



U.S. COMMODITY FUTURES TRADING COMMISSION

Three Lafayette Centre
1155 21st Street, NW, Washington, DC 20581

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OFFICE OF PROCEEDINGS

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PROCEEDINGS

ATUL MEHTA,
Complainant,

v.

OPPORTUNITIES IN OPTIONS,
Respondent.

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* CFTC Docket No. 97-R144
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INITIAL DECISION

Atul Mehta alleges: (1) that on August 13, 1997, Opportunities In Options improperly liquidated an option position to satisfy a \$60,000 margin call; (2) that on August 15, 1997, agents for Opportunities-In-Options mishandled a stop order; and (3) that on August 15, 1997, in reliance on erroneous advice by an agent for Opportunities-In-Options, Mehta allowed an option position to be exercised, which then triggered a margin call and a second forced liquidation. Respondents deny any violations, and counterclaim for the debit balance.

The findings and conclusions below are based on the parties' documentary submissions, and the oral testimony of Mehta and David L. Compton, the chief executive officer for Opportunities-In-Options. For the reasons set out below, it is concluded that Mehta has shown that he is entitled to a reparation award in connection with the erroneous advice on August 15, 1997, but that he has failed to

show any violations in connection with the liquidation on August 13 or the order fill on August 15, 1997. It is also concluded that Opportunities-In-Options has failed to show that it is entitled to the counterclaim.

All dates are in 1997, unless otherwise indicated.

Factual Findings

1. In June of 1997, Shannon Beth Stevenson, an associated person with Opportunities-in-Options ("OIO"), cold-called Mehta.¹ At the time that he opened his account with OIO, Mehta had traded commodity futures and options with Lind-Waldock for one year; was employed as a senior software consultant; and had an annual income between \$75,000 and \$100,000, and a net worth over \$100,000. [Exhibit to complaint; see pages 8-11 of hearing transcript.] Mehta told Stevenson that although he had his own trading strategy, he preferred having a broker with whom he could consult when making trading decisions. The recorded conversations between Mehta and his OIO account executive Bruce Cook, establish that Mehta was knowledgeable about futures and options trading. [Stevenson affidavit (filed March 19, 1998); Cook affidavit (filed March 19, 1998); first paragraph of complaint; transcript of recorded conversations (produced as part of OIO's reply to discovery Order, filed March 19, 1998); and pages 12-15 of hearing transcript.]

¹ The factual findings concerning the account solicitation and account opening are based principally on Mehta's oral testimony. OIO produced an unsworn statement by Stevenson, but did not produce or subpoena her as a witness at the hearing. NFA records indicate that Stevenson's registration as an associated person with OIO was terminated on March 18, 1998 (after the undersigned asked OIO to produce an affidavit by her); and that she is currently not registered. OIO represented at the hearing

2. On July 30, 1997, Mehta signed the various account-opening documents, including a Rosenthal Collins Group ("RCG") account application, and RCG customer contract, and an acknowledgment that he had received and understood the risk disclosure statement for futures and options. [OIO's reply to Order dated February 5, 1998 (filed March 19, 1998); see pages 15-16 of hearing transcript.]

Paragraphs 7 and 8 of the customer agreement governed the parties' respective rights and obligations concerning margin calls, and stated in pertinent part:

I [Atul Mehta] agree to maintain such collateral and/or margin as you [RCG] may from time to time, in your sole and absolute discretion, require and agree to pay immediately on demand any amount owing with respect to any of my accounts. . . . I shall make deposits of margin as RCG requests within a reasonable time after such request. It is agreed and understood that one hour may be deemed to be a reasonable time; provided, however, that RCG, in its sole and absolute discretion, may request that the deposits be made in a lesser period of time. . . .

In the event I fail to deposit sufficient funds . . . to satisfy variation margin, or whenever in your sole and absolute discretion you consider it necessary, you may without prior demand or notice, when and if you deem appropriate . . . liquidate positions in my account. . . . I agree that . . . the provisions of this paragraph are solely for the protection of RCG. . . .

