



U.S. COMMODITY FUTURES TRADING COMMISSION

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SHERRY R. MIDDLETON, and
MARK A. MIDDLETON,
Complainants,

v.

JAMES P. CAGNINA, Jr.,
ANTHONY GIACOMIN, and
INFINITY FUTURES, LLC,
Respondents.

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CFTC Docket No. 11-R011
Before: Philip McGuire

INITIAL DECISION

Appearances: Sherryl R. Middleton and Mark A. Middleton, Conroe, Texas,
complainants, *pro se*

Constantine J. ("Chris") Gekas, Esq., and John C. Gekas, Esq.,
Gekas Law LLP, Chicago, Illinois,
for respondent Anthony Giacomini

Brian Sass, Infinity Futures, LLC and TransAct Futures, Chicago, Illinois
for respondent Infinity Futures, LLC, *pro se*

James P. Cagnina, Jr., Chicago, Illinois,
respondent, *pro se*

Introduction

This dispute arises from two forced liquidations in Sherry and Mark Middletons' joint self-directed electronic account: on May 20, and October 20, 2010. The Middletons' account was introduced by respondent Infinity Futures, LLC, and cleared by Infinity's parent, York Business Associates, LLC d/b/a TransAct Futures. TransAct's electronic trading system

includes a “predetermined automatic liquidation feature,” also called a “default risk setting” or “predetermined daily risk assessment level.” This risk setting, which lies at the heart of the parties’ dispute, is intended to limit substantial trading losses, principally for the protection of TransAct.

TransAct’s system monitors all positions in the account, and if daily losses in the account reach the predetermined limit, the system is designed to liquidate all open positions. Also, if the account balance significantly drops, the TransAct system is designed to recalibrate automatically the daily risk assessment level to approximately sixty percent of the new account balance. In addition, the daily risk assessment level can be adjusted upward or downward after consultation between customer and account executive. For example, in late January 2010, Mark Middleton began trading with a risk setting of \$4,000, which represented five percent of the \$80,000 starting balance.

In the aftermath of the disputed May 20th liquidation, Middleton authorized his Infinity account executive, Anthony Giacomini, to instruct TransAct to maximize the risk setting, from \$4,000 to \$47,000. For the next five months, Middleton actively day traded, avoided any forced liquidations, and maintained a fairly constant account balance: on May 20, the ending account balance was \$79,214; on May 24, the account balance was approximately \$78,330; on September 30, the account balance hit an interim low of \$73,156; and on October 20, the beginning balance was \$74,069. Thus, since the account balance had dropped little more than \$5,000 over these five months, Middleton traded under the assumption that TransAct had not reduced the risk setting.

Unfortunately, on August 30, 2010, a TransAct keypunch error – the transposition of two digits in an account number – caused TransAct to re-set, down to \$6,000, the risk setting for the

wrong account, the Middleton account. Neither TransAct nor Infinity would inform Middleton about this nearly eight-fold downward adjustment in the risk setting. Thus, Middleton would not learn from Infinity that TransAct had re-set the daily risk assessment level to \$6,000 until after the liquidation on October 20, 2010.

Similarly, Middleton would not learn until well after the fact that it was on August 30th that TransAct had exponentially reduced the risk setting and that this adjustment had been a mistake caused by a TransAct keypunch error on that date. Not until late in this proceeding, and only after I asked the respondents to explain why TransAct had significantly tightened the risk setting at a time that the account balance had not significantly dropped, would any of the respondents explicitly acknowledge the existence of the drastic adjustment, or reveal that TransAct's adjustment had been a mistake caused by a TransAct keypunch error. In response to my request, Giacomini produced an explanation that revealed the existence and circumstances around TransAct's key punch error and mistaken, drastic adjustment in the risk setting.¹ His co-respondents Infinity Futures and James Cagnina did not.²

For the disputed liquidation on May 20, 2010, the Middletons lost \$5,438, and seek to recover the \$1,438 slippage past the \$4,000 daily risk assessment level in effect on that date.³ In reply, respondents deny any liability for this liquidation, and assert that TransAct executed the liquidation order diligently and obtained the best available price in volatile and illiquid market conditions.

¹ Coincidentally, this request was made just after Giacomini had ceased working for Infinity. It was at this point that Giacomini, who beforehand had appeared *pro se* and filed a joint answer with Cagnina and Infinity, hired an attorney. See Gekas Law LLP notice of appearance filed December 14, 2011; and ¶¶ 17-19, Giacomini affidavit, dated December 22, 2011.

