UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

PRECISION RATIOS, INCORPORATED, *
MILLENNIUM TRUST COMPANY, f/b/o *
GEORGE POWELL, *
Complainants, *
*
v. * CFTC Docket No. 01-R96
*
MAN FINANCIAL, INCORPORATED, *
Respondent. *
*

INITIAL DECISION

Introduction

This dispute arises from the forced liquidation of two short June U.S. Dollar Index ("DX") futures contracts a week before the last trading date for the June DX. The parties do not dispute the essential facts, but disagree about who was responsible for the forced liquidation and who bears the liability for the losses arising from the liquidation.

A year before the disputed liquidation of the June DX's, the New York Board of Trade ("NYBOT") announced to its clearing members that it would be converting the DX from a cash-settled to a deliverable contract, beginning with the next March contract. In a related development, the NYBOT's clearing corporation, the New York Clearing Corporation ("NYCC"), subsequently advised its clearing members of an additional delivery procedure for the deliverable DX. Under NYCC's new procedure, for each customer carrying an open position in the expiring deliverable DX contract, the clearing member would be required to provide -- a full week before the last trading day -- banking instructions for delivery of the basket of currencies in the U.S. Dollar Index.

A few weeks before the expiration of the initial deliverable March contract, Man Financial determined that the "onerous and burdensome process" of setting up the necessary banking relationships for the delivery of a basket of the seven DX currencies could not be justified, principally because Man Financial had never had a retail DX customer make or take delivery. Man Financial also decided that it would avoid conflicting with the exchange's new delivery procedure by compelling any customer holding a deliverable DX contract to liquidate the position before the seven-day deadline for filing banking instructions. Consequently, Man Financial had effectively moved back the last trading day for its DX customers by a full week.

Man Financial did not provide any advance notice to its customers about the shortened trading period for the DX. Rather, about a week before the last trading day for the expiring March DX, and then for the expiring June DX, Man Financial individually contacted its DX customers to instruct them to liquidate or rollover their expiring DX positions.

Thus, a week before the last trading day for the June DX, Man Financial contacted Powell and informed him that he must immediately liquidate the two short June DX's. Powell complained that Man Financial had failed to provide any advance warning and that he would have altered his exit strategy if he had received adequate notice. Powell indicated that although he had not intended to take delivery, he had planned to liquidate the June DX's sometime over the next five trading days, but at a time of his own choosing. Man Financial agents told Powell that they were merely complying with NYBOT rules, advised him to rollover into the September contract if he wanted to stay in the market, and finally convinced him to liquidate when they threatened to charge his account a $2,500 "punitive processing fee." Powell then placed an order to liquidate both June DX positions, and realized a total loss of about $12,110.

Powell claims that Man Financial prevented him from significantly reducing his losses by improperly forcing him to liquidate the two June DX's prematurely. Powell also claims that Man Financial deprived him of material information by not providing advance notice that Man Financial had determined to comply with newly revised NYBOT delivery notice requirements by moving the last trading day for its DX customers backwards by a week:

> I know that there's a big difference between using a discount broker and a full-service broker pertaining to fiduciary responsibility, but we are talking about a commodity that is thinly traded with most of the volume going to large-lot players. I don't understand the problem with Man Financial not wanting to make the effort to give their traders this notice [of moving back the last trading day] when it does not happen very often.

[Powell's supplemental closing statement (filed November 6, 2003).] Powell seeks to recover $5,240, based on the best interim price between the forced liquidation and NYBOT's last trading date.

In reply, Man Financial asserts that it had considerable discretion under the terms of the customer agreement to compel Powell to liquidate since he had not intended to deliver any currencies. Man Financial also asserts that it acted reasonably and in good faith in the manner and timing in which it notified Powell of the new DX delivery specifications. According to Man Financial, since Powell maintained self-directed discount accounts, Man Financial was not obligated to provide Powell with advance notice that the NYBOT had changed the DX from a cash-settled to a commodity delivered contract or advance notice that the NYCC had moved up the deadline for delivery instructions. Man Financial further asserts that it was not obligated to provide

Powell with advance notice that Man Financial had decided to comply with the revised exchange delivery procedures by forcing its DX customers to liquidate or roll over a week before the published last trading date. Finally, based on Powell's refusal to roll forward into the September DX, Man Financial has raised the affirmative defenses of estoppel and failure to mitigate damages.

