



U.S. COMMODITY FUTURES TRADING COMMISSION

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PROCEEDINGS

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OFFICE OF PROCEEDINGS

PROFITS PLUS, INCORPORATED,
Complainant,

v.

ROSENTHAL COLLINS GROUP, LP, and
STEPHEN FRANCIS FERGUSON,
Respondents.

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CFTC Docket No. 98-R44

INITIAL DECISION

Profits Plus alleges that Rosenthal Collins Group and its agents misrepresented its margin requirements and acted in bad faith when it force-liquidated NASDAQ100 index futures positions on November 17 and December 2, 1997.¹ Profits Plus seeks \$24,447 in damages.² Rosenthal Collins and Stephen F. Ferguson deny any violations. The findings and conclusions below are based on the parties' documentary submissions. All dates are in 1997.

¹ See pages 2-3 of factual description to complaint; page 1 of first addendum to complaint (filed December 29, 1997); page 1 of second addendum to complaint (filed January 26, 1998); Profit Plus' reply to respondent's interrogatory 11 (pages 7-8); and ¶¶15 and 23 of Pamela Harrington affidavit (filed September 14, 1998).

² See ¶¶ 22-23 of Harrington's affidavit; Profit Plus' reply to respondents' interrogatory 11; and addendum to complaint (filed December 29, 1997).

Factual Findings

1. Profits Plus, Incorporated is located in Ozark, Missouri and was organized "to purchase, sale and trade financial instruments." Pamela J. Harrington is the sole shareholder and corporate officer of President of Profits Plus, and was the only representative of Profits Plus to deal with respondents. On the account application, Harrington indicated that she had traded commodity futures for over a year with LFG, LLC. When she opened the Profits Plus account with Rosenthal Collins, Harrington owned and operated a tax-preparation and financial planning firm. [See Articles of Incorporation of Profits Plus, Incorporated (attachment to first addendum to complaint, filed December 29, 1998); account application (Exhibit 1 to RCG's answer); Profit Plus' reply to respondents' interrogatories 2, 4 and 5; and ¶1 of Harrington's affidavit (filed September 14, 1998).]

2. On October 28, 1997, Harrington completed various account-opening documents, including a Rosenthal Collins Group ("RCG") account application, and RCG customer contract, and an acknowledgment that she had received and understood the risk disclosure statement for futures and options. [Exhibit 1 to RCG's answer.]

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

Customer agrees to maintain such collateral and/or margin as [RCG] may from time to time, in [its] sole and absolute discretion, require and agree to pay immediately on demand any amount owing with respect to any of Customer's accounts. Margin requirements may be increased at RCG's sole and absolute discretion and may differ from those established by the exchange on which the

trade is executed. Margin requirements are subject to change without notice and will be enforced retroactively and prospectively. Customer 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 Customer fails to deposit sufficient funds . . . to satisfy variation margin, or whenever in [RCG's] sole and absolute discretion [RCG] consider[s] it necessary, [RCG] may without prior demand or notice, when and if [RCG] deem[s] appropriate . . . liquidate the positions in Customer's account.

[Exhibit to RCG's answer; see ¶3 of Harrington's affidavit.]

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 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 RCG's answer.]

Harrington also received an RCG speculative margin report, dated October 6, that set out the initial and maintenance margin requirements for various futures contracts traded on U.S. exchanges, and that featured the following prominent warning about fluctuations in margin requirements:

All margins are subject to change without notice. These figures are to be used only as a guide as the margin requirements can change on a daily basis. For exact figures please call your broker at [toll-free number.] Due to current volatile market conditions, certain margin requirements are subject to drastic change on a day-to-day basis.

[Exhibit B to complaint; see Profit Plus' reply to respondents' interrogatory 11 (pages 7-8)]

3. On October 31, Harrington wired \$10,000 to RCG. On November 4, Harrington began trading. By Friday, November 7, she had made three trades – two involving the December E-Mini S & P 500 index future ("S&P") contract, and one involving the December Nasdaq 100 index future ("NASDAQ") contract – which realized a total gross profit of about \$14,338. [See ¶¶ 5-6 of Harrington's affidavit; exhibits A1 to A5.2 to complaint; and ¶¶ 2 and 3 of RCG's answer.]