² See ¶¶ 4 and 5, Cagnina and Infinity December 9, 2011 joint response to order compelling production; and ¶ 5, Sass affidavit, produced by Cagnina and Infinity.

³ In this decision, amounts are rounded to the nearest dollar, and dates are in 2010, unless otherwise noted.

For the disputed liquidation on October 20, 2010, the Middletons assert that the liquidation was arbitrary and unauthorized:

The Middletons understand the markets' possible volatility and have implemented risk management guidelines, but it seems unacceptable that a trading firm can liquidate a trader's position at their whim. . . . [T]he \$47,000 loss limit wasn't even close.⁴

The Middletons seek to recover \$6,075, based on the difference between the average sell price of the nine liquidated contracts and the liquidation buy price. In reply, respondents deny any liability and assert that the Middletons are solely responsible for their trading loss:

I believe that Mr. Middleton is attempting . . . to recover trading losses for trades that Mr. Middleton made on his own accord and for his own benefit before he was risked out of his account. But Mr. Middleton alone is responsible for those trading losses. . . .⁵

In addition, Giacomini asserts that he had no causal connection to the August 30th keypunch error, because the account number that TransAct erroneously transposed was not for one his accounts.

In connection with both liquidations, respondents assert that they provided all necessary disclosures and that the liquidations were properly executed in accordance with TransAct's risk management and procedures. Respondents further assert that under the terms of the customer contract signed by the Middletons: TransAct reserved the right to liquidate the Middletons' account if TransAct determined in its sole discretion that the account was under-margined; TransAct maintained the right of liquidation without any notification to avoid any significant losses due to extreme market volatility; the Middletons acknowledged that they were solely responsible for monitoring the account and risk setting; and the Middletons acknowledged that TransAct's trading system was not perfect and agreed to hold harmless TransAct and its third party beneficiaries for any losses caused by any fault, delay, or omissions in accuracy or

⁴ Middletons' December 9, 2011 reply to order compelling production.

⁵ ¶33, Giacomini affidavit, underlining in original.

termination of the automated trading system. Respondents also assert the affirmative defenses of ratification and failure to mitigate damages.

As explained below, after carefully reviewing the parties' submissions, I have concluded: one, that the Middletons have established by a preponderance of the evidence that Infinity Futures recklessly failed to provide timely and adequate disclosure of TransAct Futures' drastic and arbitrary adjustment to the account risk setting on August 30, 2010, and that the Middletons are entitled to recover their entire trading loss on the October 20, 2010 liquidation, which was triggered by that undisclosed adjustment; two, that the Middletons have failed to establish any violations causing damages by Giacomini or Cagnina in connection with the October 20, 2010 liquidation; and three, that the Middletons have failed to establish any violations causing damages by the three respondents in connection with the May 20, 2010 liquidation.

Factual Findings

The parties

1. Sherry R. Middleton and Mark A. Middleton, wife and husband and residents of Conroe, Texas, are entrepreneurs who operate their own firm, Midsco Holdings. On their account application, the Middletons stated that Sherry had five years' experience, and Mark had fifteen years' experience, trading commodity futures. Since Mark Middleton was principally responsible for trading, all references below are to him, unless otherwise noted. [See account application, Exhibit 1, joint answer; and first paragraph of description of complaint.]

2. Infinity Futures, LLC is a registered introducing broker located in Chicago. Infinity introduced the Middleton account to its parent corporation, TransAct Futures. [NFA records; and page one of joint answer.]

3. York Business Associates, LLC d/b/a TransAct Futures, not named as a respondent, is a registered futures commission merchant and is also located in Chicago. TransAct is a “100% electronic” firm that focusses on self-directed accounts and clears Infinity customer accounts, including the Middletons’ account. [NFA records; and first paragraph of statement of case, p. 1, joint answer.]

NFA records list TransAct as holding an over 10% ownership share in Infinity. In addition, NFA records list the same set of four individual principals of TransAct as principals of Infinity. Three of these principals hold ownership interests over 10% in both firms. [NFA records.]