After carefully reviewing the documentary record,[1] it has been concluded that Man Financial recklessly deprived Powell of material information by failing to provide adequate advance notification that it had made a business decision to shorten the period that its customers could trade an expiring DX futures contract, and that Powell is entitled to an award of $4,080, based on the best interim price during the two weeks <u>before</u> Man Financial's *de facto* last trading day for its U.S. Dollar Index customers.

Findings of Fact

The parties

1. George Powell, a resident of Dayton, Ohio, was a 66 year-old, retired manufacturing engineer when he opened two non-discretionary discount accounts with Man Financial, Incorporated. Precision Ratios, Incorporated, owned by Powell and his wife, was a tool and die company. After the Powells sold the equipment, they ran the company as an engineering consulting firm. On his account application, Powell indicated that his annual income consisted chiefly of Social Security payments, and that he had a

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[1] The documentary record consists of Powell's complaint, with addenda and exhibits; Man Financial's answer; various affidavits, statements and documents, and a tape recording produced by the parties in response to two *sua sponte* discovery orders; and the parties' closing statements and supplemental closing statements. In addition, official notice has been taken of: (1) public documents concerning the CFTC's approval of the NYBOT's application to amend the terms of the DX futures contract; and (2) the following pages recently viewed on the NYBOT website (www.NYBOT.com): the press release archives, the specifications for the DX futures contract, and a NYBOT brochure titled "The U.S. Dollar Index: The Barometer of the U.S. Dollar."

net worth of $100,000, and a liquid net worth of $80,000. Powell also indicated that his investment experience was limited to an IRA account and two years trading futures contracts.

Powell opened a nondiscretionary discount account in the name of Precision Ratios (described by Powell as the "tool and die account"), and opened a second nondiscretionary discount account for Millennium Trust Company (described by Powell as the "IRA account"). Since Powell made all the trading decisions for Precision Ratios and Millennium Trust, all references to the complainants in this decision are to Powell.

2. Man Financial, Incorporated is a registered futures commission merchant located in Chicago, Illinois. Man Financial is a clearing member of all the major North American futures exchanges, including the New York Board of Trade.

The NYBOT is the parent company of the Coffee, Sugar and Cocoa Exchange and the New York Cotton Exchange ("NYCE"). The New York Clearing Corporation is the designated clearinghouse for all NYBOT markets, and in that capacity reconciles and clears all futures and options transactions for the exchanges and subsidiaries of the NYBOT, and assures the financial integrity of such transactions.

Man Financial's standard customer contract

3. When Powell opened the two non-discretionary discount accounts with Man Financial, he entered into customer agreements with Man Financial. Man Financial would invoke Paragraphs 5 and 7 of Man's standard customer agreement when it compelled Powell to liquidate the two June DX's. Paragraph 5 provided, in pertinent part, that:

> The Company may at any time, in its sole discretion and without notice to the Customer, . . . take such other actions including . . . liquidating any position in the Customer Account if the Company deems itself to be insecure or in need of protection.

Paragraph 7 of the agreement required Powell to advise Man Financial only if he intended to make or take delivery:

> [The Customer] agrees to give us timely notice if you intend to make or take delivery under a contract. . . . If so requested by us, you shall satisfy us that you can fulfill your obligations to make or take delivery.

[Exhibit to Answer.] Thus, the agreement contemplated that Powell would not notify Man Financial if he did not intend to make or take delivery.

Powell's trading

4. Powell opened the two accounts in 1998, about three years before the disputed liquidation. Over time, Powell tended to trade in just one account or the other. Most of Powell's trades involved day trades and short-term trades, exclusively in silver futures and U.S. Dollar Index futures. Powell never took delivery, never traded on the last trading day, and never rolled over an expiring position into the next contract month.

Powell made the first DX trade in the Millennium Trust account in September 1999, and made the first DX trade in the Precision Ratios account in February 2001.

The U.S. Dollar Index Futures Contract

5. The U.S Dollar Index tracks the value of the dollar against a basket of six major currencies, and is calculated continuously by using a geometrically weighted average of six currencies which represent major U.S. trading partners: the Euro, the British Pound, the Japanese Yen, the Canadian Dollar, the Swiss Franc, and the Swedish Krona.

The U.S Dollar Index future contract is traded by open outcry on the New York and Dublin trading floors of the Financial Instruments Exchange ("FINEX"), the NYBOT's currency products division. The NYBOT markets the DX future contract as a foreign exchange rate risk management tool for portfolio investors and multinational corporations, as an arbitrage tool for inter-bank traders, and a speculative tool for individuals who have a view on the future direction of dollar value.

