts. Tr. at 319-20; Ex. 19, p. 2.[11] Taylor instructed DiPlacido to "sell them down as hard as we can during the close," to which DiPlacido inquired "what's my limit down to?" Ex. 19, p. 2. Taylor told DiPlacido to "sell any number" because "we're trying to get a settlement," Tr. at 319-20; Ex. 19, p. 2, and that he wanted the sales to be "as low as possible." Tr. at 319-20; Ex. 19, p. 2. DiPlacido replied "OK, alright." Ex. 19, p. 2. Taylor placed an order to sell 10 more PV futures contracts at "market worst," which Livingstone, DiPlacido's floor clerk, relayed to DiPlacido. Livingstone indicated that although this instruction had little meaning to him at the time, he had come to understand based on his experience on the trading floor that this instruction to sell worst meant to sell at the lowest price possible. Tr. at 107, Livingstone Declaration, Ex. 1, ¶ 8.

Sometime after the April 24 Close, DiPlacido advised Livingstone not to use the term "worst" in relaying customer orders to him on the trading floor because DiPlacido might get in trouble with NYMEX for taking that kind of order from a customer. *Id.* Instead of saying "worst," DiPlacido instructed Livingstone to say "don't be shy," and DiPlacido would know that the customer wanted to be filled at the worst price. *Id.* DiPlacido also explained to Livingstone that he executed Avista's instructions to sell "worst" by taking out all existing bids (or offers, depending on what result Avista sought to achieve), or not acknowledging them, and then

[11] Citations to the record are as follows: "Tr. at ___" refers to the hearing transcript. "Ex. [number/letter]" refers to the exhibits introduced at the hearing. Numbered exhibits were introduced by the Division, and lettered exhibits were introduced by DiPlacido. In addition, seven CDs containing the recordings of the telephone conversations were admitted in their entirety as Exhibits 100-106, and written transcriptions of most of the relevant portions of these recordings were admitted as Exhibits 19-29, 31, 32, 34 and 38. Not all portions of the voice recordings were transcribed, however, and accordingly some of the citations refer to the recordings themselves. In these cases, the citation includes the exhibit number and the counter times of recorded conversations in minutes and seconds (*i.e.*, Ex. 100a at 0:00-1:00).

bidding (or offering) to trade at prices beyond those normally shown to the ring, instead of obtaining the best possible price for the customer. *Id.* As an example, if DiPlacido were trying to move prices lower and if a buyer was bidding at a certain price, DiPlacido would hit that bid (i.e. sell). Then, rather than offering to sell at what was typically the next increment, he would offer several increments lower. *Id.* At some point, DiPlacido explained to Livingstone that the reason Avista wanted to trade in this way had to do with its OTC option positions. *Id.*; Tr. at 125.

Livingstone testified that he observed DiPlacido trading in this manner during the April 24, 1998 Close, taking out bids and then offering at a much lower increment. Tr. at 124; Ex. 1, ¶ 8. DiPlacido sold 65 PV futures contracts for Avista during the April PV Close, generally at progressively lower prices. Ex. 15a; Ex. C; Declaration of Dr. Hendrik Bessembinder, ("Ex. 2"), ¶ 64. Another NYMEX member, Brian Caesar, acting at Avista's behest,[12] sold 20 contracts during the close. Ex. 14a; Ex. 14b; Ex. 2, ¶ 64. DiPlacido's trades accounted for 30.8% of the total trading volume. Ex. 2, ¶ 64. The settlement price of the May 1998 PV futures contract on April 24, 1998, was $24.14, a decrease of $.16 from the previous trading day. Ex. 2, ¶ 59, and p. 32 Table 1. The price was also $.41 less than the price of the last trade before the Close and $.31 less than the average price in the hour prior to the Close. Ex. 2, ¶ 45 and p. 32 Table 1. The settlement price decrease was completely reversed the next trading day, increasing to $25.03, which according to the Division's expert was one indication, among others, of price artificiality. Ex. 2, ¶ 55, and p. 32, Table 1.[13]

[12] Caesar's trading badge was "BWC."

[13] With regard to each of the Closes at issue, the Division's expert also noted that DiPlacido's orders in total were large relative to typical trading in the NYMEX electricity futures contracts, were all in the same direction (selling orders on the April and May Closes and buy orders during the July and August expirations), and were concentrated during the Closes. Ex. 2, ¶ 62.

2. May 22, 1998 PV Close

Kristufek placed orders with both DiPlacido and Caesar to sell June PV futures contracts "worst" during the May 22, 1998 Close. Tr. at 324; Ex. 24, p. 3; Ex. 23, p. 1. DiPlacido sold 150 PV futures contracts during the May 22 Close for Avista. Ex. 2, ¶ 64; Ex. 15b. Livingstone observed DiPlacido "violating bids" by offering at prices below the prevailing bid price in the pit. Ex. 1, ¶ 10. In a telephone conversation with Taylor after the May 22 Close, DiPlacido described how he executed Avista's orders. He compared himself to an aircraft carrier entering New York harbor and the other traders in the ring to sailboats trying to cross as he went by. Ex. 20, p. 1. DiPlacido added that "whatever bid they gave me, cause they were bidding for three's and two's, I offered right through them . . . I said 'sold,' 'at 20,' they gave me a 40 bid, 'at 20,' what do you guys want, so that made it very simple." Tr. at 326; Ex. 20, pp. 1-2. Livingstone testified that DiPlacido's statement that he "offered right through them" refers to violating bids or offering at prices below the prevailing bid, and that he observed DiPlacido trading in this manner during the May 22 Close. Tr. at 129-31.

During the May 22 PV Close, DiPlacido's trading represented 52.4% of the total trading volume in the Close. Ex. 2 ¶¶ 62, 64. The daily settlement price was $28.09 on May 22, 1998, a decrease of $.50 in the settlement price for the same contract on the previous trading day. Ex. 2, ¶ 59 and p. 32, Table 1. The settlement price decreased by $.53 relative to the average price during the hour before the Close, while the settlement price of the next nearby contract (July) increased over that same interval. Ex. 2, ¶ 46 and p. 32, Table 1.

3. July 27, 1998 PV and COB Closes

On the morning of July 27, 1998, DiPlacido told Livingstone he expected an electricity futures contract order from Avista, to be executed in the same manner as on the Option

Expiration Days in April and May 1998. Tr. at 94-95, Ex. 1, ¶¶ 12-13. DiPlacido directed Livingstone to find out if Avista wanted an additional broker to help DiPlacido execute its order. Ex. 1, ¶ 13. When Kristufek called Livingstone to say that he needed DiPlacido for the electricity futures closes that day, Livingstone asked him if he needed two traders. Ex. 28, p. 1. Livingstone told Kristufek he would contact NYMEX member Alfredo Dinten[14] to help DiPlacido with the order, and Kristufek was receptive to using two brokers. Ex. 28, p. 1. DiPlacido later told Livingstone he had decided that instead of Dinten, NYMEX member Sanford Goldfarb[15] should be the additional trader to assist with Avista's order. Tr. at 97; Ex. 1, ¶ 14; Ex. 3, ¶ 15. DiPlacido told Livingstone he wanted to use Goldfarb because he was a well-respected trader whom others in the ring would think had information about the direction of the markets. Tr. at 97-98, Ex. 1, ¶ 14. DiPlacido explained to Kristufek that using Goldfarb would be "a lot more believable if he walks in there first and starts selling it, the whole ring will think he's up or buying whatever way you want to go, the whole ring will think he knows something . . . . I'll walk in there behind him doing it . . . . Forget it, it's like murder." Ex. 38, p. 1.

Immediately before the PV close, Kristufek told Livingstone he wanted the settlement price to "go to the moon." Ex. 27, p. 1; Ex. 1, ¶ 16. Kristufek gave Livingstone an order to buy 250 PV futures contracts during the July Close, and to split up the order as Livingstone determined. *Id.* Livingstone then gave an order ticket to DiPlacido to buy 150 PV futures contracts, and one to Goldfarb to buy 100 contracts. Tr. at 100; Ex. 1, ¶ 16. Kristufek remained on the phone with Livingstone during the PV Close, instructing him that he wanted an "ugly" close, which Livingstone understood to mean disruptive, and to buy contracts at increasingly higher prices. Ex. 1, ¶ 17; Ex. 104m at 1:02-3:00.

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[14] Dinten's NYMEX trading badge was "FRDO." Ex. 1, ¶ 12.

[15] Goldfarb's NYMEX trading badge was TROT. Ex. 1, ¶ 14.

Livingstone stood immediately behind DiPlacido and could see his trading card from his location. Ex. 1, ¶ 17. He observed DiPlacido violate offers by bidding higher than the offers made during the July PV Close. Tr. at 102; Ex. 1, ¶ 19. He also testified that other traders came over to him and complained about the way DiPlacido had traded, specifically that DiPlacido was bidding through their offers. *Id.* In addition, NYMEX member John McCann testified that he observed DiPlacido violate broker NNJA by bidding to buy at $58.00 while NNJA was offering to sell at $57.00. Tr. 223-24. In a contemporaneous taped telephone conversation with Kristufek after the Closes, Caesar told him that he could have bought 2 PV contracts at $55.10, but then "all of a sudden, JADE went 55, 56, 56 bid, 57 bid, 58 bid." Ex. 25, p. 1.

DiPlacido bought 107 August PV futures contracts during the July 27 close for Avista, and Goldfarb purchased 100 contracts. Ex. 2, ¶ 64. Their combined purchases accounted for 60.5% of the total trading volume during the July PV Close. *Id.* The settlement price of the August PV futures contract on July 27 was $56.81, an increase of $2.89 from the previous day. Ex. 2, ¶ 58 and p. 32, Table 1. The following day, the settlement price decreased by $5.39, completely reversing the rise in settlement price. *Id.*

Following the PV close but before the start of the COB close, Kristufek told DiPlacido he needed him to have purchased all 250 PV futures contracts he ordered. Ex. 104m at 4:12-4:14. DiPlacido expressed surprise, asking "what do you mean you needed them all?" Ex. 10m at 4:14-4:17. Livingstone, who was present with DiPlacido during this conversation, believes DiPlacido was surprised because he understood that Avista's traders wanted to manipulate the settlement price, and not to just purchase a set number of futures contracts. Ex. 1, ¶ 17. Livingstone offered to get more PV futures contracts, but Kristufek told Livingstone not to buy more PV futures contracts unless they counted in the Close in determining the settlement price. Ex. 104m at 4:44-4:49; Ex. 1, ¶ 17.

Kristufek then gave Livingstone an order to buy 150 August COB futures contracts and said that he wanted the COB Close to be "ugly." Ex. 104m at 5:13-5:29; Ex. 1, ¶ 18. Just before the COB Close began, Livingstone verbally conveyed the order to DiPlacido, and added "don't be shy," the phrase DiPlacido had instructed Livingstone to use when an order was to be executed at the worst possible price. Ex. 1, ¶ 18. Kristufek remained on the phone instructing Livingstone during the COB Close to bid at higher prices, Ex. 104m at 6:01-6:54, and near the end of the close, instructed him to buy an additional 50 COB contracts.

Livingstone observed DiPlacido during the COB close violate offers by bidding at higher than the prevailing offers in the ring, Tr. at 102 and Ex. 1, ¶ 19, and heard complaints from other traders regarding DiPlacido's trading. *Id.* In addition, NYMEX Member McCann testified that he observed DiPlacido violate broker WLSH. Tr. at 224-25. Also in the COB Close, NYMEX member Anthony Birbilis testified that he observed DiPlacido violate broker GRAM by bidding to buy at $46.00, while GRAM was offering to sell at $45.50. Tr. at 241-42. In addition, Birbilis testified that he himself was violated by DiPlacido during the COB close, by bidding to buy at $46.00, while Birbilis was offering at $45.50. Tr. at 249.[16]

DiPlacido bought 182 August COB futures contracts during the July Close for Avista. Ex. 2, ¶ 64. His trading accounted for 34.7% of the trading volume during the July Close. *Id.* On July 27, the COB futures contract settlement price was $45.28, an increase of $3.26 from the settlement price of that contract on the previous trading day. Ex. 2, ¶ 58 and p. 32, Table 1. The

[16] Birbilis also testified that he heard complaints by traders that DiPlacido had violated offers during the July PV Close by aggressively bidding while the traders were offering at lower prices, although he did not directly observe DiPlacido making these trades. Tr. at 240-41.

following day the COB settlement price decreased by $4.79, completely reversing the rise in settlement price. *Id.*

4. After hours, noncompetitive trade on July 27, 1998

After the conclusion of both Closes, NYMEX member Patrick McHugh, who had a long position in COB futures contracts, approached Livingstone and offered to sell COB futures contracts. Tr. at 199-200; Ex. 1, ¶ 19. Livingstone called Kristufek and inquired whether he wanted to purchase more COB contracts. Ex. 1, ¶ 19. Livingstone told Kristufek that McHugh had a "problem" because he had overbought COB, and that "he'll get settlement wherever you want it . . . he'll work with us and get the settlement where we need it." Ex. 29, pp. 1-2. Kristufek then spoke with DiPlacido, who was with McHugh. Ex. 1, ¶ 19. Kristufek declined to purchase COB futures contracts from McHugh, but did agree to buy 25 more PV futures contracts from him, provided that the sale would count in the calculation of the settlement price. Ex. 1, ¶ 19; Ex. 1041 at 2:00-2:33. Kristufek, who told DiPlacido "I want the Palo close to be up there," initially proposed buying the 25 contracts from McHugh at a price of $57.00. Ex. 1041 at 2:21-2:37; Ex. 29, p. 3. DiPlacido then reminded Kristufek that, as things stood, the PV settlement was going to be above $57.00, and thus that price would "go the other way." (*i.e.*, reduce the settlement price) if they bought the additional contracts at $57.00. Ex. 1041 at 2:56-3:02; Ex. 29, p. 3. In response to DiPlacido's statement, Kristufek agreed to a purchase price of $58.00. Ex. 29, p. 3.

DiPlacido had purchased 10 PV futures contracts from McHugh during the PV close. Tr. at 202. After DiPlacido negotiated the additional 25-contract trade with McHugh after the end of trading for the day, DiPlacido altered his trading card, changing the quantity of the 10-contract trade to 35, in order to make it appear that all of his trading with McHugh was actually done on the floor during the July Close. Tr. at 202; Tr. at 294; Tr. at 296-97; Ex. 15c.

5. August 25, 1998 PV Close

On August 25, 1998, DiPlacido instructed Livingstone to call Kristufek to inform him that in view of a NYMEX investigation into DiPlacido's electricity futures trading of July 27, it would look good if Avista gave DiPlacido an order, as had been done on prior Options Expiration Days. Ex. 1, ¶ 23, Ex. 106a. Kristufek placed an order with DiPlacido to buy 75 September PV futures contracts during the August Close. Ex. 106g at 0:30-0:55 and 1:39-1:44. Livingstone indicated that there were complaints about the manner in which DiPlacido traded during the August Close. Ex. 1, ¶ 23. DiPlacido's trading accounted for 28.4% of the trading volume during the August Close. Ex. 2, ¶ 64. The settlement price of the September PV futures contract increased by $2.22 from the previous trading day. Ex. 2, ¶ 58 and p. 32, Table 1. The following day the settlement price decreased by $3.05, completely reversing the price increase. *Id.*

6. Failure to Comply Promptly with the Commission's Subpoena

On August 4, 2000, Commission representatives issued a subpoena to DiPlacido for production of certain books and records that he was required to maintain under the Act, including all records relating to his trading of PV and COB futures contracts for Avista in 1998. Tr. at 396; *see also* Ex. 8; Ex. 9, ¶ 86; Ex. 10, ¶ 86; Ex. 5c. The subpoena required DiPlacido to produce these documents by August 16, 2000. Ex. 8, p. 1. DiPlacido did not comply with this deadline. Tr. at 396. In October 2001, more than a year after the subpoena was issued, DiPlacido produced the documents responsive to the subpoena. *Id.*

C. DiPlacido's Testimony

DiPlacido testified regarding delays in obtaining records responsive to the Commission's subpoena from storage, and that he produced them to his attorney as soon as he received them. Tr. at 423-24. He also testified regarding a meeting between himself, his then attorney and trader Birbilis, during which DiPlacido claimed that Birbilis denied that he had been violated by DiPlacido or had seen others violated by him during the July Close. Tr. at 431-32. DiPlacido testified that he did not violate bids or offers during any of the Closes, Tr. at 433, 452, 480, and denied that he intended to manipulate settlement prices. Tr. at 480. He also testified regarding various terms used in the telephone conversations. For example, he claimed that when Taylor told him to sell market "worst" that meant to trade aggressively, Tr. at 443, that making a Close "ugly" meant active and noisy, Tr. at 462. He also provided generally innocent explanations to the telephone conversations noted above. DiPlacido further testified that he did not trade the low of either day and "beat" settlement during the April and May Closes, meaning that the average of his trades exceeded the settlement price, Tr. at 449, 452, and that he beat settlement during the July PV Close as well. Tr. at 467.[17]

D. Initial Decision

The ALJ issued his Initial Decision ("ID") on September 14, 2004.[18] The ALJ concluded that the testimony of the witnesses who testified on behalf of the Division was "credible, reliable and honest." ID at 5. On the other hand, the ALJ found the testimony of DePlacido to be "self serving and unreliable." *Id.* The ALJ found that Bessembinder's expert testimony was informed

[17] Goldfarb also testified on DiPlacido's behalf. Although he stated that he did not observe DiPlacido violating offers during the July PV Close, he indicated that he was paying attention to what he was doing and not paying much attention to others. Tr. at 519. Goldfarb also testified that he would not have executed the order during the July PV Close had he known of the conversation between DiPlacido and Kristufek noted above. Tr. at 521.