In addition to common ownership and control, the operations of TransAct and Infinity are closely coordinated. For example, as described below: one, on October 20, 2010, after Middleton had declined multiple opportunities to re-instate the liquidated positions at a better price, a TransAct/Infinity principal instructed the Middleton’s Infinity broker, Anthony Giacomini, not to further accommodate Middleton and not to bother disclosing that TransAct had mistakenly re-set the risk setting as the result of a TransAct keypunch error; two, TransAct in practice relied on Infinity to disclose to its customers any TransAct adjustments to account risk settings; and three, TransAct and Infinity used the identical boilerplate language in their e-mail messages to customers describing TransAct’s automatic liquidation feature.

As also described below, a human keypunch error – *i.e.*, number transposition -- by a TransAct employee, on August 30, 2010, would cause TransAct mistakenly to reduce drastically the daily risk assessment level for the Middleton account. This in turn would trigger the disputed liquidation on October 20, 2010. [See ¶5, Sass affidavit; and ¶¶18 -19, Giacomini affidavit.]

4. James Cagnina, Jr. is a listed principal and registered associated person with Infinity. Cagnina also is a registered associated person with TransAct. After the disputed October 20th liquidation, Cagnina would speak to Mark Middleton in an ultimately unsuccessful effort to resolve the dispute. Although, Cagnina and Middleton have produced differing versions of their conversation, both versions support the conclusion that Cagnina would not explain the circumstances around TransAct's eight-fold contraction of the risk level to \$6,000 on August 30. That is, he would not reveal that TransAct's keypunch error had caused TransAct mistakenly to tighten drastically the risk level for the Middleton account on that date. [See NFA records; second and third paragraphs, factual description of Middletons' reparations complaint; first full paragraph of Middletons' amendment to complaint; pp. 6-9, joint answer; ¶¶18, 19, and 24-26, Giacomini affidavit; ¶¶4 and 5, Cagnina and Infinity joint response to order compelling production; and ¶5, Sass affidavit.]

5. Mark Gordy, not named as a respondent, is a listed principal of TransAct and Infinity and is the head risk manager at TransAct. On October 20, 2010, after the disputed liquidation on that date, and after Middleton had repeatedly declined to re-instate his liquidated positions at better prices, but before Cagnina spoke to Middleton, Gordy would reveal to Anthony Giacomini that TransAct on August 30th had made a key punch error which had caused TransAct mistakenly to recalibrate the risk level for the Middleton account. Gordy also would signal to Giacomini to do nothing more after Giacomini responded: "Crap. What should we do?" [See ¶18, Giacomini affidavit; and October 20, 2010 e-mail chain, Exhibit J, Giacomini affidavit.]

6. Anthony Giacomini, who acted as the broker for the Middleton account, was a registered associated person with Infinity from January 2009 to November 15, 2011. Giacomini's duties involved opening new electronic self-directed trading accounts and providing

customer service to clients after their accounts were opened, funded, and activated. [See NFA records; pp. 1-6, joint answer; and ¶¶ 1-5, Giacomini affidavit.]

As described below: one, during the account opening process, Giacomini would discuss with Middleton, via phone and e-mail, TransAct's daily risk assessment level; two, in the aftermath of the disputed May 20, 2010 liquidation, Giacomini and Middleton would agree to maximize the daily risk assessment level to \$47,000; and three, in the aftermath of the disputed October 20, 2010 liquidation, Giacomini would try unsuccessfully to reach an accommodation with Middleton. Respondents produced a recording of the May 20th and October 20th conversations between Giacomini and Middleton. [Exhibit L (CD), Giacomini affidavit; and Exhibit 5 (CD), joint answer.]

TransAct's daily risk assessment level

7. For customer accounts, TransAct utilizes a predetermined "daily risk assessment level," also known as a "default risk setting" or an "auto liquidation feature," which is intended to protect customer accounts from "catastrophic" trading losses, principally for the benefit of TransAct. [See ¶6, Giacomini affidavit.] In this connection, section 8 of the TransAct customer agreement reads in pertinent part:

The [TransAct electronic trading] system includes an automatic feature that monitors all positions in the account. If daily losses in the account reach a predetermined limit, the feature is designed to liquidate all positions in the account. . . . Customer acknowledges and understands that any automatic liquidation feature may be imperfect.

[Exhibit K, Giacomini affidavit.] As explained below, it would be simple human error followed by human omission, rather than any technological imperfection in the automatic liquidation feature, which would lead to the disputed October 20th liquidation.