The DX delivery months are March, June, September and December. The Last Trading Day ("LTD") for the DX is the second business day prior to the third Wednesday of the expiring month. Thus, the LTD for the March 2001 DX was March 16, and the LTD for the June 2001 DX was June 18. The Delivery Day for the DX is the third Wednesday of the expiring month.

Before March 2001, DX contracts held to expiration were settled in cash on the last trading day. Since March 2001, the DX has been settled by physical delivery. At expiration, a long DX position receives US dollars and pays the component currencies, and a short DX position receives the component currencies and pays the U.S. dollar. [*See* "The U.S. Dollar Index: The Barometer of the U.S. Dollar," at www.nybot.com.]

NYBOT converts the DX to physical delivery

6. On June 12, 2000, the NYBOT issued a "Release to Membership" titled *Amendment Converting the NYCE U.S. Dollar Index to physical delivery from cash settlement.*[2] This release announced:

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[2] On April 13, 2000, the NYCE had submitted the proposed amendments to the DX contract for fast track approval by the CFTC. By Federal Register release dated May 5, 2000, the CFTC sought comments on the proposed amendments. The CFTC received three comment letters -- from two market makers and one arbitrageur – which all supported the proposal to convert the DX to physical delivery. On May 24, 2000, the CFTC approved the amendments, effective on May 30, 2000. [CFTC records.]

> Effective upon the opening of business on June 14, 2000, commencing with the March 2001 contract, the U.S. Dollar Index futures contract will be settled by physical delivery. At expiration, . . . a short position in the DX will receive the component currencies and pay the US dollars.

The release highlighted the principal amended terms of the DX contract, including the NYBOT's revised delivery procedure that called for clearing members to submit delivery commitments no later than the last trading day for the deliverable contract:

> The short Clearing Member is responsible for assuring the timely delivery of the U.S. Dollars into the appropriate Clearing Corporation account at the Exchange-approved delivery bank and to provide complete information for the timely transfer of the appropriate Settlement Currencies into the short Clearing Member's account . . . .

The amended terms also included a provision that any delinquency in performance would result in the clearing member being financially liable to the clearing corporation and to the opposite clearing member for any losses, and would subject the clearing member to disciplinary or membership responsibility action.

7. On October 5, 2000, the NYBOT followed up with an e-mail notice to all clearing members that reminded them of the change to physical delivery for the DX.

8. On February 27, 2001, the NYBOT issued a press release titled "NYBOT Announces USDX Settlement," which stated in pertinent part:

> The [NYBOT] announced today changes for the [DX].
>
> Due to a bank holiday in Japan on Tuesday, March 20, 2001, the last trading day for the March [DX] will be Friday, March 16, 2001. The settlement date for these contracts, Wednesday, March 21, 2001, is not affected.[3]
>
> Other changes in the settlement process for the DX futures contract beginning with the March 21, 2001 expiration are as follows:

[3] In this connection, two documents available to Powell at the relevant time – one, the NYBOT broadsheet that listed the last trading dates for all of its futures contracts, and two, the commodity calendar published by *Futures* magazine, and distributed by Man Financial -- identified the last trading day for the DX as the second business day prior to the third Wednesday of the expiring month: *i.e.*, June 18 for the June DX. Neither document mentioned the seven-day deadline for filing delivery instructions.

Trading will cease at 10:16 am on the last day of trading.

Settlement will be physical delivery.

At expiration:

A long DX position will be settled with the U.S dollar credits and debits of the component currencies respective to their weightings.

A short DX position will be settled with the U.S dollar debits and credits of the component currencies respective to their weightings.

[Underlining added for emphasis.] As can be seen, the release did not mention any obligation to provide delivery instructions a week before the published last trading date.[4]

9. In late February 2001 – eight months after the NYBOT's Notice to its members, four months after the NYBOT's reminder to its members, and two weeks before the last trading day for the March contract -- Man Financial took its first concrete steps in anticipation of the conversion of the DX to physical delivery. Man Financial's senior vice president of operations, Thomas Vera, spoke to a NYCC vice president, Brian Saylor, about the NYCC's new physical delivery requirements that commenced with the March DX.[5] During this conversation, Saylor confirmed that the NYCC had granted Man Financial a two-day extension to file delivery instructions in exchange for Man Financial's assurances that no Man Financial DX client intended to make or take delivery, and that all Man Financial DX clients would liquidate their March DX's by the

[4] A recent review by the undersigned of the press release archive at the NYBOT's website indicates that this was the only NYBOT press release about the conversion of the DX to physical delivery issued during the relevant time. Also, the current version of the NYBOT website provides the principal contract specifications of the DX, such as stating that the DX is settled by physical delivery and explaining how the Last Trading Day and the Delivery Day are determined. However, the NYBOT website but does not mention that clearing members must provide banking instructions seven days before the last trading day. In this connection, neither side has produced a copy of the DX page of the NYBOT website from the relevant time.

