UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

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In the Matter of	**CFTC Docket No:** 05-06
Hencorp Becstone Futures LC, **Jorge Mattos,** **and Oscar Schaps,** **Respondents.**	**ORDER INSTITUTING PROCEEDINGS PURSUANT TO SECTIONS 6(c) AND 6(d) OF THE COMMODITY EXCHANGE ACT, MAKING FINDINGS AND IMPOSING REMEDIAL SANCTIONS**

I.

The Commodity Futures Trading Commission ("Commission") has reason to believe that Hencorp Becstone Futures LC ("Hencorp") and Jorge Mattos have violated Section 4c(a) of the Commodity Exchange Act, as amended (the "Act"), 7 U.S.C. § 6c(a) (2002), and Section 1.38(a) of the Commission's Regulations, 17 C.F.R. § 1.38(a) (2004); and that Oscar Schaps has violated Section 166.3 of the Commission's Regulations, 17 C.F.R. § 166.3 (2004). Therefore, the Commission deems it appropriate and in the public interest that public administrative proceedings be, and they hereby are, instituted to determine whether Hencorp, Mattos, and Schaps (collectively, the "Respondents") engaged in the violations set forth herein and to determine whether any order should be issued imposing remedial sanctions.

II.

In anticipation of the institution of an administrative proceeding, Respondents have submitted a Joint Offer of Settlement ("Joint Offer"), which the Commission has determined to accept. Respondents acknowledge service of this Order Instituting Proceedings Pursuant to Sections 6(c) and 6(d) of the Act, and Making Findings and Imposing Remedial Sanctions ("Order"). Respondents, without admitting or denying the findings of fact or conclusions of law herein, consent to the use of the findings contained in this Order in this proceeding and in any other proceeding brought by the Commission or to which the Commission is a party.[1]

[1] Respondents do not consent to the use of the Joint Offer or this Order, or the findings consented to in the Joint Offer or this Order, as the sole basis for any other proceeding brought by the Commission other than a proceeding in bankruptcy, or to enforce the terms of the Order. Nor do Respondents consent to the use of the Joint Offer or this Order, or the findings consented to in the Joint Offer or this Order, by any other party in any other proceeding.

III.

The Commission finds the following:

A. SUMMARY

Between May 2000 and July 2000, on at least three occasions, Jorge Mattos, an employee and agent of Hencorp, used non-*bona fide* coffee exchange for physical transactions ("EFPs")[2] to facilitate the transfer of at least $385,000 between foreign futures accounts that he knew were under common control and ownership. None of the EFPs involved any actual exchange of physical coffee. Instead, the sole purpose of the EFPs was to transfer money from one foreign entity's futures account to the futures account of another foreign entity under common control and ownership. The futures transactions were posted on the Coffee, Sugar & Cocoa Exchange ("CSCE"), at the time, a subsidiary of the New York Board of Trade ("NYBOT"). The EFPs resulted in the reporting of non-*bona fide* prices. During the relevant time period, Oscar Schaps was a principal and managing director of Hencorp.

Because Mattos' intention was to negate market risk and price competition, and thereby to avoid a *bona fide* market transaction, Mattos violated Section 4c(a) of the Act, 7 U.S.C. § 6c(a) (2002), which, *inter alia*, prohibits any person from entering into a transaction that is, or is of the character of, or is commonly known to the trade as, a 'wash sale.' By entering into wash sales, Mattos also violated the proscription contained in Section 4c(a) of the Act, 7 U.S.C. § 6c(a) (2002), against entering into a transaction that is used to cause any price to be reported, registered or recorded that is not a true and *bona fide* price. Further, by transmitting an order that was not executed openly and competitively, but in a manner that avoided the market risk and price competition that legitimate, competitive trading entails, Mattos violated Commission Regulation 1.38(a), 17 C.F.R. § 1.38(a) (2004). Because Mattos was an employee of Hencorp and undertook his actions within the scope of his employment with Hencorp, Hencorp is liable for the violation of Section 4c(a) of the Act, 7 U.S.C. § 6c(a) (2002) and Commission Regulation 1.38(a), 17 C.F.R. § 1.38(a) (2004), pursuant to Section 2(a)(1)(B) of the Act, 7 U.S.C. § 2(a)(1)(B) (2002).