8. If the account balance dropped by a predetermined amount, TransAct automatically would recalibrate the risk level to approximately 60% of the new account balance. In this connection, respondents have made inconsistent assertions about whether TransAct routinely notified its customers of such adjustments. Cagnina and Infinity produced an affidavit by Brian Sass, a principal with Infinity and TransAct, in which Sass stated it was TransAct policy to notify customers of adjustments: “TransAct provides an electronic notice to customers of unilateral adjustments made to the daily loss assessment amount when such changes are reassessed overnight.” [¶6, Sass affidavit.] However Sass’ assertion cannot be squared with Giacomini’s assertion:

Although Mr. Middleton was not able to access his daily risk assessment level online, he could call me at any time to learn where it was set. Furthermore, TransAct offers a 24-hour support desk that Mr. Middleton could call at any time to learn his daily risk assessment level.

[¶14, Giacomini affidavit.] Sass’ assertion also cannot be squared with the absence of any proof that TransAct actually provided a timely notification to Middleton about the August 30th adjustment from \$47,000 to \$6,000. [See ¶5, Sass affidavit; ¶¶4 and 5, Infinity and Cagnina reply to order compelling production; and ¶2 Middletons’ reply to order compelling production.]

9. For the Middleton account, the default risk setting would be lowered and raised several times. Initially, when the account was opened on January 26, 2010, TransAct would set the default risk setting at \$50,000.⁶ However, before trading began and after consulting with Giacomini, Middleton would authorize TransAct to lower the default risk setting to \$4,000.

On May 20, 2010, after a forced liquidation and another consultation with Giacomini, Middleton would authorize TransAct to increase the default risk setting to \$8,000 for that day only, reverting back to 4,000 the next day. Then on May 24, 2010, Middleton would authorize

⁶ This initial setting represented 62.5% of the opening account balance.

Giacomin to instruct TransAct to maximize the default risk setting to \$47,000.⁷ Three months later, on August 30, 2010, as the result of its keypunch error, TransAct would mistakenly decrease the default risk setting to \$6,000, without notifying Middleton or Giacomin. It was this erroneous adjustment which in turn would help trigger the disputed liquidation on October 20, 2010.

The account-opening

10. On January 26, 2010, the Middletons funded their account with \$80,000, and TransAct set the default risk setting for their account at \$50,000. In this connection, TransAct e-mailed a “funding notification” to the Middletons, with instructions to contact Infinity to confirm the default risk setting before placing their first trade:

A deposit to your TransAct account has been made in the amount of \$80,000. Please contact your broker if you need to change your risk limits based upon this deposit. TransAct will not automatically make risk limit changes based upon this deposit. Please confirm your current risk trading parameters before you trade your account.

[Exhibit E, Giacomin affidavit.]

11. About half an hour later, Giacomin sent the Middletons a standard Infinity “account activation” e-mail, with detailed information concerning the default risk setting:

Your account is set up and ready to trade! Your account number is 18256. If you have any questions about what you see here, contact me. If you want anything changed (maximum contract/daily loss limits, for example) or added (such as additional markets), please notify me via email.

Please read the policy on daily loss limits carefully. Daily loss limits will never be increased without a request from you - even if your account grows a result of profitable trading OR a cash infusion. If you want loss limits increased you must contact me. Daily Loss Limits are designed to prevent a catastrophic loss -

⁷ Neither side has documented the account balance for this date. However, the balance can be reasonably estimated for purposes of this decision: the May 24th \$47,000 risk setting represents 60% of \$78,333, which is in the same ballpark with the reported \$79,124 month-end account balance on May 31.

however, do NOT use PnL daily loss limits as a stop-loss order, as they are not guaranteed as per the customer agreement.

If your account reaches your daily loss limit your open position may be auto liquidated and your open orders may be auto cancelled.

NQ: E-Mini Nasdaq TF: Mini Russell YM: Mini Dow
Current Risk Limits
Daily P/L loss limit: \$50,000
Max lot size: 160 contracts

You have been enabled to trade ES, TF, NQ, and YM with a lot size limit of 160 per contract. Your daily risk assessment level is currently set to \$50,000. This is your current predetermined risk assessment level for your account. This amount has and will change as risk levels change. The System's automatic feature monitors all positions in the account and may liquidate based on the above level being reached. Substantial losses may result. There is no certainty that the System will actually liquidate when the predetermined daily risk assessment level is reached; there is no certainty that the System may not commence liquidation even if the predetermined daily risk assessment level has not been reached (for example, if the System receives bad data quote). Per your Customer Agreement you have already acknowledged and confirmed your understanding that the automatic liquidation feature may be imperfect. Nevertheless, you have authorized any such automatic liquidation by the System and agreed that that you shall be solely responsible for any such losses arising directly or indirectly as a result of such automatic liquidation. We monitor your daily loss limit to the downside. If you need to raise the limits you must inform us. The account trader should be aware of the current risk assessment level at all times. The account trader is responsible for knowing the account limits before starting to trade. [p.2]

[Exhibit F, Giacomini affidavit; *see* ¶7, Giacomini affidavit.]