[18] *In re DiPlacido*, [2003-2004 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 29,866 (ALJ Sept. 14, 2004). Citations are to the slip opinion.

and persuasive, but that Kyle's expert testimony lacked specificity and dealt directly with only the PV Close of July 27, 1998. *Id.* He thus accorded Kyle's testimony very little weight. *Id.*

After making findings of fact generally consistent with the narrative above, the ALJ concluded that DiPlacido had violated Sections 6(c), 6(d) and 9(a)(2) of the Act during each of the 5 Closes at issue. ID at 17-18. In reaching this conclusion, the ALJ noted that in order for a charge of manipulation to be sustained, the Division must establish four elements by a preponderance of the evidence: (1) that the respondent had the ability to influence market prices; (2) that the respondent specifically intended to influence market prices; (3) an artificial price existed; and (4) the respondent caused the artificial price. ID at 11 (citing *In re Cox*, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,786 at 34,061 (CFTC July 15, 1987).

With regard to the first element, DiPlacido's ability to influence market prices, the ALJ noted that DiPlacido executed large orders during the Closes, violating offers and bids to raise or lower the settlement prices. Because of the illiquidity of the markets for PV and COB futures contracts, the ALJ found that DiPlacido had the ability to influence prices by executing the relatively large orders for Avista during the Closes. ID at 11.

Concerning the second element, whether DiPlacido had the specific intent to influence market prices, the ALJ noted that proving intent requires a showing that DiPlacido acted (or failed to act) with the purpose or conscious object of causing or effecting a price or price trend in the market that did not reflect the legitimate forces of supply and demand. ID at 12 (citing *In re Indiana Farm Bureau Cooperative Ass'n*, [1982-1984 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,796 at 27,283 (CFTC Dec. 17, 1982). The ALJ found that DiPlacido specifically intended to influence market prices through repeatedly violating bids and offers by offering at prices higher or lower than outstanding prices, and that his actions had no apparent business or economic rationale except to influence market prices. ID at 12.

With respect to the third element, that artificial prices existed, the ALJ noted that an artificial price is one "that does not reflect the market or economic forces of supply and demand" and that is created by illegitimate factors not intrinsic to the market. ID at 12-13. The ALJ found that DiPlacido's violation of bids and offers during the Closes and his non-competitive, after-hours trades were illegitimate factors, and concluded that the prices were artificial. ID at 13. Moreover, the ALJ found that artificial prices were created because on each date at issue, DiPlacido had paid more or less than was required, creating illegitimate factors and making the settlement prices artificial. *Id.* (citing *Henner* and the Judicial Officer's finding that "[t]he inference is inescapable that the respondent paid more than he had to . . . for the purpose of causing the closing price to be at that high level. No further proof is needed to show that the settlement price was artificial.").

Finally, with regard to the fourth element, causation, the ALJ noted that "causation of artificial prices is established when it is shown that artificial prices resulted from the conduct of a trader, or group of traders acting in concert, rather than from the legitimate forces of supply and demand." ID at 13 (citing *Cargill v. Hardin*, 452 F.2d 1154, 1171-72 (8th Cir. 1971). The ALJ found that DiPlacido caused the artificial prices during all of the Closes, by executing orders, all in one direction, outside prevailing prices, and which he knew would influence prices. ID at 14.

Having found that DiPlacido manipulated the settlement prices, the ALJ concluded that DiPlacido was additionally liable for attempted manipulation of the settlement prices during each of the Closes at issue. *Id.* The ALJ noted that proving attempted manipulation requires establishing only "an intent to affect the market price of the commodity and some overt act in furtherance of that intent." *Id.* (citing *In re Hohenberg Brothers*, [1975-1977 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,271 at 21,477 (CFTC Feb. 18, 1977). The ALJ found that DiPlacido had the specific intent to affect market prices and that "[a]ll of the steps DiPlacido took to carry out the manipulative scheme and cover it up constitute overt acts sufficient to sustain a count of attempted manipulation." ID at 14.

Citing the elements for aiding and abetting liability, the ALJ also found that DiPlacido aided and abetted the manipulation violations committed by Taylor and Kristufek.[19] ID at 15. In this regard, the ALJ concluded that the evidence established that the Act was violated, that DiPlacido had knowledge of the manipulation and DiPlacido intentionally assisted Taylor and Kristufek in manipulating the settlement prices. *Id.*

With regard to the non-competitive trade allegation, the ALJ found that DiPlacido executed a 25 PV futures contract noncompetitive trade with NYMEX member McHugh after the end of the trading on July 27, 1998, which was negotiated between them and not done by open outcry in the trading ring. *Id.* Accordingly, the ALJ found that DiPlacido violated Section 4c(a)(A) of the Act, which prohibits accommodation trades, as charged in Count VI of the Complaint. ID at 15-16. Further, the ALJ found that DiPlacido falsified his trading card to make it appear as though the negotiated, after hours trade had occurred on the trading floor and had been subject to open outcry. Because DiPlacido had falsified his trading card to report to NYMEX the noncompetitively determined price of the after-hours trade, the ALJ found that the price reported to the exchange and other market participants was not bona fide. The ALJ therefore concluded that DiPlacido had violated Section 4c(a)(B)'s prohibition against

[19] Citing *In re Nikkhah*, [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 28,129 at 49,888 n.28 (CFTC May 12, 2000) (aiding and abetting 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.").

confirming the execution of transactions used to cause the reporting of a non-bona fide price, as charged in Count VII of the Complaint. ID at 16. Also with regard to the non-competitive trade, the ALJ found that DiPlacido had violated Commission Regulation 1.38(a), which requires that trading be conducted openly and competitively, as charged in Count VIII of the Complaint. *Id.*

The ALJ also found that DiPlacido had violated Section 4g of the Act, which requires every registered floor broker to make reports as required by the Commission and to keep such books and records open to inspection by any representative of the Commission, and Commission Regulation 1.35(d), which requires that members of contract markets document their trades through trading cards or similar records and that these records include certain information about these trades, as charged in Count IX of the Complaint. *Id.* The ALJ concluded that by falsely recording and reporting the July 27, 1998 non-competitive trade as bona fide and altering his trading card to conceal the trade, DiPlacido had violated Section 4g and Commission Regulation 1.35(d). ID at 16-17.

In addition, the ALJ found that, as charged in Count X of the Complaint, DiPlacido violated Section 4g and Commission Regulation 1.31(a), the latter of which specifically requires registrants to promptly provide records when requested by Commission subpoena. The ALJ found that the Commission had subpoenaed DiPlacido to produce certain records on August 4, 2000, and DiPlacido did not complete production of records pursuant to that subpoena until October 2001. In this regard, the ALJ noted that the Commission had previously found that "[r]egistrants are strictly liable for recordkeeping violations, for which a showing of scienter is not required." ID at 17 (quoting *In re Kelly*, [1998-1999 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,514 at 47,373 (CFTC Nov. 19, 1998).

After concluding that the Division had proven by a preponderance of the evidence that DiPlacido had violated the Act and regulations as charged in the Complaint, the ALJ turned to sanctions, noting that DiPlacido's violative conduct was "deliberate, flagrant and egregious," that DiPlacido had not exhibited "a scintilla of remorse" for his wrongful conduct, and that there was nothing in the record to show rehabilitation. ID at 19. Finding that DiPlacido's violations occurred repeatedly over several months and did not appear likely to stop without NYMEX's or the Commission's intervention, the ALJ concluded that a cease and desist order was appropriate. ID at 19-20. In addition, by repeatedly manipulating and attempting to manipulate settlement prices, DiPlacido demonstrated a disregard for rules designed to protect the futures market and investor interest, and accordingly the ALJ imposed a 20-year trading prohibition. ID at 20-21. Because DiPlacido had repeatedly violated the Act and Commission regulations, the ALJ revoked DiPlacido's registration.

Finally, with regard to monetary sanctions, the ALJ noted that civil money penalties are imposed to deter the wrongdoer from repeating the violations and to deter others from engaging in similar activity, and that the penalty should be sufficiently high to make the unlawful activity unprofitable. Citing Section 6(e)(1) of the Act's requirement that the appropriateness of the penalty to the gravity of the violation must be weighed, the ALJ found that DiPlacido's violations were "deliberate, extremely serious, and inflicted great harm to the integrity" of the futures industry generally and to NYMEX. The ALJ ordered DiPlacido to pay a civil money penalty of $50,000 for each of the counts in the Complaint, for a total of $500,000. ID at 22.

E. <u>Arguments on Appeal</u>

On appeal, DiPlacido argues that procedurally the Commission was collaterally estopped from bringing the present action against him on the basis of the findings of the NYMEX disciplinary proceeding that he did not manipulate the market. Respondent's Appeal Brief ("R.App.") at 6 n.2 and 35. Further, DiPlacido contends that the ALJ's conduct of the hearing denied him his due process rights as evidenced by the ALJ's evidentiary rulings and limitation of cross-examination. In addition to these issues, DiPlacido argues that the ALJ possessed a bias against him. R.App. at 26-27. DiPlacido also contends that the ALJ improperly admitted the Avista telephone voice recordings into evidence. R.App. at 29.

Substantively, DiPlacido argues that the Division failed to prove the existence of a scheme to manipulate the NYMEX PV and COB futures contract settlement prices. R.App. at 36. He contends that the credible evidence shows only that DiPlacido placed large orders on behalf of Avista during each of the Closes at issue. In addition, DiPlacido claims that the Division failed to prove the four required elements of manipulation. In this regard, DiPlacido maintains that "market power" is a required component of the ability to influence prices, the first element of a manipulation charge, R.App. at 38, and that the evidence does not show this.

Moreover, DiPlacido contends that the evidence does not show that he intended to influence prices improperly, the second element of manipulation. He claims that there is no direct evidence of intent, because Kristufek and DiPlacido at the hearing denied any intent to manipulate settlement prices. R.App. at 48. DiPlacido also argues that the intent element requires proof of motive for the manipulation, and that there is no evidence regarding Avista's OTC positions that allegedly benefited from the manipulated prices. R.App. at 48. Further, DiPlacido claims that the evidence that DiPlacido violated bids and offers is equivocal, based on facially ambiguous broker's jargon, uncorroborated hearsay complaints or perjury. R.App. at 51.

With regard to the third element, that an artificial price existed, DiPlacido contends that settlement prices are not legally cognizable as to being manipulated under the CEA. R.App. at

54. DiPlacido also argues that Bessembinder's report does not show that the settlement prices were artificial—that is, that they did not reflect the forces of supply and demand—but rather show only that the settlement prices were statistically unusual on the dates at issue.

Concerning the final element, causation, DiPlacido contends that, even if artificial prices were established, he did not cause the artificial prices. R.App. at 60. In this regard, DiPlacido contends that the average prices of DiPlacido's sales were above the settlement prices of the April and May Closes, which he claims had the effect of raising rather than lowering settlement prices as Avista allegedly desired, that the average price of DiPlacido's bids equaled the settlement prices of the July PV Close and thus had no effect on price, and that there was no direct evidence of DiPlacido's August trades.

DiPlacido also argues that he did not have proper notice of the Division's interpretation of manipulation law, and that the *Henner* case was decided under a "predecessor" statute and represents questionable authority. R.App. at 63 *et seq*.

In addition, DiPlacido contends that he did not violate the requirements to produce records promptly, on the basis that the records sought by the Division were not required to be kept by Commission Regulation 1.35(a). He claims that the subpoenaed records were not readily accessible when the subpoena was received, and that he made a good faith effort to retrieve and promptly produce documents. R.App. at 71 *et seq*.

Finally, DiPlacido contends that the sanctions imposed by the ALJ were excessive. R.App. at 74 *et seq*. In this regard, DiPlacido argues that imposing the same $50,000 penalty for each count of the Complaint is unfair, because the charged offenses ranged from manipulation to recordkeeping violations, and these offenses are not equally blameworthy. DiPlacido also contends that the CFTC must consider financial consequences in setting a penalty as a deterrent, and there is no evidence in the record regarding financial benefit to DiPlacido. Arguing that the CFTC has a duty to ensure that similar misconduct is given consistent treatment, DiPlacido states that punishing him at a higher level than the settling respondents is contrary to this duty. Finally, DiPlacido asserts that his "extensive disciplinary history" cited by the Division consists mainly of decorum and minor record keeping violations, and that he has already been punished by the NYMEX for the after-hours trade.

DISCUSSION

I. Procedural Challenges

A. Collateral Estoppel

DiPlacido contends that the Commission should have been collaterally estopped from issuing a Complaint against him, on the basis of the findings of the NYMEX Disciplinary Committee with regard to the same conduct at issue in this proceeding. In order for collateral estoppel to apply, the litigant against which it is asserted must have been either a party to the prior proceeding or be in privity with a party to that proceeding. *In re Murphy*, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,798 at 31,345 (CFTC Sept. 25, 1985). Because the Commission was not a party to the NYMEX Disciplinary Committee proceeding regarding DiPlacido, the Commission may only be collaterally estopped if it was in privity with the NYMEX. In *Murphy*, the Commission held:

> [w]e conclude that exchanges and futures associations conducting disciplinary proceedings involving violations of their own rules do not act as representatives of this Commission, are not "in privity" with this Commission, and cannot bind this Commission's hands in subsequent administrative enforcement proceedings arising out of the same circumstances.

Id. at 31,346. In this case, the NYMEX Complaint charged DiPlacido with violations of exchanges rules; it did not charge DiPlacido with violations of the Act or Regulations that are at issue in the Commission's Complaint. *See* Exhibit B to DiPlacido's Motion to Dismiss the Complaint.[20] Even if this were the case, the Commission is not in privity with the NYMEX under *Murphy*, and therefore we conclude that collateral estoppel is inapplicable to the Commission's Complaint based on the NYMEX disciplinary action.

B. Bias

Preliminarily, with respect to the ALJ's bias, DiPlacido attaches to his brief an Affidavit of Joseph S. Rosenthal ("Rosenthal Affidavit"), DiPlacido's counsel at the hearing, which documents allegedly abusive behavior committed by the ALJ. The Rosenthal Affidavit is the subject of the Division's January 28, 2005 Motion to Strike, on the basis that the filing of the Rosenthal Affidavit after the close of the hearing represents an impermissible attempt to supplement the record without leave of the Commission, in contravention of Commission Regulation 10.107.