[5] On this record, it cannot be determined when the NYCC first advised its members of its new delivery requirements.

close on March 12 -- five days before the last trading day, March 16. [*See* Vera affidavit.]

Next, on February 28 and March 1, Thomas Vera sent e-mails to Man Financial managers regarding Man Financial's determination to compel its clients to liquidate any March DX positions by the close on March 12. The first e-mail, sent out on the afternoon of February 28, stated in pertinent part:

> We have a bit of a dilemma with the US Dollar Index Contract traded on the FINEX. Commencing with the March contract, it goes from a cash settled contract to a deliverable, which entails a whole basket of currencies. Joyce has already indicated that she will not be able to support handling this delivery as she does on some other cross-rates. <u>Nor, absent of any substantial hedgers, do we want to allow customers (and certainly not our retail spec accounts) to go into delivery</u>. . . .
>
> <u>The problem we face is primarily a timing issue</u>. . . . Commencing on 3/12, all [clearing members] with positions must report to the clearinghouse their banking instructions. <u>As we have no intention of allowing our clients to go into delivery, we do not have the banking arrangements set up</u>. . . .
>
> As we stand today, we hold approximately 150 longs by 275 shorts, for the most part all 1 lots.

The second e-mail, sent out on the afternoon of March 1, stated in pertinent part:

> Be advised that, commencing the MAR '01 contract, the US $ Index on the FINEX becomes deliverable. . . . As this contract involves a basket of seven different currencies, <u>the banking arrangements are quite complicated. As such, it will be our policy not to allow our clients to go into delivery</u>. As the LTD is 3/16, we are requiring all clients to liquidate their positions by 3/12. <u>We have begun the process today of informing all accounts with positions of our policy by telephone.</u>

[Underlining added for emphasis. *See* ¶ 3 of Vera's affidavit dated July 8, 2003, and ¶ 6 of Pinkerton's affidavit dated November 7, 2003.]

The March DX liquidation

10. As of March 1, 2001, Powell was short one March DX in the Millennium Trust account. On March 9, the March DX was liquidated. Throughout the course of this proceeding, neither side had mentioned this trade, let alone addressed the circumstances around this trade. Thus, both sides had been operating on the assumption that June 12, 2001 was the first time that Man Financial had compelled Powell to liquidate a DX a week before the last trading day. However, while reviewing a tape-recording of a conversation on June 12, in which Powell complained about being forced to liquidate, I noticed that Powell had also mentioned in passing that: "You pulled the same crap last time." As a result, I asked both sides to supplement their closing statements with descriptions of the circumstances around the liquidation of the March DX on March 9.

Man Financial, in its reply, conceded that none of Man Financial's trading center personnel could recall the circumstances around the March liquidation. But Man Financial asserted that since Powell had held an expiring March DX contract, its employees would have followed Man Financial's newly instituted procedure for expiring deliverable DX contracts, and thus would have instructed Powell sometime before March 12 to liquidate the March DX. [Pinkerton affidavit dated November 7, 2003 (attachment to Man Financial's supplemental closing statement).]

In his reply, Powell similarly indicated that he could remember little about the March liquidation. However, Powell did specifically recall that he had been "mad" that Man Financial had abruptly changed the last trading date. More significantly, Powell also recalled that Man Financial had not explained that it would be similarly accelerating the last trading date for the June DX, and for all the subsequent deliverable DX contracts:

I had one March DX futures contract that ran into an altered maturing date, in that the published last trading date was March 21 [*sic.*][6]

At sometime, I must have been called and told that the last trading date had been changed to Monday, March 12, and that I had to be out of my March DX contract by Friday, March 9. I did [liquidate] at a $3,000 loss. In this case, staying in this contract longer would have created a higher loss.

I did not raise Cain or request a fix from the powers that be. Nor did I inquire of future revisions. <u>Nor did the desk broker indicate that the June DX contracts would be affected in a similar manner</u>.

