

UNITED STATES OF AMERICA  
Before the  
COMMODITY FUTURES TRADING COMMISSION

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In the Matter of: : CFTC Docket No. 98-4  
: :  
Competitive Strategies for Agriculture, :  
Ltd.; CSA Investor Services, Inc.; Lee :  
Donald Amundson; Terry Allan Dirksen; :  
Jeffery James Wichmann; William Eugene :  
Arnold; Great Plains Co-op; and Herman :  
Gerdes, :  
: :  
Respondents. :  
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1999 SEP 17 P 1:51  
OFFICE OF PROCEEDINGS

INITIAL DECISION

Appearances:

Terry S. Arbit, Esq., Lidian Pereira, Esq., and Charles F. Wright, Esq. on behalf of  
Commodity Futures Trading Commission Division of Enforcement.

John A. Andreasen, Esq., James Niemeier, Esq., and Thomas McGowan, Esq. on behalf  
of Respondents Great Plains Co-op and Herman Gerdes.

Before:

Painter, ALJ

**OPINION**

On December 22, 1999, the Commodity Futures Trading Commission ("Commission") Division  
of Enforcement ("Division") filed a six count complaint alleging that Respondents violated the  
Commodity Exchange Act ("CEA") by (1) trading illegal off-exchange futures contracts;<sup>1</sup> (2)  
making fraudulent representations in the trading advisor capacity;<sup>2</sup> (3) using the mails, or any

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<sup>1</sup> Count one of the complaint, that Section 4(a) of the CEA was violated, was alleged as against respondents,  
Competitive Strategies for Agriculture, Ltd., CSA-Investor Services, Inc., Jeffery James Wichmann, William  
Eugene Arnold, Lee Donald Amundson, Great Plains and Gerdes.

means of instrumentality of interstate commerce to defraud a client or prospective client;<sup>3</sup> (4) committing fraud with respect to futures contracts;<sup>4</sup> (5) failing to diligently supervise their employees;<sup>5</sup> and (6) failing to hold out to the public the name of the firm of which it is a branch office.<sup>6</sup> All other issues having been resolved,<sup>7</sup> the only issues awaiting resolution are (1) whether Great Plains Co-op and Herman Gerdes ("Respondents") violated Section 4(a) of the CEA by offering and entering into futures contracts illegally off of an exchange; and (2) whether Herman Gerdes violated Section 4(a) of the CEA by aiding and abetting the Great Plains Co-op unlawful off-exchange futures trading venture.

The issues here concern only the Cross Country Hedge-To-Arrive contracts between CSA customers and Great Plains.<sup>8</sup>

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<sup>2</sup> Count two of the complaint, that Section 4o(1)(B) of the CEA was violated, was alleged as against respondents, Competitive Strategies for Agriculture, Ltd., CSA-Investor Services, Inc., Jeffery James Wichmann, William Eugene Arnold, Lee Donald Amundson, and Terry Allan Dirksen.

<sup>3</sup> Count three of the complaint, that Section 4o(1)(A) of the CEA was violated, was alleged as against respondents, Competitive Strategies for Agriculture, Ltd., CSA-Investor Services, Inc., Jeffery James Wichmann, William Eugene Arnold, Lee Donald Amundson, and Terry Allan Dirksen.

<sup>4</sup> Count four of the complaint, that Section 4b(a) of the CEA was violated, was alleged as against respondents, Competitive Strategies for Agriculture, Ltd., CSA-Investor Services, Inc., Jeffery James Wichmann, William Eugene Arnold, Lee Donald Amundson, and Terry Allan Dirksen.

<sup>5</sup> Count five of the complaint, that Section 166.3 of the Regulations was violated, was alleged as against respondent, CSA-Investor Services.

<sup>6</sup> Count six of the complaint, that Section 166.4 of the Regulations was violated, was alleged as against respondents, CSA-Investor Services, Jeffery James Wichmann, and William Eugene Arnold.

<sup>7</sup> Competitive Strategies for Agriculture, Ltd.; CSA Investor Services, Inc.; Lee Donald Amundson; Terry Allan Dirksen; Jeffery James Wichmann; and William Eugene Arnold, all settled with the Commodity Futures Trading Commission. Thus, all that is left in need of judicial resolution is count one with respect to respondents, Great Plains Co-op and Herman Gerdes. See notes, supra, 1-6.

<sup>8</sup> During the entire course of these proceedings, Respondents have attempted to blur the lines between their general hedge-to-arrive contract business and their CSA-Cross Country Hedge-to-Arrive contract enterprise. However, the evidence shows not only that there is a very clear distinction between the two, but that Respondents were deliberate in making the distinction on paper and in practice. The contracts in question were sent via fax order exclusively to Great Plains' Nebraska office, all of the customers were CSA customers and all of the contracts were requested by CSA, and almost every request from CSA contained notation on the fax order as well as notation on the contract order form which indicated that a Cross Country Hedge-to-Arrive contract was being requested.

## FINDINGS OF FACT AND CONCLUSIONS OF LAW

### Competitive Strategies for Agriculture

1. Competitive Strategies for Agriculture, Ltd. is an Iowa corporation that provides marketing advice and services to farmers.<sup>9</sup>
2. A separately incorporated company, CSA Investor Services, Inc. ("CSA-IB"), provides Competitive Strategy for Agriculture's brokerage services. During the time period relevant to this case, CSA-IB was registered as an introducing broker clearing through ADM.<sup>10</sup>
3. Lee Donald Amundson ("Amundson") was a senior grain analyst at CSA and owned 50% of Competitive Strategy for Agriculture Ltd. and CSA-IB.<sup>11</sup>
4. Terry Allan Dirksen ("Dirksen") owned the remaining 50% of Competitive Strategy for Agriculture Ltd. and CSA-IB.<sup>12</sup>
5. CSA-IB opened a branch office in Grand Island, Nebraska in 1993 ("CSA").<sup>13</sup>
6. Primarily, CSA's marketing services were twofold. The first service, cash grain market consulting dealt with how to sell grain to local elevators and feedlots.<sup>14</sup> The second, brokerage

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<sup>9</sup> Hearing Tr. 1/7/99 PM 98:13-20, 98:23-99:1, Hearing Tr. 1/5/99 AM 20:19-21:1. CSA's advice and services included a bi-weekly newsletter, seminars and individual consultation.

<sup>10</sup> Hearing Tr. 1/7/99 PM 99:2-9. CSA Investor Services, Inc. was incorporated in 1989 by Lee Donald Amundson and Terry Allan Dirksen. Hearing Tr. 1/7/99 PM 99:2-9. ADM is Archer Daniels Midland Company. For the time period relevant to this case, ADM was registered with the National Futures Association as a futures commission merchant.

<sup>11</sup> Hearing Tr. 1/7/99 PM 98:5-12, 98:23-99:1, 99:10-14.

<sup>12</sup> Hearing Tr. 1/7/99 PM 98:23-99:1.

<sup>13</sup> Hearing Tr. 1/5/99 AM 21:12-14, 1/6/99 AM 6:1-3.

<sup>14</sup> Hearing Tr. 1/6/99 AM 6:12-24.

services for farmers, was for the purpose of managing risk on crops that were not sold before harvest.<sup>15</sup>

7. William Eugene Arnold ("Arnold") and Jeffrey James Wichmann ("Wichmann") operated CSA as a partnership until its dissolution in 1996.<sup>16</sup>

8. Arnold was involved with CSA from 1993 to 1997 and was registered with the Commission for various intervals between May 19, 1992 and October 8, 1996.<sup>17</sup>

9. Wichmann was registered with the Commission for various intervals between January 18, 1993 and April 1, 1996.<sup>18</sup>

#### Great Plains Co-op and Herman Gerdes

10. Great Plains Co-op ("Great Plains"), one of the oldest cooperatives in Nebraska<sup>19</sup> had between 1,000 to 1,200 members<sup>20</sup> and operated elevators in Benedict and Stromsburg, Nebraska.<sup>21</sup>

11. Great Plains hired Herman Gerdes ("Gerdes") in September 1992, to manage the grain department and grain origination.<sup>22</sup>

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<sup>15</sup> Hearing Tr. 1/6/99 AM 7:2-11.

<sup>16</sup> Hearing Tr. 1/6/99 AM 6:7-9.

<sup>17</sup> Hearing Tr. 1/6/99 AM 5:23-25 and Answer and Cross Claim of Great Plains Co-op, ¶ 7. Arnold was registered with the Commission as an associated person ("AP") of Financial Investor Services ("FIS"), a registered introducing broker ("IB"), from May 19, 1992 through March 1, 1993; as an AP of Harmon Demet Verle, a registered IB, from July 20, 1993 through September 13, 1993; and as an AP of CSA-IB from September 27, 1993 through October 8, 1996.

<sup>18</sup> Answer and Cross Claim of Great Plains Co-op, ¶ 8. Wichmann was registered with the Commission as an AP of FIS from January 18, 1993 through February 16, 1993; and as an AP of CSA-IB from June 23, 1993 through April 1, 1996.

<sup>19</sup> Hearing Tr. 3/29/99 AM 165:19-22. Formerly Farmers' Co-op Grain, the name was changed to Great Plains Co-op in the 1990's. Hearing Tr. 1/6/99 PM 7:6-11.

<sup>20</sup> Hearing Tr. 3/30/99 AM 184:8-11. (Note: all testimony found in the March 27-30, 1999 transcript binder will be referred to as "Hearing Tr. 3/30/99 AM").