Under Commission Regulation 10.67(f), affidavits may be admitted only if the evidence is otherwise admissible and the parties agree that affidavits may be used. As has been noted by the Commission, this limitation is consistent with the right to cross-examine witnesses conferred in Commission Regulation 10.66(b). *In re R&W Technical Services, Ltd.*, [2003-2004 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 29,556 at 55,390 n.9 (CFTC Aug. 6, 2003). The Division has not agreed to the use of the Affidavit, and has had no opportunity to cross-examine Rosenthal with respect to its contents. Accordingly, we grant the Division's Motion to Strike the Rosenthal Affidavit.

[20] It should also be noted that the NYMEX Complaint charged DiPlacido with attempted manipulation of the settlement price for only one of the dates at issue and for the non-competitive trade. Thus the NYMEX charges did not encompass all of conduct charged in the Commission's Complaint.

In general with regard to bias, DiPlacido contends that the entire conduct of the hearing was "replete with displays of biased and unfair treatment." R.App. at 27. DiPlacido specifically alleges that the ALJ prejudged the case as evidenced by a remark made by the ALJ that DiPlacido's counsel "had a tough job here" because of what the ALJ had read in the record before the hearing, that the ALJ has a "long history of antipathy toward floor brokers," that a disproportionate number of DiPlacido's objections were overruled compared to the Division, and that the ALJ conducted a "coercive," off-the-record conference during the hearing in which he threatened counsel with contempt if he would not stop objecting.

Under Commission Rule 10.8(b), disqualification of a presiding officer is appropriate when the record establishes that he has either (1) a personal bias stemming from an extrajudicial source, or (2) a deep-seated favoritism or antagonism that would make fair judgment impossible. *In re R&W Technical Services, Ltd.*, [1998-1999 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,582 at 47,746 (CFTC Mar. 16, 1999), *aff'd in relevant part, R&W Technical Servs. v. CFTC*, 205 F.3d 165 (5th Cir. 2000). As DiPlacido's allegation does not arise from an extrajudicial source, his showing must be based upon application of the latter standard. In applying the latter standard, we look for evidence that the presiding officer has an "unfavorable disposition" toward a party that is undeserved or excessive in degree. *In re Mayer*, CFTC Docket No. 92-21, 1998 WL 80513 at *16 (CFTC Feb. 28, 1998), *aff'd sub nom. Reddy v. CFTC*, 191 F.3d 109 (2d Cir. 1999).

As a general rule, views expressed in earlier decisions are not considered evidence that a decisionmaker has preconceived notions as to either culpability or sanctions. *See Garver v. U.S.*, 846 F.2d 1029, 1031 (6th Cir. 1988). Moreover, a showing of disqualifying bias requires more than references to unfavorable rulings or intemperate, impatient, or inappropriate remarks. *See*

Olson v. Ulmer, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,987 at 37,627 (CFTC Jan. 23, 1991). Rather, "the ALJ's conduct must be so extreme that it deprives the hearing of that fairness and impartiality necessary to that fundamental fairness required by due process." *Gimbel v. CFTC*, 872 F.2d 196, 198 (7th Cir. 1989).

The points that DiPlacido raises concerning the history of antagonism to floor brokers, the disproportionately unfavorable rulings to him, and the "tough job" remark, do not establish that the ALJ had the type of deep-seated favoritism or antagonism that would merit disqualification consistent with Commission or court precedent. With regard to the off-the-record conference conducted by the ALJ, we generally do not favor such conferences because they are an impediment to review. *See, e.g., McDaniel, Trustees v. Amerivest Brokerage Services, et al.*, [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 28,264 (CFTC Sept. 26, 2000) (directing Commission presiding officers to record certain off-the-record telephone conferences). However, DiPlacido's counsel did not object to the off-the-record conference at the hearing. In these circumstances, these claims are deemed waived. *See Drew v. First Nat'l Monetary Corp. et al.*, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,859 at 31,530 (CFTC Jan. 10, 1986) (failure to challenge off-the-record remarks made by ALJ at the hearing constituted waiver of the claim).[21] Accordingly, we conclude that disqualification of the ALJ is not warranted.

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[21] Moreover, DiPlacido alleges that the ALJ engaged in *ex parte* communications with the Division's expert in this case. R.App. at 6. Again, however, he made no attempt to object at the time of the hearing, and the only evidence of these communications in the record is contained in the Rosenthal Affidavit, which we have stricken from the record and in any event is unsupported. Accordingly, this claim likewise is deemed waived. *See Drew*, ¶ 22,859 at 31,530 (assertions of bias must be made as soon as practicable after a party has reasonable cause to believe that grounds for disqualification exist).

C. Due Process

In addition to bias, DiPlacido contends that the ALJ denied him minimal due process. DiPlacido alleges several errors: that the Livingstone Declaration, which he claims was not properly authenticated, should not have been admitted into evidence; that Livingstone improperly gave "expert opinion" in his direct testimony regarding conversations on the tapes even though he was not an expert witness; and that the ALJ improperly limited DiPlacido's cross-examination of Livingstone. R.App. at 12-21.

Moreover, DiPlacido contends that the ALJ improperly limited his cross-examination of the Division's expert, Bessembinder, R.App. at 21-23. DiPlacido also argues that the ALJ improperly refused to allow live testimony by DiPlacido's expert, Kyle, to supplement his expert report and to comment on evidence presented at the hearing to rebut Bessembinder's testimony, R.App. at 23-26. He also contended that the tape recordings of telephone conversations should not have been admitted into evidence. R.App. at 29-34.

1. Livingstone

The Livingstone Declaration. With regard to the Livingstone Declaration, DiPlacido claims that the admission of and the ALJ's reliance on the Declaration were unfair because "one cannot cross-examine" an Affidavit, R.App. at 12, and there was "little justification for allowing the Division to present evidence on some of the most important issues in this case by written declaration." R.App. at 14. However, the hearing transcript shows that DiPlacido agreed to the admission of the Declaration. When the Division moved to admit the Declaration into evidence, DiPlacido's counsel responded, "You can put it in. I'll question him about it." Tr. at 134.

As noted above, Commission Regulation 10.67(f) provides that affidavits may be admitted by the ALJ, (1) if the evidence is otherwise admissible and (2) the parties agree that affidavits may be used. Commission Regulation 10.67(a) provides that "[r]elevant, material and reliable evidence shall be admitted. Irrelevant, immaterial, unreliable and unduly repetitious evidence shall be excluded." The evidence contained in Livingstone's Declaration is hearsay and double hearsay, but such evidence may be admitted in Commission proceedings if it is otherwise truthful, reasonable and credible. *In re Stotler*, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,298 (CFTC Sept. 30, 1986).

There is no reason to believe that Livingstone's Declaration does not meet these requirements, in light of the ALJ's determination that Livingstone was a "credible, reliable and honest" witness and the other corroborative evidence in the record. Livingstone testified on direct to matters contained in the Declaration and was cross-examined by DiPlacido concerning the Declaration, at the ALJ's direction. Tr. at 134 ("If you have a question about Exhibit 1 [the Livingstone Declaration], you may inquire"). DiPlacido cross-examined Livingstone regarding both the circumstances under which the Declaration was prepared and its substance. Tr. at 150-152. Although DiPlacido attempts to impugn Livingstone's credibility in his appeal brief by suggesting that Livingstone now works for one of DiPlacido's "bitterest business rivals," he makes this assertion without any foundation in the record. R.App. at 12.

In addition, the Declaration was properly authenticated as a predicate to its admission. When examined, Livingstone testified that he signed the Declaration in August 2001, Tr. at 118, that the Division's Exhibit 1 was, in fact, that Declaration, Tr. at 150-51, and that he had "no problem with what this statement says." Tr. at 152. Having agreed at the hearing to the admission of Livingstone's Declaration, which is otherwise admissible, DiPlacido cannot now claim that the document was improperly admitted.[22]

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[22] In his Reply Brief, DiPlacido mentions that he formally objected to the Livingstone Declaration's admission prior to the hearing and characterizes his agreement to the admission of the document at the hearing as an "offhand

Livingstone's "Expert" Testimony. DiPlacido also claims that during direct examination, Livingstone was permitted to give expert opinion testimony even though he was not an expert witness. In this regard, DiPlacido contends that at the hearing, the Division played recordings of telephone conversations that included DiPlacido speaking to others at Avista and then asked Livingstone what DiPlacido meant by his words. R.App. at 13.[23] The specific instance to which DiPlacido objects occurred when the Division asked Livingstone about what DiPlacido meant in the recorded conversation when DiPlacido said "I offered right through them." Tr. at 129-130. Over DiPlacido's objection, Livingstone testified that DiPlacido meant that he violated bids by offering at lower prices than were currently bid. Tr. at 130.

We have permitted lay witnesses to give opinion testimony in our proceedings, and we have noted that "trial courts have broad discretion to determine whether a lay witness is qualified to testify on matters of opinion, and whether to permit the witness to testify as to his conclusions." *In re Rousso*,[1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,133 (CFTC July 29, 1997) (citations omitted). Rule 701 of the Federal Rules of Evidence provides that opinion testimony by lay witnesses is admissible in certain circumstances. Although the Commission is not required to follow the Federal Rules of Evidence, *Peabody Coal Co. v. Jane W. McCandless and Director, Office of Workers' Compensation Programs*, 255 F.3d 465, 469 (7th Cir. 2001), we have looked to the Federal Rules of Evidence as "guidance and support" in considering whether certain evidence is admissible. *In re Gorski*, 2004 WL 584254 at *23

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attempt to placate a hostile judge." Respondent's Reply Brief ("R.Reply") at 5. Nonetheless, after agreeing to its admission, DiPlacido cross-examined Livingstone extensively regarding the contents of the Declaration. Accordingly, he made a valid, knowing agreement as to its admission, and should not now be heard to claim otherwise.

[23] Although DiPlacido objects that the recordings were not transcribed during the hearing and that the parties used transcripts that were not entered as exhibits, R.App. at 13 n.4, the transcripts of the portions of CDs that were played at the hearing were in fact admitted into evidence. Tr. at 381 (admitting transcribed portions of recordings as Exhibits 19 through 29, 31, 32, 34, 35 and 38).

(CFTC Mar. 24, 2004); *see Rousso*, ¶ 27,133 at 45,307 n.18 (specifically citing Rule 701 and discussing admissibility of lay witness testimony).

Rule 701 provides that lay witness opinion testimony is admissible if it is "(a) rationally based on the perception of the witness, (b) helpful to a clear understanding of the witness' testimony or the determination of a fact in issue, and (c) not based on scientific, technical, or other specialized knowledge within the scope of Rule 702."[24] In applying these standards, courts have permitted lay witnesses to give their opinion regarding the meaning of terms in recorded conversations, even where the witness was not present during the conversation, provided that the witness had personal knowledge of the subject discussed and the persons involved. *U.S. v. Saulter*, 60 F.3d 270, 276 (7th Cir. 1995); *see also U.S. v. Flores*, 63 F.3d 1342, 1359 (5th Cir. 1995). As the Advisory Committee Notes to the Federal Rules of Evidence make clear, such testimony is not scientific, technical or specialized within Rule 702's ambit if the witness has "particularized knowledge" by virtue of his or her employment.

In this case, Livingstone was present during the recorded conversation, had personal knowledge of the subject discussed and the persons involved in the conversation, and thus his opinion was rationally related to his perception. Moreover, his testimony was helpful to a clear understanding of a fact in issue, namely whether DiPlacido violated bids by offering at lower prices. Finally, his testimony was not of the type within the scope of Rule 702, because

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[24] The latter requirement was added with the 2000 amendments to the Federal Rules of Evidence. The Advisory Committee Notes indicate that the amendment was not intended to affect the "prototypical example[s] of the type of evidence contemplated by the adoption of Rule 701 relat[ing] to the appearance of persons or things, identity, the manner of conduct, competency of a person, degrees of light or darkness, sound, size, weight, distance, and an endless number of items that cannot be described factually in words apart from inferences." As an example, the Advisory Committee noted that "most courts have permitted the owner or officer of a business to testify to the value or projected profits of the business, without the necessity of qualifying the witness as an accountant, appraiser, or similar expert. Such opinion testimony is admitted not because of experience, training or specialized knowledge within the realm of an expert, but because of the particularized knowledge that the witness has by virtue of his or her position in the business. The amendment does not purport to change this analysis." (citation omitted).

Livingstone had particularized knowledge based on his position as DiPlacido's floor clerk on the NYMEX trading floor. Accordingly, we find that the ALJ did not abuse his discretion in admitting this testimony.

Cross-Examination of Livingstone. DiPlacido further claims that the ALJ improperly limited his cross-examination of Livingstone by not permitting him to inquire about Livingstone's credibility and by cutting short his cross-examination. We have stated that "[c]ross-examination should be limited to the subject matter of the direct examination and matters affecting the credibility of the witness." *In re Reddy,* [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,271 (CFTC Feb. 4, 1998). *See also* Commission Regulation 10.66(b) (authorizing ALJ "to limit cross-examination to the subject matter of the direct examination and matters affecting the credibility of the witness.").. Thus, the right to cross-examine a witness does not mean that a party can do so in "whatever way, and to whatever extent" it desires. *Douglas v. Owens,* 50 F.3d 1226, 1230 (3d Cir. 1995). Rather, a party is guaranteed only "an opportunity for effective cross examination," and the trier of fact may properly exercise discretion to impose reasonable limits on the scope of cross-examination. *Id.; see also Maatschappij v. A.O. Smith Corp.,* 590 F.2d 415, 421 (2d Cir. 1978); *accord, In re Air Disaster at Lockerbie, Scotland on December 21, 1988*, 37 F.3d 804, 825 (2d Cir. 1994). The question is whether the ALJ's decision to limit the scope of questioning so prejudiced the substantial rights of the respondents that it amounted to an abuse of discretion. *Rousso*, ¶ 27,133 at 45,306.

DiPlacido claims that the ALJ prohibited him from cross-examining Livingstone on his credibility, pointing to the ALJ's statement at the hearing that "[i]f [the cross-examination] strays beyond the direct, you are in trouble. That's all I'm going to tell you." Tr. at 133. The full exchange between the ALJ and DiPlacido's counsel shows that the ALJ's direction was not as categorical as DiPlacido represents.[25] In any event, the hearing record reveals that the ALJ permitted DiPlacido to cross-examine Livingstone regarding his credibility. DiPlacido was permitted to question Livingstone regarding the agreement he entered into with the Division conferring limited immunity. Tr. at 136, 160.

He was also allowed to question Livingstone regarding his disciplinary history with the NYMEX, Tr. at 139-141, 157-58, including the fact that Livingstone was fined $10,000 and suspended for his conduct on July 27, 1998, as well as other violative conduct in which Livingstone might have engaged, Tr. at 141-145. Further, DiPlacido was permitted to ask whether Livingstone had given any false statement to the Commission during this proceeding, Tr. at 150. All of these questions clearly were designed to probe the credibility of the witness. Although DiPlacido complains that while cross-examining Livingstone regarding his Declaration and the foundation for its statements, the ALJ cut off examination and directed Livingstone to

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[25] The full exchange was as follows:

> ALJ PAINTER: On the cross, who will be doing the cross?
>
> MR. ROSENTHAL: Can we take a brief break, Your Honor?
>
> ALJ PAINTER: How about ten minutes. I'm going to ask you to try to limit your cross to matters that came up on the direct.
>
> MR. ROSENTHAL: I assume I can also go into matters that are not collateral which affect this witness' credibility?
>
> ALJ PAINTER: If it strays beyond the direct, you are in trouble. That's all I'm going to tell you.
>
> Mr. ROSENTHAL: I use the word "collateral" because clearly if it's on collateral matters—
>
> ALJ PAINTER: We will see what surfaces. You've got ten minutes to think it over, how you want to do it.
>
> (Recess taken).

Tr. at 133. Thus, the ALJ did not completely foreclose cross-examination on matters outside the direct, but stated that "we will see what surfaces."

read from the Declaration, the record shows that DiPlacido's counsel was permitted to inquire about the foundation of statements in the Declaration, including whether Livingstone could specifically name any brokers who were violated, Tr. at 154.