I just took my lumps and continued with my existing open positions.

I have searched my notes and other records and cannot determine when or who called. But I distinctly remember being mad about the published last trading day of March 21 [*sic*] being moved backwards seven business days to March 12. My records show that to offset my short March DX contract, I placed a buy order on March 8, and that it filled on March 9.

[Underlining added for emphasis; Powell's supplemental closing statement.]

The disputed June DX liquidation

11. As previously mentioned, the disputed liquidation involved two short June DX contracts. Powell had shorted the first June DX on March 7 (at 111.60), in the Millennium Trust account, and had shorted the second June DX contract on May 11 (at 116.50), in the Precision Instruments account.

Set out below is a summary of the daily high and low prices for the June DX from Tuesday, May 29, to Monday, June 18 (the NYBOT's last trading day), and for the September DX from Monday, June 11 (when Man advised Powell to rollover into September) to Monday, June 18:

[6] Powell sometimes has confused the last trading day and the delivery day.

Date	*June High*	*June Low*	*Sep. High*	*Sep. Low*
5-29	118.70	118.06	--	--
5-30	118.54	118.03	--	--
5-31	119.33	118.34	--	--
6-01	119.45	118.75	--	--
6-04	119.44	118.63	--	--
6-05	119.60	118.70	--	--
6-06	119.68	118.54	--	--
6-07	119.64	119.00	--	--
6-08	119.67	119.14	--	--
6-11	120.33	119.28	120.65	119.56
6-12	120.20	119.57	120.48	119.85
6-13	119.49	118.87	119.79	119.15
6-14	119.51	117.97	119.83	118.25
6-15	118.34	117.50	118.68	117.75
6-18	118.70	118.13	119.00	118.40

[FINEX Historical Data File, www.nybot.com.]

12. On Friday, June 8, Man Financial broadcast an e-mail to its managers advising them that all clients holding the June DX must liquidate by the close on Monday, June 11. This e-mail message was almost identical to the March e-mail message, with the notable exception that the June message stated that any client who refused to liquidate would face a punitive processing fee of up to $2,500:

> Be advised that, commencing the MAR '01 contract, the US $ Index on the FINEX becomes deliverable. . . . Consistent with the exchange's policy on currency deliveries, all clearing members with positions must submit banking instructions commencing five [sic] days prior to LTD and every day thereafter. As this contract involves a basket of seven different currencies, the banking arrangements are quite complicated. As such, it will be our policy not to allow our clients to go into delivery. As the LTD is 6/18, we are requiring all clients to liquidate their positions by 6/11.
>
> Accordingly all clients holding positions in the June U.S. Dollar Index contract must liquidate by the close of business June 11th 2001. Any client not liquidated by this date will be promptly liquidated on the

> opening on June 12th and may be subject to a punitive processing fee of up to $2,500.

At the close on Friday, July 8, Man was carrying a total of 677 long and 166 short June DX contracts, for approximately 200 customers.

13. On June 11, Powell's two June DX's were down about $12,000. That morning, a Man Financial trading desk broker called Powell, informed Powell that June 11th was the last trading day, and asked Powell to provide an exit price for two liquidation orders. Powell refused, complained that the published information provided by NYBOT and by Man Financial had stated that the last trading day was June 18, and demanded written proof that the last trading day had been accelerated to June 11. The broker then faxed a copy of the June 8th e-mail. Powell was upset by the threat of a $2,500 fine and found the explanation in the e-mail less than clear and complete.

Later that day, Powell spoke to Emil Lubinetz, a supervisor at Man Financial's trading desk:

> POWELL: Yeah, I got a big problem. It's running -- it's running it up and multiplying my loss. Okay, this is a thinly traded market; there isn't but about 8,000 open-enders accounts in it. So, I mean, what's the deal with you've got to get me out today instead of the 20th?
>
> LUBINETZ: Have you been read the memorandum -- the memo that was sent?
>
> POWELL: That's -- I sure.
>
> LUBINETZ: Have you read -- have you read the memo?
>
> POWELL: Yes, I have it right in front of me.
>
> LUBINETZ: Okay. It was faxed over to you, correct?
>
> POWELL: That's correct.
>
> LUBINETZ: What is it that you don't understand about the memo?

POWELL: I don't understand why I was called today and told I had to get out today when the last trading day, according to your information, is the 20th.

LUBINETZ: That's correct.

POWELL: Well, I don't understand the memo. The memo don't -- doesn't explain why?