12. As manager of the Great Plains grain department, Gerdes had full authority to decide whether or not to enter into a contract and to decide the terms and conditions of that contract.<sup>23</sup>

As an agent of Great Plains, Gerdes was authorized to sign checks on its behalf.<sup>24</sup>

13. Under Gerdes' management, Great Plain's grain department incurred severe losses. Partially due to these losses, Gerdes left Great Plains in April 1995.<sup>25</sup>

14. During the summer of 1995, the financial problems of Great Plains continued to escalate<sup>26</sup> and by February 1, 1996 Great Plains' assets were by and large purchased by United Co-op of Hampton.<sup>27</sup>

#### The Cross Country Hedge-to-Arrive Contract

15. On behalf of Great Plains, Gerdes had a series of meetings ("initial meetings") with representatives from CSA, Arnold and Wichmann, where the three parties discussed the "Cross Country HTA business venture."<sup>28</sup> Two weeks after the first meeting CSA initiated its first

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<sup>21</sup> Hearing Tr. 1/6/99 PM 8:21-25; Answer and Cross Claim of Great Plains Co-op, ¶ 9.

<sup>22</sup> Hearing Tr. 3/30/99 AM 180:12-20, 244:4-6. Gerdes remained in this position at Great Plains until he took medical leave in April 1995. Answer and Cross Claim of Herman Gerdes, ¶ 10.

<sup>23</sup> Hearing Tr. 3/30/99 AM257:14-17, 257:25-258:4.

<sup>24</sup> Great Plains' Response to the Division of Enforcement's Request for Admissions ("RFA") # 20 and RFA # 23.

<sup>25</sup> Hearing Tr. 3/30/99 AM 181:5-18, 286:21-25 and Hearing Tr. 3/30/99 PM 343:1-3, 351:12-13. Gerdes departure from Great Plains is also partially attributable to illness. Answer and Cross Claim of Herman Gerdes, ¶ 10.

<sup>26</sup> Great Plains' losses for the fiscal year ending on January 31, 1995 were approximately \$1.5 million. Hearing Tr. 3/30/99 AM 352:18-352:5. Losses were estimated in a subsequent audit, around mid-1995, to be approximately \$1.5 million. Hearing Tr. 3/30/99 AM 354:7-16.

<sup>27</sup> Hearing Tr. 3/30/99 PM 298:11-13, 325:22-326:2 and Answer and Cross Claim of Great Plains Co-op, ¶ 9.

<sup>28</sup> Hearing Tr. 3/30/99 AM 281:9-19 and Hearing Tr. 1/6/99 AM 12:4-9. Gerdes introduced the Cross Country HTA to Arnold and Wichmann. Hearing Tr. 1/6/99 AM 12:2-16, 46:11-14. In the initial meetings, all three parties used the term "Cross Country Hedge-to-Arrive" to refer to the Cross Country HTA contract. Hearing Tr. 1/6/99 AM 12:2-16 and 46:11-14.

position with Great Plains.<sup>29</sup> The contracts between CSA customers and Great Plains will hereinafter be referred to as "Cross Country HTA."

16. In the initial meetings with Arnold and Wichmann, Gerdes described how the Cross Country HTA contract functioned. *Theoretically*, producers could sell grain to Great Plains by either delivering to a Great Plains elevator or, if the producer was outside of Great Plains' geographic range, by delivering to any elevator in the producer's local cash market.<sup>30</sup> In the latter case, the receiving elevator was to pay Great Plains and Great Plains would then make price adjustments and pay the producer accordingly.<sup>31</sup> The Court finds that, *in practice*, Great Plains did not require or even expect delivery on these modified hedge-to-arrive contracts.<sup>32</sup>

17. It is important to note here that throughout these proceedings, Respondents claimed that the distinction between the Cross Country HTA contract and their local contract is a fictitious one and they point to the fact that not all contracts named in this proceeding are expressly entitled "Cross Country."<sup>33</sup> However, the substantive issue being decided in this case is not the title of the contracts but their function. 'Findings of Facts and Conclusions of Law,' *infra*, 18 through 22 serve to definitively delineate the group of contracts in question. In addition, 'Finding of Facts and Conclusions of Law,' *infra*, 22 through 29 establish that the contracts in question functioned as futures contracts.

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<sup>29</sup> Hearing Tr. 1/7/99 AM 61:7-15.

<sup>30</sup> Hearing Tr. 1/6/99 AM 12:17-13:5.

<sup>31</sup> *Id.* See also Hearing Tr. 3/30/99 AM 50:4-8 (Arnold testifying that CSA customers could decide where to deliver).

<sup>32</sup> See Hearing Tr. 1/7/99 AM 18:25-19:3 (Wichmann testifying that delivery was not required); Hearing Tr. 3/30/99 AM 259:10-16 (Gerdes testifying that no CSA customer ever delivered to Great Plains); and Hearing Tr. 1/6/99 PM 33:2-5 (Joyce Brazda (note, *infra*, 35) testifying that no CSA customer delivered to Great Plains pursuant to a hedge-to-arrive contract).

<sup>33</sup> Hearing Tr. 1/5/99 AM 25:14-25.

18. All of the CSA Cross Country HTA contract orders were faxed to Great Plains' Stromsburg office where Gerdes worked.<sup>34</sup> Gerdes and two other Great Plains employees<sup>35</sup> were the only people who could handle the CSA customer contracts and only Gerdes could enter into the Cross Country HTA contract.<sup>36</sup>

19. The fax orders from CSA indicated to Great Plains that the contract being requested was a Cross Country HTA.<sup>37</sup> CSA informed Great Plains that it was placing an order for a Cross Country HTA contract by denoting "CCHTA," "CC," or "588 Account" on the fax offers.<sup>38</sup>

20. The term "Cross Country Hedge-to-Arrive" was not consistently used on every document but the documents did not have to say "Cross Country Hedge-to-Arrive" in order for the contract to function as a Cross Country HTA contract.<sup>39</sup>

21. Great Plains maintained a separate account with FCC for their Cross Country HTA business and Great Plains kept its CSA Cross Country HTA contracts separate from their local contracts<sup>40</sup> and even had an account, the 588 account, used to hedge the Cross Country HTA contracts.<sup>41</sup>

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<sup>34</sup> Hearing Tr. 1/6/99 PM 18:6-19:3.

<sup>35</sup> Joyce Brazda was a employee at Great Plains' Stromsburg Branch who worked under the direct supervision of Gerdes. Hearing Tr. 1/6/99 PM 9:22-23. Margaret Topil worked with and then as a substitute for Gerdes at Great Plains' Stromsburg Branch. Hearing Tr. 1/6/99 PM 9:7-12.

<sup>36</sup> Hearing Tr. 1/6/99 PM 18:-19:3.

<sup>37</sup> Hearing Tr. 1/6/99 PM 33:23-34:2. Joyce Brazda testified that the Great Plains-CSA business and the Cross Country HTA contracts were "one in the same." Great Plains also knew that a Cross Country HTA contract was being ordered by CSA simply by receiving a fax order from CSA because that was the nature of their business relationship. Hearing Tr. 1/6/99 AM 8:9-15, 16:2-5, Hearing Tr. 1/6/99 PM 33:23-34:2, and Hearing Tr. 1/7/99 AM 18:25-19:3.

<sup>38</sup> Hearing Tr. 1/7/99 AM 18:19-19:10. See also DX 311, DX 356, DX 414 and DX 417.

<sup>39</sup> Hearing Tr. 1/6/99 AM 36:4-17, 39:4-10, 66:14-23, Hearing Tr. 1/7/99 AM 40:19-41:3, DX 351, DX 373A, DX 420 and DX 508.

22. The destination boxes on Great Plains's cash forward contract forms which read, "seller's call," "seller's option," or "open," or which are left blank, informed Great Plains that the contract form was a Cross Country HTA contract.<sup>42</sup> The boxes with this distinct notation and the blank destination boxes were (1) an indication that the contracts being entered into were Cross Country HTA contracts and also (2) an indication that delivery on these Cross Country HTA contracts would not occur.

23. The documents of record establish that Great Plains referred to its CSA Cross Country HTA contracts as a futures trading enterprise.<sup>43</sup> The checks that Great Plains paid to CSA customers stated "Futures Payable" or "Cross Country Trading for CSA."<sup>44</sup>

24. The checks and invoices that Great Plains sent to CSA Cross Country HTA customers are for futures profits minus Great Plains service fees<sup>45</sup> and do not have deductions for moisture

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<sup>40</sup> See Hearing Tr. 1/6/99 PM34:3-35:21 (Joyce Brazda testifying that generally the month-end reports for the Cross Country HTA contracts were printed separately). See also, DX 415 (A spreadsheet of only "Local Customer Hedge-to-Arrive Contracts").

<sup>41</sup> Hearing Tr. 3/30/99 PM 297:12-18, Hearing Tr. 1/6/99 AM 62:6-14, Hearing Tr. 1/7/99 AM 13:18-14:10, 14:22-15:11, Hearing Tr. 1/7/99 PM 44:1-2, 71:1-20 and DX 414. Great Plains had an account with Farmers Commodities Corporation used to hedge only the Cross Country HTA contracts. Hearing Tr. 1/6/99 AM 62:15-23. The Farmer's Commodities Corporation is the same FCM that handled the "Flex Hedge-to-arrive" contracts, also found to be illegal off exchange contracts, in In re Grain Land Co-op, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,459 at 47,180-47,181 (CFTC Nov. 6, 1998).