During the relevant time period, defendant Oscar Schaps was a principal and managing director of Hencorp and managed the coffee trading desk. Schaps failed to diligently supervise Mattos' handling of the customer accounts at issue. Accordingly, Schaps violated Section 166.3 of the Regulations, 17 C.F.R. § 166.3 (2004).

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[2] An EFP is a transaction in which the buyer of a physical commodity transfers to the seller a corresponding amount of long futures contracts or receives from the seller a corresponding amount of short futures, at a price difference mutually agreed upon.

B. RESPONDENTS

Hencorp Becstone Futures LC was throughout the relevant time period a Florida corporation with its principal place of business at 777 Brickell Avenue, Suite 1010, Miami, Florida, 33131. Hencorp has been registered with the Commission as an introducing broker ("IB") from April 9, 1999 through the present.

Jorge Mattos, who resides in Miami, Florida, was registered as an associated person ("AP") of Hencorp from April 9, 1999 to December 31, 2002. He is not currently registered.

Oscar Schaps, who resides in Miami, Florida, has been a principal of Hencorp from April 9, 1999 to the present, and a managing director of Hencorp from May, 2000 to the present. Schaps has been registered as an associated person ("AP") of Hencorp from April 9, 1999 to the present.

C. FACTS

In June 1999, a Brazilian coffee company (the "Primary Account Holder") opened a futures trading account (the "Primary Account") through Hencorp. Jorge Mattos was the Hencorp AP who handled the Primary Account. Coffee futures trading activity in 1999 in the Primary Account was limited, but resulted in significant losses in the Primary Account.

In December 1999, a representative of the Primary Account Holder met with Mattos in Miami, Florida, to explore the possibility of generating profitable transactions in the Primary Account. At this meeting, Mattos stated that the Primary Account Holder could recognize a profit in the Primary Account without being exposed to any economic risk. Mattos stated that the Primary Account Holder would have to open a new account that would incur a corresponding loss more or less equal to the profit recognized in the Primary Account. Shortly thereafter, a related company incorporated in the British Virgin Islands (the "Counterparty") opened a futures trading account (the "Counterparty Account") for the purpose of acting as the counterparty to the Primary Account Holder in the transactions proposed by Mattos. Mattos and Schaps knew that the Primary Account Holder and the Counterparty were commonly owned, and that the same individual called in trades for the two accounts.

On three occasions between May 18, 2000, and July 11, 2000, Mattos simultaneously established equal and opposite futures positions on behalf of the Primary Account and the Counterparty Account. Within ten minutes of each of these three transactions, Mattos then transmitted orders for the futures side of the EFPs between the Primary Account Holder and the Counterparty liquidating the previously established futures positions, resulting in futures profits in the Primary Account of $385,000 and corresponding futures losses in the Counterparty Account of $385,000.

None of the three EFPs involved an actual transfer of physical coffee between the parties, and no such transfer was ever comtemplated. Instead, the parties only executed the futures portion of the EFPs at a non-competitive price. The transactions were intentionally structured by

Mattos so that the Primary Account holder was not exposed to any economic risk. CSCE rules require that there be a buyer and a seller on the physical side of every EFP transaction.

D. LEGAL DISCUSSION

1. Hencorp and Mattos entered into Wash Sales in Violation of Section 4c(a) of the Act

Section 4c(a) of the Act makes it "unlawful for any person to offer to enter into, enter into, or confirm the execution of a transaction" that "is, is of the character of, or is commonly known to the trade as, a 'wash sale' . . . ." A wash sale is a form of fictitious transaction. *In re Gimbel,* [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,213 at 35,003 (CFTC Apr. 14, 1988), *aff'd as to liability*, 872 F.2d 196 (7th Cir. 1989); *In re Goldwurm,* 7 A.D. 265, 274 (CEA 1948).