12. Soon after Giacomini sent the account activation email, he spoke to Middleton about the daily risk assessment level limit. After this consultation, Middleton decided to re-set his daily risk assessment level to \$4,000. [See call #1, Exhibit L, Giacomini affidavit, and ¶8, Giacomini affidavit.]

Disputed May 20, 2010 liquidation

13. The first disputed liquidation, on May 20, 2010, involved seven short Euro FX futures. The Middletons do not dispute respondents' assertions that the Euro FX market was

volatile and thinly traded that day. In turn, respondents do not deny the Middletons' assertions that the trigger price for the disputed automatic liquidation on May 20th was 1.2474. [See Time and Sales report for June Euro FX on May 20, 2010, Exhibit C, Cagnina and Infinity joint response to order compelling production.]

14. Between 5:12:33 and 5:27:29 p.m., TransAct reported fills for seven, one-lot, limit-sell Euro FX orders for the Middleton account: the first five orders were filled between 1.2381 and 1.2436 (between 5:12:33 and 5:27:22 p.m.), and the last two orders were filled at 1.2485 and 1.2484 (between 5:27:45 and 5:27:49 p.m.). Thus, sometime in the 23 seconds between 5:27:22 and 5:27:45 p.m., the market traded through or hit the 1.2474 trigger price, and shortly afterward the two pending limit orders with limit prices above that trigger price were filled. [See May 20, 2010 daily statement, Exhibit 2, joint answer; and daily trading activity report for May 20, 2010 (server log excerpt), Exhibit 4b, joint answer.]

15. When the unrealized loss on the seven Euro FX contracts hit the \$4,000 loss limit, TransAct's risk system automatically "locked" the account to prevent Middleton from placing new orders, and automatically triggered market orders to liquidate the seven Euro FX positions. At 5:28:02 p.m., 47 seconds after TransAct had filled the last of the limit-sell orders, TransAct liquidated the seven open positions. Two contracts were bought back at 1.2496, and five contracts were bought back at 1.2497, for an aggregate loss of \$5,737.50. Thus, the slippage on the May 20th liquidation was \$1,737.50. [See May 20, 2010 daily statement, Exhibit 2, joint answer; liquidation calculations for May 20, 2010 (server log excerpt), Exhibit 4a, joint answer; and daily trading activity for May 20, 2010 (server log excerpt), Exhibit 4b, joint answer.]

16. Not long afterwards, Middleton called Giacomini. Middleton remained under control, but his assertive tone and colorful language support the conclusion that he was surprised by the

sudden liquidation and displeased by the amount of slippage: “What the hell just happened here? . . . They just knocked me completely out of the trade!” Giacomini maintained a consistently calm, measured tone and professional demeanor, and offered to unlock the account and raise the loss limit so that Middleton could resume trading. Middleton conceded that he had forgotten about the automatic liquidation feature. Giacomini put Middleton on hold to check with a TransAct agent. When the TransAct agent confirmed the amount of slippage on the liquidation, Giacomini exclaimed “Yikes!”

Giacomini next explained to Middleton that TransAct had obtained the best price on the market orders and that the slippage was due to price volatility and thin trading conditions. Giacomini repeated the offer to unlock the account and raise the loss limit so that Middleton could resume trading. Middleton replied that he would have to think on it.

A little later, Middleton called back, and Giacomini asked TransAct to unlock the account, and adjust the daily loss limit to \$8,000, with the daily loss limit to revert back to \$4,000 the next day. Middleton then made two more Euro FX trades. [See first page of complaint; pages 3 to 4 of joint answer; ¶9 of Giacomini affidavit; May 20, 2010 daily statement, Exhibit 2, joint answer; daily trading activity server log excerpt for May 20, 2010, Exhibit 4b, joint answer; and recordings of May 20, 2010 conversations, call #2, Exhibit L, Giacomini affidavit, and Exhibits 5a and 5b, joint answer.]