<sup>42</sup> See Hearing Tr. 1/6/99 AM 66:18-67:18, 68:8-12, 104:12-12, Hearing Tr. 1/6/99 PM 17:6-18, 36:1-9, Hearing Tr. 1/7/99 AM 20:17-21:7, 21:9-13, 32:4-6, Hearing Tr. 3/30/99 AM 233:2-12 and 233:17-19. See also DX325, DX 337, DX 338, DX 341 and DX 508.

<sup>43</sup> See the documents Respondents used to track their CSA customers accounts: DX 438 and DX 518 ("Futures Statement"); DX 435A ("Futures Trading Statement"); DX 520 and DX 547 ("Great Plains Commodities Trading Statement"); DX 506 and DX 526 ("Profit & Loss on Closed Trades"). See also DX 116, DX 249, DX 262A, DX 263A, DX 274, DX 331A, DX 342, DX 346, DX 438, DX 441, DX 444, DX 503, DX 518, DX 520, DX 528, and DX 547.

<sup>44</sup> See DX 117 (check for \$4,000 "Futures Payable"), DX 151 (\$4,637 "Futures Payable"), DX 248 (\$2,975 "Futures Payable"), and DX 504 (\$2,685 "Futures Payable"), DX 525 (\$6,500 "Cross Country Trading for CSA"), DX 501 (\$1,800 "Cross Country Trading for CSA"), and DX 484 (\$1,300 "Cross Country Trading for CSA").

<sup>45</sup> DX 151, DX 311, and DX 365.

content or taxes.<sup>46</sup> Also, the "Cash Basis," "Cash Pricing," "Final Pricing Date," "Date," and "Final Contract" boxes were never filled in on the Cross Country HTA contract forms.<sup>47</sup>

25. Great Plains entered into Cross Country HTA contracts with CSA customers who were located outside of its traditional territory,<sup>48</sup> CSA customers that operated seed corn businesses,<sup>49</sup> CSA customers that operated feedlot business,<sup>50</sup> and people who were not farmers and did not own farmland.<sup>51</sup> None of the CSA Cross Country HTA contract holders (whether in one of the aforementioned categories or not) ever delivered grain to Great Plains.<sup>52</sup>

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<sup>46</sup> A witness called by Respondents, Richard E. Gruber, is a producer that delivered to Great Plains for 18 years. He testified that Great Plains typically made deductions for grain tax, ethanol tax, or drying. Hearing Tr. 3/30/99 AM 157:29-158:6. However, none of the stubs attached to the checks sent to CSA customers had these standard deductions. See the following exhibits, all of which are check stubs that read "Futures Payable": DX 117, DX 151, DX 248, and DX 504. See the following exhibits, all of which are check stubs that contain notation denoting the 588 sub-account: DX 203, DX 242, DX 322, DX 349, DX 353, DX 360, and DX 532. See the following exhibits, all of which are check stubs that refer to trade numbers: DX 203, DX 242, DX 343, DX353, DX 360, DX 434, DX 519, and DX 532.

<sup>47</sup> Hearing Tr. 1/5/99 AM 50:5-13 and DX 449; Hearing Tr. 1/5/99 AM 97:5-13 and DX 261; Hearing Tr. 1/7/99 SM 17:3-5 and DX 369; and DX 127 and DX 197.

<sup>48</sup> Gerdes testified that the fax orders normally included the address of the CSA customers. Hearing Tr. 3/30/99 255:16-23. Gerdes further testified that there were "probably half a dozen" CSA customers within the traditional territory and that the remaining CSA customers were outside of the traditional territory and most of these were located to other elevators. Hearing Tr. 3/30/99 254:-255:15. See also notes, *infra*, 91-93.

<sup>49</sup> See notes, *infra*, 95-100.

<sup>50</sup> See notes, *infra*, 101-102.

<sup>51</sup> See notes, *infra*, 103-105.

<sup>52</sup> Gerdes testified there was never an instance in which grain was delivered to Great Plains by a CSA customer. Hearing Tr. 3/30/99 AM 259:10-16. Respondents did not offer any evidence into the record that would prove otherwise.

Respondents did, however, argue that delivery "through" Great Plains was sufficient to qualify as a cash forward contract and thus, fits within the narrow exclusion to the CEA's jurisdiction. The Court finds that delivery "through" Great Plains does not amount to a cash forward contract.

First, this defense can only apply to the few CSA customers who do not fall into the categories described in Finding of Fact 25 (CSA customers with no available grain). Delivery "through" only occurred a couple of times in the beginning of the Cross Country HTA contract scheme and was then abandoned. Hearing Tr. 1/6/99 AM 47:2-10. Thereafter, any CSA customers who delivered grain to an elevator did so without mention of Great Plains. See Joint Stipulations of the Division of Enforcement and Respondents Great Plains Co-op and Herman Gerdes, ¶ 1, ¶ 4a, ¶ 4b, and 4c. See also, Hearing Tr. 1/5/99 APM 8:20-9:25, 10:1-6, and 11:6-9.

26. Great Plains routinely permitted CSA customers to roll their Cross Country HTA contracts.<sup>53</sup> In fact, Great Plains entered into Cross Country HTA contracts with CSA customers knowing that the customer planned to roll the contract.<sup>54</sup>

27. Great Plains allowed all CSA customers to offset their Cross Country HTA contracts.<sup>55</sup> All that was required to do so was a fax or telephone call.<sup>56</sup> Great Plains entered into subsequent Cross Country HTA contracts with CSA customers who had cash liquidated Cross Country HTA contracts in the past.<sup>57</sup>

28. There were 43 instances in which Great Plains paid CSA customers futures profits derived from a Cross Country HTA contract.<sup>58</sup> There were 7 instances in which Great Plains

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Second, delivery was not mandatory as evinced by the fact that Great Plains allowed CSA customers to cash liquidate and roll without any regard for whether they had grain or whether it had been sold to the local elevator. Hearing Tr. 1/6/99 AM 48:13-25.

Finally, delivery "through" Great Plains "d[oes] not change the status of the contract." Hearing Tr. 1/8/99 AM 42:2-20 (testimony of division expert, Peter R. Locke). Delivery "through" Great Plains never resulted in a transfer of title Great Plains and Great Plains never received "possession and control of the commodity." Locke Declaration ¶ 24.

The bottom line: delivery by CSA customers to other elevators does not insulate Great Plains from liability because the record clearly establishes that delivery in those circumstances had nothing to do with Great Plains.

<sup>53</sup> See notes, *infra*, 130-133.

<sup>54</sup> Great Plains entered into all contracts requested from CSA including contracts on which CSA employees wrote that the contracts would be rolled at some point in the future. See DX 169 ("will be rolling to Dec 95"), DX 423 ("will be rolling to Dec 95"), and DX 373-388 (all sixteen contracts read "Plan on rolling this to Z6 sometime" meaning Dec 96). This is at odds with Respondents' assertion that they intended to accept delivery on the Cross Country HTA contracts and Respondents' assertion that these were cash forward contracts.

<sup>55</sup> See DX 115, DX 116, DX 117, DX 150, DX 151, DX 132, DX 172, DX 175, DX 203, DX 242, DX 248, DX 254, DX 261A, DX 262, DX 263, DX 272, DX 287, DX 288, DX 304, DX 305, DX 322, DX 323, DX 324, DX 328, DX 331, DX 343, DX 347, DX 349, DX 352, DX 353, DX 363, DX 365, DX 413, DX 419, DX 428, DX 429, DX 434, DX 360, DX 437, DX 438, DX 439, DX 439A, DX 440, DX 443, DX 457, DX 471, DX 501, DX 504, DX 507, DX 519, DX 521, DX 525, DX 527, DX 529, DX 532 and DX 647.

<sup>56</sup> Hearing Tr. 1/7/99 AM 23:5-11. See DX 129, DX 131, DX 150, DX 173, DX 174, DX 396, DX 397, DX 442, DX 483, DX 513, and DX 523.

<sup>57</sup> Hearing Tr. 1/7/99 AM 26:25-27:4, 27:12-14, 40:13-17, DX 347, DX 379, DX 530, RFA # 54, and RFA # 90.

<sup>58</sup> Hearing Tr. 1/7/99 PM 42:5-8. See DX 115, DX 116, DX 117, DX 150, DX 151, DX 132, DX 172, DX 175, DX 203, DX 248, DX 254, DX 262, DX 263, DX 287, DX 288, DX 304, DX 305, DX 322, DX 328, DX 331, DX 343, DX 347, DX 349, DX 352, DX 353, DX 434, DX 360, DX 440, DX 443, DX 457, DX 471, DX 501, DX 504, DX 507, DX 519, DX 521, DX 525, DX 527, DX 529, and DX 532.

charged CSA customers for futures losses associated with their Cross Country HTA contracts.<sup>59</sup> Delivery did not occur in relation to any of these transactions.<sup>60</sup>

29. The promotional brochure, which Gerdes used to present the Cross Country HTA contract<sup>61</sup> to Arnold and Wichmann and which used to solicit customers,<sup>62</sup> permits Cross Country HTA contract holders to “offset[] the contract” if they decided that they “would rather not make delivery of the grain.”<sup>63</sup> The Court finds that this statement grants unilateral authority to the CSA customer to cancel the Cross Country HTA contract, which defeats any expectation that delivery will occur.<sup>64</sup>

## DISCUSSION

### Introduction

The Commodity Futures Trading Commission (“Commission”) has jurisdiction over all “contracts for the purpose or sale of a commodity for *future* delivery.”<sup>65</sup> (emphasis added). The definition of “future delivery” set forth by the Commodity Exchange Act (“CEA”) “does not

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<sup>59</sup> Hearing Tr. 1/7/99 PM 64:19-20, 65:1-7, DX 323, DX324; DX 363, DX 365; Hearing Tr. 1/6/99 AM 63:6-125, DX 429; DX 428; Hearing Tr. 1/5/99 AM 98:8-18, 1085-12, 110:8-23, 111:8-16, 123:8-24, 123:8-24, DX 261A, DX 272; Hearing Tr. 1/5/99 PM 24:8-15, 50:4-9, DX 242, DX 647; and Hearing Tr. 1/5/99 AM 26:12-14, 28:5-15, 29:15-24, 29:25-30:7, DX 437, DX 438, DX 439, DX 439A.

