

UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

Redwood Trust, Inc.,

Complainant,

v.

R. J. O'Brien & Associates, Inc.,

Respondent.

CFTC Docket No. 00-R040

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COMMODITY FUTURES TRADING COMMISSION

SUMMARY DISPOSITION

Appearances:

Paul E. Gaspari, Esq. on behalf of Redwood Trust, Inc.
Lloyd Kadish, Esq. on behalf of R. J. O'Brien, Inc.

Before: George H. Painter, Administrative Law Judge

Complainant Redwood Trust ("Complainant") filed a reparations claim on February 2, 2000, against its broker, Respondent R. J. O'Brien Associates, Inc. ("Respondent").

Complainant seeks to recover losses in the amount of \$164,874.00 caused by a trade for Eurodollar futures that was placed on October 21, 1999, by Respondent on behalf of Complainant. Complainant alleges that the trade was in fact unauthorized and transacted in violation of Commission Rule 166.2, 17 C.F.R. § 166.2. Complainant alleges that Respondent

acted negligently as Complainant's broker in initiating the trade, thereby violating Chicago Mercantile Exchange Rule 540, and that Respondent is liable for the losses from the trade. After concluding that no significant discrepancy exists between the parties' respective versions of the facts surrounding the October 21, 1999, trade, this Court elected¹ to decide this case pursuant to Reparations Rule 12.310(d)-(e), 17 C.F.R. § 12.310(d)-(e). The findings of fact set out below are based upon evidence submitted by the parties and placed in the evidentiary record.

FINDINGS OF FACT:

1. Respondent is a futures commission merchant ("FCM"), registered with the Commodity Futures Trading Commission ("Commission") since June 30, 1982, whose place of business is 555 W. Jackson Boulevard, Suite 700, Chicago, IL 60661.²
2. Complainant is a Maryland corporation whose place of business is 591 Redwood Highway, Suite 3100, Mill Valley, CA 94941.³
3. Andrew Sirkis ("Sirkis") was at all relevant times a Vice President of Redwood Trust and the person authorized to place commodity futures orders for Complainant.⁴
4. Rob Powell ("Powell") and Rich Goldblatt ("Goldblatt") are employees of Respondent. Powell is the person Sirkis normally dealt with in placing orders for Redwood.⁵

¹ See NOTICE AND ORDER dated June 26, 2000.

² Commission Records.

³ Reparations Complaint.

⁴ COMPLAINANT'S AMENDED REPARATIONS BRIEF (hereinafter titled "Amended Complaint") dated June 26, 2000, page 1.

⁵ Amended Complaint at 1-3.

5. At 9:34 a.m.⁶ on October 21, 1999, Sirkis contacted Respondent via telephone (hereinafter referred to as “the first telephone conversation”) to place a trade for ten Eurodollar futures on behalf of Complainant. Sirkis spoke with Goldblatt who informed Sirkis that Powell was currently unavailable. Sirkis nonetheless proceeded with placing the futures trade with Goldblatt. At 9:39 a.m., during the first telephone conversation, Goldblatt informed Sirkis that Powell had “just walked in” and asked Sirkis if he would prefer to deal with Powell, to which Sirkis replied that “it doesn’t make any difference.” Sirkis finished placing the trade with Goldblatt, and the first telephone conversation ended at 9:43 a.m.⁷
6. Sirkis initiated the first telephone conversation by stating that he was interested in “selling some Eurodollar futures.” During this conversation at 9:38 a.m., Sirkis again indicated that he was interested in being short. At 9:42 a.m., however, Sirkis asked Goldblatt what would be the “best way to put in an order,” to which Goldblatt responded, “an *up 4 bid*” (emphasis added). This language clearly indicated that Goldblatt was referring to a buy order. Sirkis’ reply to this suggestion was, “Ok, let’s try it there.”⁸
7. At 9:54 a.m. on October 21, 1999, Powell telephoned Sirkis (hereinafter referred to as “the second telephone conversation”) to orally confirm execution of the trade. This telephone conversation lasted approximately two minutes, during which Powell said, “You *paid up 4*” referring to the trade, to which Sirkis replied, “Good.” When Sirkis asked about the potential profitability of the trade, Powell said, “it is probably going higher, so I think you are going to make money.” These two comments made by Powell clearly indicate that Complainant was

⁶ All times herein are in accordance with Chicago time.

⁷ Amended Complaint, Exhibit C.