[Exhibit to complaint; see pages 16-19 of hearing transcript.]

The risk disclosure statement included warnings about the specific risks associated with selling options:

Transactions in options carry a high degree of risk. . . . Selling ("writing" or "granting") an option generally entails considerably greater risk than purchasing options. Although the premium received by the seller is fixed, the seller may sustain a loss well in excess of that amount. The seller will be

on September 1st that it did not know the whereabouts of Stevenson. In any event, Mehta's testimony substantially accorded with Stevenson's description.

liable for additional margin to maintain the position if the market moves unfavorably. The seller will also be exposed to the risk of the purchaser exercising the option. . . . If the option is on a future, the seller will acquire a position in a future with a associated liabilities for margin.

[Exhibit to complaint; see pages 19-20 of hearing transcript.]

3. On August 5, Mehta wired \$11,000 from his checking account, and on August 8 wired another \$9,000 from the Lind-Waldock account. Bruce Stewart Cook acted as Mehta's account executive.²

On Friday, August 8, Mehta initiated two trades: a British Pound option spread that would be liquidated on August 18 for a net profit of about \$1,950, and an August S&P 500 call position that would be liquidated on August 11 for a net profit of about \$875. On Monday, August 11, Mehta day-traded August S&P calls for a net loss of about \$1,975. [See page 21 of hearing transcript.]

During the initial three days of trading, Mehta called Cook numerous times each day, sometimes every ten minutes, for reports on market conditions and fill prices. Mehta never asked Cook to call him, and never indicated to Cook, or any other OIO agent, that he expected to be called about matters such as market conditions and fill prices. [Pages 21-22 of hearing transcript.]

4. On Tuesday, August 12, the beginning account balance was \$15,762, and Mehta shorted five August S&P 500 (900 strike price) put options. The market closed sharply against Mehta's short S&P put position which triggered a margin call

² NFA records indicate that Cook's registration as an associated person with OIO was terminated on April 30, 1998 (after the undersigned asked OIO for an affidavit by Cook), and that he is currently a registered associated person with Alaron. OIO did not produce or subpoena Cook as a witness at the

for \$59,100. Although he had been following the market, and before had spoken to Cook frequently in the midst of less volatile market conditions, Mehta did not call OIO either after the close that day or any time the next day. When asked to explain this drastic change in behavior, Mehta testified that he believed that “there was nothing worrisome about the market,” and that he was “under the assumption” that he had adequate funds to cover his position “if the market moved a little bit.” According to Mehta he based that assumption on “consultations” with Cook about the margin requirements. However, Mehta did not describe any specific statements by Cook that supported this assumption.³ [Pages 24-33 of hearing transcript.]

5. On Wednesday August 13, OIO instructed Rosenthal-Collins to liquidate the position to meet the margin call. It is undisputed that OIO did not consult with Mehta before the liquidation. Mehta claims that he was home that day and that his answering machine was on. In contrast, OIO produced an unsworn statement by Cook in which he asserted that he twice unsuccessfully tried to reach Mehta by phone. However, OIO did not produce or subpoena Cook as a witness at the hearing. In the absence of any sworn testimony by Cook, Mehta’s plausible sworn version must be credited, and thus it is found that Cook did not call Mehta before liquidating the position. [See OIO answer; Alvarez and Cook affidavits (filed May 16, 1998); and pages 29-31 of hearing transcript.]

hearing, and represented at the hearing on September 1st that it did not know the whereabouts of Cook.

³Mehta’s failure to describe any specific assurances by Cook is underscored by the fact that during the recorded conversation on August 14 when Cook criticized Mehta for not calling him, Mehta did not refer to any advice about margin requirements and otherwise offered no explanation for not calling Cook.