LUBINETZ: Consistent with the exchange's policy on currency deliveries, all clearing members with a position must submit banking instructions commencing five days prior to LTD and every day thereafter. So, we have to know from you whether you want to take delivery or not --

POWELL: No, I don't --

LUBINETZ: -- or how to take delivery.

POWELL: No, I don't want to take delivery.

LUBINETZ: Okay, so why don't we just buy you a June and sell a September dollar index, sir, and then be done with it?

POWELL: Wait a minute. You're trying -- I've already got substantial losses. I can't do that. In other words, I have --

LUBINETZ: You're going to be subject to -- fee of $2,500 to -- to get out today.

POWELL: Wait a minute. On the one account, 37360 I'm short at 111.60, okay?

LUBINETZ: Uh-huh.

POWELL: Now, on the other account, 26695, I'm short at 116.50.

LUBINETZ: Okay.

POWELL: And because you're forcing everyone to sell today, the market is being run up. This is the rape of the June shorts. You're not letting the market get out. You know we got till the 20th [sic] to get out in an orderly fashion and you're forcing everyone out the door today.

LUBINETZ: No, the exchange is, sir. Not us. The exchange.

POWELL: Well --

LUBINETZ: Don't forget, though, we don't have control over the Japanese yen or the Euro currency or the British pound. They're all down, too. So we're not forcing people out of those markets. And those are down.

POWELL: Well, why -- why --

LUBINETZ: Do you see what I'm saying here?

POWELL: No --

LUBINETZ: The dollar is up naturally. It's not because we're forcing people out, sir.

POWELL: Well, that sure -- that sure doesn't hurt it. At least it helps it. Hell, it's up to what, 120.20, or something like that?

LUBINETZ: That's correct. That's correct.

POWELL: Okay. I want to take longer to get out.

LUBINETZ: You can't, sir. You have to be out today.

POWELL: Well, why don't you change the thing -- the last trading day today then? Why are you putting it [out as] 6-20? Change -- change what you're telling us then. You pulled the same crap last time.

LUBINETZ: Well, I --

POWELL: We don't have anything firm to base our decisions on anymore. I don't want a one-day notice that I have to get out of the market. Don't you understand?

LUBINETZ: I do, sir. I do. And I feel for you.

POWELL: Yeah, I know you do.

LUBINETZ: I really do. I mean, I understand it's a really bad situation to be in and if -- you know, if you wanted to be in the position, you'd buy the June and sell [the September] -- and you'd still be in the same position.

Powell then decided to liquidate to avoid the $2,500 fine. After placing a couple of limit orders that were not filled, Powell placed a market order that was filled at 120.12, for a total loss of $12,140. Powell decided not to roll over into the September DX, because he had felt bullied by the threat of the fine, had lost trust in Man Financial's reliability, and was not sure that he had sufficient margin to cover two September DX's.[7] In a subsequent conversation, Man Financial advised Powell to plan in the future on liquidating any open expiring DX positions a week before the last trading day.

According to Man Financial, out of all of Man's DX traders, only Powell and one customer had complained about the early liquidation of the June DX's.

14. Powell and Man Financial's general counsel then exchanged a series of letters in which Powell complained that Man Financial had unreasonably forced him to liquidate without adequate warning and that Man Financial had roiled June DX prices by forcing its customers to liquidate *en masse*. The general counsel replied by providing Powell with the first coherent explanation about Man Financial's revised DX delivery policy. The general counsel also asserted that Man had absolute discretion under the customer agreement to force Powell to liquidate since he had not intended to make delivery. Set out below are pertinent portions of the general counsel's letter dated June 25, 2001:

> I have investigated the allegations in your letter and can report to you the following:
>
> Your information regarding the last trading day is correct. However, your assumption that you, or any other customer, may hold a position in a deliverable contract until the close of trading on the last trading is not correct. . . . [Under paragraphs 5 and 7 of the customer agreement,] <u>Man had the right on June 11 to ask you to liquidate your short position, or to liquidate it without your consent, with or without notice to you.</u>
>
> <u>If a futures contract has no associated physical delivery, and is simply cash-settled upon expiration of the contract, then there is generally no problem with allowing a customer to hold the contract until the last trading day, or expiration, so long as the customer's account is adequately</u>

[7] Both sides dispute whether Powell had sufficient margin to cover two short September DX positions. However, neither side has produced conclusive evidence in support of their assertions on the margin issue.