DiPlacido also complains that lines of inquiry during his cross-examination of Livingstone were unreasonably cut off and that the examination was unreasonably cut short by the ALJ. Commission Regulation 10.8 makes the ALJ responsible for the "fair and orderly conduct of the proceeding," and grants him the authority to "regulate the course of the hearing." If the ALJ provides an opportunity for "effective" cross-examination, the Commission will not interfere with his efforts to impose reasonable limits on the scope of counsel's examination. *In re Fisher*, [2003-2004 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 29,725 (CFTC Mar. 24, 2004). Our review of the hearing transcript leads us to conclude that the ALJ imposed reasonable limitations on the cross-examination of Livingstone, and these limitations did not prejudice the respondents.[26]

2. <u>Bessembinder</u>

DiPlacido argues that the ALJ unreasonably cut off his cross-examination of the Division's expert witness. He also alleges that the ALJ refused to allow cross-examination by hypothetical questions and on the subject of DiPlacido's expert, Kyle, and directed DiPlacido to seek only clarification or explanation of Bessembinder's report. R.App. at 21-23.

We have held that an "ALJ has broad discretion to determine the scope of expert testimony and to limit cross-examination to the issues raised in the direct testimony." *Reddy*,

[26] Moreover, it appears that at the hearing, while DiPlacido was still permitted to ask a question, DiPlacido's counsel refused to question Livingstone on the basis that he had "at least 15 or 20 questions," and that "[t]he time you allotted me of cross-examination was substantially less than the time the government spent on their case." Tr. at 160-61. Where DiPlacido refused to use the opportunity given to him for cross-examination, his complaint that his cross-examination of Livingstone was unduly cut short should not be entertained.

¶ 27,271 at 46,209. As noted above, the ALJ required the parties to file written expert reports in advance of the hearing, pursuant to Commission Regulation 10.66(d).[27] In the instant case, the Division on direct examination asked Bessembinder to authenticate his written statement, inquired whether anything he had heard during the hearing had changed his opinion, and then moved the document into evidence. Tr. at 336-37. Accordingly, direct examination essentially was limited to Bessembinder's written testimony.

During cross-examination, the ALJ permitted DiPlacido's counsel to pursue numerous lines of inquiry, including questions regarding Bessembinder's opinions in his written statement, the materials reviewed in its preparation, and Bessembinder's methodology. Contrary to DiPlacido's contention, the ALJ permitted DiPlacido to ask many hypothetical questions, twelve of which are documented in the Division's answering brief ("D.Ans.") at 10 n.9. The ALJ only intervened when DiPlacido's counsel questioned Bessembinder about NYMEX Member Goldfarb's potential liability for manipulation, at which point he directed DiPlacido's counsel to "give me the page and the line of his [Bessembinder's] Declaration that they are inquiring about, and to limit it to an explanation of what was meant." Tr. at 351. DiPlacido's counsel did not comply with this direction, and the ALJ did not enforce this order. *See generally* Tr. at 352 *et seq.*

Later, after having permitted DiPlacido's counsel to ask Bessembinder more questions regarding Goldfarb's potential liability and a number of hypothetical questions, the ALJ directed DiPlacido's counsel to end hypothetical questions and to ask questions about Bessembinder's Declaration. Tr. at 366. When DiPlacido's counsel attempted to ask Bessembinder about his

[27] Commission Regulation 10.66(d) provides that the ALJ "at his discretion, may order that direct testimony of expert witnesses be made by verified written statement rather than presented orally at the hearing. Any expert witness whose testimony is presented in this manner shall be available for oral cross-examination, and may be examined orally upon re-direct following cross-examination."

expert, Kyle's Declaration, the ALJ directed DiPlacido's counsel to cross-examine Bessembinder over the contents of Bessembinder's written declaration, to seek to "clarify" anything contained therein, and not to question Bessembinder about Kyle's Declaration. Tr. at 369-70.

The ALJ's direction was not improper, because he may limit cross-examination to direct testimony, and Bessembinder in preparing his report did not review Kyle's Declaration. In any event, this order also was not enforced, as the ALJ permitted DiPlacido's counsel to question Bessembinder regarding Kyle's Declaration. Tr. at 371-75. Ultimately, DiPlacido's cross-examination was not cut off as he contends, but ended when he indicated that he had "[n]o further questions." Tr. at 377. DiPlacido's cross-examination filled 40 pages of transcript and appears comprehensive. In these circumstances, we conclude that the ALJ did not abuse his discretion and DiPlacido sustained no prejudice.

3. Kyle

In addition, DiPlacido contends that the ALJ improperly prohibited him from examining his own expert witness, Kyle, after DiPlacido had submitted Kyle's written statement. R.App. at 23-26. As noted above, the ALJ prior to the hearing had directed the parties to file their experts' written statements, pursuant to Commission Regulation 10.66(d). At the hearing, Kyle took the stand, and the ALJ questioned him in order to authenticate the report, which was admitted into evidence. Tr. at 614. The Division declined to cross-examine Kyle. Commission Regulation 10.66(d) provides that an expert may be examined "orally upon redirect following cross-examination." Accordingly, where there is no cross-examination, there should be no redirect, and we find that the ALJ properly precluded DiPlacido from examining the witness.

Although DiPlacido contends that Kyle should have been permitted to testify regarding evidence presented at the hearing and to rebut Bessembinder, R.Reply at 7-8, this testimony is not permitted by Commission Regulation 10.66(d). Further, while DiPlacido argues that he did not intend to have his expert "necessarily" supplement his report, which dealt with only the July 27 Close, R.Reply at 7-8, his Appeal brief states otherwise, R.App. at 24, and by his own admission, Kyle stated in response to the ALJ that "my report deals exclusively with the July case, and there has been a lot of evidence here about other months, and the other months would strengthen my conclusion." Tr. at 615. However, he indicated that "I would not modify any of my conclusions," based on what he had heard. *Id.* DiPlacido had clear notice regarding the scope of the charges in the Complaint, which included all Closes. That his expert only considered one of the Closes in his written report was DiPlacido's choice.

Accordingly, we conclude that the ALJ did not abuse his discretion either in precluding DiPlacido from conducting redirect examination or in prohibiting DiPlacido's expert from supplementing his written testimony.

4. <u>Recordings of Telephone Conversations</u>

DiPlacido contends that the recordings of telephone conversations involving Avista employees that included their interactions with DiPlacido and others should not have been admitted into evidence. In this regard, he claims that the tapes were not properly authenticated and that certain portions of the recordings were redacted or deleted, rendering them unreliable. R.App. at 29-34.[28]

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[28] DiPlacido also claims that in response to a pre-hearing motion on the admissibility of the recordings, the ALJ failed to follow his own procedure in requiring the Division to make an offer of proof regarding the recordings. R.App. at 30. However, the record indicates that on September 23, 2003, the ALJ issued an Order directing the Division to submit a motion to enter the taped telephone conversations into evidence, which would include a description of how the Division intended to authenticate the tapes, including the names of the witnesses to be called. Pursuant to the September 23 Order, the Division filed a Motion to Enter Certain Recorded Telephone Conversations into Evidence on October 3, 2003, including a list of witnesses to authenticate the recordings. DiPlacido filed an Affidavit and Memorandum of Law in opposition to the Division's Motion, and the Division filed a reply. As a preliminary matter at the hearing, the ALJ announced his ruling granting the Division's Motion to enter the telephone conversations, when offered. Tr. at 13. Accordingly, we see no merit in DiPlacido's claim that the ALJ did not follow the established procedure, and in any event, the Division's Motion contained all the

The Division presented four witnesses at the hearing to authenticate the recordings and establish the chain of custody from when they were produced to the Division and the hearing. Mengheang Synn, a programmer analyst at Avista, testified about Avista's recording systems and the production of one group of recordings to Avista's outside counsel in response to the Division's request. Synn testified that all Avista trader phone lines were recorded, with the exception of a few lines for management. Tr. at 33. Synn further testified that all recorded lines were connected to a recording system that recorded telephone conversations onto a hard drive, which was then backed up to a DAT tape used for storage. Tr. at 34. According to Synn, the DAT tapes of conversations were stored in a fireproof box in a locked room in Avista's Houston office, and could not be altered in any way. Tr. at 35. In response to the Division's request for production, Synn testified that when he retrieved data from the DAT tapes, the data was saved in a different computer-readable format and burned into a CD. Tr. at 38. He testified that during this process, no alterations or deletions were made or could have been made. Tr. at 38-41. The CDs Synn created were then sent to Avista's attorney, Samuel Abernethy. Tr. at 42.

Christine Porter, an Avista employee since 1997, testified regarding additional recordings that were stored in Avista's Spokane Office. The recordings had been shipped to Avista's Spokane Office after closure of the Houston Office. This group of recordings was prepared in the same manner described by Synn—from DAT tapes, the data was saved to a different computer-readable format and burned into a CD. Tr. at 18. Porter also testified that at no point in the process could conversations be altered or deleted in any way. Tr. at 19, 21. She indicated that the CDs that she prepared were sent to Abernethy. Porter also testified that the DAT tapes are still securely stored with Avista. Tr. at 21-22.

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information required by the ALJ, as well as an explanation of the evidence's relevance and admissibility, as generally required in offers of proof.

Samuel Abernethy testified that he received the Division's requests for recordings from Avista's general counsel, and that he was retained to conduct Avista's response to the requests. Tr. at 51. Abernethy reviewed the requests and directed Avista's retrieval of the recordings the requests sought. *Id.* After receiving the CDs of the recordings from Avista, Abernethy listened to the recordings in order to determine if any of the conversations were privileged or private, before copies were made for and forwarded to the Division. Tr. at 51-52. A few privileged and personal conversations were withheld from production, but no business related material was withheld. Tr. at 52-53. Abernethy testified that no portions of conversations were deleted. Tr. at 52. After the loss of the recordings in the destruction of the Commission's New York office on September 11, 2001, Abernethy supplied a duplicate production to the Division. Tr. at 54-55. The 43 CDs supplied by Abernethy to the Division were entered into evidence. Tr. at 55-57 (Division Exhibits 6-A, 6-B, and 6-C).

Division investigator Armand Nakkab testified that under the direction of Division attorneys, he created 7 CDs (Division Exhibits 100-106) containing specified conversations from the 43 CDs; he testified that he did not delete or alter any conversations in this process. Tr. at 71-72.

Commission Regulation 10.67(a) requires that in order to be admissible, evidence must be relevant, material and reliable. Although we have not commented on authentication requirements for tape recordings in the past, we have considered them to be reliable evidence. *See Venesky v. Murlas Commodities, Inc, et al.*, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,218 at 32,600 (CFTC Aug. 14, 1986) (tape recordings made by private parties admissible) (citing *Stoller v. Siegler Trading Co., Inc.*, [1984-1986 Transfer Binder] Comm. Fut.

L. Rep. (CCH) ¶ 22,224 (CFTC June 6, 1984) (tapes made by private parities in violation of statutes prohibiting interception of oral communications admissible).

Even under the criminal case law cited by DiPlacido, in order to establish admissibility, "[t]he government has the duty of laying a foundation that the tape recordings accurately reproduce the conversations that took place, i.e., that they are accurate, authentic, and trustworthy. Once this is done, the party challenging the recordings bears the burden of showing that they are inaccurate." *U.S. v. Thompson*, 130 F. 3d 676, 683 (5th Cir. 1997). The testimony of the Division's four authentication witnesses establishes that Avista recorded the telephone lines of its traders, that the recorded data was recorded by an automated system, that the data was unalterable by Avista employees, both in its stored format and as produced to the Division, and that the transfer of the recordings was handled with reasonable care. Accordingly, the Division established that the recordings were accurate, authentic and trustworthy.

DiPlacido points to nothing that would show the inaccuracy of the tapes, but cites Abernethy's testimony that a few privileged and private conversations were withheld as evidence of redactions and deletions that call the Avista recordings into question, and that at the law firm, there may have been an opportunity to tamper with the tapes, based on Abernethy's testimony that the Avista CDs were kept in an unlocked office and not inventoried. R.App. at 33-34. However, Abernethy testified that all business related conversations were produced, that no portions of conversations were deleted and that where a private conversation was included within a business related conversation, the entire conversation was produced. Tr. at 52. Moreover, DiPlacido's latter suggestion only demonstrates that there is a possibility that someone could have altered the tapes. He produced no evidence that someone did alter or tamper with the tapes or that they were otherwise inaccurate, even though he could have subpoenaed Avista for the

DAT tapes that it still retains to confirm their accuracy. In these circumstances, we hold that the recordings were properly admitted.

II. Substantive Challenges

A. Liability for Manipulation

DiPlacido argues on appeal that the Division did not prove the existence of a scheme to manipulate and that the four factors required to establish manipulation were not proven.

The prohibitions against manipulation of prices are contained in Sections 6(c), 6(d) and 9(a)(2) of the Act. Section 6(c) and 6(d) authorizes the Commission to issue a Complaint if it "has reason to believe that any person . . . is manipulating or attempting to manipulate or has manipulated or attempted to manipulate the market price of any commodity, in interstate commerce, or for future delivery on or subject to the rules of any registered entity." 7 U.S.C. §§ 9, 13b. Section 9(a)(2) makes it unlawful 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 registered entity." 7 U.S.C. § 13(a)(2). Although the term manipulate is not defined in the Act, the constitutionality of the statute has been upheld as not void for vagueness,[29] and courts generally have taken a pragmatic approach in defining manipulation. Thus for example, the Eighth Circuit has stated:

> We think the test of manipulation must largely be a practical one if the purposes of the Commodity Exchange Act are to be accomplished. The methods and techniques of manipulation are limited only by the ingenuity of man. The aim must be therefore to discover whether conduct has been intentionally engaged in which has resulted in a price which does not reflect basic forces of supply and demand.

Cargill v. Hardin, 452 F.2d 1154, 1163 (8th Cir. 1971). In *Volkart Brothers, Inc. v. Freeman,* 311 F.2d 52, 58 (5th Cir. 1962), the court adopted the definition of manipulation given by Arthur

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[29] *Bartlett Frazier Co. v. Wallace*, 65 F.2d 350 (7th Cir. 1933).

R. Marsh, a former president of the New York Cotton Exchange, in a hearing before a Senate subcommittee in 1928:

> Manipulation, Mr. Chairman, is any and every operation or transaction or practice, the purpose of which is not primarily to facilitate the movement of the commodity at prices freely responsive to the forces of supply and demand; but, on the contrary, is calculated to produce a price distortion of any kind in any market either in itself or in its relation to other markets. If a firm is engaged in manipulation it will be found using devices by which the prices of contracts for some one month in some one market may be higher than they would be if only the forces of supply and demand were operative.... Any and every operation, transaction, device, employed to produce those abnormalities of price relationship in the futures markets, is manipulation.

The Commission and the courts have developed the following four-factor test to determine whether a respondent has manipulated prices:

(1) The accused had the ability to influence market prices;
(2) The accused specifically intended to do so;
(3) The "artificial" prices existed; and
(4) The accused caused the artificial prices.

In re Cox, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,786 at 34,061 (CFTC July 15, 1987); *In re Indiana Farm Bureau Cooperative Ass'n*, [1982-1984 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,796 at 27,285 (CFTC Dec. 17, 1982); *Frey v. CFTC*, 931 F.2d 1171, 1175 (7th Cir. 1991).

Does the test apply in a trade-based manipulation case? As an initial matter, we must decide whether the four-factor manipulation test applies to this case, a trade-based manipulation. The four-factor test announced by the Commission in its caselaw was developed from cases involving "corners" and "squeezes," which generally involve manipulation of futures prices through control of the cash market rather than the trade-based type manipulation at issue in this case. However, in the *Henner* case, which involved a trade-based manipulation, the Judicial Officer discussed each of these elements in his decision, including price artificiality and causation, even though he did not specifically enumerate the four factors. We believe it is appropriate to apply the four-factor manipulation test in this case. Even without the *Henner* precedent, we believe that we may apply the four-factor test, on the grounds that it is logical and reasonable to do so.