Wash sales are deemed harmful, in part, because they draw victims into the market through the creation of illusory price movements. *See Wilson v. CFTC,* 322 F.3d at 559; *Reddy v. CFTC*, 191 F.3d 109, 115 (2d Cir. 1999). *See also CFTC v. Savage*, 611 F.2d 270, 284 (9th Cir. 1980) (wash sales may mislead market participants because they do not reflect the forces of supply and demand); *In re Piasio*, [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 28,276 at 50,691 (CFTC Sep. 29, 2000) (wash sales are "grave" violations, even in the absence of customer harm or appreciable market effect, because "they undermine confidence in the market mechanism that underlies price discovery.")

The central characteristic of a wash sale is the intent to avoid making a *bona fide* transaction or taking a *bona fide* market position. *In re Citadel Trading Co. of Chicago, Ltd.*, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,082 at 32,190 (CFTC May 12, 1986). The factors that indicate a wash result are (1) the purchase and sale (2) of the same delivery month of the same futures contract (3) at the same (or a similar) price. *In re Gilchrist*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,993 at 37,653 (CFTC Jan. 25, 1991). Here, the Respondents' customers purchased and sold the same delivery month of the same futures contracts at the same price with the intention of avoiding a *bona fide* transaction.

In addition to the factors enumerated in *Gilchrist*, the liability of the customer initiating the wash sale depends upon evidence demonstrating that the customer intended to negate market risk or price competition. *Piasio*, ¶ 28,276 at 50,685. Market risk or price competition is negated "when it is reduced to a level that has no practical impact on the transactions at issue." *Gimbel,* ¶ 24,213 at 35,004 n.7. Similarly, the liability of a participant in the wash sale depends upon the demonstration that the participant knew, at the time he chose to participate in the transaction, that the transaction was designed to achieve a wash result in a manner that negated risk. *In re Bear Sterns & Co.*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,994 at 37,665 (CFTC Jan. 25, 1991).

"Just as a customer has a duty not to initiate transactions with an intent to avoid a bona fide market position, . . . an FCM has a duty not to accept such orders and transmit them to the trading floor." *In re Three Eight Corporation*, [1992-1994 Transfer Binder] Comm. Fut. L. Rep.

(CCH) ¶ 25,749 at 40,445). (CFTC June 16, 1993). Therefore, "[a] broker is responsible for evaluating the orders he receives for indications that his participation in the transaction is legally prohibited." *Id.*, ¶ 25,749 at 40,445; *see also Piasio*, ¶ 28,276 at 50,689 (an account executive has a duty to inquire about a customer's intent when he receives simultaneous orders to buy and sell the same spread).

Mattos knew that his customers were entering into EFPs with related entities and intentionally structured the trades with the intent to negate market risk and price competition, and thereby to avoid a *bona fide* market transaction. Nevertheless, Mattos transmitted to the CSCE floor the futures side of the EFPs. Accordingly, Mattos knowingly participated in wash sales and therefore violated Section 4c(a) of the Act. Because Mattos was a Hencorp employee and acting within the scope of his employment, Hencorp is liable for such violation pursuant to Section 2(a)(1)(B) of the Act.

2. Hencorp and Mattos Caused Prices to be Reported, Registered, or Recorded at Non-*Bona Fide* Prices in Violation of Section 4c(a) of the Act

Section 4c(a) of the Act makes it unlawful to offer to enter into, enter into, or confirm the execution of any commodity futures transaction "if such transaction is used to cause any price to be reported, registered or recorded which is not a true and bona fide price." Consequently, by knowingly participating in wash sales, Mattos violated Section 4c(a) of the Act. *Gilchrist*, ¶ 24,993 at 37,653. Further, because Mattos was a Hencorp employee and acting within the scope of his employment, Hencorp is liable for such violation pursuant to Section 2(a)(1)(B) of the Act.