A tape-recording of an August 14 conversation between Mehta and Cook indicates that if Cook had spoken to Mehta on August 13, he would have demanded that Mehta immediately satisfy the margin call:

Cook [You] had a sixty thousand-dollar margin call in the S&P. Did you not see it moving all the way down to like nine-ten, nine-sixteen area?

Mehta Uh, yes.

Cook And you were not worried about it? Or you didn't want to call? I mean the compliance guy is here with five short puts and the market ten ticks away, and your account is almost going to zero. . . .

Mehta Um.

Cook They pulled the plug on the nine hundreds.

Mehta Do you remember asking me, or. . .

Cook Well, yes of course. We have a sixty thousand-dollar margin call and the market is moving within ten points of the S&P.

Mehta Then it can bounce back again.

Cook Well no, who knows its going to bounce back again. You know, the markets opens up twelve and then erases all of that and goes limit down the other way on a first limit. Who knows what is going to happen on it.

Mehta So how much did we lose there?

Cook We bought them back at three, which was not the low of the day but that you know, is about a five thousand dollar loss here. You know, these are things that we really have to watch around here. You know when it opens up the day before when we sold them and the market closes down very sharply like it did and it bounces back up and it starts trading down ten points lower than the close of the day before, with bonds on the down side. These guys around here don't fool around. I mean they can't take the risk of losing twenty or thirty thousand dollars in an account. And it will do that on five [contracts.]

Mehta So what now?

Cook Well, that is basically what I am asking you. I mean I don't control your account. I am not the guy doing the trading and you're the guy that is doing the trading in it and if you want to trade S&P and you want to be there and you want to be there moving in and out in there trades, you got to be either right on top of it or whatever, you know. I try to do the best I could for all my clients but when we got huge big moves like this, um happening and all my clients are big traders in the S&P. These guys are all over it, and I am just a little disappointed this happened. We have had a bad few days with the S&P here in your account and we have got to figure out a better way to make money in this here market, um, or at least a clear idea of what you are looking at. Again they are not going to let these things go deficit. Because this account could've easily have gone into negative. Then you would be getting a call from someone in the legal department.

Mehta I just wish somebody had called me.

Cook Well I can tell you that when we are in a fast market and the market is limit down, nobody has a chance to call and ask, Atul, do you think you can wire another twenty thousand dollars? I mean that is what they are going to ask you. Well, they're actually gonna ask you for \$60,000, is what they're gonna ask you for.

Mehta Well, that's the rules isn't it.

Cook What? Would you've wired sixty thousand?

Mehta Why not?

Cook Pardon?

Mehta Why not, I said. When I have all the accounts I can wire to.

Cook It's easy to say that now.

Mehta No, I am not kidding. I truthfully have it, I am sure of that.

Cook Well, that is where we are at right now anyway. You know, I really believed you were following this thing by a tick-by-tick basis. Everyday of this week, you have been calling me practically every ten minutes, and I don't mind that, I would of preferred that. Then we did the S&P, limit down one night, then it opens up 12, and goes down 12, to 15, and I'm not hearing hide-nor-hair from you.

Mehta I am here right now. Is there nothing we can do?

Cook Nothing we can do here, no, not at this point in time. Unless this thing sells off dramatically here today. . . . Well they don't give anybody any choice. There is a sixty thousand-dollar margin call and that thing is limit down. They are all over the place to cover these things. They are not going to fool around with five S&P puts on an account that is ten or twenty thousand dollars. They are just not going to play around with it.

Mehta What is the [unintelligible] in my account right now?

Cook I know you have experience and you have traded in the S&P before, but when you get a move like what happened yesterday, if this thing goes down and start touching on nine hundred, which it could easily do yesterday and it could easily do today again here. You know, this account could be twenty or thirty thousand dollars under water.

Mehta Uh huh.

Cook Now that does not mean you are going to spend twenty thousand dollars to bring your account back to zero does it?