1. <u>The ability to influence prices</u>

DiPlacido contends that he did not have the ability to influence market prices because the evidence does not show that he possessed market power. R.App. at 38. He argues that the ALJ's decision "essentially reads the market power requirement right out of manipulation entirely." R.App. at 40. However, market power is not a required element under manipulation. As the Commission has stated, "[a] dominant or controlling position in the market is not a requisite element to either manipulation or attempted manipulation and is not essential to altering successfully the forces of supply and demand." *Hohenberg*, ¶ 20,271 at 21,477. Thus, the Commission noted that "one of the most common manipulative devices, [is] the floating of false rumors, which [can] affect futures prices." *Id.* (quoting *Cargill v. Hardin*, 452 F.2d at 1163). *Accord, CFTC v. Enron Corp.*, 2004 WL 594752 at *5 (S.D. Tex. Mar. 10, 2004) ("proof of manipulation does not always require market control"); *In re Soybean Futures Litigation*, 892 F.Supp. 1025, 1047 (N.D. Ill. 1995) (citing *Hohenberg*).

Henner found liability for manipulation based on a floor trader's activity on the exchange's trading floor without evidence of market power or control of the cash market. The Judicial Officer determined that Henner had manipulated the November 1968 Chicago Mercantile Exchange shell egg futures contract, where Henner entered trading with a large long futures position and engaged in intensive buying at the close, entering a final bid immediately before the closing bell 11 ticks higher than his previous purchase. The Judicial Officer concluded that by paying more than he would have had to pay for the shell egg futures contract, Henner had purposely created an artificially high closing price. *Henner*, 30 Agric. Dec. at 1174.

The Division's evidence concerning DiPlacido's ability to influence prices was presented in the written testimony of the Division's expert, Bessembinder, who analyzed each of the four elements of manipulation for the five Closes at issue. With regard to the ability to influence prices, Bessembinder's testimony indicates that the NYMEX electricity futures contracts were "relatively illiquid" during the spring and summer of 1998. Ex. 2, ¶ 24. In comparison to NYMEX natural gas and crude oil contracts, according to Bessembinder the average daily volume of NYMEX electricity futures contracts was less than 1% of NYMEX's natural gas and crude oil contracts for the period from April 1 to August 31, 1998.[30] Because of this illiquidity, Bessembinder concluded that even relatively small orders for the PV and COB futures contracts would have had an appreciable effect on prices. Ex. 2, ¶ 25.

DiPlacido's orders on behalf of Avista during the five Closes were large relative to trading activity in NYMEX electricity contracts by others, according to Bessembinder. Not taking into consideration trading done by other Avista traders, DiPlacido's trading activity accounted for 28% to 52% of the trading volume during the Closes at issue. Ex. 2, ¶¶ 64, 66. Bessembinder's report indicates that DiPlacido's average closing volume during the Closes at issue was 14% of the average <u>full</u> day volume (Avista's average closing volume was 17% when its other traders are included), and in Bessembinder's view, "the arrival and rapid execution (within two minutes) of an unexpected order imbalance (i.e. an excess of buy over sell orders, or vice versa) equal to 14% to 17% of a day's trading volume [would] influence prices substantially

[30] From April 1 to August 31, 1998, Bessembinder's testimony indicates that a daily average volume of 661 PV and 530 COB futures contracts traded; a daily average of 64,944 natural gas contracts and 118,061 crude oil contracts traded on NYMEX. Ex. 2, ¶ 24.

in *any* financial market." Ex. 2, ¶ 67 (emphasis in the original). We believe that this evidence demonstrates that DiPlacido had the ability to influence prices.

DiPlacido essentially contends that the Division expert's conclusion would render all large traders potentially liable for manipulation of prices in illiquid markets, and that such proof cannot constitute an "illegal" ability to influence prices. R.Reply at 9. However, this element of the manipulation test does not require a showing of an "illegal" ability to influence prices as DiPlacido contends, but only the ability to do so. To be sure, large traders in illiquid markets will have this ability, but that alone does not make them liable for manipulation—the other three elements must also be proven by a preponderance of the evidence, including specific intent, an artificial price and causation.

2. Specific intent to influence prices

In order to show the specific intent to influence prices:

> it must be proven that the accused acted (or failed to act) with the purpose or conscious object of causing or effecting a price or price trend in the market that did not reflect the legitimate forces of supply and demand influencing futures prices in the particular market at the time of the alleged manipulative activity.

Indiana Farm Bureau, ¶ 21,796 at 27,283. Intent may "be inferred from the objective facts and may, of course, be inferred by a person's actions and the totality of the circumstances." *Hohenberg*, ¶ 20,271 at 21,477. Moreover, "it is enough to present evidence from which it may reasonably be inferred that the accused 'consciously desire[d] that result, whatever the likelihood of that result happening from his conduct.'" *Indiana Farm Bureau*, ¶ 21,796 at 27,283 (citation omitted). As with all of the elements of manipulation, intent must be proved by a preponderance of the evidence. In *Henner*, the Judicial Officer inferred manipulative intent from the fact that Henner "purposely paid more than he would have had to pay" in order to create an artificially high closing price. 30 Agric. Dec. at 1174.

DiPlacido contends that the evidence is "equivocal" or "unreliable" that he violated bids and offers, and that the ALJ made no finding with regard to the August 1998 Close that DiPlacido engaged in improper trading tactics.

There is ample evidence in the record that DiPlacido had specific intent to engage in manipulation. The evidence from which intent may be inferred includes:

- the above-described taped telephone conversations;
- the testimony of NYMEX members who witnessed DiPlacido violating bids and offers by offering at lower than prevailing bids or bidding at higher than prevailing offers in the ring;
- the testimony of one broker, Birbilis, who testified that he was violated by DiPlacido during the July COB Close when Birbilis was offering at a lower price than DiPlacido was bidding; and
- testimony from witnesses that they heard complaints about DiPlacido's trading activity.

The ALJ found that each of the witnesses who testified that they observed DiPlacido violating bids and offers was "credible, reliable, and honest." ID at 5. On the other hand, the ALJ found DiPlacido—who denied that he violated bids and offers and denied that he intended to manipulate prices—to be "self-serving and unreliable." *Id.* In general, the Commission defers to a presiding officer's credibility determinations in the absence of clear error. *In re Nikkhah*, [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 28,129 at 49,886 (CFTC May 12, 2000). DiPlacido has failed to demonstrate the type of error that would warrant a detailed review of the ALJ's credibility assessments.

Intent established in four out of five Closes. We believe that evidence of DiPlacido's specific intent to manipulate prices is established with respect to four of the five Closes: the

April PV Close, May PV Close, July PV Close and July COB Close. DiPlacido contends that the evidence only shows he had an intent to move the settlement price a certain way, without creating an artificial price, R.App. at 46. The record, to the contrary, includes evidence that during each of these four Closes he engaged in uneconomic trading strategies—violating bids and offers—in order to influence prices. Under *Henner*, such evidence, which has no apparent economic rationale, is sufficient to show manipulative intent.

With regard to the April PV Close, the evidence includes Livingstone's Declaration and Livingstone's testimony at the hearing that he observed DiPlacido trading in the manner described in his affidavit, *e.g.* offering to sell well below prevailing bid prices in the ring.

Concerning the May PV Close, the most compelling evidence includes Livingstone's observation of DiPlacido violating offers and the taped telephone conversation between DiPlacido and Kristufek in which he described how he offered at 20 through bids at 40.

With respect to the July PV Close, the evidence includes Livingstone's testimony that he observed DiPlacido bidding higher than prevailing offers, the testimony of NYMEX member McCann that he observed DiPlacido bidding higher than another broker was offering, the contemporaneous telephone conversation of Caesar regarding DiPlacido's trading tactics, as well as evidence that DiPlacido brought in NYMEX member Goldfarb who would be "believable" to the ring in order to drive up the price.

Concerning the July COB Close, the evidence includes Livingstone's testimony that he observed DiPlacido bidding higher than prevailing offers, Birbilis's testimony that he observed DiPlacido bidding higher than another broker's offer as well as bidding higher than his own offer, and the testimony of NYMEX member McHugh that he observed DiPlacido bidding higher than another broker's offer. There is also the taped conversation with regard to the after hours, non-competitive trade, in which DiPlacido indicated that the trade needed to be executed at a higher price in order for the settlement price to be increased.

All of this evidence compellingly demonstrates that DiPlacido had the specific intent to manipulate prices during these four Closes.

The foregoing analysis is consistent with a statement made in an earlier case involving a traditional market squeeze. *Cf. In re Abrams*, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,479 at 43,136 (CFTC July 31, 1995). We held therein that even if a dominating long played no role in the creation of a congested market, and thus was not culpable in achieving his dominant position, he nevertheless has a duty to avoid conduct that exacerbates the situation. Consistent with that holding, we find that where, as here, a trader executes large orders all on the same side of an illiquid market during the Close, a corollary duty exists to execute orders so as to minimize price impact. Bidding at higher than prevailing prices or offering at lower than prevailing prices self-evidently maximizes price impact in derogation of that duty. We hold that DiPlacido's intentional, repeated breaches of duty further support the inference that he acted with manipulative intent.[31]

Intent not proved on the last Close. With regard to the last, August PV Close, we agree with DiPlacido that manipulative intent was not shown by a preponderance of the evidence.

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[31] Obviously, such trading also violates exchange rules. *See, e.g.*, NYMEX Rule 6.06, which provides:

> 6.06 Transactions Made at Other Than Current Market
>
> (A) Transactions made on the Exchange trading floor at a price above that at which the same futures contract or options series is offered, or below that at which such futures or options contract is bid, are not made at the current market price for such futures or options contracts and shall be disallowed by any floor official designated by the President or by any member of the Floor Committee. If so disallowed, such transactions shall not be reported or recorded by the Exchange.
>
> (B) The determination of a member of the Floor Committee or any designated floor official shall be final.

During that Close, the evidence consists only of an assertion in Livingstone's Declaration that he heard "complaints about DiPlacido's trading," Ex. 1, ¶ 23, but did not assert that he directly observed DiPlacido. The ALJ made no finding that during this Close, DiPlacido violated bids. The assertion in Livingstone's Declaration regarding complaints from other brokers is double hearsay, and we have stated that double hearsay alone generally is insufficient to meet the Division's burden of proof. *Abrams*, ¶ 26,479 at 43,137. There is no other evidence in the record for the August PV Close that would establish manipulative intent.

Motive not required to prove intent. DiPlacido also argues that proof of speculative intent requires proof of motive. He asserts that the Division did not present evidence of Avista's OTC positions, the alleged motivation for the manipulation of prices, and that absent preponderant evidence establishing motive, as a matter of law, the Division cannot show intent. R.App. at 48. Proof of motive, however, is not a required element to establish manipulation under the Act. *See Hohenberg*, ¶ 20,271 at 21,478 (profit motive or demonstrated capability of realizing a manipulation is not an essential element of manipulation); *Cargill*, 452 F.2d at 1162-63. *Accord*, *Henner*, 30 Agric. Dec. at 1181 (noting that "[i]t is not necessary to determine the respondent's precise motive. If he intentionally traded in a manner to distort the closing price, that is manipulation."). Nevertheless, whether a respondent had a demonstrable motive may support an inference of specific intent, and there is evidence of Avista's motive in the record. Livingstone testified that Avista's trading strategy was linked to its OTC positions, and that DiPlacido told him that this was the case. Ex. 1, ¶ 8; Tr. at 125.

3. Existence of an Artificial Price

In order to establish the existence of an artificial price, the Division must show that the price "does not reflect the market or economic forces of supply and demand." *Cox*, ¶ 23,786 at

34,064; *Indiana Farm Bureau*, ¶ 21,796 at 27,283. One Commissioner has commented: "[t]his is more an axiom than a test." *Indiana Farm Bureau*, ¶ 21,796 at 27,300 (Commissioner Stone, concurring). In determining whether an artificial price has occurred, we have stated:

> 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 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.

Indiana Farm Bureau, ¶ 21,796 at 27,288. The Commission's limited case law in this area has looked at such factors as the relationship between an allegedly artificial price and historic price trends, the relationship between cash market prices and the futures price, etc. These factors are germane in the context of traditional corners and squeezes and have little relevance here.

The Commission has identified one generally applicable factor, namely, that a statistically unusual high (or low) price will not on that basis alone be deemed artificial. The Commission refused to find that an artificial price existed in *Cox* when the evidence showed only that the price at issue departed from an historical trend. It held 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 . . . it is incumbent on the parties to explain or justify the relevance of such evidence." *Cox*, ¶ 23,786 at 34,064.[32]

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[32] Commissioner West's dissent in *Cox* captures the difficulty of proving that a price is artificial in light of the majority's holding in that case:

DiPlacido's arguments. (1) Settlement prices cannot be manipulated as a matter of law. As an initial matter, DiPlacido contends that settlement prices are not legally cognizable as prices that can be the subject of a manipulation charge under the Act. R.App. at 54. In this regard, DiPlacido cites *Vitanza v. Board of Trade of the City of New York*, 2002 WL 424699 (S.D.N.Y. Mar. 18, 2002), in which the district court found that manipulation of settlement prices could not be the subject of a claim brought pursuant to Section 22 of the Act, 7 U.S.C. § 25, the private right of action provision. The court specifically was interpreting Section 22(a)(1)(D), which provides that a person may be liable in damages to any other person for violating the Act "if the violation constitutes a manipulation of the price of any such [futures] contract or the price of the commodity underlying such contract." The court concluded that settlement prices, which generally are weighted average prices of futures contracts, are not actual prices of futures contracts or prices of the underlying commodity, and thus the court ruled that the plaintiffs could not bring a claim for manipulation of settlement prices pursuant to Section 22(a)(1)(D). *Id.* at *5.

Even if we were to accept this non-binding authority, the court rendered no opinion regarding the Commission's authority to bring an administrative enforcement action for manipulating settlement prices, pursuant to Sections 6(c), 6(d) and 9(a)(2) of the Act. We do not

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> 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?
> ***
> 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."

Cox, ¶ 23,786 at 34,074-76.

believe that the statutory language in those sections could be construed to limit the Commission's authority in the same way as the court found with regard to a litigant pursuing a private right of action under Section 22.

Moreover, settlement prices are market prices that can be manipulated. Settlement prices as noted above generally are based on a weighted average of futures contract prices over a certain period, known as the Close. The price of an individual futures contract during the Close can be unlawfully manipulated. Where this is the case, the artificially obtained price is included in the calculation of the settlement price, and accordingly causes the settlement price to be subject to artificial influence as well. Accordingly, manipulation of settlement prices can be the subject of an administrative enforcement action. *Henner*, 30 Agric. Dec. at 1180 (discussing the influence of Henner's trade on the settlement price).

(2) The Division's expert testimony did not establish price artificiality. DiPlacido further argues that the Division's evidence regarding price artificiality contained in Bessembinder's Declaration does not demonstrate the existence of an artificial price. He contends that Bessembinder's analysis shows only that the price movements during the Closes at issue were statistically unusual. We believe that Bessembinder's Declaration was flawed in this respect and does not demonstrate the existence of artificial prices. Bessembinder defined prices as artificial if they did not reflect the normal forces of supply and demand. This definition is consistent with Commission precedent noted above. However, the statistical analysis in the Declaration demonstrates no more than that the prices were statistically unusual, without explaining how that demonstrates that the prices did not reflect the normal forces of supply and demand. As stated above, the Commission has held that this is insufficient to prove artificiality. Accordingly, we

accord little weight to Bessembinder's conclusion regarding the existence of artificial prices based on his statistical analysis.[33]

Nonetheless, we find that artificial prices existed without relying on the Division's expert, resting instead on the artificial price analysis in *Henner*. There, the Judicial Officer found that the inference was inescapable that Henner "paid more than he had to for November futures on June 25 for the purpose of causing the closing price to be at that high level. No further proof is needed to show that the closing price . . . was artificially high." 30 Agric. Dec. at 1194. In this regard, the Judicial Officer explained:

> In short, the very essence of a normal price on a futures market is a price arrived at by the free forces of supply and demand on the Exchange (*viz.*, the sellers and the buyers) acting rationally, *i.e.*, the buyers trying to buy as cheaply as they can and the sellers trying to sell as high as they can.
>
> Whenever a buyer on the Exchange intentionally pays more than he has to for the purpose of causing the quoted price to be higher than it would otherwise have been (or, conversely, a seller on the Exchange intentionally sells cheaper than necessary for the purpose of causing the quoted price to be less than it would otherwise have been), the resultant price is an artificial price not determined by the free forces of supply and demand on the Exchange.