3. Hencorp and Mattos Executed Non-competitive Trades in Violation of Commission Regulation 1.38(a)

Commission Regulation 1.38(a) requires that all purchases and sales of commodity futures be executed "openly and competitively." The purpose of this requirement is to ensure that all trades are executed at competitive prices and that all trades are directed into a centralized marketplace to participate in the competitive determination of the price of futures contracts.[3] Non-competitive trades are generally transacted in accordance with expressed or implied agreements or understandings between and among the traders. *Gilchrist*, ¶ 24,993 at 37,652. Trades can be noncompetitive even though they were executed in the pit. *In re Buckwalter*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,994 at 37,683 (CFTC Jan. 25, 1991) (citing *Laiken v. Dep't of Agriculture*, 345 F.2d 784, 785 (2d Cir. 1965)).

By transmitting the futures side of the EFP transactions so as to avoid the market risk and price competition which legitimate, competitive trading entails, Mattos, acting within the scope of his employment with Hencorp, violated Commission Regulation 1.38(a). Accordingly, pursuant to Section 2(a)(1)(B) of the Act, Hencorp is liable for this violation.

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[3] *See* Disapproval of Contract Market Rules (CFTC Apr. 27, 1981), 46 F.R. 23516 (Commission disapproving of the Commodity Exchange, Inc.'s proposal to conduct a trading session after the close of regular trading); and Senate Committee on Agriculture and Forestry, Report on H.R. 13113, S. Rep. No. 93-1131, 93rd Cong., 2nd Sess. 16 (1974).

4. Schaps Violated Section 166.3 of the Commission's Regulations

Commission Regulation 166.3 imposes on each Commission registrant, except associated persons with no supervisory duties, a duty to "diligently supervise the handling by its partners, officers, employees and agents . . . of all commodity interest accounts carried, operated, advised or introduced by the registrant, and all other activities . . . relating to its business as a Commission registrant." The "focus of any proceeding to determine whether Rule 166.3 has been violated will be on whether such review occurred and, if it did, whether it was 'diligent.'" *In re Paragon Futures Ass'n.*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,266 at 38,850 (CFTC April 1, 1992). The duty to diligently supervise "include[s] the broader goals of detection and deterrence of possible wrongdoing" by the registrant's employees and agents. *Lobb v. J.T. McKerr & Co.*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,568 at 36,444 (CFTC Dec. 14, 1989). Evidence of violations which "should be detected by a diligent system of supervision, either because of the nature or because the violations have occurred repeatedly" is probative of a failure to supervise. *In re Paragon Futures Ass'n., supra.* The Eleventh Circuit has found a violation of Section 166.3 where a firm and its principal "failed to establish or maintain meaningful procedures for detecting fraud by their employees" and the principal "knew of specific incidents of misconduct, yet failed to take reasonable steps to correct the problems." *See CFTC v. Sidoti*, 178 F.3d at 1137.

Schaps, a registered principal of Hencorp, failed to diligently supervise Mattos, an employee and agent of Hencorp. Schaps was Mattos' direct supervisor. He often interacted with the customers at issue and was aware that the customer corporations engaging in the non *bona-fide* transactions were commonly owned. Given the evidence of Schaps' day-to-day involvement with Mattos and the accounts at issue, and the repeated violations detailed above, Schaps disregarded his supervisory responsibilities and violated Regulation 166.3.

IV.

OFFER OF SETTLEMENT

Respondents have submitted a Joint Offer in which they, without admitting or denying the findings herein: (1) acknowledge service of the Complaint and the Order; (2) admit the jurisdiction of the Commission with respect to the matters set forth herein; (3) waive a hearing, all post-hearing procedures, judicial review by any court, any objection to the staff's participation in the Commission's consideration of the Joint Offer, all claims which they possess under the Equal Access to Justice Act, 5 U.S.C. § 504 (2000) and 28 U.S.C. § 2412 (2000), and the rules promulgated by the Commission in conformity therewith, Part 148 of the Regulations, 17 C.F.R. §§ 148.1-30 (2004), relating to, or arising from this action, and any claim of Double Jeopardy based upon institution of this proceeding or the entry of any order imposing a civil monetary penalty or any other relief; (4) stipulate that the record basis on which the Order may be entered shall consist solely of the Complaint, Order and findings in the Order consented to in the Joint Offer; and (5) consent to the Commission's issuance of the Order, which makes findings as set forth below and: (a) orders Hencorp, Mattos, and Schaps to cease and desist from violating the provisions of the Act and Regulations that they have been found to have violated; (b) imposes a

total civil monetary penalty upon Respondents of $50,000; and (c) orders Hencorp, Mattos, and Schaps to comply with the undertakings consented to in the Joint Offer.