<sup>60</sup> See Hearing Tr. 1/7/99 AM 18:25-19:3 (Wichmann testifying that delivery was not required); Hearing Tr. 3/30/99 AM 259:10-16 (Gerdes testifying that no CSA customer ever delivered to Great Plains); and Hearing Tr. 1/6/99 PM 33:2-5 (Joyce Brazda (note, supra, 35) testifying that no CSA customer delivered to Great Plains pursuant to a hedge-to-arrive contract).

<sup>61</sup> Hearing Tr. 3/30/99 AM 228:22-229:5, and 229:13-230-9.

<sup>62</sup> Hearing Tr. 1/7/99 AM 72:22-73:1, Hearing Tr. 3/30/99 AM 228:22-229:5, 229:13-230-9, DX 413 and DX 419.

<sup>63</sup> DX 413 and DX 419.

<sup>64</sup> See In re Grain Land Co-op, [Current transfer binder] Comm. Fut. L. Rep. (CCH) ¶ 27,459 at 47,192 (CFTC Nov. 6, 1998).

<sup>65</sup> Commodity Exchange Act Section 4(a).

include any sale of any cash commodity for *deferred* shipment or delivery.”<sup>66</sup> (emphasis added). Resolution of this case turns on whether the contracts between CSA customers and Great Plains were futures contracts as alleged by the Division, or cash forward contracts as argued by the Respondents.

Though the emphasized terms are not explicitly defined in the CEA, an examination of legislative history, as elucidated in applicable case law, demonstrates that Congress intended to exclude cash forward contracts from the Commission’s jurisdiction.<sup>67</sup> The legislation enacted to regulate commodity futures, the Futures Trading Act of 1921,<sup>68</sup> the Grain Futures Act of 1922<sup>69</sup> (the predecessors to the CEA) and the CEA, were enacted for the purpose of regulating futures trading where price risks are generally transferred from “suppliers, processors and distributors (hedgers) to those more willing to take the risk (speculators).”<sup>70</sup> Cash forward contracts, like those transacted between farmer and local grain elevator, are not accompanied by the same risks of price manipulation, speculation, “outright wagering,” and other trade abuses which are inherent in futures trading.<sup>71</sup> Accordingly, in legislation regulating commodity futures, Congress consistently and purposefully distinguished between futures contracts i.e. commodity contracts transacted “primarily for the purpose of assuming or shifting the risk” on commodity prices, and

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<sup>66</sup> Commodity Exchange Act Section 1a (11).

<sup>67</sup> In re Stovall, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941 at 23,777 (CFTC Dec. 6, 1979); In re Grain Land Co-op, [Current transfer binder] Comm. Fut. L. Rep. (CCH) ¶ 27,459 at 47,190 (CFTC Nov. 6, 1998); CFTC v. Co. Petro, 680 F.2d 573, 581 (9th Cir. 1982).

<sup>68</sup> Futures Trading Act, Pub. L. No. 67-66, 42 Stat. 187 (1921).

<sup>69</sup> Grain Futures Act of 1922, Pub. L. No. 67-331, 42 Stat. 998 (1922).

<sup>70</sup> Salomon Forex, Inc. v. Tauber, 8 F.3d 966, 971 (4th Cir. 1993).

<sup>71</sup> Id.

cash forward contracts, i.e. commodity contracts transacted primarily for the actual transfer of ownership of the tangible commodity through delivery.<sup>72</sup>

Because the [Commodity Exchange] Act was aimed at manipulation, speculation, and other abuses that could arise from the trading in futures contracts and options, as distinguished from the commodity itself, Congress never purported to regulate “spot” transactions (transactions for the immediate sale and delivery of a commodity) or “cash forward” transactions (in which the commodity is presently sold but its delivery is, by agreement, delayed or deferred).<sup>73</sup>

In other words, the narrow exclusion was to ensure that the legislation did not affect “the farmer selling his grain to the mill.”<sup>74</sup>

This, however, is not a case of a farmer selling his grain to the mill. Instead, this is a case in which Respondents entered into illegal off-exchange futures contracts on behalf of the customers they acquired through CSA. In the summer of 1993, on behalf of the Great Plains grain department, Gerdes met with Arnold and Wichmann.<sup>75</sup> In this meeting they devised the Cross Country HTA contractual relationship wherein CSA would solicit customers to enter into Cross Country HTA contracts with Great Plains.<sup>76</sup> Delivery was not mandatory, and not one bushel of grain was ever delivered to Great Plains pursuant to the terms of the contract.<sup>77</sup> Great Plains’ role in servicing the Cross Country HTA contracts was to take the opposite side of the CSA customer in a futures contract. Great Plains maintained a separate futures account to hedge

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<sup>72</sup> In Re Stovall, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941 at 23,777 (CFTC Dec. 6, 1979).

<sup>73</sup> Salomon Forex, Inc. v. Tauber, 8 F.3d 966, 970 (4th Cir. 1993).

<sup>74</sup> In Re Stovall, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941 at 23,777 (CFTC Dec. 6, 1979) (quoting Hearings on Futures Trading Before the House Committee on Agriculture, 66th Cong., 2d Sess. 213 (1921)(testimony of George T. McDermott, representative of the Kansas Grain Dealer’s Association)).

<sup>75</sup> Hearing Tr. 3/30/99 281:9-19.

<sup>76</sup> Hearing Tr. 1/6/99 AM 12:17-13:35.

<sup>77</sup> Gerdes testified that although delivery through Great Plains occurred, no grain was delivered to Great Plains by a CSA customer. Hearing Tr. 3/30/99 AM 259:10-16.

its risk vis a vis the CSA customer obligations.<sup>78</sup> This account, the 588 sub-account, was carried with the Farmer's Commodities Corporation ("FCC"),<sup>79</sup> a futures commission merchant ("FCM"), and the contracts were executed on the Chicago Board of Trade. The CSA clients did not have an account with FCC, owned no interest in the 588 sub-account, and were not parties to any exchange traded futures contracts. Neither the CSA introduced customers nor Great Plains intended to make or take delivery of grain on the Cross Country HTA contracts. Speculation was the sole purpose of the transactions.

A futures contract, roughly speaking, is a fungible promise to buy or sell a particular commodity at a fixed date in the future. Futures contracts are fungible because they have standard terms and each side's obligations are guaranteed by a clearing house. Contracts are entered into without prepayment, although the markets and clearing house will set a margin to protect their own interests. *Trading occurs in "the contract" not in the commodity.*<sup>80</sup> (emphasis added)

The Cross Country HTA contracts at issue fit four square with the Seventh Circuit's definition of a futures contract. Furthermore, Section 4d of the CEA requires anyone "involv[ed] in any contracts of sale of any commodity for future delivery, on or subject to the rules of any contract market" to be registered as an FCM or introducing broker.<sup>81</sup> Although Great Plains' role in the Cross Country HTA scheme was analogous to that of an FCM or an introducing broker, Great Plains was not registered with the Commission.

Since Great Plains was not registered with the Commission, it did not comply with the record keeping requirements of section 4g(c) of the CEA.<sup>82</sup> Consequently, there are no office

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<sup>78</sup> Hearing Tr. 1/6/99 AM 62:6-14, 62:15-23, 1/7/99 AM 13:18-14:20, 14:12-15:11, Hearing Tr. 1/7/99 PM 44:1-2, 71:1-12, 72:1-20, and DX 414, 417.

<sup>79</sup> Hearing Tr. 3/30/99 PM 297:12-18.

<sup>80</sup> Chicago Mercantile Exchange v. SEC, 883 F.2d 537, 542 (7th Cir. 1989).

<sup>81</sup> Commodity Exchange Act Section 4d.

order tickets, floor order tickets, or trading cards confirming that CSA customer positions were backed by an identical position in Great Plains' 588 account. In fact, there is no evidence that Great Plains executed trades that corresponded precisely to every Cross Country HTA contract. Instead, the evidence shows that Great Plains used the 588 account to hedge its obligations to CSA customers. Furthermore, CSA customers had no control over the 588 account, and Great Plains alone determined how it would hedge its obligations to the customers. Simply put, the CSA-Great Plains enterprise constituted a bucket shop operation.<sup>83</sup>

As noted above, the Seventh Circuit Court of Appeals has provided a clear and unambiguous definition of a futures contract. The contract at issue, devised by Herman Gerdes for Great Plains, was nothing less than an off-exchange futures contract. The CSA customers who entered into Cross Country HTA contracts with Great Plains were exposed to all the risks inherent in futures trading, and had none of the protections afforded to customers trading lawful futures contracts through a registered entity. Unfortunately, there was no clearinghouse to enforce the obligations of the parties to the contract.

