Commodity Futures Trading Commission
CEA CASES

NAME: VOLKART BROTHERS, INC., VOLKART BROTHERS COMPANY, ALFRED BOEDTKER, AND KURT MULLER

CITATION: 20 Agric. Dec. 306

DOCKET NUMBER: 82

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(No. 7097)

In re VOLKART BROTHERS, INC., VOLKART BROTHERS COMPANY, ALFRED BOEDTKER, AND KURT MULLER. CEA Docket No. 82. Decided April 17, 1961.

Manipulation of Prices of Cotton Futures -- Suspension of Registration -- Denial of Trading Privileges

Where evidence established (1) that futures prices rose in the last day of trading because of the fact that respondent corporation owned almost all the outstanding long interest on the New York Cotton Exchange and the New Orleans Cotton Exchange which interest was about twice as large as the stocks of certificated cotton and (2) that respondents intended to bring about such a price rise by their trading, it is held that respondents attempted to and did manipulate prices of cotton futures on both exchanges.

Review of Ruling of Referee Denying Motion to Dismiss -- Prima Facie Case

Referee properly denied motion to dismiss after presentation of complainant's case-in-chief since a prima facie case was made even as to the individuals who were respondents since they were the chief officers of the corporate respondent and were also partners in the futures commission firm through which the trading on the New York Cotton Exchange was done.

Mr. Benj. M. Holstein, for Commodity Exchange Authority. *Messrs. J. Donald Duncan and Irving L. Schanzer,* of Hooker, Alley & Duncan, New York, New York, and *Mr. Harry B. Kelleher,* of Lemle & Kelleher, New Orleans, Louisiana, for respondents. Intervenors: *Rein, Mound & Cotton,* of New York, New York, for New York Cotton Exchange; *Monroe & Lemann,* of New Orleans, Louisiana, for New Orleans Cotton Exchange;

and *Mr. John C. White,* of Washington, D. C., for American Cotton Shippers Association.

Decision by Thomas J. Flavin, Judicial Officer

PRELIMINARY STATEMENT

This is an administrative proceeding under the Commodity Exchange Act (7 U.S.C. Chapter 1), instituted by a complaint and notice of hearing issued under section 6(b) of the act (7 U.S.C. § 9) on April 24, 1958, by the Assistant Secretary of Agriculture.

Respondent Volkart Brothers, Inc., is a New York corporation engaged in the cotton merchandising business. Respondent Alfred Boedtker is president and respondent Kurt Muller is vice-president of the corporation. Each of the individual respondents is a partner in respondent Volkart Brothers Company, a registered futures commission merchant located in New York. This proceeding is

concerned with certain transactions in October 1957 cotton futures executed for the account of respondent Volkart Brothers, Inc., through the facilities of respondent Volkart Brothers Company, the carrying broker in New York, and through another carrying broker in New Orleans.

The complaint charges that the respondents attempted to and did manipulate prices of cotton futures. The complaint alleges that on October 15, 1957, the last day for trading in the October cotton future, respondent Volkart Brothers, Inc., held 104 long contracts n1 in such future (10,400 bales) on the New York Cotton Exchange, which represented 89 percent of the total open interest in the future on that exchange, and 17 long contracts (1700 bales) or 97 percent of the open interest on the New Orleans Exchange; that there was an insufficient supply of certificated n2 cotton available at the time to satisfy such contracts; that the respondents thereupon ordered and caused the futures which they held, less any deliveries received, to be sold at prices which were fixed and arbitrary, and in excess of the true market value of October futures and of spot cotton, thereby bringing about increases in the price of the future not justified by supply and demand; and that

the respondents acted for the purpose and with the intent of causing such increases in order to enable the respondent corporation to liquidate its futures at higher prices.

n1 One contract consists of 100 bales, each bale containing about 500 pounds of cotton.

n2 As is seen hereinafter, only cotton certificated as to grade, etc., by the Board of Cotton Examiners, United States Department of Agriculture, or cotton in the process of such certification, is eligible for delivery upon short futures contracts.

The complaint also alleges that in the course of such transactions and in furtherance of the manipulative purpose, the respondent corporation received approximately 5000 bales of certificated cotton on delivery against its long October futures position, of which it subsequently redelivered 3700 bales against a short December futures position. The complaint further alleges that the transactions in question were initiated and carried out under the direction and supervision of the individual respondents in their capacities as officers of and partners in the respondent firms.