17. After the market close on May 20, 2010, Brian Sass, a Transact/Infinity principal, e-mailed Middleton a TransAct standard new account message which included language about the predetermined risk assessment level that was identical to the Infinity standard account activation e-mail that Giacomini had sent Middleton on January 20, 2010. [Exhibit G, Giacomini affidavit; see ¶¶10 and 11, Giacomini affidavit.]

18. On May 24, 2010, Middleton authorized Giacomini to ask TransAct to max out the daily risk assessment level to \$47,000. Giacomini confirmed this adjustment in an e-mail:

As discussed, your account limits are set up as the following:

\$47,000 is your daily loss limit

Currencies - 79 contracts ZB/E-minis -165 contracts
SI/GC/KC - 39 contracts

These will only adjust on the down side automatically. On the upside you will need to request the changes with me directly.

[Exhibit H, Giacomini affidavit, *see* ¶¶12 and 13, Giacomini affidavit; and ¶5, Sass affidavit.]

On October 20, in the aftermath of the second forced liquidation, Middleton would forward a copy of this e-mail back to Giacomini to remind him that he had told Middleton that the risk setting for his account was \$47,000, not \$6,000. [See Middleton reply to order compelling production.]

As noted above, the account balance for May 24th has been estimated to be \$78,330.

TransAct's key punch error and mistaken adjustment to risk level on August 30, 2010

19. Middleton was an active day trader, who avoided large losses and captured small profits, and avoided forced liquidations with the exceptions of the two disputed liquidations on May 20, and October 20, 2010. As a result, Middleton maintained a fairly constant account balance: on May 20, the ending account balance was \$79,214; on May 24, the account balance was approximately \$78,330; and on October 20, the beginning balance was \$74,069. [See May 20, and October 20 account statements, attachments to complaint.]

As can be seen from the following summary of monthly account balances, on September 30, the account hit an interim low balance of \$73,156, which represented an approximately \$5,200 drop from the balance on May 24:

<i>Month</i>	<i>Beginning balance</i>	<i>Contracts traded</i>	<i>Ending balance</i>
May	\$81,288	640	\$79,124
Jun.	79,124	382	76,961
Jul.	76,961	238	74,567
Aug.	74,657	330	75,263
Sep.	75,263	374	73,156
Oct.	73,156	234	68,033

[See January to October 2010 monthly statements, Exhibit A, Cagnina and Infinity response to order compelling production.]

Respondents have produced no evidence of any market conditions between May 24th and October 20th that would have independently justified any significant downward adjustments to the risk setting for the Middleton account. Therefore, the only known factor on this record justifying any adjustments would have been the approximately \$5,200 account balance decline from May 24, to September 30. Thus, from late May to mid-October, Middleton had good reason to trade with the assumption that TransAct either had not reduced the risk setting or, if it had reduced the setting without telling him, it would not have reduced it significantly. Based on the approximately \$5,200 decline in the account balance between May 24 and September 30, the most that Middleton could have reasonably expected TransAct to automatically tighten the risk limit would have been by approximately \$3,100 ($60\% \times \$5,200$), from \$47,000 to \$43,900. [See ¶¶ 1 and 5, Middleton affidavit.]

20. On August 30, 2010, as a result of its employee's key punch error, TransAct exponentially reduced the daily risk assessment level for the Middleton's account, from \$47,000 to \$6,000. Two months later, after the disputed liquidation on October 20, 2010, TransAct would inform Giacomini that a Transact employee had misread a request to change the daily risk assessment level for another account, with account number 18265, and mistakenly transposed the

last two numbers to 18256, which was the account number for the Middletons' account. [See email chain between Giacomim and Gordy, Exhibit J, Giacomim affidavit, and ¶18, Giacomim affidavit.]

Neither Infinity nor TransAct provided contemporaneous notice of this adjustment to Middleton. Similarly, neither Infinity nor TransAct provided Middleton any explanation of the circumstances around the adjustment. [See ¶2, Middleton reply to order compelling production; ¶1, Middleton affidavit; ¶¶16 to 19, Giacomim affidavit; ¶¶4 and 5, Cagnina and Infinity joint response to order compelling production; October 20, 2010, Giacomim-Gordy e-mail chain, Exhibit J, Giacomim affidavit; and recordings of the October 20th conversations between Giacomim and Middleton, Exhibit L, Giacomim affidavit, and Exhibit 5, joint answer.]