An examination of Great Plains' intent with respect to the Cross Country HTA contracts demonstrates that these contracts do not fall within the narrow cash forward exclusion to the CEA's jurisdiction. An examination of the characteristics of the contract further evinces the fact that these contracts do not fall within the exclusion and that they were, in fact, illegal off-exchange futures contracts.

### **The Cross Country HTA Does Not Fall Within the Cash Forward Exclusion**

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<sup>82</sup> Commodity Exchange Act Section 4g(c).

<sup>83</sup> The Commodity Futures Trading Commission Glossary of terms defines bucket shop as "A brokerage enterprise which 'books' (i.e., takes the opposite side of) a customer's order without actually having it executed on an exchange.

The cash forward exclusion primarily “entails not only the legal obligation to perform, but also the generally fulfilled *expectation* that the contract will lead to the exchange of commodities for money.”<sup>84</sup> (emphasis added). Thus, to determine whether a contract falls under this exclusion, the Court must examine not only the function of the contract, but also the intent of the parties. The contracts between CSA customers and Great Plains do not fall within the cash forward exclusion because not only did delivery not occur as a result of any Cross Country HTA contract, the evidentiary record clearly illustrates that Respondents did not intend to accept delivery as a result of the Cross Country HTA contract.

Respondents argue that the inclusion of express contract terms requiring delivery is proof that their intention was to accept delivery on these contracts.<sup>85</sup> However, the fact that Respondents includes “self-serving” contract provisions “should not deter the conclusion that their contracts, as a matter of law, are futures contracts subject to the CEA.”<sup>86</sup> In order to determine intent, the Court must examine the transaction in its entirety, not just the written

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<sup>84</sup> In Re Stovall, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941 at 23,778 (CFTC Dec. 6, 1979).

<sup>85</sup> But see the earliest Great Plains contract forms used for the CSA customers. One contract form states that “Buyer confirms that the following futures transaction was made for seller today on the Chicago Board of Trade.” DX 338. Another contract form states that Seller agrees that this transaction shall be subject to the trading rules of the Chicago Board of Trade and the marketing policies of the Buyer.” DX 325.

<sup>86</sup> CFTC v. American Metal Exchange Corp., 693 F. Supp. 168, 192 (D.N.J. 1988) (citations omitted). See also CFTC v. Noble Metals International, Inc., 67 F.3d 766 (9th Cir. 1995), cert. denied sub nom. Shulze v. CFTC, 519 U.S. 815 (1994) (finding contracts in the “Forward Delivery Program” to be futures contracts despite express contract terms requiring “delivery of the merchandise contracted” and stating that “[t]his transaction cannot be liquidated or offset.”); CFTC v. American Metal Exchange Corp., 693 F. Supp. 168, 180 (D.N.J. 1988) (holding that the contracts in question were futures contracts despite the fact that the order forms, brochure and promotional pamphlet expressly required delivery of the metals in order to satisfy the contract); In re Grain Land Co-op, [Current transfer binder] Comm. Fut. L. Rep. (CCH) ¶ 27,459 at 47,176 (CFTC Nov. 6, 1998) (concluding that despite the fact that delivery occurred on a portion of the Flex HTA contracts in question, the contracts were nevertheless futures contracts within the meaning of the CEA); In re Stovall, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941 at 23,782 (CFTC Dec. 6, 1979) (declaring that the contracts in question are illegal off-exchange futures contracts despite the contracts express statement: “Client agrees that any and all purchases and/or sales with Stovall contemplate actual delivery and/or receipt of the (actual) commodities”).

contract form. Of critical importance here is the group of people with whom Respondents entered into Cross Country HTA contracts.

First, most customers that CSA sent to Great Plains were located 30-200 miles from Great Plains, which is outside of Great Plains' "traditional territory."<sup>87</sup> The Division established that a 1995-96 Great Plains interim manager, Gary Maxwell, was quoted in the *Wall Street Journal* stating that delivery from more than approximately 30 miles away could not realistically occur.<sup>88</sup> In contrast, Respondents witness testified that, it is not unusual to deliver grain up to 70 miles away—at least for some CSA customers.<sup>89</sup> In addition, under cross-examination Seim testified that for delivery to occur at an unusually far distance, the grain price had to be worth the distance.<sup>90</sup>

The Court does not base its decision upon opinions concerning the customary range of delivery and "practical" deviations from that range. Nevertheless, in most instances, Great Plains received a fax order that included the name, address and telephone number of the CSA customer with whom Great Plains was entering into a Cross Country HTA contract.<sup>91</sup> This put Great Plains on notice of the distance that would have to be traveled in order for delivery to occur. But as Seim testified, the distance would have to be worth the price. Admittedly aware of

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<sup>87</sup> Gerdes, in fact, testified that he estimated that only "half a dozen" Great Plains/CSA customers were located in the traditional "trade territory;" the rest were located outside of this traditional territory. Hearing Tr. 564 March 29-30.

<sup>88</sup> DX 743.

<sup>89</sup> Hearing Tr. 3/30/99 21:25-22:9. Testimony of Clyde Haskins, senior vice-president and specialist in agriculture lending at Geneva State Bank of Geneva, Nebraska.

<sup>90</sup> Hearing Tr. 1/5/99 AM 104:3-105:18. Seim owns a trucking business and he was testifying here as to his observations concerning geographic delivery patterns and motivations to deliver a great distance.

<sup>91</sup> Hearing Tr. 3/30/99 255:16-23 (Gerdes), Hearing Tr. 1/6/99 AM18:2-5 and 38:11-13 (Arnold), and Hearing Tr. 1/7/99 AM 19:11-15 (Wichmann). See also, DX 126, DX 169, DX 195, DX 245, DX 257, DX 279, DX 296, DX 316, DX 327, DX 337, DX 359, and DX 433.

the distance between the CSA customer and Great Plains' receiving elevators, Respondents did not assert, consonant with Seim's testimony, that they intended to offer a grain price that was high enough to entice them to deliver grain from a distant location.

Respondents' claim that delivery was possible even from as far as 70 miles away as long as the elevator's price was worth the distance. Respondents did not assert either that their price was worth the distance, or that there were any other benefits that producers from outside of the traditional territory could derive from entering into Cross Country HTAs, especially since many producers were located closer to other elevators.<sup>92</sup> Respondents' defense also fails to address the feasibility of delivery occurring on their contract with JRA Farms,<sup>93</sup> located approximately 200 miles away (nearly triple the distance quoted by their witness). The bottom line is that Great Plains entered into a contract with any producer that CSA sent to it regardless of the impracticality or sheer burden of delivery. In point of fact, none of the producers alleged to be outside of traditional delivery territory (and for that matter none within the traditional delivery territory) ever delivered a bushel of grain to Great Plains as an obligation of a Cross Country HTA contract.<sup>94</sup>

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<sup>92</sup> Hearing Tr. 3/30/99 AM 255:8-15.

<sup>93</sup> James Amundson entered into a Cross Country Hedge-to-Arrive contract with Great Plains under the name JRA farms. The fax order from Wichmann clearly stated JRA Farm's Radcliffe, Iowa address, which was located 200 miles away from Great Plains. Respondents, therefore, were fully aware of the distance when they entered into the contract with JRA Farms. Hearing Tr. 1/7/99 PM 108:13-21 and Hearing Tr. 1/7/99 AM 49:4-6.

<sup>94</sup> See Hearing Tr. 1/7/99 AM 18:25-19:3 (Wichmann testifying that delivery was not required); Hearing Tr. 3/30/99 AM 259:10-16 (Gerdes testifying that no CSA customer ever delivered to Great Plains); and Hearing Tr. 1/6/99 PM 33:2-5 (Joyce Brazda (note, supra, 35) testifying that no CSA customer delivered to Great Plains pursuant to a hedge-to-arrive contract).

However, Respondents cite Mr. Arbit's opening statement, claiming that delivery occurred *through* Great Plains: "There are 30-40 instances where farmers, CSA clients, ... made delivery to their local facility and received these checks from Great Plains." Respondents' Counterstatement Finding of Fact and Concl. of Law 3 & 4. From this, Respondents would have the Court conclude that their contracts were cash forward contracts in accordance with the exclusion. However, it is essential to note here that delivery *through* Great Plains is not the equivalent of delivery *to* Great Plains. The Court finds that the instances referred to above are instances in which

Second, some of the producers that entered into Cross Country HTAs with Respondents were seed corn producers whose grain was contractually bound for delivery to seed corn buyers.<sup>95</sup> These seed corn obligations begin before the crop is planted and, based on the contract specifications, the seed corn producers plant, harvest and deliver to the destination required by the contract.<sup>96</sup> For example, Respondents entered into Cross Country HTAs with Seim<sup>97</sup> and Wagner,<sup>98</sup> both seed corn producers whose corn was entirely spoken for, in terms of legal contractual obligations, by Pioneer Hybrid International. In other words, neither Seim nor Wagner had any corn available for sale or delivery to Great Plains or any other commercial buyer. In fact, though neither of these producers delivered to Great Plains, both Seim<sup>99</sup> and Wagner<sup>100</sup> received checks from Great Plains. Respondents entered into Cross Country HTA

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producers delivered to their local elevators as part of an ordinary course of business and also received checks for the futures positions that Great Plains held on behalf of that client.