30 Agric. Dec. at 1198. Thus, the placement of uneconomic bids or offers results in artificial prices because those prices are not determined by the free forces of supply and demand <u>on the exchange.</u> For this reason, it is not relevant whether Avista was a "net seller" during the July Close, when Avista's OTC positions are factored in, or to consider the market "as a whole" as DiPlacido contends. R.App. at 59-60; R.Reply at 8.[34] Because the evidence shows that

[33] We do not believe that the statistical evidence presented by Bessembinder deserves no weight, however. Bessembinder's analysis does demonstrate that the prices were statistically unusual, which the Judicial Officer considered in *Henner* as buttressing his conclusion that prices were artificial.

[34] In this regard, we accord little weight to the Report of DiPlacido's expert, Kyle. Kyle's analysis, which examines only the July Close, focuses on the role of Avista as a "net seller" when Avista's OTC positions are considered in light of Avista's futures position on NYMEX. But as noted above, this conclusion runs counter to the *Henner* case's focus on uneconomic trading on the exchange. Although Kyle suggests that the trading in this case was unlike the trading in *Henner* because here the trading was profitable considering the OTC positions, and therefore could be

DiPlacido placed uneconomic bids and offers during four of the five Closes at issue, the prices were not determined by the free forces of supply and demand on the NYMEX. Accordingly, we find that the existence of artificial prices was established.

This outcome is consistent with the holding in *Indiana Farm Bureau* that "one must look . . . for those factors which . . . are not a legitimate part of the economic pricing of the commodity." ¶ 21,796 at 27,288. The illegitimate actions here are DiPlacido's flagrant violations of exchange rules established to maintain orderly markets through incremental price moves. "[W]hen a price is affected by a factor which is not legitimate, the resulting price is necessarily artificial." *Id.*

4. Causation

Proof of causation requires the Division to show that "the respondents' conduct 'resulted in' artificial prices." *Cox*, ¶ 23,786 at 34,067 (*quoting Great Western Food Distributors, Inc. v. Brannan,* 201 F.2d 476 (7th Cir. 1953). The Commission has concluded that there can be multiple causes of an artificial price:

> Where these causes can be sorted out, and respondents are a "proximate" cause of the artificial price, a charge of manipulation can be sustained. 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.

Cox, ¶ 23,786 at 34,066;[35] *CFTC v. Enron*, 2004 WL 594752 at *7.

DiPlacido contends that the evidence does not show that he caused artificial prices. In this regard, he argues that during the April and May PV Closes he did not trade the low price on

considered rational, Ex. K at 7, the trading in *Henner* was in fact profitable. As the Judicial Officer demonstrated, Henner's trade influenced the settlement price which increased the value of Henner's already established large long futures position. 30 Agric. Dec. at 1180. Accordingly, Kyle's suggestion is unpersuasive.

[35] The Commission further explained that "[i]t 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." *Cox*, ¶ 23,786 at 34,066 n.8.

either day and that his average trades were above the settlement price, which he claims would have had the effect of raising, rather than lowering, the settlement prices on those dates. Further, he contends that during the July PV Close, his and Goldfarb's average trades on behalf of Avista equaled the July PV Close settlement price, which he asserts could not have made the price manipulatively high.[36] In addition, DiPlacido contends that Goldfarb drove the settlement price up $1.50 during the July PV Close, but he was not charged with manipulation. R.App. at 60-62; R.Reply at 15.

DiPlacido's arguments are not persuasive. The Division's exercise of prosecutorial discretion is presumptively unreviewable, and any challenge regarding selective prosecution must show both that a respondent was singled out for prosecution among others similarly situated and that the prosecutorial decision was made based on an improper standard such as race, religion or the prevention of the exercise of a constitutional right, a showing that DiPlacido has not made here. *In re Antonacci*, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,038 at 32,066 (CFTC Apr. 21, 1986). To the extent DiPlacido suggests that he was not the sole cause of price artificiality, as noted above, Commission precedent has recognized that there may be multiple causes of an artificial price and that a manipulation charge may be sustained if the respondent's actions were a proximate cause of the artificial price. The fact that DiPlacido did not trade the lowest price during a Close has no probative value with regard to settlement prices, which are determined based on a weighted average of prices during the Close.

[36] DiPlacido does not present argument in his brief regarding causation for the July COB Close. With regard to the August PV Close, DiPlacido contends that there is no direct evidence in the record regarding his August trades. Although this question is moot since we believe the evidence does not support a finding of intent to manipulate during the August Close, DiPlacido's trading cards for August were admitted into evidence as direct evidence of DiPlacido's trading. Ex. 15d.

With regard to the average trade argument, DiPlacido's own expert describes a trading strategy by which a trader could have achieved "both the objective of a higher settlement price and the objective of having the customer buy at an average price lower than the settlement price." Ex. K at 41. The converse necessarily follows, that a trader may achieve a lower settlement price with trades that have an average price higher than the settlement price.[37]

While DiPlacido has not demonstrated that he did not cause artificial prices, the burden of proof lies with the Division. The evidence presented by the Division with respect to causation is contained in Bessembinder's Declaration. In this regard, Bessembinder found that DiPlacido's trades were large relative to typical trading in the PV and COB futures contracts, and would have been expected to move the market. Moreover, Bessembinder noted that DiPlacido's trades were all directed to the same side of the market (all sell orders in the April and May Closes when Avista sought to drive settlement prices down and all buy orders during the July and August

[37] DiPlacido's trading reflected in the NYMEX streetbooks that DiPlacido had admitted into evidence (Ex. C) supports this point. For example, in the May Close, when the initial trade of the settlement period was $28.50, DiPlacido sold 49 contracts at $28.00. These sales, which comprised in the aggregate the largest transaction at a given price executed during the Close, caused a significant downward movement in the weighted average price. The weighted average price never meaningfully recovered during the two-minute settlement period. Part way through the Close, DiPlacido executed another series of trades totaling 40 contracts at $28.00—at a point when the weighted average price was moving upward—thereby stalling the upward trend. DiPlacido's trades at $28.00 account for more than half his total trading during the settlement period, and nearly one-third of the 286 trades executed by all traders during the Close. Although DiPlacido had smaller trades at higher prices during the settlement period, which caused the average price of his trades ($28.17) to be higher than the settlement price of $28.09, these trades had a much smaller impact on the weighted average price than his large initial low trades at $28.00, which drove the weighted average settlement price down significantly, while not lowering the price of his personal average trade below the settlement price.

A simple numerical example illustrates this. Trader A executes 2 trades to sell 10 contracts at $15 and 1 contract at $5. Trader B executes 1 trade to sell 5 contracts at $10 (assume that there are buyers to take the opposite side of these trades). The settlement price based on a weighted average of these trades would be $12.81 (205/16). Without A's 1 contract trade at $5, the settlement price would be $13.33 (200/15)--clearly the $5 trade caused a downward movement in the settlement price. However, despite this downward price influence, the average price of Trader A's trades is $14.09 (155/11), above the settlement price of $12.81. In this example, Trader A could execute up to 10 contracts at $5, causing the settlement price to further decline, while maintaining an average trade price at or above the settlement price.

The lowest price recorded during the May settlement period was $27.95, below DiPlacido's lowest priced trades. However, only three transactions totaling 18 contracts were executed at this price, and as such, these trades had a minimal impact on the weighted average price during the May Close.

Closes when Avista sought to drive settlement prices up), and that his trades occurred during the two minute Closes during which settlement prices are calculated in order to influence them. Ex. 2, ¶ 62. Based on this evidence, and the evidence regarding DiPlacido's uneconomic trades, Bessembinder concluded that it was "highly probable" that the orders submitted by Avista and executed by DiPlacido and others caused artificial prices. Ex. 2, ¶ 68.

Bessembinder's analysis essentially asks us to draw the inference that artificial settlement prices were a "reasonably probable consequence" of or were proximately caused by DiPlacido's trading. In light of the large size of DiPlacido's trades in aggregate that were made all on one side of an illiquid market—either buying or selling depending on which direction Avista intended to drive the settlement price—which were all made during the Close when settlement prices were calculated, and the evidence with regard to DiPlacido's uneconomic trading, we find that the record supports an inference that DiPlacido's trading proximately caused artificial settlement prices during four of the five Closes at issue.[38]

Alternatively, because the evidence shows that DiPlacido engaged in uneconomic trading by bidding higher than prevailing offers or offering below prevailing bids during four of the five Closes at issue, such evidence necessarily demonstrates artificial prices for those transactions. Because those prices were included in the settlement price calculation, we also conclude that the settlement price itself is artificial on that basis.[39]

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[38] *Compare Henner*, where the Judicial Officer concluded that by Henner's trading activity—intentionally paying more than he had to pay—caused the price distortion at issue. 30 Agric. Dec. at 1174, 1180. The Judicial Officer in *Henner* noted that a trade-based manipulation may include "buying or selling in a manner calculated to produce the maximum effect upon prices, frequently in a concentrated fashion and in relatively large lots." *Henner*, 30 Agric. Dec. at 1227 (citation omitted).

[39] Contrary to DiPlacido's contention in his Reply Brief that there is no evidence that the prices of particular trades executed by DiPlacido were artificial, R.Reply at 17, the testimony of the witnesses who observed DiPlacido violate bids and offers is just such evidence.

Accordingly, we find that all four elements of the manipulation offense have been established by the weight of the evidence with respect to four of the five Closes at issue, and therefore, we affirm the ALJ's findings that DiPlacido may be held liable for manipulating settlement prices during those Closes.

B. Attempted Manipulation

DiPlacido does not specifically challenge the ALJ's attempted manipulation findings other than to say that attempts merge into the completed offense and may not be punished separately. R.Reply at 18.

Proof of manipulation necessarily includes proof of an attempted manipulation. *Brannan*, 201 F.2d at 477; *Cox*, ¶ 23,786 at 34,061 n.3. Accordingly, we affirm the ALJ's finding that DiPlacido attempted to manipulate settlement prices during four of the five Closes at issue. Because attempted manipulation requires intent, *Hohenberg*, ¶ 20,271 at 21,477, which we have found was not established with respect to the August PV Close, the evidence does not support a finding that DiPlacido attempted to manipulate the settlement price of the August 25, 1998 PV contract. As discussed below, we agree with DiPlacido that he may not be punished for both manipulation and attempted manipulation.

C. Lack of Notice

DiPlacido claims that he lacked fair notice that his conduct could be the subject of a manipulation charge under the Act. In this regard, DiPlacido characterizes the *Henner* case as "questionable authority," as a "pre-CEA case decided under the old law," and as not "controlling authority under the present statutory scheme." R.App. at 40, 66. However, the *Henner* case interpreted the long-standing manipulation provisions of the CEA. Moreover, as noted above, the Commission has cited *Henner* favorably in its adjudicated decisions, *see Indiana Farm*

Bureau, ¶ 21,796 at 27,282 and *In re Cox*, ¶ 23,786 at 34,068, and at least one district court has cited the decision favorably. *See CFTC v. Enron*, 2004 WL 594752 at *5. DiPlacido cites the district court's decision in *In re Soybean Litigation* as questioning *Henner*, R.App. at 67, but in that case, the district court found that certain administrative decisions by U.S. Department of Agriculture ("USDA") (the parent agency of the Commodity Exchange Authority) might not carry strong precedential weight because they did not consider whether prices could be manipulated by the dissemination of false information, which was at issue in the soybean case. 892 F. Supp. at 1047. Also, the court did not specifically mention *Henner* as one of the administrative cases not deserving precedential weight, but only certain USDA administrative decisions involving consent decrees and default judgments. The *Henner* case on the other hand was the final decision of USDA.

Moreover, the Commission has pursued trade-based manipulation cases after its establishment as an independent agency. *See In re Perlmutter*, CFTC Docket No. 79-33, 1979 WL 11474 (CFTC Dec. 3, 1979) (settlement order involving a trade-based manipulation on the New York Cotton Exchange); *see also* complaints cited in D.Ans. at 45 n.43. More recently, the Commission brought an enforcement case alleging attempted manipulation of the Treasury bond futures market based on trading activity on the exchange floor. *In re Catalfo and Zimmerman*, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,636 (CFTC Feb. 29, 1996) (affirming the ALJ's entry of a default judgment against Catalfo for failing to answer the complaint).[40] Thus, even if an abandonment by the Commission of prosecuting trade-based manipulations could be construed as a lack of notice of proscribed misconduct, there was no such abandonment.

[40] The default judgment against both respondents is reported at *In re Catalfo and Zimmerman*, 1994 WL 524393 (C.F.T.C.) (ALJ Sept. 26, 1994). Zimmerman did not appeal.

Legal commentators also have recognized that prices may be manipulated and subject to liability under the Act through "rigged trading." *See, e.g.*, Markham, Manipulation of Commodity Futures Prices—the Unprosecutable Crime, 8 Yale J. on Reg. 281, 283 (1991). Testimony before Congress also has recognized that manipulation of prices proscribed by the Act can involve "heavy trading usually concentrated on the opening or closing of the market . . . [t]he purpose [of which] is to move futures prices either upward or downward for a brief period" and that "[t]his type of price manipulation is usually done for some purpose outside the futures market itself." Hearings on Russian Grain Transactions, Hearings Before The Senate Permanent Subcommittee on Investigations of the Committee on Government Operations (Part 1), 93d Cong., 1st Sess. at 166 (1973) (testimony of Alex Caldwell, Administrator, Commodity Exchange Authority).

DiPlacido cites the NYMEX Adjudicatory Panel's decision finding him not liable for manipulation under NYMEX rules, and argues that the NYMEX Panel considered federal case law and decisions of the CFTC in arriving at its decision that DiPlacido did not attempt to manipulate the market. He contends that the NYMEX decision is evidence of what brokers like DiPlacido generally had notice of what manipulation was believed to be.

When a statute or regulation exposes private persons to quasicriminal sanctions, the government must provide fair notice of what is forbidden. *See, e.g., United States v. Chrysler Corp.*, 158 F.3d 1350, 1354 (D.C. Cir. 1998) ("The simple answer to the question . . . is that a manufacturer cannot be found to be out of compliance with a standard if NHTSA has failed to give fair notice of what is required by the standard."); *General Elec. Co. v. EPA*, 53 F.3d 1324, 1328-29 (D.C. Cir. 1995) ("In the absence of notice—for example, where the regulation is not sufficiently clear to warn a party about what is expected of it—an agency may not deprive a party of property by imposing civil or criminal liability."); *Stoller v. CFTC*, 834 F.2d 262, 267 (2d Cir. 1987) ("The Commission may well have the power to construe the statute in . . . a subtle and refined way, but the public may not be held accountable under this construction without some appropriate notice."). Fair notice occurs when a hypothetical reasonable person who was acting in good faith could have identified, with ascertainable certainty and in light of the regulated community's common understanding, the standards with which the agency expected the public to conform. *Chrysler*, 158 F.3d at 1355; *General Elec.*, 53 F.3d at 1329. Fair notice may be actual or constructive. *See Martin v. OSHA*, 941 F.2d 1051, 1058 (10th Cir. 1991).

In light of the inherent flexibility in the legal concept of manipulation as recognized by the courts and the existence of the *Henner* decision which found liability for manipulation based on uneconomic trading, as well as the commentary of legal scholars, Congressional testimony, and the Commission's pursuit of this type of manipulation after its establishment, we believe that a reasonable person in DiPlacido's position could have determined that his conduct could be punished as manipulation under the Act. Moreover, the evidence indicates that DiPlacido's actions, such as using the code words "don't be shy" in order to hide misconduct, shows that he had actual knowledge that his conduct was wrongful.[41]

D. Aiding and Abetting

DiPlacido does not directly appeal the ALJ's finding that he aided and abetted Kristufek and Taylor in manipulating the settlement prices, other than to claim that it would be "unfair" to pick and choose among the ALJ's findings to cobble together some lesser offense to punish. R.Reply at 19. As such, we deem the issue admitted under Commission Regulation

[41] There is also additional evidence in the record of DiPlacido's attempts to obstruct NYMEX Compliance's investigation of his misconduct, which shows that he had actual knowledge that his misconduct was wrongful. *See infra*.