Disputed October 20, 2010 liquidation

21. The morning of October 20, 2010, Middleton began scaling into a short December Euro FX futures trade with the expectation of a downward move. The market spiked up, and TransAct automatically liquidated all open positions in the account. Respondents do not dispute Middleton's calculation that he lost \$6,075 on this liquidation. [See factual description of complaint; Exhibit D, Giacomim affidavit (chart of the events on October 20, 2010, created by Giacomim on or about that date from "information sources available to [him]"); ¶¶14 and 15, Giacomim affidavit.]

22. Soon afterwards, Middleton called Giacomim for an explanation. Giacomim in turn called TransAct. Giacomim contacted TransAct to reactivate the account, and to provide him a history report of the risk limit changes for the Middletons' account. The TransAct agent informed Giacomim that TransAct had lowered the Middletons' daily risk assessment level to \$6,000, on August 30, 2010. Giacomim passed on this information to a surprised and displeased

Middleton, who forwarded to Giacomini a copy of Giacomini's May 24th e-mail confirming the \$47,000 risk setting. Giacomini also told Middleton that TransAct had reactivated his account, and suggested that Middleton re-establish his positions. However, Middleton demanded that his positions be "reinstated." Giacomini told Middleton that his positions would not be reinstated, but that he should reestablish his positions himself. Giacomini also stated that they could discuss a credit for his commissions after he did so, to which Middleton responded "very good." The conversation concluded with Middleton refusing to reestablish his positions or accept that he should be on the hook for a plus-\$6,000 loss, and Giacomini promising to further investigate what had happened and call back later. [See call #3, Exhibit L, Giacomini affidavit.]

23. Next, Mark Gordy, TransAct risk manager and co-owner of TransAct and Infinity, told Giacomini that TransAct had accidentally lowered the daily risk assessment level for the Middletons' account to \$6,000 on August 30, 2010. Gordy revealed that TransAct had inadvertently misread a request to change the daily risk assessment level for another account, and accidentally transposed the numbers and changed the daily risk assessment level for the wrong account, the Middletons' account. Set out below in condensed script form, is the e-mail exchange, from 10:20 a.m. and 11:25 a.m., between Giacomini and Gordy. As can be seen, at the end Gordy signaled to Giacomini not to disclose to Middleton the fact that a TransAct keypunch error had led to a drastic and *de facto* arbitrary adjustment in the risk setting:

Giacomini: What is the history of loss limit changes in the account?

Gordy: What are you looking for?

Giacomini: The history of loss-limit changes. Last I have is a change for \$47,000 on 5/24/2010.

Gordy: Looks like a typo on our part. 18256 versus 18265.

Giacomini: Crap. What should we do? Sorry, new to this.

Gordy: He was unlocked immediately and had plenty of time to re-establish the price at the p[rice or better. He chose not to.

[Exhibit J, Giacomini affidavit; and ¶¶16 to 19, Giacomini affidavit.]

24. In multiple conversations later that day, Giacomini followed Gordy's lead and did not report the fruits of his promised investigation: that is, Giacomini did not tell Middleton about TransAct's keypunch error. Giacomini did tell Middleton that he would try to get a commission credit for Middleton and eventually offered a \$550 credit. In each conversation, Giacomini urged Middleton to re-establish his positions. Each time, Middleton refused because he was still smarting from the May 20 liquidation, because he had lost trust in TransAct and Infinity, because neither Giacomini nor Cagnini offered any rationale for the inexplicable, drastic reduction in the risk setting, because he thought that the latest liquidation was arbitrary and unfair, and because he did not think it was right to be stuck with the resulting loss of over \$6,000. Conversely, TransAct and Infinity took the position that, since Middleton had declined multiple opportunities to re-enter the market at a favorable price, they were freed of any obligations including candor.

[See calls ## 4 -10, Exhibit L, Giacomini affidavit; and ¶¶20 to 27, Giacomini affidavit.]

Conclusions

Initial and maintenance margins are instituted for the protection of futures commission merchants, and reflect the amount of risk a futures commission merchant is willing to accept for a customer's position. For this reason, it is well established that a futures commission merchant has considerable discretion to set and enforce its margin policies, absent evidence of fraudulent or bad faith conduct. *Baker v. Edward D. Jones & Company*, Comm. Fut. L. Rep. ¶21,167 (CFTC 1981). Therefore, in order to establish wrongdoing by respondents, the Middletons must

show by a preponderance of the evidence either that respondents misled Mark Middleton about TransAct's margin policy or executed the October 20, 2010 liquidation in bad faith.