⁸ *Id.*

long. Sirkis voiced no objections and did not request clarification. It is concluded that Sirkis knowingly ordered a long position for Redwood, and that he intended to purchase Eurodollar futures for the Redwood account.⁹

8. At 10:05 a.m. on October 21, 1999, Respondent sent Complainant a Bloomberg e-mail that clearly read "REDWOOD BOUGHT," referring to the previously placed trades.¹⁰ Powell informed Sirkis during the second telephone conversation that Powell would be sending the e-mail, leaving Powell to believe that Sirkis would receive and review the e-mail.¹¹ Sirkis admits that he did in fact receive and review the e-mail, and he did not object to the fact that Complainant was long instead of short.¹²
9. Between 3:18 p.m. on October 21, 1999, and 10:35 p.m. on October 22, 1999, Respondent sent Complainant, via both e-mail and Expedite fax, several statements, including equity runs for October 21 and 22 and a duplicate written confirmation, that clearly indicated Complainant had purchased, not sold, ten Eurodollar futures. No employee of Complainant objected to any of these statements.¹³

⁹ *See Id.*

¹⁰ ANSWER AND AFFIRMATIVE DEFENSES OF R. J. O'BRIEN & ASSOCIATES, INC. dated March 23, 2000 (hereinafter "Answer"), Exhibit B.

¹¹ Amended Complaint, Exhibit C.

¹² Answer, Exhibit J.

¹³ Answer at 7.

10. Complainant did not object to the trade until the morning of October 25, 1999, when Sirkis telephoned Powell. Referring to the trade, Sirkis claimed that “those were sells, they all came in as buys.”¹⁴

11. After Sirkis objected to the trade on October 25, 1999, Respondent immediately offset Complainant’s long positions by selling 10 Eurodollar futures on behalf of Complainant.¹⁵

DISCUSSION

Complainant claims that the Eurodollar futures trade in question was unauthorized and placed in violation of Commission Rule 166.2, 17 C.F.R. § 166.2.¹⁶ Telephone transcripts submitted by both Respondent and Complainant show that Sirkis intended to place an order to trade Eurodollar futures.¹⁷ Goldblatt stated during the first telephone conversation that, given the prices and liquidity of Eurodollar futures at that time, the best way to proceed with placing a Eurodollar futures trade would be “an *up 4 bid*” (emphasis added). Even a novice commodity futures trader would understand that a “bid” indicates a futures purchase and an “offer” indicates a futures sale. Given the fact that Sirkis is a vice-president of Redwood Trust, and the officer authorized to place futures orders for Complainant, this Court concludes that he was suitable to

¹⁴ Amended Complaint, Exhibit C.

¹⁵ Amended Complaint at 6.

¹⁶ Commission Rule 166.2 states in part:

No futures commission merchant . . . may directly or indirectly effect a transaction in a commodity interest for the account of any customer unless before the transaction the customer . . . [s]pecifically authorized the futures commission merchant . . . to effect the transaction

17 C.F.R. § 166.2

¹⁷ See *supra* note 10; Answer, Exhibit H.

trade commodities on behalf of Redwood. In sum, he is not a novice. Despite some initial conflicting language in the first telephone conversation with Goldblatt, it is clear from that conversation that he authorized the purchase of Eurodollar futures. All doubt was removed during the confirmation telephone conversation with Powell, for in this conversation Sirkis was told in plain English that he had purchased Eurodollar futures. Sirkis' use of sophisticated trading language in the second telephone conversation (with Powell) further establishes that Sirkis understood the term "bid."¹⁸

Complainant claims that Respondent failed to "exercise due diligence" in its placing the trade in question, in violation of Chicago Mercantile Exchange Rule 540, and that Respondent should be held liable for losses caused by this allegedly negligent behavior.¹⁹ This argument fails because Respondent and its employees, Goldblatt and Powell, exercised due diligence in placing Complainant's order. Goldblatt advised Sirkis to place "an up 4 bid" on behalf of Complainant, to which Sirkis agreed. Goldblatt used the word "bid" continuously during this conversation (in referring to the bid price in a bid-ask spread), and Sirkis never requested clarification. Minutes after the trade was executed, Powell orally confirmed the purchase of Eurodollars for Complainant's account, and transmitted a Bloomberg e-mail description of the transaction. In fourteen-point print, the e-mail informed Complainant that it had "BOUGHT," not sold, Eurodollars. As noted in the findings, Sirkis admits that he reviewed the Bloomberg e-mail showing the purchase and made no objections to Respondent. The efforts of Respondent's agents establish that they acted with due diligence in placing the Eurodollar trade for Complainant.