Mehta I just think I should have been given a fair chance, you know.

Cook Well, fast market, and it's limit down. Nobody has a chance to try to find you and try to tell you, hey, its limit down. You know its that close to the market. You knew the conditions of the market the day before and we certainly had a good opening, but that erased very quickly. You know, in fast market conditions nobody has a chance to do anything, and if this thing keeps going further down, we are not going to play around with it. It is just not worth is. We have accounts that go negative twenty or thirty thousand dollars and you don't see that money, the guy just says "sue me." It just does not work.

Mehta So I guess at his point we just have to be more careful and bring back what is lost.

Cook Yes that is what we need to step back and look a little and see how to bring that back but doing it on a little safer level here. Or, if the market is making you think swing [unintelligible] I don't care if you phone me every five minutes. At least I know you're in touch and you know what is going on. But when you get limit up, limit down into day, um, you get five contracts out there again, a twenty thousand dollar account can turn into a minus fifty thousand dollar account very easily. So I don't know if you are watching or looking at the S&P right now, but if we see a good sell off now, that can easily happen, anytime through today, then maybe

responsibly we can get in there and then just try to look for some premium to bring back in without risking too much over the next day here. Now again, I am sorry for it happening, but there just not going to fool around in an account like that. They just don't give us much leeway at all.

Mehta No.

Cook And I would like to sit there and phone all the clients and let them know but you know, I have got all these guys trading the S&P and they are all over it. So maybe if you are watching it, lets look for a good down move here and see if we can get some premium out of it.

Mehta So, anything important that you are looking at?

Cook If we can get that then I think you are going to see some real good premium that we can get our hands on.

Mehta The eight eighties now?

Cook Oh no, I think we can get the nine hundreds, but I would like to see the market really mover sharply down to that kind of an area. Let's keep an eye on it. Bonds are just starting to come down off there high. Lets watch it and look at it and keep in touch with me through the day here and see if we can get something.

Mehta Sure.

Cook First pound is up, that is good. Lets keep our eye on it and see if we can get half of this thing back here in the next day or two.

Mehta Ok, sure.

[Recording of August 14 conversation produced March 19, 1998; see pages 29-37 of hearing transcript.]

6. On Friday, August 15 – the expiration day for the August S & P options – Mehta placed an order to sell four August S&P 500 puts with a 900 strike price (“900 S&P puts”) and an order to sell five August S&P 500 puts with a 905 strike

price ("905 S&P puts"). Mehta also placed a protective stop on the 905 S&P puts, but left the 900 S&P puts unprotected.

Later that day, Mehta asked that the protective stop be moved from 200 to 150. Cook immediately forwarded the new order. However, the market – near limit and in a fast market condition – simultaneously hit the 200 stop, and the order was filled at 400. The resulting debit charge put the account into deficit. [See Time and sales report, produced as exhibit to complaint; and pages 38-42, 50-52, 54-55 of hearing transcript.]

Mehta and Cook also discussed the looming expiration of the unprotected in-the-money 900 puts.⁴ Mehta asked Cook what would happen if the market closed below the 900 strike price. Cook replied that Mehta would only have to pay the difference between 900 and the closing market price. Relying on this advice, Mehta decided not to liquidate the options.

The puts expired in the money and were exercised. The resulting futures position triggered a \$125,000 margin call. When Mehta told Felipe deJesus Alvarez of OIO told that it would "take some time" to wire the funds to cover the margin call, Alvarez replied "time is not a commodity that we have much of these days." Mehta then decided to liquidate the open positions in his account. [OIO answer; Alvarez and Compton statements; and pages 44-45 of hearing transcript.]

⁴ The factual findings concerning this discussion are based principally on Mehta's unrebutted oral testimony.

On Sunday night, August 17, the S&P opened lower on Globex and the long futures position was liquidated on Globex, for a net loss of \$10,919. [See pages 45-47 of hearing transcript.]