> margined. The US Dollar Index contract was a cash-settled contract until the March 2001 contract. [However, from] March 2001 on, the Dollar Index became a physical delivery contract. The attached Notice to Clearing Members from the exchange dated May 31, 2001 informs all clearing brokers that customers who wish to hold their positions in the Dollar Index beyond June 11 must provide the exchange with delivery instructions by 9:00 a.m. Chicago time. Since you were not intending to make delivery on the contract, you could not provide the information required by the exchange and Paragraph 7 of the Agreement. Therefore, you had to exit your June position by the close of trading that day. . . .
>
> You had ample opportunity to replace your short June position with a short September position and refused to do so for your own reasons. There are no "rules" limiting a broker's right, exercising its business judgment in its sole discretion, to liquidate a customer's position under these circumstances. Furthermore, to maintain an action for damages against a broker, a customer must show that he or she took appropriate action to mitigate the alleged damages. You failed to do so.

[Italics in original; underlining added for emphasis.]

Set out below, are pertinent portions of the general counsel's letter, dated July 24, 2001, reiterating Man Financial's position that it had absolute discretion to force the liquidation. As can be seen, Man Financial asserted that Powell could have "avoided this problem" by tendering delivery instructions and depositing the full amount of the contracts, despite the fact that Man Financial's agents had not suggested that course of action to Powell, and despite the fact that Man Financial had no intention to permit Powell, or any other retail customer, to make or take delivery:

> I am in receipt of your letter dated July 23. Again, I think you are missing the point. Under the Customer Agreement (the "Agreement"), you had no right to remain in the June Dollar Index contract beyond the point where Man Financial Inc ("Man") asked you to liquidate or roll into the September contract. You agreed, when you opened your account, that Man had the absolute right to liquidate any open position in your account should it desire to do so for its own protection and [you agreed] to provide delivery instructions upon Man's request. Man opened an account for you in reliance on that Agreement.

> Man is not aware of what other futures brokers did with their customers holding June Dollar Index positions, nor does Man consider it relevant. For example, other futures brokers may have had customers making or taking delivery on the contract, and therefore had to provide the delivery information to the exchange anyway and thus decided to allow speculators to remain in the contract until expiration and accept the risk therefore. Other firms may be willing to accept such risks. Man was certainly under no obligation to do so.
>
> Man believes that under all circumstances, some of which you are not aware, Man had a duty to inform its customers holding positions in the June Dollar Index contract to roll into September or liquidate on June 11 if they were not intending to make or take delivery. . . . Man is confident that its actions were taken in good faith to comply with exchange requirements. However, as I pointed out to you in previous correspondence, this issue is irrelevant to your complaint, which is that Man acted improperly in requiring you to exit your June position on June 11. Man took the action it did in accordance with its rights under the Agreement and for its own (*not your*) protection. Your conviction that Man acted unreasonably is also *irrelevant*. The authority you granted to Man was to take such action *in its sole discretion* with or without notice to you. If you did not intend to give Man that right, you should not have entered into the Agreement. . . .
>
> Speculators who do not make or take delivery on a futures contract know that they may be asked or forced to liquidate open positions during the delivery month. *You* certainly knew because you agreed to Man's right to demand delivery instructions and to liquidate positions in your account. We believe that this is in the best interest of the futures markets as a whole, speculators included, since it helps minimize the possibility of delivery defaults, even if there are occasions when some individual speculators may object to the application of this principle to themselves. Obviously you could have avoided this entire problem simply by giving us notice of your intent to take delivery and depositing the full contract value in your account. . . .

[Italics in original.] The letter concluded by informing Powell that it had closed Powell's two accounts, "to avoid the possibility of other trade disputes in the future."

Conclusions

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, rather than the waivers implicit in certain provisions of standardized agreements between FCMs and their customers. Once an FCM opens an account for a customer, the Act imposes duties that relate to the control the FCM exercises over its customers' money and property as well as its superior access to material information. For example, Section 4d of the Act compels FCMs to treat and deal with a customer's money as belonging to the customer, and thus to follow customer instructions regarding their money and property. *Lee v. Lind-Waldock & Company*, [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 28,173 at 50,159-50,160 (CFTC 2000). Here, Powell's two accounts included cash and two open DX futures positions that he had initiated after Man Financial had decided to comply with the exchange's revised delivery procedures by requiring its customers to liquidate expiring DX contracts a week before the exchange's published last trading day. When Man Financial imposed a special *de facto* last trading day for its DX customers, Man Financial significantly shortened the time that Powell could speculate on daily changes in the value of the June DX. This new restriction on trading privileges, known only to Man Financial managers and exchange officials, was a patently material fact to a trader in Powell's position, and Man Financial had a duty to disclose this fact to Powell under Section 4b of the Act. *See Sudol v. Shearson Loeb Rhoades, Inc.*, [1984-1986 Transfer Binder] ¶ 22,748 (CFTC 1985).