<sup>95</sup> Seed corn producers, Kenyon Seim, Leroy Seim (Kenyon's father), Robyn Seim (Kenyon's brother), and Wagner all held Cross Country HTA contracts with Great Plains. Hearing Tr. 1/5/99 AM 87:3-16.

<sup>96</sup> Kenyon Seim testified that he made it clear to Wichmann "that we grew seed corn, which is a contractually bound product and therefore cannot be delivered to an elevator." Hearing Tr. 1/5/99 AM 82:13-15.

<sup>97</sup> Kenyon Seim's corn is contractually bound to Pioneer Hybrid International ("Pioneer"). "[T]hey provide us with the hybrids, they determine what hybrids we will grow. And then we plant and cooperate with them according to their direction." Furthermore, Pioneer "contact[s] the people to harvest it and...the people to truck it" to Pioneer's receiving facility. The grain is always under "Pioneer's control and ownership." Hearing Tr. 1/5/99 AM 78:24-79:4.

<sup>98</sup> Wagner testified that his farm, TNST, Inc., was also bound to deliver to Pioneer:

Q. Are you obligated – is TNST, Inc. obligated to sell all of its seed corn to Pioneer?

A. Yes, we are.

Q. At the time that you entered into the cross country hedge to arrives with Great Plains for corn, did you have any seed corn that you could have delivered to Great Plains?

A. No.

Hearing Tr. 1/5/99 PM 27:13-20.

<sup>99</sup> Seim testified that when CSA contacted Great Plains on his behalf and "lifted the contract" he received a check for \$4,475. Hearing Tr. 1/5/99 AM 90:1-25 and DX 262.

<sup>100</sup> Wagner testified that when he closed out his contract with Great Plains he received a check for \$800, the difference in futures prices from when he entered into the contract with Great Plains to when he closed out his contract. Hearing Tr. 1/5/99 PM 21:14-22:2.

contracts with seed corn producers despite the fact that they had no grain available to satisfy contracts other than their seed corn contracts.

Third, some of the producers introduced to Great Plains by CSA were feedlot operators, meaning that their grain was raised exclusively to feed livestock. For example, Bumgarner Land & Cattle Company used all of the corn it grew for its primary business of feeding cattle.<sup>101</sup> In other words, Bumgarner Land & Cattle Company raised corn for a specific purpose, used it solely for that purpose and did not have any corn for sale or delivery outside of that purpose.<sup>102</sup> Despite this fact, Respondents entered into a Cross Country HTA with Bumgarner Land & Cattle. None of the seed corn producers or feedlot operators (and for that matter no producers of any sort) delivered to Great Plains as an obligation of a Cross Country HTA contract.

Fourth, some of the parties with whom Respondents entered into Cross Country HTA contracts were not farmers<sup>103</sup> and did not own farmland.<sup>104</sup> Once again, the cash forward

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<sup>101</sup> Tom Roger Bumgarner testified that his family corporation, Bumgarner Land & Cattle Company's "primary operation is feeding, fattening out cattle for slaughter." Hearing Tr. 1/5/99 AM 60:16-24.

<sup>102</sup> Q. Mr. Bumgarner, over the past five years, for all of the farmlands that you described to the Court...what if anything have you done with the corn that you grow on your farm, on those farms?  
A. All of the corn that's been grown on any of our acres has been fed to cattle.  
Q. Has any corn ever been sold outside the Bumgarner lands?  
A. No.

<sup>103</sup> Lee Amundson and his wife held Cross Country HTA contracts with Great Plains on behalf of their businesses, L&D Farms and Five-A Enterprises. Both L&D Farms and Five-A Enterprises existed for the purpose of trading Cross Country HTA contracts with Great Plains and neither business had agriculture production capability. Hearing Tr. 1/7/99 PM 106:16-22, 106:25-107:3, 107:4-8. However, each business entered into Cross Country HTA contracts with Great Plains for 90,000 bushels of corn. Hearing TR. 1/7/99 PM 108:7-12.

<sup>104</sup> Great Plains had a Cross Country HTA contract with Jacy Steeple Wichmann (Jeff Wichmann's wife) under the name, C&J Farms. C&J Farms owned no farmland and grew no grain. Hearing Tr. 1/7/99 AM 28:7-23, 30:14-17, 34:11-16 and DX 340, 341.

However, C&J Farms cash liquidated its contracts with Great Plains and received two checks, one for \$37,375 and the other \$33,150. DX 343, DX 347, RFA #380, RFA #394. The decision to cash liquidate was based on the differential of the sell price on the Chicago Board of Trade—not the local cash price. Hearing Tr. 1/7/99 AM 36:11-22. In fact, after these contracts were cash liquidated, Great Plains entered into subsequent contracts with C&J Farms. Hearing Tr. 1/7/99 38-40, RFA #432. Great Plains sent two checks to C&J Farms as a result of these contracts, one for \$7,650 and the other \$1,850. DX 349 and DX 353. To clarify, C&J Farms never delivered any grain to Great Plains or through Great Plains, yet it received \$80,025 in checks based on futures profits.

exemption applies only to contracts between producers and buyers where delivery is fully expected to take place. With respect to its contracts with non-producers, Respondents could not have intended delivery to occur. Even if they had, however, the contract does not meet the requirements of the narrow cash forward exemption. The CSA customer was not a “farmer selling his grain to the mill” and Great Plains was not an elevator accepting delivery from CSA customers especially since delivery never occurred.<sup>105</sup>

The fact that Respondents did not intend to receive delivery on Cross Country HTA contracts is further evinced by their failure to investigate whether CSA customers had the capacity to deliver, which is especially illustrative of Respondent’s intent when compared to the thorough investigation that Respondents made into their local customers’ capacity to deliver. With regard to Great Plains’ local contracts—the contracts on which Great Plains intended delivery to occur—Gerdes had at least a general knowledge of the acreage, production capacity, and annual production of the farmers.<sup>106</sup> Furthermore, when Great Plains entered into contracts with local producers, Gerdes would conduct an investigation to ensure that the producer was not contracting for more grain than he could deliver.<sup>107</sup> Gerdes stated that this was “just like checking out a man’s credit. Some way we would find out what type of operation he had.”<sup>108</sup> Yet, this procedure is in stark contrast with Respondents’ handling of Cross Country HTAs.

Gerdes testified that in the first meeting between CSA and Great Plains, which established their Cross Country HTA relationship, he “spelled out the criteria which [Great

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<sup>105</sup> See note, *supra*, 32. Delivery from a non-producer never occurred to or through Great Plains, but there were instances in which non-producing CSA customers received checks or bills from Great Plains. The Court holds that the checks were payments of profits on the futures contracts and the bills for were for losses on the futures contracts.

<sup>106</sup> Hearing Tr. 3/30/99 AM 240:24-241:2, 252:10-253:11.

<sup>107</sup> *Id.*

Plains] would work with. No. 1 the person...had to be a producer. No. 2, he had to be able to deliver the grain."<sup>109</sup> However, when CSA requested that Great Plains enter into a Cross Country HTA with a CSA customer, Gerdes never made any follow-up inquiries with respect to that criteria. All that was required to enter into a Cross Country HTA with Great Plains was a fax from CSA requesting the contract and recommending the customer.<sup>110</sup> Upon receipt of this request, Great Plains and the new customer would then enter into a Cross Country HTA contract.<sup>111</sup> Essentially, CSA entered into the Cross Country HTA contracts on behalf of Great Plains and then faxed the contracts to the Nebraska office where Gerdes and his staff finalized the deal. At no time did Gerdes or any other employee of Great Plains request proof from CSA as to whether the producer could deliver.<sup>112</sup>

Respondents differential treatment of their local contracts and their Cross Country HTA contracts demonstrates their different intentions with respect to delivery. Respondents thoroughly investigated local customers' capacity to deliver because delivery was the heart of those cash forward contracts. Respondents did not investigate CSA customers' capacity to deliver because the Cross Country HTA contracts had nothing to do with delivery of grain; they existed exclusively for the purpose of trading futures.

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<sup>108</sup> Hearing Tr. AM 3/30/99 253:8-10.

<sup>109</sup> Hearing Tr. AM 3/30/99 256:27-31.

<sup>110</sup> Hearing Tr. 1/7/99 AM 40:19-41:3, 94:7-11, and Hearing Tr. 3/30/99 AM 255:16-23.

<sup>111</sup> *Id.* In fact, as this process developed, Great Plains simply provided CSA with a blank contract form. This made the procedure easier because CSA could then process the forms for new customers and fax them to Great Plains, where the last couple of blanks were filled in and the contract was signed. Hearing Tr. 1/6/99 AM 37:13-38:5 and DX 420.

<sup>112</sup> Gerdes had full authority to enter into contracts on behalf of Great Plains and according to his testimony, no inquiry was made to CSA as to whether the producers that they were sending over had the capacity to deliver. He instead relied on his assertion that he gave CSA Great Plains' requirements when their Cross Country HTA relationship began. Hearing Tr. 3/30/99 AM 256:11-258:4.