Conclusions

Mehta has established by a preponderance of the evidence that Cook provided erroneous advice about the expiration of an in-the-money option, and that Mehta relied on this advice to his detriment when he permitted the S&P puts to be exercised and exposing his to a margin call on the resulting futures position. The fact that this advice was patently wrong and given as expiration loomed supports the conclusion that Cook acted with gross negligence in violation of CFTC rule 33.10 and Section 4c(b) of the Commodity Exchange Act. The proper measure of damages is Mehta's net \$10,919 out-of-pocket loss on the transaction. OIO is liable for Cook's violation pursuant to Section 2(a)(1)(A) of the Act.

However, Mehta has failed to establish the remainder of the alleged violations. Mehta has produced no evidence of any negligent, reckless or deliberate misconduct by OIO, RCG or its agents on the exchange floor in the handling and execution of the stop order on August 15, 1997. Mehta has merely made speculative and unsubstantiated allegations that: "[T]he fill price was manipulated by my broker. It could be misallocation of trades, bucketing, noncompetitive trading, or even accommodation trading." [Page 2 of complaint.] In contrast, OIO has established that the market was volatile and in a fast market condition, that the market hit the stop price converting the order to a market order, and that the order

was filled within the price range. In these circumstances, Mehta is not entitled to any recovery for his loss on this trade.

It is well established that a futures commission merchant has considerable discretion to set and enforce its margin policies, absent a showing of fraudulent or bad-faith conduct. See *Baker v. Edward D. Jones & Company*, [1982-84 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶21,167 (CFTC 1981). Therefore, Mehta must show, by a preponderance of the evidence, either that Opportunities In Options misled him about Rosenthal-Collins' margin policy or that on August 13, 1997, OIO liquidated the S&P position in bad faith. On this record, Mehta has not shown any deception by OIO or its agents concerning Rosenthal-Collins' margin policy. The customer agreement authorized Rosenthal-Collins to liquidate open positions under certain circumstances, including unmet margin calls. Although the agreement contemplated that Rosenthal-Collins would give Mehta one hour to meet a margin call, the agreement also authorized Rosenthal-Collins, "in its sole and absolute discretion," when it considered it "necessary," to liquidate positions without prior demand or notice. Here, Mehta argues that, notwithstanding the terms in the customer contract, OIO and Rosenthal Collins could not liquidate a position without notice in any circumstances simply because the account was non-discretionary. However, Mehta produced no evidence that he ever informed OIO that he expected OIO or Rosenthal-Collins to assume his risk regardless of the circumstances or that OIO should otherwise have been aware of this purported reliance. In the absence of special instructions, Mehta could not shift to OIO the responsibility to monitor the account or to assume his risk, and could not disregard

his obligation to provide adequate margin. Had Mehta contacted OIO during trading hours, as he had done repeatedly before, he could have wired additional margin if he actually intended to stay in the market. Mehta's decision not to re-enter the market after the liquidation undermines his assertion that he would have remained in the market had he received notice of the margin call at an earlier time. Mehta has also failed to show that OIO acted unreasonably by quickly liquidating the position where his account was in deficit and the open position was rapidly deteriorating in a volatile market. Finally, even if Mehta had established that respondents should have made more strenuous efforts to contact him before the liquidation, he has failed to show how his losses would have been less had he held the declining put position. See *Grist v. Shearson Lehman Brothers, Incorporated*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶24,962 (CFTC 1990). In these circumstances, Mehta has failed to establish that OIO acted in bad faith.

ORDER

Opportunities-In-Options is ORDERED to pay to Atul Mehta reparations of \$10,919, plus interest on that amount at 4.730% compounded annually from August 18, 1997, to the date of payment, plus \$125 in costs for the filing fee. Opportunities-In-Options' counterclaim is DISMISSED.

Dated September 25, 1998.


Philip V. McGuire,
Judgment Officer