4. Also on Friday November 7, Harrington bought ten S&P contracts. At the close on November 7, these contracts had a liquidating value of \$2,150; and the account had a cash balance of \$20,464.

5. On Monday November 10, the Chicago Mercantile Exchange raised the margin requirements for the S&P and the NASDAQ contracts.³ [See ¶15 of Parks' affidavit (filed August 31, 1998); and margin reports dated October 6 and November 10, 1997 (exhibits B1 and B2 to complaint).]

On Wednesday November 12, Harrington bought two more S&P contracts. The S&P lost value, resulting in an open trade equity of debit \$10,195 for the twelve contracts, and triggering a \$10,225 margin call.⁴ Gregory Parks of RCG informed Harrington that the account was under-margined; and Harrington

³ Profits Plus has produced no evidence rebutting RCG's assertion that the CME raised the margin requirements for index products November 10.

⁴ RCG calculated the margin call by first determining the \$10,210.14 margin deficit, which was the difference between the \$19,945.86 total equity and the \$30,156 initial margin requirement, and then rounding-up to the next \$25, which was \$10,225. [See ¶¶ 1-2 of Park's affidavit.] Even if the CME had not increased margin requirements on November 10, the S&P position would have been under-

"immediately" wired \$9,700.⁵ [See ¶4 of Harrington's affidavit; exhibit A6 to complaint; and ¶4 of RCG's answer.]

6. On Thursday, November 13, Harrington liquidated the twelve S&P contracts for a \$6,875 gross loss. Harrington then sold five new S&P contracts, and sold two new NASDAQ contracts. The new NASDAQ position required an initial margin of \$15,970. At the close on November 13, the account value was \$17,087. [See ¶¶3 and 5 of Parks affidavit; ¶9 of Harrington's affidavit; and ¶4 of RCG's answer.]

7. On Friday, November 14, Harrington liquidated the five S&P contracts for a \$1,500 gross loss. At the close on November 14, the two NASDAQ contracts had an open trade equity of debit \$9,750, and the account value was \$11,787. As a result, the NASDAQ position was under-margined by about \$4,143. [See ¶¶4,5 and 6 of Parks affidavit; ¶10 of Harrington's affidavit; ¶5 of RCG's answer; exhibit A11 to complaint; and Profit Plus' reply to respondents' interrogatory 11.]

8. On Monday, November 17, at approximately 9:05 a.m. CST, Parks called Pam Harrington and informed her that the market margin deficit on the two Nasdaq contracts had increased and was likely to increase further, and that she should either wire another \$10,250 or liquidate one of the contracts.⁶ During the course of this

margined by \$4,230, triggering a margin call for \$4,250. [See margin report dated October 6, 1997 (exhibit B1 to complaint).]

⁵ Neither side has explained why Harrington wired this particular amount – \$525 less than the amount of the margin call – or whether Parks or Ferguson discussed the shortage with Harrington on November 12, 13 or 14. During the recorded conversation on November 17, Harrington expressed surprise and confusion when Parks informed her that RCG records showed that the November 12th margin call had not been satisfied as a result of the \$525 deficiency.

⁶ If the CME had not increased margin requirements on November 10, the NASDAQ position would have been adequately margined on Friday, November 14, but by the close on November 17 would

conversation, Parks instructed Harrington to wire the funds "before the close," "by the end of the day," and "sometime this afternoon." Harrington said she needed to consult with her partner before deciding whether to meet the margin call or to liquidate.