V.

FINDINGS OF VIOLATIONS

Solely on the basis of the consents evidenced by the Joint Offer, and prior to any adjudication on the merits, the Commission finds that Mattos has violated Section 4c(a) of the Act, 7 U.S.C. § 6c(a) (2002), and Section 1.38(a) of the Regulations, 17 C.F.R. § 1.38(a) (2004); Hencorp is liable for Mattos' violations of Section 4c(a) of the Act, 7 U.S.C. § 6c(a) (2002), and Section 1.38(a) of the Regulations, 17 C.F.R. § 1.38(a) (2004) pursuant to Section 2(a)(1)(B) of the Act; and Schaps violated Section 166.3 of the Regulations, 17 C.F.R. § 166.3.

VI.

ORDER

Accordingly, it is hereby ordered that:

1. Hencorp and Mattos cease and desist from violating Section 4c(a) of the Act and Section 1.38(a) of the Regulations;

2. Schaps cease and desist from violating Section 166.3 of the Regulations;

3. Mattos shall not seek registration with the Commission in any capacity for a period of five years after the date of this Order;

4. Respondents shall be jointly and severally liable for a civil monetary penalty in the amount of fifty thousand dollars ($50,000) due within ten days of the date of the Order; payment is to be made by electronic funds transfer, U.S. postal money order, certified check, bank cashier's check, or bank money order, made payable to the Commodity Futures Trading Commission, and sent to Dennese Posey, Division of Enforcement, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, N.W., Washington, D.C. 20581, under cover of a letter that identifies the Respondent as the payee and the name and docket of this proceeding. Respondents shall simultaneously transmit a copy of the cover letter and the form of payment to Gregory Mocek, Director, Division of Enforcement, Commodity Futures Trading Commission, 1155 21st Street, N.W., Washington, D.C. 20581. In accordance with Section 6(e)(2) of the Act, 7 U.S.C. § 9a(2), if Respondents fail to pay the full amount within fifteen (15) days of the due date, it shall be automatically prohibited from the privileges of all registered entities until it shows to the satisfaction of the Commission that payment of the full amount with interest thereon to the date of payment has been made;

5. Respondents acknowledge that failure to comply with the Order shall constitute a violation of the Order and may subject it to administrative or injunctive proceedings, pursuant to the Act; and

6. Respondents Hencorp and Schaps are directed to comply with the following undertakings:

   a. to implement immediately, to the extent not already in place, and enforce procedures reasonably designed to detect and prevent the conduct described in the Order;

   b. to provide, to the extent not already provided, training to Hencorp APs concerning their duties when accepting and confirming the execution of customer orders generally and orders for EFPs in particular; and

   c. to deliver within three months of the date of this Order a report to the Division confirming and providing a detailed description of Respondents' compliance with the undertakings set forth in subsections a and b of this paragraph 6.

7. Respondents are directed to comply with the following undertakings:

   a. neither Hencorp, Mattos, nor Schaps, nor any of their agents or employees, shall take any action or make any public statement denying, directly or indirectly, any findings or conclusions in the Order, or creating, or tending to create, the impression that the Order is without a factual basis; provided, however, that nothing in this provision affects their: (i) testimonial obligations; or (ii) right to take legal positions in other proceedings to which the Commission is not a party. Respondents shall take all steps necessary to ensure that their agents or employees, if any, understand and comply with this undertaking.

b. Hencorp, Mattos, and Schaps will cooperate fully with the Commission's Division of Enforcement in this proceeding and any investigation, civil litigation and administrative proceeding related to this proceeding by, among other things: (i) responding promptly, completely, and truthfully to any inquiries or requests for information; (ii) providing authentication of documents; (iii) testifying completely and truthfully; and (iv) not asserting privileges under the Fifth Amendment of the United States Constitution.

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

By the Commission

Jean A. Webb

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

Dated: December 22, 2004