Finally, Respondents' intention with respect to delivery on the Cross Country HTA contracts could not be more clearly stated than in the promotional brochure that Gerdes wrote and gave to Arnold and Wichmann in the initial meeting.<sup>113</sup> The promotional brochure, which Arnold and Wichmann used to solicit Cross Country HTA customers,<sup>114</sup> states in pertinent part: "*Offsetting the contract is less costly in the event the producer can't or would rather not make delivery of the grain.*"<sup>115</sup> (emphasis added) This message is clear: customers who enter into Cross Country Hedge-to-Arrive contracts can decide that they would rather not make delivery and simply cash liquidate their contracts.<sup>116</sup> This quote is of paramount importance because it is analogous to the cancellation provision of the contracts in question in Grain Land.<sup>117</sup> In Grain Land, the Flex HTA contracts contained a provision that allowed customers to unilaterally cancel the contract in order to avoid delivery.<sup>118</sup> Here, Respondents included provisions in the contract that made delivery a legal obligation but only as a formality to give the contracts the appearance of cash forward contracts. The promotional brochure, used to entice customers to enter into Cross Country contracts, stated the true way in which the contract would operate. That is,

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<sup>113</sup> Respondents claim that Arnold and Wichmann are to blame for CSA customers belief that delivery was not required on the Cross Country HTA contract. However, any representation made by Arnold and Wichmann to CSA customers that delivery was not required is consonant with the brochure provided to them by Gerdes. In fact, they used the same brochure to solicit customers.

<sup>114</sup> Gerdes did not place any restriction on Arnold and Wichmann's use of the promotional brochure. Hearing Tr. 1/7/99 AM 72:22-73:1 and DX 413. See also Hearing Tr. 3/30/99 AM 228:22-229:5 and 229:13-230:9.

<sup>115</sup> DX 413 and DX 419.

<sup>116</sup> The written message of the promotional brochure is further clarified by Respondents' actual administration of the contract. Arnold testified that Great Plains placed no restrictions on a customer's ability to cash liquidate until the end portion of the Great Plains-CSA enterprise when Great Plains was experiencing serious financial difficulty. Hearing Tr. 1/6/99 33:10-17.

<sup>117</sup> In re Grain Land Co-op, [Current transfer binder] Comm. Fut. L. Rep. (CCH) ¶ 27,459 at 47,192 (CFTC Nov. 6, 1998).

<sup>118</sup> Id.

despite the written terms of the contract, the customers were assured that they had the ability to unilaterally offset the contract through cash liquidation.<sup>119</sup>

The narrow cash forward exclusion was “intended to cover only contracts for sale which are entered into with the *expectation that delivery...will eventually occur* through performance on the contract.”<sup>120</sup> (emphasis added) The “unilateral and unequivocal” ability of customers to cancel “precludes a finding that the producer was obligated to deliver grain,” and the absolute discretion afforded to CSA customers to cash liquidate defeats any assertion of Respondents that they intended delivery to occur on the Cross Country HTA contract.<sup>121</sup> In short, the evidence firmly establishes that the Great Plains-CSA enterprise was not that of “private commercial merchandising transactions which create[d] enforceable obligations to deliver but in which delivery is deferred for reasons of commercial convenience or necessity”<sup>122</sup> and therefore the transactions in question do not fall within the narrow cash forward exclusion to the CEA’s jurisdiction.

### **The Contracts Between CSA Customers and Great Plains Were Futures Contracts**

In the 1989 Policy Statement Concerning Swap Transactions, the Commission stated that,

In determining whether a transaction constitutes a futures contract, the Commission and the courts have assessed the transaction ‘as a whole with a critical eye toward its underlying purpose.’ Such an assessment entails a review

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<sup>119</sup> All that was required in order to cash liquidate a Cross Country HTA contract was a telephone or fax request from CSA to Great Plains’ Nebraska office. Hearing Tr. 1/7/99 AM 23:5-11. No negotiations occurred, in fact, Respondents did not even require an explanation. They just liquidated the contract on command. See DX 129, DX 131, DX 150, DX 173, DX 174, DX 396, DX 397, DX 442, DX 513, DX 483, and DX 523.

<sup>120</sup> In re Grain Land Co-op, [Current transfer binder] Comm. Fut. L. Rep. (CCH) ¶ 27,459 at 47,191—47,192 (CFTC Nov. 6, 1998).

<sup>121</sup> In re Grain Land Co-op, [Current transfer binder] Comm. Fut. L. Rep. (CCH) ¶ 27,459 at 47,192 (CFTC Nov. 6, 1998).

<sup>122</sup> 1990 Statutory Interpretation Concerning Forward Transactions, [1990-1992 Transfer binder] Comm. Fut. L. Rep. (CCH) ¶ 24,925 at 37,367 (CFTC Sept. 25, 1990).

of the 'overall effect' of the transaction as well as a determination as to 'what the parties intended.'<sup>123</sup>

As established in the preceding discussion, Respondents' actions, namely, (1) entering into contracts with customers for whom delivery was a sheer burden or mere impossibility; (2) failing to ensure that these producers had the capacity to deliver; (3) marketing the contracts using a promotional brochure that assures customers they could cancel the contract; and (4) never receiving delivery as a result of the Cross Country HTA contract, all unquestionably establish that Respondents' did not expect to receive delivery. "In general, if delivery of the commodity is not an expectation, the investment presumably [sic] has the character of a futures contract."<sup>124</sup> Furthermore, examination of the overall effect of the transaction, through Respondents' administration of CSA customers' contracts, demonstrates that the underlying purpose of the Great Plains-CSA enterprise was to trade futures and necessitates a finding that these were illegally traded off-exchange futures contracts.

Although "no bright line definition or list of characterizing elements is determinative" of what constitutes a futures contract, there are fundamental identifying characteristics.<sup>125</sup> The identifying characteristics that are of significance in the determination that the Cross Country HTA contracts are futures contracts are: (1) Respondents' designation of these transactions on paper; (2) the unlimited rolling that Respondents allowed Cross Country HTA contract holders; and (3) the fact that delivery never occurred in order to satisfy a Cross Country HTA contract.

First, the documents of record do not give any indication that grain was being sold. Instead, an examination of Great Plains' CSA customers' accounts on paper confirms that this

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<sup>123</sup> Policy Statement Concerning Swap Transactions, 54 F.R. 30,694 (July 21, 1989).

<sup>124</sup> In re Grain Land Co-op, [Current transfer binder] Comm. Fut. L. Rep. (CCH) ¶ 27,459 at 47,196 (CFTC Nov. 6, 1998) (quoting CFTC v. American Metal Exchange Corp., 693 F. Supp. 168, 192 (D.N.J. 1988)).

was a futures trading enterprise. Great Plains tracked its CSA customers' accounts with various account statements whose titles refer to futures trading.<sup>126</sup> None of these statements contained any columns or calculations for the cash basis, dryness, ethanol or grain tax, or any other information that would reflect that grain was being sold.<sup>127</sup> Notably, on the "Great Plains Commodities Trading Statement[s]" that were used to track CSA customers' accounts, Gerdes made notation about whether to pay the customer profits at that time.<sup>128</sup> Finally, Great Plains paid or charged CSA customers in at least 50 instances although no CSA customer ever delivered.<sup>129</sup>

Second, Gerdes told CSA that Cross Country HTA contracts could be rolled<sup>130</sup> and CSA requests to roll were not restricted<sup>131</sup> until Great Plains fell into serious financial trouble.<sup>132</sup> During the time period in which this unlimited rolling was permitted, Great Plains even allowed rolling from one crop year into the next.<sup>133</sup> Unlimited rolling is "proof that the...contract served

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<sup>125</sup> CFTC v. Co. Petro, 680 F.2d 573, 581 (9th Cir. 1982).

<sup>126</sup> See the documents Respondents used to track their CSA customers accounts: DX 438 and DX 518 ("Futures Statement"); DX 435A ("Futures Trading Statement"); DX 520 and DX 547 ("Great Plains Commodities Trading Statement"); DX 506 and DX 526 ("Profit & Loss on Closed Trades"). See also DX 116, DX 249, DX 262A, DX 263A, DX 274, DX 331A, DX 342, DX 346, DX 438, DX 441, DX 444, DX 503, DX 518, DX 520, DX 528, and DX 547.

<sup>127</sup> *Id.*

<sup>128</sup> See DX 520 and DX 547 ("NOTE: DO THEY WANT PROFIT[S] ON TRADES AT THIS TIME? HERM").

<sup>129</sup> See note, *supra*, 58-60.

<sup>130</sup> Hearing Tr. 3/30/99 AM 200:22-201:1.

<sup>131</sup> Hearing Tr. 1/6/99 AM (Arnold testifying that during the time period in which Gerdes was with Great Plains, "there weren't any limitations" on rolling.) The following contracts were rolled: DX 153, DX 169, DX 170, DX 197 (rolled twice: "to July '95" and "to September '95"), DX 198 (rolled twice), DX 200 (rolled twice), DX 202 (rolled twice), DX 373-388, DX 423, DX 473, DX 488, DX 514, DX 195, DX 199, DX 446, DX 449 (rolled between crop years).