10.102(d)(3). In any event, the ALJ properly found that DiPlacido aided and abetted Kristufek and Taylor.[42] Aiding and abetting liability 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. *Nikkhah*, ¶ 28,129 at 49,888 n.28 (CFTC May 12, 2000); *R&W Technical Services, Ltd.*, ¶ 27,582 at 47,746. The evidence shows that DiPlacido intentionally engaged in unlawful trading strategies designed to manipulate prices in furtherance of Kristufek's and Taylor's instructions. Such evidence is sufficient to establish that DiPlacido aided and abetted Kristufek and Taylor in manipulating and attempting to manipulate settlement prices during four of the five Closes at issue. *See R&W Technical Services* ¶ 27,582 at 47,746, *aff'd in relevant part, R&W Technical Servs. v. CFTC*, 205 F.3d 165 (5th Cir. 2000).

E. Failure to Respond to Commission Subpoena

The ALJ found that DiPlacido violated Section 4g of the Act and Commission Regulation 1.31(a) by failing to respond promptly to a Commission subpoena requesting certain documents. Section 4g of the Act requires that floor brokers like DiPlacido make such reports as required by the Commission regarding, among other things, transactions for customers, keep books and records pertaining to such transactions in the form and manner required by the Commission and keep such books and records "open to inspection" by Commission representatives. Commission

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[42] Section 13(a) of the Act provides that:

> Any person who commits, or who willfully aids, abets, counsels, commands, induces, or procures the commission of, a violation of any of the provisions of this Act, or any of the rules, regulations, or orders issued pursuant to this Act, or who acts in combination or concert with any other person in any such violation, or who willfully causes an act to be done or omitted which if directly performed or omitted by him or another would be a violation of the provisions of this Act or any of such rules, regulations, or orders may be held responsible for such violation as a principal.

7 U.S.C. § 13c(a).

Regulation 1.31(a) requires that all books and records required to be kept by the Act be "open to inspection" by any representative of the Commission, provided to such a representative "upon the representative's request," and provided "promptly."

DiPlacido contends that the only records required to be produced "promptly" are those records required to be kept pursuant to Commission Regulation 1.35(a), and that the Commission's subpoena went far beyond the books and records required to be kept by that regulation. R.App. at 72. DiPlacido further argues that the evidence does not show that documents required to be kept by Commission Regulation 1.35(a) were not promptly produced. *Id.* He claims that in response to the Commission subpoena issued in August 4, 2000, he made a good faith effort to produce documents on a "rolling basis" until October 2001 when production was completed. *Id.* He also asserts that the Division failed to prove that his trading cards, required to be kept by Commission Regulation 1.35(a), were not produced until October 2001. *Id.* at 73.

The evidence indicates that by January 17, 2001, more than four months after the subpoena had been issued, the Division had not received such documents as DiPlacido's order tickets and trading cards for COB and PV futures contracts. Ex. B. By his own admission, DiPlacido in his Memorandum of Law in Support of Motion to Dismiss CFTC's Compliant (Ex. 11, p. 31) indicated that his production on October 26, 2001, more than year after the subpoena was issued, included "4,240 pages of trading records." At the hearing, DiPlacido stipulated that his attorney had not produced documents he was required to maintain under the Act, including all records relating to his trading of PV and COB futures contracts, until October 2001. Tr. at 396-97.

Commission registrants are strictly liable for recordkeeping violations, for which a showing of scienter is not required. *In re Kelly*, [1998-1999 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,514 at 47,373 (CFTC Nov. 19, 1998); *In re Mayer*, 1998 WL 80513 at *20. In *Kelly*, where there was a five-month delay in the production of documents required to be kept under the Act, the Commission found that the respondent in that case violated Commission Regulation 1.31's requirement to produce records promptly. The evidence in this case indicates that DiPlacido failed to produce trading records more than a year after the subpoena was issued. Accordingly, we affirm the ALJ's finding that DiPlacido violated Section 4g of the Act and Commission Regulation 1.31(a).

F. Non-Competitive, After-hours trade

As noted above, DiPlacido does not address in his briefs the ALJ's liability findings regarding the non-competitive, after hours trade. He also did not address the issue in his post-hearing brief. Accordingly, pursuant to Commission Regulation 10.102(d)(3), the matter is deemed admitted. In any event, the ALJ's findings and conclusions that DiPlacido violated Sections 4c(a)(A) and (B) of the Act,[43] Commission Regulation 1.38, Section 4g of the Act and

[43] The Commodity Futures Modernization Act of 2000, Appendix E of Pub. L. No. 106-554, 114 Stat. 2763 (2000), reorganized Section 4c of the Act and eliminated the prohibition against cross trades. Prior to 2000, when DiPlacido's conduct occurred, the relevant portion of Section 4c of the Act, which like the current version prohibited accommodation trades and transactions used to cause any price to be reported that was not bona fide, read as follows:

> (a) It shall be unlawful for any person to offer to enter into, enter into, or confirm the execution of, any transaction involving any commodity, which is or may be used for (1) hedging any transaction in interstate commerce in such commodity or the products or byproducts thereof, or (2) determining the price basis of any such transaction in interstate commerce in such commodity, or (3) delivering any such commodity sold, shipped, or received in interstate commerce for the fulfillment thereof—
>
> (A) if such transaction is, is of the character of, or is commonly known to the trade as, a "wash sale," "cross trade," or "accommodation trade," or is a fictitious sale; or
>
> (B) if such transaction is used to cause any price to be reported, registered or recorded which is not a true and bona fide price.

Commission Regulation 1.35(d), as charged in the Complaint, are supported by the weight of the evidence.[44]

III. Sanctions

The ALJ imposed sanctions on DiPlacido including a cease and desist order, a 20-year trading ban, a registration revocation and a civil money penalty of $500,000.

Sanctions in enforcement proceedings are imposed "to further the Act's remedial policies and to deter others in the industry from committing similar violations." *In re Volume Investors Corp.*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,234 at 38,679 (CFTC Feb. 10, 1992). In selecting the appropriate sanctions in a particular case, the Commission takes into account the ALJ's assessment of the gravity of respondent's violations[45] as well as the sanctions imposed in the initial decision. Nevertheless, the Commission's review of the relevant factual

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7 U.S.C. § 6c(a) (1994).

[44] Section 4c(a)(A) of the Act prohibits accommodation trades or fictitious sales, and Section 4c(a)(B) of the Act prohibits any transaction that is used to cause any price to be recorded which is not a true and bona fide price. Commission Regulation Section 1.38(a) requires that all trades on a contract market, unless otherwise specified, shall be executed openly and competitively during regular trading hours. Section 4g requires every registered floor broker to make such reports as required by the Commission and to keep such books and records open to inspection by any representative of the Commission. Regulation 1.35(d) requires that members of contract markets document their trades through trading cards or similar records and that for each transaction, the card or record must include: (a) the members' name or identification; (b) the identity of the clearing member; and (c) the date, hour and minute of the transaction.

Generally, fictitious sales include transactions that appear to have been submitted to the open market while negating the market risk or price competition inherent in competitive trading. *In re Three Eight Corp.*, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,749 at 40,444-45 (CFTC June 16, 1993). Noncompetitive trading consists of the use of trading techniques that negate risk or price competition that is incident to an open, competitive market. *In re Bear Stearns*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,994 at 37,662 (CFTC Jan. 25, 1991).

By entering into a noncompetitive trade on July 27, 1998 to raise the settlement price in the August 1998 PV electricity futures contract with McHugh and reporting the noncompetitive price as bona fide to the exchange, DiPlacido violated Section 4c(A) and (B) of the Act and Commission Regulation 1.38(a). In addition, DiPlacido violated Section 4g and Commission Regulation 1.35(d) by falsely recording the noncompetitive trade on his trading card.

[45] Gravity refers to the seriousness of a violation. *In re Gordon*, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,326 at 42,592 (CFTC Mar. 6, 1995).

issues is *de novo* and reflects its independent judgment about the appropriate mix of sanctions. *In re Grossfeld,* [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,921 at 44,467 (CFTC Dec. 10, 1996), *aff'd sub nom. Grossfeld v. CFTC*, 137 F.3d 1300 (11th Cir. 1998).

A. Gravity of the Violations

Determining the gravity of DiPlacido's violations involves several related inquiries. The first focuses on the underlying conduct's relationship to the regulatory purposes of the Act. *In re Premex*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,165 at 34,890 (CFTC Feb. 17, 1988). Generally, violations of the "core provisions" of the Act, such as manipulation, warrant more serious sanctions. Without question, the gravity of market manipulation is high because such conduct is contrary to one of the Act's core regulatory protections. Section 3 of the Act, 7 U.S.C. § 5, specifically identifies the deterrence and prevention of price manipulation as one of the Act's central purposes. Indeed, the Commission has described market manipulation as the "gravest offense under the Act." *In re Sundheimer*, [1980-1982 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,245 at 25,221 (CFTC Sept. 16, 1981). *See also* H.R Conf. Rep. 102-978 at 3200 (Oct. 2, 1992) (recognizing manipulation as violation of a more serious nature warranting high penalties); A Study of CFTC and Futures Self-Regulatory Organization Penalties, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,264 at 42,219 (CFTC Nov. 1, 1994) ("Penalties Study") (mentioning manipulation as core violation).

Like the trade-based manipulation at issue in this case, a violation of Section 4c(a)—DiPlacido's noncompetitive trade which he has not appealed—is always serious because such a violation undermines confidence in the market mechanism that underlies price discovery. *In re Piasio*, [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 28,276 (CFTC Sept. 29, 2000). A shortcoming in recordkeeping, while serious, is lower in gravity, because recordkeeping requirements are ancillary to the Act's core regulatory provisions. *See generally In re Premex*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,165 at 34,890-91 CFTC Feb. 17, 1988).

The second inquiry focuses on the facts and circumstances of the particular case. In making this inquiry, the Commission often considers whether a respondent's conduct was knowing and whether respondent cooperated with authorities following discovery of his violations or undertook other steps to ameliorate the harm flowing from the violations. *Grossfeld*, ¶ 26,921 at 44,467-44,468 and nn.29 & 31; *Premex*, ¶ 24,165 at 34,891. In addition, the Commission has looked at whether the violative conduct was isolated or continuous, the length of time the violative conduct continued, the number of customers affected, the financial benefit to the respondent, and the financial harm to customers. *Grossfeld*, ¶ 26,921 at 44,468 and n.30. Finally, the Commission considers evidence that a respondent may offer to show that the gravity of his violations was mitigated or that there has been a change in his conduct since the time of his violations. *In re Piasio*, [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 28,276 at 50,691 (CFTC Sept. 29, 2000).[46]

The record indicates that DiPlacido was a knowing participant in unlawful conduct. He intentionally and willingly engaged in trading strategies that he designed to drive up or down the settlement price in furtherance of Avista's goals, he deliberately entered into an accommodation trade at a price that he recommended in order to influence the settlement price, and he recruited another trader to participate in the scheme for one of the Closes. Moreover, far from taking steps to ameliorate his misconduct, DiPlacido directed his floor clerk to use code words to conceal the

[46] Cases frequently refer to evidence of these circumstances as evidence of mitigation or rehabilitation.

misconduct, he altered his trading card to conceal the noncompetitive trade, and refused to comply promptly with the Commission's subpoena.

Further, there is evidence in the record regarding DiPlacido's attempts to obstruct the NYMEX investigation into his trading for Avista. The evidence includes testimony that DiPlacido told Kristufek that Avista should "lose" its recordings of conversations concerning electricity futures trading on July 27, 1998. Ex. 1, ¶ 22; Tr. at 259-261; Tr. at 112-17. Livingstone also testified that DiPlacido told him that phone recordings made by DiPlacido's firm and requested by NYMEX Compliance for its investigation had been "edited." Ex. 1, ¶ 20; Tr. at 108-110. Also, DiPlacido, together with his attorney, told Livingstone that he, DiPlacido, could get in trouble for working with Avista to manipulate electricity futures settlement prices, and that Livingstone should falsely tell NYMEX Compliance that whatever Avista told him was not relayed to DiPlacido. Ex. 1, ¶ 21; Tr. at 110-12.

In addition, DiPlacido's proven misconduct was not infrequent or isolated, but took place repeatedly over several months. On multiple occasions, he entered the trading ring with the intention of executing trading strategies that would manipulate settlement prices. The record also indicates that DiPlacido told Livingstone that he had executed a similar strategy years earlier at Taylor's request, although this conduct went undetected. Ex. 1, ¶ 8. DiPlacido has offered no evidence of mitigation or rehabilitation.

B. <u>Cease and Desist Order</u>

A cease and desist order is appropriate where there is a reasonable likelihood that a respondent will repeat his wrongful conduct in the future. *Piasio,* ¶ 28,276 at 50,692. In general, evidence of a knowing violation or a pattern of violative conduct is sufficient to support an inference that it is likely wrongful conduct will be repeated. *Id.* Here the record shows both that DiPlacido acted knowingly and that he repeated his violative conduct over several months. In these circumstances, imposition of a cease and desist order is appropriate.[47]

C. Registration Revocation

Because the record establishes that DiPlacido violated the Act and Commission regulations, he is subject to a statutory disqualification from registration under Section 8a(2)(E) of the Act, 7 U.S.C. § 12a(2)(E). He may rebut the presumption of unfitness arising from his disqualification with clear and convincing evidence that his continued registration poses no substantial risk to the public. *Piasio*, ¶ 28,276 at 50,692. DiPlacido did not present any mitigation or rehabilitation evidence or argue that he would not pose a substantial risk to the public. As a consequence, in light of DiPlacido's repeated violations of the Act and regulations, a registration revocation is an appropriate sanction to protect the public interest.

D. Trading Prohibition

Trading prohibitions are appropriate when the record shows that a respondent's misconduct represents an inherent threat to the integrity of the futures markets in the public eye. *In re Miller,* [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,440 at 42,914 (CFTC Jun. 16, 1995). The term of the prohibition turns on the gravity of the violations. *Id.* Permanent trading prohibitions, however, are rarely appropriate, but are reserved for conduct that is "both intentional and egregious." *Id.* (citing *In re GNP Commodities,* [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,360 at 39,222 (CFTC Aug. 11, 1992). The Commission also takes into consideration any evidence of mitigation or rehabilitation in assessing trading

[47] DiPlacido argues that his disciplinary history does not show that he is an "extreme recidivist," likely to engage in further violations, because that history generally consists of minor recordkeeping or decorum violations. R.App. at 76. However, we do not believe that DiPlacido's disciplinary history is necessary to establish a reasonable likelihood of repeated misconduct, in light of the record evidence showing that DiPlacido acted knowingly and repeatedly over several months in manipulating settlement prices in this case.

prohibitions, *In re Staryk*, [2003-2004 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 29,826 at 56,452 (CFTC July 23, 2004), but as noted above, DiPlacido presented no such evidence.

The ALJ imposed a 20-year trading ban on DiPlacido. The Division did not appeal the length of the ALJ's trading prohibition, and DiPlacido does not directly address the trading prohibition, other than to label it as "what would be a lifetime ban . . . ." R.App. at 75. In light of the gravity of DiPlacido's misconduct, a 20-year trading prohibition is appropriate.

The ALJ limited the trading ban to trading on "any designated commodity exchange." The Division requests that the Commission affirm the trading ban but conform the language of the ban to that found in Section 6(c) of the Act, which provides that the Commission may prohibit trading "on or subject to the rules of any registered entity." Division Cross Appeal Brief ("D.App.") at 2 n.2. We grant the Division's request.

E. Civil Money Penalty

With regard to the civil money penalty, the Act requires the Commission to consider the "appropriateness" of a civil money penalty to the "gravity" of respondent's proven violations. The Act authorizes alternative approaches for determining the maximum money penalty for a particular respondent. Under Section 6(c), the Commission may impose a penalty of not more than the higher product of (1) $100,000 times the number of a respondent's proven violations; or (2) three times respondent's "monetary gain" from the proven violations.