Harrington and Parks next spoke at approximately 2:40 p.m. CDT. Parks told Harrington that she had to wire the funds within twenty minutes. Harrington replied that she was on the way to her bank which was five miles away. A few minutes later, Harrington reported to Parks that her van had broken down before she could reach the bank. Parks then told her that he had to liquidate one of the contracts. When Harrington complained that Parks should give her more time, he replied that she must bear the consequences of her decision not to wire the funds until late in the day and that RCG would no longer allow her to carry an under-margined and deteriorating position. RCG then liquidated one Nasdaq contract for a loss of \$6,850. [See audiocassette of conversations (produced June 10, 1998); ¶¶6-11 of Parks' affidavit; ¶¶11-15 of Harrington's affidavit.]

9. The remaining NASDAQ contract was also under-margined. The margin deficit gradually diminished until November 29, when the equity run reported a margin surplus. [See equity runs for November 20, 21, 26 and 28, 1997 (exhibits to second addendum to complaint, filed January 26, 1997).] However, by the close on December 1, the market reversed, and the position was again under-margined.

have been under-margined by \$2,480, triggering a margin call for \$2,450. [See margin report dated October 6, 1997 (exhibit B1 to complaint).]

On the morning of December 2, Parks informed Harrington that she either had to meet a margin call for \$2,925, or liquidate the remaining NASDAQ contract.

Harrington told Parks that she had no intention of wiring additional funds. RCG then offset the remaining NASDAQ contract to meet the call, for a loss of \$6,800.

[See audiocassette of conversations; ¶¶12-15 of Parks' affidavit; ¶¶20-21 of

Harrington's affidavit; and ¶¶31-35 of RCG's answer.]

CONCLUSIONS

Profits Plus alleges that Parks and Ferguson "lied to [Harrington] on November 17 and December 2 about the margin required to hold positions and that in my account.⁷ Profits Plus also alleges that the message on the November 20 equity run that the CME had raised the margin requirements for Nasdaq 100 index constituted an "outrageous lie."⁸ According to Profits Plus: "But for these misrepresentations . . . , [Harrington] would have held onto the [NASDAQ] contracts . . . until they became profitable and offset them around 960.00 each, [which] would have yielded a profit of \$3,300."⁹ However, Profits Plus has failed to produce any evidence that the CME did not raise its margin on the relevant dates, or that Parks or Ferguson misrepresented Rosenthal-Collins margin requirements or

⁷Page 1 of first addendum to complaint.

⁸Page 1 of second addendum to complaint. Harrington also stated that she contacted another unidentified broker in Kansas City who informed her that the broker "was unable to locate any other [firm] charging this higher margin;" and also asked rhetorically: My thinking may be wrong, but shouldn't the margin deficit be the difference between the [maintenance] margin requirement and the trade equity. . . ?" [¶18 of Harrington's affidavit; and last paragraph on page 3 of complaint.] However, Profits Plus produced no reliable evidence showing that RCG's margin requirements were out of line with other firms or otherwise grossly unreasonable, and has produced no evidence that a margin calculation should be based on maintenance rather than initial margin.

⁹¶23 of Harrington's affidavit.

margin policy. The tape-recordings of the conversations on November 17 and December 2, 1997 establish that Rosenthal-Collins gave Harrington reasonable notice of the margin calls; that Harrington informed Rosenthal-Collins that she could not and would not, on November 17 and December 2, respectively, forward the funds as requested; and that Rosenthal-Collins acted reasonably and in good faith when it exercised its rights under the customer contract and properly liquidated the under-margined position. See *Roberts v. Ray A Friedman & Co.*, [1987-90 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶23,063 (CFTC 1986); and *Baker v. Edward D. Jones & Company*, [1982-84 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶21,167 (CFTC 1981). Finally, even if Profits Plus had shown bad faith liquidations, Profits Plus would not be entitled to damages because the basis for its damage calculation is merely a speculation with the benefit of hindsight that it would have held both NASDAQ positions for a maximum profit. See *Grist v. Shearson Lehman Brothers, Incorporated*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶24,962 (CFTC 1990).

ORDER

Profits Plus has failed to establish any violations by respondents.
Accordingly, the complaint is DISMISSED.

Dated September 28, 1998.


Philip V. McGuire,
Judgment Officer