¹⁸ Amended Complaint, Exhibit C.

¹⁹ Amended Complaint at 12.

Even if the trade in question had been placed erroneously or negligently by Respondent,²⁰ Complainant would be estopped from collecting damages due to Complainant's failure to object at its first reasonable opportunity. The Commission has insisted that a customer should not be liable for trades placed erroneously by the customer's broker.²¹ The Commission has also maintained that a customer has a duty to object to any erroneous trades at the customer's first reasonable opportunity.²² Complainant argues that its customer agreement with Respondent should establish what constitutes a reasonable time period in which to object.²³ Because the customer agreement states that written confirmations of all trades "shall be conclusive if not objected to . . . within five days" after their mailing, Complainant claims that Sirkis' objection on October 25 should absolve Complainant of any liability for losses incurred by the trades.

Complainant's argument is flawed. Nothing in the customer agreement provides that a customer may wait up to five days before accepting or rejecting a trade. Complainant argues that the agreement permits a customer to place an order, wait up to five days to watch the market, and then decide whether to accept or reject the transaction. Such an arrangement would force the

²⁰ This Court reiterates that the undisputed evidence strongly suggests that Sirkis intended to place an order to purchase Eurodollar futures; therefore, this Court is making that finding.

²¹ See *Sherwood v. Madda Trading Co.*, [1977-1980 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,728, 23,018 (CFTC Jan. 5, 1979) (maintaining customer's "absolute right not to incur liability for any trade not authorized by him").

²² See *Id.* at 23,021. The Commission's rationale for imposing this duty is founded upon the following reasoning:

By not complaining at the first reasonable opportunity, a customer, in effect, usurps the proper role of the persons ultimately responsible for the trade, the [FCM] and its officers and agents. Moreover, by failing to protest, the broker would undoubtedly presume the regularity of the unprotected transactions and knowingly forego potential opportunities to liquidate the positions.

Id.

²³ Amended Complaint at 9.

broker to bear any loss that may be incurred during this five day “waiting period.” Customer agreements, including the agreement in the case at bar, are not so foolishly worded. The language of the agreement provides that a transaction is conclusive unless objected to within five days after the transaction. In the case at bar, Respondent acted with reason and diligence in initiating the trade, and in immediately liquidating the position once Complainant’s protest was received. To hold Respondent liable for losses incurred in the time between the transaction and Complainant’s protest would be inequitable in light of Respondent’s diligence.

Complainant’s reliance on the customer agreement to shift liability to Respondent is also flawed because the Commission has not held that a customer may reject a trade if he objects within a reasonable time. Rather, it has held that to recover damages for an erroneous trade, a customer must object at the *first reasonable opportunity*.²⁴ Complainant was given several opportunities on October 21 to object to the trades placed by Respondent. In particular, Sirkis could have easily objected to the trades after the oral confirmation in the second telephone conversation or after receiving the Bloomberg e-mail, both of which occurred within minutes of the order being placed.

The Commission has maintained that if a customer “should have known of the state of his account, but did not as the result of his own negligence or intellectual acumen . . . [he] may be legally estopped from receiving any damages.”²⁵ Here, Sirkis received clear and repeated notices that Complainant was long instead of short.²⁶ Had Respondent inadvertently placed an

²⁴ See *supra* note 24.

²⁵ *Kessenich v. Rosenthal & Co.*, [1980-1982 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,181, 24,861 (CFTC Mar. 24, 1981).

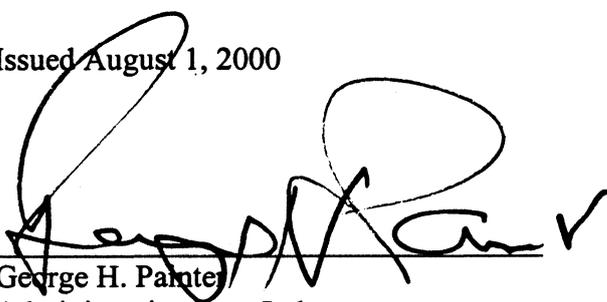
²⁶ Answer at 7. Complainant claims that Respondent “should have known that Sirkis was not authorized to confirm his own trades on behalf of [Complainant],” but Complainant makes no

erroneous order, Complainant would be estopped from collecting damages by reason of its failure to make a timely protest.