The respondents filed a joint answer in which they admit the jurisdictional allegations of the complaint and the holdings and transactions in October futures as described therein, but they deny that they intended to or did in fact manipulate prices, or that the prices at which they sold their October futures were arbitrary or not justified by supply and demand, or in excess of the true market value of such futures or of spot cotton. The answer also denies that respondents Alfred Boedtker and Kurt Muller were responsible for the transactions in question.

As affirmative defenses, the respondents aver in the answer that the transactions referred to in the complaint were executed in conformity with the rules of the exchanges and of the Commodity Exchange Authority, and were lawful in all respects; that the long October futures which the respondent corporation held constituted hedges against forward sales commitments of the corporation; and that the corporation intended to take delivery of cotton in satisfaction of such futures and preferred such delivery but, at the specific request of the New York Cotton Exchange and in the interest of orderly liquidation, the corporation established liquidating price limits and sold its futures, less deliveries received, at the prices so established.

The answer further maintains that certificated cotton does not constitute the sole source of supply available to satisfy futures contracts, because the rules of both exchanges provide that a delivering party may, under certain

circumstances, tender a "Deliverer's Class" notice covering cotton which has not yet been classed and certificated by the Board of Cotton Examiners; that the delivery notices which the respondent

corporation received October 15, 1957, in the amount of 5100 bales, included "Deliverer's Class" notices with respect to 1192 bales; and that there were additional quantities of uncertificated cotton available in commercial channels on October 15 which could have been tendered under "Deliverer's Class" notices.

John J. Curry, Office of Hearing Examiners, United States Department of Agriculture, was assigned as referee and presided at the hearing. The respondents were represented by J. Donald Duncan and Irving L. Schanzer, of Hooker, Alley & Duncan, a New York law firm, and by Harry B. Kelleher of Lemle & Kelleher, a New Orleans law firm. Benjamin M. Holstein, Office of the General Counsel, United States Department of Agriculture, appeared as counsel for the complainant. On October 10, 1958, the referee granted leave to the New York Cotton Exchange, the New Orleans Cotton Exchange, and the American Cotton Shippers Association to file suggested findings of fact, conclusions, orders, and briefs in support of their positions in this matter, and at the hearing a brief on behalf of the New Orleans Cotton Exchange was received and made a part of the record.

The hearing began November 19, 1958, and after intervening recesses, was concluded February 5, 1959. Sessions of the hearing were held in New Orleans and New York. The respondent's motion to dismiss, made after the complainant had concluded the presentation of its evidence, was denied by the referee. Both sides offered oral and documentary evidence. Twenty-one witnesses testified and numerous exhibits were received on behalf of each side. Both sides thereafter submitted suggested findings of fact, conclusions, orders, and briefs in support thereof. Briefs were also filed by the American Cotton Shippers Association and the New York Cotton Exchange, Intervenors.

Much of the evidence is documentary. The complainant introduced exhibits in the form of tabulations showing the respondent corporation's trading and receipts of delivery in the October 1957 future during the last four weeks in the life of the future (Complainant's Exhibit 4); the positions in the October future of all clearing members on the New York Cotton Exchange during the same period (Complainant's Exhibit 45); the respondent corporation's sales of December futures and deliveries made against such sales (Complainant's Exhibits

6, 28); its position in futures and spot cotton as of October 11, 1957, with details concerning its inventory and commitments (Complainant's Exhibits 27, 50, 51-51G); bids for spot cotton which it submitted to the Commodity Credit Corporation October 14, 1957 (Complainant's Exhibits 24A, 24B, 29); and an analysis of its trading in the October 1957 future in relation to its cash position (Complainant's Exhibit 52).

Other exhibits introduced by the complainant showed the quantity of certificated stocks in existence near the close of trading in October 1957 (Complainant's Exhibit 16); the source and status of the cotton tendered by the shorts on deliverer's class notices in October 1957 (Complainant's Exhibits 17-23B); the prevailing market prices of October and December futures and of spot cotton in October 1957 and during the previous 10 years (Complainant's Exhibits 7, 11, 12-15, 25, 26); and the prices paid by other cotton merchants for spot cotton during September and October 1957 (Complainant's Exhibits 32-36, 82-82C).