Because there is no evidence in the record of DiPlacido's monetary gain, the Commission must use the $100,000 per violation alternative in assessing a civil money penalty. The maximum civil money penalty permitted under the Act's $100,000 per violation test is subject to adjustments for inflation, based on when the violative conduct occurred. Commission Regulation 143.8, 17 C.F.R. § 143.8. Because all of the violative conduct in this case occurred in 1998, the Commission may impose an inflation-adjusted civil penalty of $110,000 per violation.

As noted above, the ALJ imposed a $500,000 civil money penalty by multiplying each of the ten counts in the Complaint by $50,000. DiPlacido argues that the civil money penalty imposed by the ALJ is excessive. He criticizes the ALJ's approach as mechanically applying the same penalty to violations ranging from manipulation to recordkeeping without explanation. R.App. at 75. Moreover, he argues that Counts VI through IX of the Complaint charge four violations for the same behavior involving the after-hours, non-competitive trade, and that it is unfair to punish him four times for the same conduct. *Id.* He also mentions that NYMEX already punished him for this misconduct. DiPlacido further contends that the CFTC must consider financial consequences as a result of his misconduct, and that there is no such evidence in the record. *Id.* DiPlacido also argues that the penalties imposed in the settlements entered into with Kristufek and Taylor, the Avista employees who planned the scheme, were substantially lower than the penalty imposed by the ALJ, and that any penalty imposed on DiPlacido should be no more than the other participants in the alleged scheme. *Id.* at 75-76.

The Division cross-appeals the civil money penalty, urging that the Commission review the penalty *de novo* and impose a higher penalty. The Division contends that DiPlacido's violative conduct involving manipulation cuts to the core of the Commission's mission as expressed in its very statute. D.App. at 31. In addition, the Division contends that the non-competitive, after hours trade, which violates Section 4c of the Act, is considered to be "pure, unadulterated fraud," and that such violations are not mere technicalities but malum in se. *Id.* at 28 (citations omitted). The Division argues that because the conduct charged in Counts IX (false reporting) and X (failure to promptly respond to a Commission subpoena) was committed either in furtherance of the manipulation or to conceal misconduct from Commission investigators, it must be viewed as equally grave as the principal misconduct. Accordingly, the Division urges the Commission to impose the maximum fine per count charged in the Complaint, or $1.1 million. *Id.* at 33.

We agree with DiPlacido that the ALJ's approach to calculating the civil money penalty did not comport with Commission precedent. The Commission normally does not calculate penalties in an enforcement proceeding by equating the number of violations with the number of counts charged in the Complaint. *In re Slusser*, [2003-2004 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 29,411 at 54,745 (CFTC Feb. 28, 2003). Moreover, the ALJ's approach of imposing the same penalty of $50,000 for each violation does not take into consideration the relative level of gravity of the violations, as discussed above.

Commission precedent states that to determine the number of violations committed by a respondent, a "broad but common sense approach" is taken for purposes of the $100,000 per violation alternative. *Id.*; *accord, In re Miller*, [2003-2004 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 29,825 at 56,441 (CFTC July 23, 2004). In determining an appropriate penalty, the Commission "focuses on the overall goal of effective deterrence rather than emphasizing approaches to violation counting that might justify expansive statutory maximums." *In re Staryk*, [2003-2004 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 29,826 at 56,453 (CFTC July 23, 2004).[48] Nonetheless, the Commission has counted the number of violations in order to

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[48] As the Commission explained in *In re Incomco, Inc.*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,198 (CFTC Dec. 30, 1991):

> In enacting [then] Section 6(b) of the Act, Congress established a relationship between the number of violations a respondent commits and the maximum level of civil [money] penalty the Commission may impose. Nevertheless, our selection of appropriate sanctions in a particular case turns more on an examination of the overall nature of the wrongful conduct respondent has committed than a simple enumeration of the violations established on the record.

determine the maximum liability to which a respondent could reasonably be found to have notice that he was subject, and to ensure that the ultimate penalty imposed falls within the statutory maximum. *See Staryk*, ¶ 29,826 at 56,453 (notice of violations); *Slusser*, ¶ 29,411 at 54,745 (citing court of appeal's emphasis in *Slusser v. CFTC*, regarding notice of liability and duty to determine statutory maximum); *Miller*, ¶ 29,825 at 56,441 (counting violations to determine whether penalty fell within statutory maximum).

In this case, the Complaint charged DiPlacido with five counts of manipulation and attempted manipulation of settlement prices during the five Closes[49] and five counts of other violations relating to a non-competitive trade, false reporting of that trade, altering a trading card, and failure to produce records. Each count of the Complaint alleging manipulation and attempted manipulation states with respect to these charges that "[e]ach and every act or transaction engaged in by Kristufek, Taylor and/or DiPlacido in furtherance of the manipulative scheme, as described above, is alleged herein as a separate and distinct violation." Given that the Complaint alleged numerous transactions and overt acts in furtherance of the manipulative scheme,[50] along with five additional counts of separate and distinct violations, DiPlacido was on

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Id. at 38,535-36 n.16.

[49] We agree with DiPlacido that he cannot be punished for both manipulation and attempted manipulation, but only one or the other violation, based on the merger doctrine. *See U.S. v. Tarricone*, 242 F.2d 555, 558 (2d Cir. 1957) (conviction of attempt crime merges into aggravated offense for purposes of sentencing); *U.S. v. Helmsley*, 941 F.2d 71, 99 (2d Cir. 1991); Model Penal Code Section 1.07(1)(b) (prohibiting convictions for both an attempt and substantive offense that is its object).

[50] *See, e.g., In re Global Telecom, Inc.*, [2005-2007 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 30,143 at 57,571 (CFTC Oct. 4, 2005) (where Complaint alleged "[e]ach material misrepresentation or omission and each willful deception" as a separate and distinct violation of Section 4b and misleading statements appeared in six issues of special interest magazines (of unknown circulation), in an unknown number of direct mailings and on Global Telecom's website, concluding that a high penalty was justified); *Staryk*, ¶ 29,826 at 56,453 (finding that respondent was on notice that the proceeding involved allegations that he defrauded at least 30 customers and thus faced a potential maximum civil penalty of $3 million); *In re Carr*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶24,933 at 37,397 n.3 (CFTC Oct. 2, 1990) (each day of noncompliance with a Commission rule may constitute a separate violation"); *In re Rosenthal & Co.*, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶22,221 at 29,191 (CFTC June 6, 1984) (a nationwide solicitation fraud scheme involving 25 offices and a sales force of 500 entailed "multiple" violations, not a single violation, as respondents claimed).

notice that he was being charged with violations that could lead to imposition of a fine in the millions of dollars.

The Complaint was sufficient to put DiPlacido on notice that he could potentially face a civil money penalty in the millions of dollars. Based upon the Commission's findings of liability, and counting the number of violations in the manner most favorable to DiPlacido, he could have been assessed a penalty of $1.43 million for thirteen violations, *to wit*: four occasions of manipulating the settlement price of the PV or COB electricity contract; four instances of aiding and abetting Kristufek and/or Taylor in manipulating the settlement price of the PV or COB electricity contract; and one instance each of entering into a fictitious trade; at a non-bona fide price; trading non-competitively off the floor; submitting a false trading card; and failing to promptly produce documents to the Commission.

Given the gravity of DiPlacido's offenses and potential maximum fine, the focus of the Commission's analysis shifts to assessing a specific penalty appropriate to the level of gravity and suitable to deter future violations. *Staryk*, ¶ 29,826 at 56,454. The Commission has consistently held that the penalty appropriate to the gravity of proven violations is not normally equated with the statutory maximum. *Miller*, ¶ 29,825 at 56,438 (citing *Incomco*, ¶ 25,198 at 38,535-36). The Commission has also eschewed any formulaic approach to determining the penalty appropriate to the gravity of proven violations. *Grossfeld*, ¶ 26,921 at 44,467.

Financial consequences flowing from a respondent's misconduct generally have played a prominent role in assessing a specific penalty. *Staryk*, ¶ 29,826 at 56,438. However, in cases involving trade practice violations such as a violation of Section 4c, the Commission has emphasized that such violations are grave even in the absence of direct harm to customers. *In re Buckwalter*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,995 at 37,688 (CFTC

Jan. 25, 1991). The Commission has stated that such violations are not mitigated by the fact that the challenged trades caused no specific, quantifiable injury to particular customers or other traders. *In re Elliott*, [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,243 at 46,008 (CFTC Feb. 3, 1998), *aff'd Elliott v. CFTC*, 202 F.3d 926 (7th Cir. 2000). This is because the violative conduct has the potential for threatening the integrity of the markets and the confidence of those who rely on them for risk shifting and price discovery. *Mayer*, 1998 WL 80513 at *30. Thus, the Commission has imposed civil penalties in these cases without evidence of financial consequences.

Although the Commission has not commented specifically with respect to trade-based manipulation in this regard, a similar rationale applies. The trade-based manipulation violations at issue in this case impugn the integrity of the market mechanism. Manipulation of settlement prices in particular, which are used for, among other things, calculating variation margin and as reference points for the valuation of many OTC contracts, necessarily has a widespread effect on market participants both on and off exchange. Where settlement prices are not derived from prices discovered according to the forces of supply and demand, an unfair and unlawful allocation of gains and losses results. Moreover, both the courts and the Commission have held that specific evidence of economic gain or loss to the manipulator is immaterial in determining intent, because they have found that economic harm to the market is sufficiently grave. *See Cargill*, 452 F.2d at 1163 (holding that "the question of whether an alleged manipulator has made a profit is largely irrelevant, for the economic harm done by manipulation is just as great whether there has been a profit or a loss in the operation"); *Hohenberg*, ¶ 20,271 at 21,478.

Artificial trading, such as non-competitive trading and the trade-based manipulation involved here, warrants substantial penalties due to the difficulty of detecting such violations. As the U.S. Court of Appeals for the Second Circuit has explained:

> While artificial trading can over time be profitable, it is also difficult to detect. Because the gains available from artificial trading can be great and the danger of detection may seem low, the temptation to engage in such practices may be great. If deterrence is to be achieved, substantial penalties may be necessary.

Reddy v. CFTC, 191 F.3d 109, 125 (2d Cir. 1999).

Another consideration in assessing penalties is the level of involvement of the respondent in the wrongful misconduct where that misconduct involves several actors. *See, e.g., In re Glass*, [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,337 (CFTC April 27, 1998). Although there is no evidence in the record that DiPlacido profited from the manipulative scheme, the record reveals him as more than a willing accommodator to Avista and its employees. DiPlacido devised the unlawful trading practices to influence prices in furtherance of Avista's objectives, actively recruited another person to participate during one of the Closes, entered into an accommodation trade with another trader at a price that he recommended in order to influence the settlement price and attempted to cover up the misconduct. His involvement was more akin to a principal in the manipulative scheme, and a substantial penalty is warranted.

DiPlacido claims that any penalty should be no higher than those imposed on Kristufek and Taylor, which as noted above were $155,000 each. Those penalties were imposed in settlement orders, both of which were entered before this matter proceeded to hearing. Factors that may justify a reduction in the level of sanctions in settlement orders, as opposed to penalties imposed in an adjudicatory context, include savings attributable to the Commission's reduced cost of prosecution or a settling respondent's cooperation with other Commission investigations. *In re Gordon*, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,667 at 40,181 n.4

(CFTC Mar. 16, 1993).[51] Conservation of resources is an especially important factor in manipulation cases, which generally consume significant resources and are difficult to prosecute. *See generally In re Global Minerals and Metals Corp.*, 2004 WL 1416174 (CFTC June 22, 2004). Since such considerations are absent in the adjudicatory context, the penalties imposed on Kristufek and Taylor are not an appropriate guide for setting a civil money penalty for DiPlacido.[52] Moreover, because of DiPlacido's significant involvement in the manipulative scheme, akin to a principal as noted above, a high civil money penalty for DiPlacido is justified.

In light of the extreme gravity of DiPlacido's violations involving manipulation, which undermine the integrity of the market mechanism, have a widespread adverse effect on market participants and are difficult to detect, as well as the other serious misconduct established in the record and the other considerations discussed above, an appropriate civil money penalty in this case is $1 million.[53] While this penalty is higher than that imposed by the ALJ, such a penalty in our judgment is appropriate to address DiPlacido's multiple violations which include price manipulation, the gravest offense under the Act. In addition, this penalty is necessary to act as a meaningful deterrent to others who may be tempted to engage in a similar manipulative scheme

[51] *See also* Penalties Study, ¶ 26,264 at 42,224 ("The Commission reasonably may decide to impose a lower money penalty when a respondent has cooperated with the Commission, offered assistance in other enforcement matters, or settled a case. Like any litigant, the Commission may accept a lower money penalty in order to conserve resources or avoid the risk of litigation.").

[52] Additionally, in the past the Commission has imposed substantially higher money penalties on non-settling respondents versus settling respondents who engaged in similar misconduct based on an independent assessment of the record. *See In re Mayer*, 1998 WL 80513 (CFTC Feb. 25, 1998) *aff'd sub nom. Reddy v. CFTC*, 191 F.3d 109 (2d Cir. 1999) (imposing penalties ranging from $150,000 to $500,000 on non-settling respondents after having settled with two respondents imposing penalties of $20,000 to $55,000).

[53] In addition to the considerations discussed above, the Commission in other cases has considered penalties imposed in comparable cases in assessing civil penalties. *See Miller*, ¶ 29,825 at 56,440. However, consideration of comparable cases is inapposite here, since the Commission has not heretofore imposed liability for manipulation in an adjudicated decision. Moreover, as stated in the body of this opinion, prior adjudicated manipulation cases have involved corners and squeezes rather than the trade practice abuse involved here.

or who may be tempted to engage in activity designed to cover up their own misconduct or the misconduct of others.

In exercising its discretion to determine the appropriate civil money penalty to impose in this case, in light of the analysis and discussion above regarding relevant factors to consider and the gravity of each offense, we arrived at the $1 million civil money penalty as follows: $110,000 for each manipulation of the settlement price of the PV or COB electricity contract ($440,000); $80,000 for each instance of aiding and abetting Kristufek and/or Taylor in the manipulation of the settlement price of the PV or COB electricity contract ($320,000); $70,000 for executing a fictitious and non-competitive trade; $65,000 for reporting a non-competitive trade as bona fide; $65,000 for altering a trading card; and $40,000 for failure to promptly produce documents to the Commission.

CONCLUSION

For the forgoing reasons, the initial decision is affirmed in part, and vacated and modified in part. We affirm the ALJ's findings that DiPlacido manipulated and attempted to manipulate settlement prices for the PV electricity futures contracts on April 24, 1998, May 22, 1998, and July 27, 1998 and the COB electricity futures contract on July 27, 1998.[54] We vacate the ALJ's finding that DiPlacido manipulated and attempted to manipulate the settlement price of the PV electricity futures contract on August 25, 1998. In addition, we affirm the ALJ's findings that DiPlacido aided and abetted Kristufek's and Taylor's violations during four of the five Closes and the ALJ's findings of liability for the non-competitive, after hours trade because DiPlacido has not appealed the ALJ's liability findings in this regard, which are supported by the weight of the evidence. Finally, we affirm the ALJ's finding DiPlacido liable for failure to respond

[54] As we explained earlier, based on the merger doctrine, we do not impose sanctions for both the manipulations and attempted manipulations.

promptly to the Commission's subpoena. In light of the gravity of DiPlacido's violations, we affirm the ALJ's imposition of a cease and desist order and registration revocation. We modify the 20-year trading ban imposed by the ALJ and prohibit DiPlacido from trading on or subject to the rules of any registered entity for a period of 20 years. Finally, DiPlacido shall pay a civil money penalty of $1 million.

IT IS SO ORDERED.[55]

By the Commission (Acting Chairman LUKKEN and Commissioners SOMMERS and CHILTON; Commissioner DUNN not participating).

David A. Stawick
Secretary of the Commission
Commodity Futures Trading Commission

Dated: November 5, 2008

[55] Sanctions shall become effective 30 days after the date this order is served. A motion to stay any portion of this order pending reconsideration by the Commission or judicial review shall be filed and served within 15 days of the date that this order is served. *See* Commission Rule 10.106, 17 C.F.R. § 10.106.