ORDER

Complainant has failed to establish by the weight of the evidence that Respondent violated the Commodity Exchange Act in the handling of Complainant's account. Accordingly, this matter is DISMISSED WITH PREJUDICE.

Issued August 1, 2000



George H. Parter
Administrative Law Judge

Legal Intern: C. L. McQuality

assertion that it ever actually articulated to Respondent that *none* of Complainant's employees could have confirmed the trade. Reparations Brief at 11.



U.S. COMMODITY FUTURES TRADING COMMISSION

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**OFFICE OF
PROCEEDINGS**

CERTIFIED RETURN REQUESTED

August 1, 2000

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Re: Redwood Trust, Inc. v. R. J. O'Brien & Associates, Inc.
CFTC Docket No. 00-R040

Dear Parties:

Enclosed is a copy of the decision in your reparations case. This decision will automatically become a Final Order of the Commission thirty-five (35) calendar days after the date of this letter unless a Notice of Appeal¹ and proof of service² is mailed by you or another party to the Commission within 20 days of the date of this letter.

The Right to Appeal

As provided in Commission Regulation 12.401, any party may appeal this decision to the Commission. To file an appeal, you must mail to the Office of Proceedings an original and one copy of both a Notice of Appeal and proof of service, along with the \$50 filing fee. Copies **must** also be provided to all other parties. The documents and the fee **must** be mailed to us within twenty (20) calendar days of the date of this letter.

¹The requirements for a Notice of Appeal are found in the CFTC Reparations Rules at 12.401.

² The requirements regarding proof of service can be found in the CFTC Reparations Rules at 12.10(2).

This 20-day reply deadline already includes a 5-day grace period (added to the 15 days provided in the CFTC Reparations Rules) to allow time for this to reach you through the mails. The CFTC Reparations Rules do not allow for additional delays. Therefore, in order for your appeal to be considered, you must mail your appeal documents and the filing fee to us within 20 calendar days of the date of this letter, regardless of when you actually received this letter. For your convenience, we have enclosed sample formats for the Notice of Appeal and proof of service.

Summary of the Appeal Process

If you choose to appeal, you must mail an original and one copy of your brief to the Office of Proceedings within thirty (30) calendar days of the date you mailed your Notice of Appeal. Copies must be provided to all other parties. If you do not file a brief, your appeal will not be considered and the initial decision will stand.

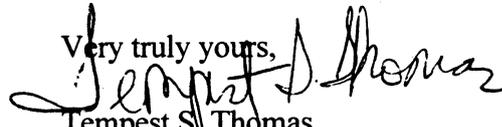
The other parties are allowed, but not required, to file an answering brief to your appeal brief. Any party who decides to file an answering brief must mail it to the Office of Proceedings and to all other parties within thirty-five (35) calendar days of the date indicated on the proof of service attached to the appeal brief. This 35-day answering deadline includes a 5-day grace period (added to the 30 days provided in the CFTC Reparations Rules) to allow time for appeal briefs to reach the other parties through the mails.

After briefs by all the parties have been filed, an appeal is ready for decision by the Commission. As a general rule, reparations appeals are decided on a "first in, first out" basis. The time required for deciding appeals varies from case to case and is largely dependent on the complexity of the issues presented. Most appeals are decided within six to nine months after briefs have been filed. When the Commission reaches a decision, all parties will be notified by the Office of Proceedings.

If There Is No Appeal

If there is no appeal and the decision becomes a Final Order and the respondent loses, the respondent has fifteen (15) calendar days, or such time as provided in the Order, whichever is longer, within which to make full payment of the reparation award. The respondent then has an additional fifteen (15) calendar days to mail to the Office of Proceedings documentary proof that the award has been satisfied. If the losing party is registered with the Commission and does not satisfy the reparation award within the required period, the registration of the losing party is automatically suspended from registration and the party is prohibited from trading in the contract markets until the award is satisfied. If the complainant wants to collect the award and the respondent refuses to pay, the winning party may request a certified decision package from the Office of Proceedings which must be taken to federal district court for enforcement of the award as provided by Section 14 (d) of the Commodity Exchange Act. The Commission does not have the authority to pursue the collection of the award.

For more detailed information concerning your appeal rights, you may consult Sections 12.10, 12.11, and 12.400 through 12.408 of the CFTC Reparations Rules.

Very truly yours,

Tempest S. Thomas
Proceedings Clerk

Enclosures