The Commission also has long recognized that an FCM's duties under Section 4d of the Act may be conditioned in certain circumstances. For example, an FCM's duty to protect the financial position of its customers and its right to protect its own financial position will almost always supercede any duties it owes to a customer who defaults on a margin call. In such circumstances, the FCM may make a good faith judgment about the steps necessary to protect its interest and the interest of the other non-defaulting customers. Similarly, the Commission has held that an FCM may exercise its right to close an account of a litigious and unreliable customer, as long as the FCM provides the customer a fair opportunity to protect his financial interests. *Lee*, at 50,159. Here, Man Financial's business decision that it could not justify setting up the necessary banking relationships for the delivery of a basket of the seven DX currencies appeared to be reasonable. Similarly, Man Financial's determination to compel any customer holding a deliverable DX contract to liquidate, or to roll over, the position before the seven-day deadline for delivery instructions appeared to be a reasonable step to avoid any resulting conflicts with the exchange's revised delivery procedures.

However, Man Financial failed to take the practical steps necessary to assure that Powell received timely and meaningful notice of this significant restriction on trading privileges unique to customers of Man Financial. Man Financial had several opportunities to provide a timely explanation of the decision it made in late February 2001 to impose restrictions on its customers holding expiring DX contracts. For example, Man Financial could have included a written notice in Powells' monthly account statements, could have instructed its trading desk personnel to remind Powell of the new restrictions when he opened the DX positions, and at the very least could have provided Powell with more than a same-day or one-day notice. Man Financial's delay deprived Powell of meaningful disclosure during the days leading up to Man Financial's *de facto* last trading day. In these circumstances, Man Financial's delay in disclosing its new DX expiration procedure was reckless, and breached its duty under Section 4b to disclose material facts to Powell. This untimely disclosure also was a breach of Man Financial's duty under section 4d of the Act.

A rebuttable presumption exists that Powell relied on the missing information in making his decision to hold the DX contracts into mid-June. *Maloley v. R.J. O'Brien & Assoc., Inc.,* [1987-1990 Transfer Binder] ¶ 24,293 (CFCT 1988). Man Financial argues that Powell could first have learned from the NYBOT website that the DX had been changed to a deliverable contract and then should have learned from the forced liquidation in March that Man Financial "might" force an early liquidation in June. However, these arguments are not sufficiently compelling to overcome the presumption of reliance in light of the overall circumstances. First, Man Financial's general counsel effectively acknowledged in his first letter that DX traders may have become accustomed to the freedom to trade expiring cash-settled DX's up to the last trading date. Second, Man Financial had never clearly explained to Powell in March that it had instituted a new *de facto* last trading day for its customers holding expiring DX contracts. Third, Man Financial waited until after the June liquidation to advise Powell for the first time to plan in the future on liquidating any open expiring DX positions a week before the NYBOT's last trading day. And fourth, the NYBOT website, and the written materials provided by Man Financial, mentioned neither the NYCC's new seven day deadline for delivery instructions nor Man Financial's related new trading restriction, and otherwise indicated that the DX could be traded up to the NYBOT's last trading day. In addition, a finding of reliance is supported by the fact that on the day of the forced liquidation Powell had complained, "We don't have anything firm to base our decisions on anymore."

The proper measure of damages for a failure to disclose material information should restore Powell to where he would have been had he received timely notice of Man Financial's business decision to shorten the period that its customers could hold June DX futures contracts. Thus, Powell is entitled to an award of $4,080, based on the best interim price during the two weeks before Man Financial's *de facto* last trading day for its U.S. Dollar Index customers: 118.03 on May 30.

ORDER

Complainants have established that Respondent violated Sections 4b and 4d of the Act, and that these violations proximately caused $4,080 in damages. Accordingly, Man Financial, Incorporated is ORDERED to pay to the Millennium Trust Company and Precision Ratios, Incorporated reparations of $4,080, plus interest on that amount at 1.35% compounded annually from May 30, 2001, to the date of payment, plus $125 in costs for the filing fee.

Dated December 11, 2003.

Phil McGuire,
Judgment Officer