<sup>132</sup> Hearing Tr. 1/6/99 PM 54:17-20 and 55:10-23. See also DX 251, letter Great Plains sent to CSA customers proposing different rates to be charged for rolling and stating that rolling would not be permitted past July 1996. See also DX, \ 566 and RX 1174.

as a means for the producer to speculate,” thereby making it a futures contract.<sup>134</sup> Respondents (as well as CSA customers) were in fact “motivated by a single factor – the opportunity to make a profit (or to minimize the risk of loss) from a change in the market price.”<sup>135</sup>

In addition, Respondents used this enterprise to gain profit at the expense of CSA customers in any way they could. For example, Great Plain’s “Farm to Market Position Report” had numerous columns designated for rolling and a column designated for the fees charged for rolling.<sup>136</sup> This indicates that Great Plains anticipated numerous rolls per contract and did not object to rolling because they benefited financially from allowing the numerous rolls.<sup>137</sup> In fact, Respondents entered into certain contracts with full knowledge that the customer planned to roll the contract.<sup>138</sup> Respondents did so because the purpose of the Cross Country HTA contract was to enable customers to speculate on the futures market without having to pay margin or deliver.<sup>139</sup> Permitting CSA customers to roll their contracts enabled the customers to try to get

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<sup>133</sup> See DX 424, DX 449, Hearing Tr. 1/5/99 48:9-49:18 (Solomon testifying that he rolled between crop years with a zero spread without any objection from Great Plains), and Hearing Tr. 1/5/99 AM 97:14-98:1 (Seim testifying that he was permitted to roll between contract years without any objection from Great Plains).

<sup>134</sup> In re Grain Land Co-op, [Current transfer binder] Comm. Fut. L. Rep. (CCH) ¶ 27,459 at 47,194 (CFTC Nov. 6, 1998). See also, Hearing Tr. 1/6/99 AM 67:19-21 and 68:1-7, Arnold testified that prior to its serious financial trouble, Great Plains did not refuse requests to roll contracts.

<sup>135</sup> Merrill Lynch v. Curran, 456 U.S. 353, 358 (1982) (discussing the motivations behind entering into futures contracts).

<sup>136</sup> See DX 116, DX 444, DX 249, DX 263A, DX 309, DX 311, DX 335, DX 503, DX 520, DX 528, DX 529, and DX 547.

<sup>137</sup> Great Plains charged “[\$.02]” for rolling “Futures” and “[\$.01]” for rolling “Spreads.” See Hearing Tr. 3/30/99 AM 277:5-9, 277:14-22 and DX 444. See also DX 116, DX 249, DX 263A, DX 503.

<sup>138</sup> Great Plains entered into all contracts requested from CSA including contracts on which CSA employees wrote that the contracts would be rolled at some point in the future. See DX 169 (“will be rolling to Dec 95”), DX 423 (“will be rolling to Dec 95”), and DX 373-388 (all sixteen contracts read “Plan on rolling this to Z6 sometime” meaning Dec 96). This is at odds with Respondents’ assertion that they intended to accept delivery on the Cross Country HTA contracts and Respondents’ assertion that these were cash forward contracts.

<sup>139</sup> Hearing Tr. 1/5/99 PM 48:14-16 and 49:8-13.

the best price when speculating on the market and enabled Great Plains to make a profit vis a vis its rolling fee.

Finally, “futures contracts are undertaken principally to assume or shift price risk without transferring the underlying commodity. As a result, futures contracts providing for delivery may be satisfied either by delivery or offset.”<sup>140</sup> Delivery never occurred as a result of the Cross Country HTA contract because, despite its title, this contract served as the functional equivalent of a futures contract. Every CSA customer had the option to offset and every CSA customer exercised this option. Non-delivery in this case is precisely consistent with the characteristics of a futures contract.<sup>141</sup>

Whether the contract is offered to the general public is a classic element of a futures contract.<sup>142</sup> For all intents and purposes, the CSA customers who entered into Cross Country CSA contracts did not serve as producers intending to sell their grain to Great Plains. Instead, their role in the Cross Country HTA enterprise was precisely analogous to the role of the general public in futures trading. All CSA customers who entered into Cross Country HTA contracts used these contracts to try to profit from the price differential on the futures market. Just as Respondents did not expect them to deliver, the CSA customers knew that they did not have to deliver and used the contracts to speculate.<sup>143</sup>

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<sup>140</sup> Policy Statement Concerning Swap Transactions, 54 F.R. 30,694, 30,695 (July 21, 1989).

<sup>141</sup> In re Stovall, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941 at 23,780 (CFTC Dec. 6, 1979) (“[A] major difference between an excluded cash commodity-deferred delivery contract and contracts of sale of a commodity for future delivery is that the former entails...the legal obligation...In contrast, parties to a futures contract do not usually expect delivery and it rarely occurs.”).

<sup>142</sup> In re Stovall, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,941 at 23,778 (CFTC Dec. 6, 1979).

<sup>143</sup> The following CSA customers testified that they did not intend to deliver when they entered into their contracts with GreatPlains:

T-4 Farms, Hearing Tr. 1/5/99 AM 50:17-19;

Bumgarner Land & Cattle Company, Hearing Tr. 1/5/99 AM 69:19-22;

Moreover, an offset contract gave Great Plains one final opportunity to derive profit from the CSA customers' contracts. That is, upon receipt of a request to offset, Great Plains would calculate the contract price against a futures price and either send the customer a bill for any loss, or a check for any gain.<sup>144</sup> Great Plains had full authority to decide which futures price to use in this calculation. For example, Randy Solomon testified that when he closed out his contract with Great Plains he received a statement calculating the losses on his contracts.<sup>145</sup> However, "the final figure that Great Plains used...had never traded on that day."<sup>146</sup> In other words, Great Plains selected a grain price that did not necessarily correspond to a futures price traded on the board of trade for the day the customer liquidated his position. Nevertheless, Great Plains calculated the offset according to that price and, in Solomon's case, billed for the losses.

Great Plains also miscalculated when cash liquidating the Cross Country HTA contracts of Kenyon Seim, Leroy Seim and Robyn Siem.<sup>147</sup> Kenyon Seim testified that he, his father and his brother all held separate Cross Country HTA contracts and when they liquidated their contracts with Great Plains, they received checks that did not reflect the contracts that they held.<sup>148</sup> In all three cases, the prices were correct but the volume of contracts held were

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Kenyon Seim, Hearing Tr. 1/5/99 AM 100:12-17;  
TNST, Inc., Hearing Tr. 1/5/99 PM 18:18-19:3, 25:22-26:5, 34:3-6, 36:3-6, 36:25-37:3, and 40:2-5; and  
Tom Bauder, Hearing Tr. 1/6/99 PM 57:12-17.

<sup>144</sup> There are no office order tickets, floor order tickets, or trading cards that confirming that CSA customers had positions backed by identical positions in Great Plains' 588 account. So, we cannot conclude that Great Plains sold positions that corresponded with CSA customers liquidations. Hearing Tr. 1/6/99 AM 75:23-24, 76:11-16, Hearing Tr. 1/7/99 AM 32:22-33:2.

<sup>145</sup> Hearing Tr. 1/5/99 AM 26:2-27:10.

<sup>146</sup> Hearing Tr. 1/5/99 AM 26:21-23.

<sup>147</sup> Hearing Tr. 1/5/99 AM 91:1-19 and 93:15-20.

<sup>148</sup> Hearing Tr. 1/5/99 AM 82:13-15, 91:1-19 and 93:15-20.

incorrect.<sup>149</sup> The bottom line is that Great Plains did not have to give CSA customers accurate figures that reflected the volume of contracts held by the customer, a futures price that reflected the correct time the contract was entered into, or the correct time that it was liquidated.

The probative evidence of record proves beyond peradventure that the Great Plains-CSA enterprise was a bucket shop operation masquerading as a "cash forward hedge-to-arrive" business. Great Plains took not one bushel from a CSA customer. The Great Plains-CSA operation could have been housed in the backroom of a tavern or pawn shop. There was certainly no need for a grain elevator.

In the case at bar, Great Plains took the opposite side of CSA clients who bought or sold futures contracts. Great Plains maintained a futures account with Farmers Commodity Corporation (FCC), a futures commission merchant, and it hedged its bets with the CSA customers by taking futures positions through FCC. The hedge, however, did nothing to protect the CSA customer. The CSA customers owned no interest in the account, and could make no claim against FCC or the designated exchange. As noted by the Seventh Circuit,<sup>150</sup> the exchange clearinghouse guarantees the obligations of both sides of a contract traded on a designated futures exchange. In the case at bar, the CSA customers were strangers to the futures exchanges and to the future commission merchant handling the Great Plains' hedge account. Unfortunately, the CSA customers had none of the protections afforded to persons trading on a designated futures exchange.

The overwhelming weight of the evidence establishes that Great Plains and Gerdes operated a bucket shop in contravention of Section 4(a) of the Commodity Exchange Act.

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<sup>149</sup> Hearing Tr. 1/5/99 AM 92:16-23.

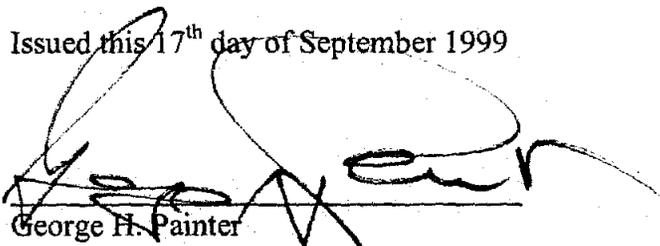
<sup>150</sup> See note, *supra*, 80.

**ORDER**

Respondents Great Plains Co-op and Herman Gerdes are hereby ORDERED to CEASE and DESIST from violating Section 4(a) of the Commodity Exchange Act.

Respondent Herman Gerdes shall be prohibited from trading on or subject to the rules of any contract market for a period of ten (10) years from the date this decision becomes final.

Issued this 17<sup>th</sup> day of September 1999

A handwritten signature in black ink, appearing to read "George H. Painter", is written over a horizontal line. The signature is stylized and somewhat cursive.

George H. Painter  
Administrative Law Judge

Legal Intern:  
Christina A. Barone