Here, the Middletons have established that Infinity recklessly failed to provide timely and adequate disclosure of TransAct's adjustment to the account risk setting on August 30, 2010. The underlying cause of that adjustment may have been an inadvertent and at worst negligent keypunch error. However, in the absence of objective readily knowable factors – such as a substantial drop in account balance or volatile and illiquid market conditions -- the reduction of the account risk setting from \$47,000 to \$6,000 constituted a *de facto* arbitrary adjustment of great magnitude. This downward adjustment was patently material to a trader in Middleton's position, particularly in the absence of any objective factors which would have flagged a significant tightening in the risk setting. Infinity was in the best position to disclose this unanticipated and drastic decrease in the account risk setting, and thus had an affirmative duty to disclose it promptly to Middleton under Section 4b of the Act. However, Infinity recklessly failed to provide timely and unambiguous disclosure of the August 30, 2010 adjustment. Infinity's ongoing gross indifference to its disclosure duty was underscored by respondents' deliberate lack of candor in their dealings with Middleton in the aftermath of the disputed liquidation on October 20, 2010. *See Sudol v. Shearson Loeb Rhoades, Inc.*, ¶ 22,748 (CFTC 1985). *See also Precision Ratios v. Man Financial*, 2004 WL 1657545, Comm. Fut. L. Rep. ¶29,646 (Initial Decision CFTC Dec. 11, 2003), affirmed summarily Comm. Fut. L. Rep. ¶29,813 (CFTC July 23, 2004); and *Human v. Alaron Trading Corporation*, Comm. Fut. L. Rep. ¶27,470 (Newsome and Spears concurring opinion, 1998).

The various exculpatory provisions and warnings in the customer agreement that TransAct could adjust the account risk setting are insufficient to overcome the duty to disclose a

material fact of the magnitude of the August 30th adjustment. *See Lee v. Lind-Waldock & Company*, Comm. Fut. L. Rep. ¶28,173 at 50,159-50,160 (CFTC 2000). (In resolving disputes under the Commodity Exchange Act, the Commission has traditionally focused on the obligations that Sections 4d and 4b of the Commodity Exchange Act impose on futures commission merchants and introducing brokers, rather than the waivers implicit in certain provisions of standardized agreements between firms and their customers.) Similarly, respondents' various e-mail messages about the risk setting do not shield Infinity from its disclosure duty.

A rebuttable presumption exists that Mark Middleton relied on the missing information when he traded on October 20, 2010. *See Maloley v. R.J. O'Brien & Assoc., Inc.*, ¶24,293 (CFTC 1988). Middleton's reliance on Infinity's omission is underscored by his statements to respondents that based on Giacomini's previous representations he understood that the account risk setting had remained at \$47,000. Respondents otherwise have failed to produce sufficient evidence to rebut the presumption of reliance.

The proper measure of damages for Infinity's disclosure failure should restore the Middletons to where they would have been had they received timely notice of the material information and been able to factor it into Mark Middleton's trading decisions on October 20, 2010. Thus, the Middletons are entitled to an award based on the loss realized on the liquidation: \$6,075.⁸

In connection with the October 20, 2010 liquidation, the Middletons have failed to establish any violations causing damages by Giacomini or Cagnina. In connection with the May

⁸ Respondents base their ratification and mitigation defenses on Middleton's rejection of their advice to re-establish the liquidated positions on October 20. Respondents have the burden to establish these affirmative defenses. However, respondents' deliberate lack of candor when they gave that advice precludes both defenses.

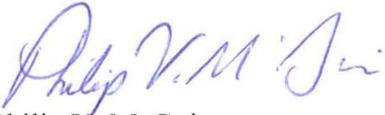
20, 2010 liquidation, the Middletons have failed to establish any violations causing damages by the three respondents

ORDER

The Middletons have established that Infinity Futures violated Section 4b(a) of the Commodity Exchange Act, and that this violation proximately caused \$6,075 in damages. Accordingly, Infinity Futures is ordered to pay to Sherry Middleton and Mark Middleton reparations of \$6,075, plus interest on that amount at 0.12% compounded annually from October 20, 2010, to the date of payment, plus \$125 in costs for the filing fee.

The Middletons have failed to establish any violations causing damages by Anthony Giacomini and James P. Cagnina, Jr. Accordingly, the complaint against Anthony Giacomini and James P. Cagnina, Jr. is dismissed.

Dated February 3, 2012.


Philip V. McGuire,
Judgment Officer