Among the witnesses called by the complainant were six cotton merchants and brokers, who testified variously to the effect that the respondent corporation had a controlling long position in the October future on October 15, 1957, and that this fact was generally known to the trade (Tr. pp. 56, 81, 120, 133-34, 142-43); that this brought about a rise in the price of the October future on October 15 and caused the price to be out of line with prices of December

futures and spot cotton (Tr. pp. 56-57, 65, 68-69, 76-77, 101, 143); that as of October 15 there was not sufficient time remaining in which a short could get cotton classed for delivery and, in any event, no cotton merchant who had cotton for sale would sell such cotton for less than the price of the October future minus the cost of delivery (Tr. pp. 77-78, 85, 113-16, 128, 889-92); and that the situation on October 15 constituted a squeeze (Tr. pp. 59, 66-68, 81-83, 122).

Alex C. Caldwell, an employee of the Commodity Exchange Authority, testified that the respondent corporation's inventory figures showed that it had enough cotton on hand on October 15, 1957, to supply all its sales commitments for several months in advance (Tr. pp. 945-49). Mr. Caldwell analyzed the corporation's futures trading in October 1957 in relation to its spot position and concluded that its futures transactions were not

hedges and did not evidence use of the futures market in connection with merchandising operations (Complainant's Exhibit 52; Tr. pp. 949-50, 958-59, 962-68).

The respondents introduced numerous tabulations, charts, and other documents. These showed, among other things, the respondent corporation's position in the October 1957 cotton future from May 1956 forward, together with total open contracts and total certificated stocks (Respondents' Exhibits Series 1); the corporation's position in all futures during the last six months of 1957, together with certain aspects of its spot position (Respondents' Exhibits Series 7); prevailing prices of various futures and of spot cotton during the last four months of 1957 and in other periods (Respondents' Exhibits Series 3-5, Series 8); the cost of spot cotton purchased by the respondent corporation from mid-September through October 1957 (Respondents' Exhibits Series 6); the cost of similar purchases by other cotton merchants (Respondents' Exhibits 20, 22, 29); bids and prices paid by the respondent corporation and by other cotton merchants for cotton offered for sale by the Commodity Credit Corporation (Respondents' Exhibits Series 9, Series 11, Series 23-27; Respondents' Exhibit 28); stocks of cotton stored at the ports on specified dates in October 1957 (Respondents' Exhibits 12, 21); and estimates of production in 1957 compared with actual production in 1956 (Respondents' Exhibits Series 15).

C. W. Cooper, a data processing expert, was the principal witness for the respondents. Mr. Cooper prepared most of the tabulations and charts described above and explained their significance (Tr. pp. 268-350, 483-506, 603-96, 700-30, 865-78). In the course of such testimony, he concluded that the percentage increase in the respondent corporation's position in the October future was due not to purchases of futures by it but to liquidation by other traders (Tr. pp. 275-78). He also testified that such exhibits showed that prices of spot cotton were in a continuous rise over the two-year period May 1956 to May 1958, but that prices in October 1957 were an exception to this general trend (Tr. pp. 293-94, 297); that the spot price quotations rose suddenly on October 28, 1957, which indicated distortion on the low side in such quotations prior to October 28 (Tr. pp. 319-21, 676, 685-86); and that this distortion was also evidenced by the fact that the respondent corporation's buying prices for spot cotton in October 1957 exceeded the spot quotations (Tr. p. 684).

Trade witnesses called by the respondents testified variously to the effect that there was no squeeze on October 15, 1957, and that the October future was liquidated in an orderly fashion and without control (Tr. pp. 365-66, 380, 384-85, 403-04, 429, 538, 542, 586, 769-71, 776); that the price limits set by the respondent corporation with respect to its sales of futures on October 15 were reasonable, and that there was no distortion between such prices and the prices of spot cotton (Tr. pp. 366, 381, 384, 392-93, 429, 772, 776); that the spot price quotations in all 14 spot markets were too low (Tr. pp. 395, 431-33); and that the quantity of certificated stocks in existence on October 15, 1957, was not significant because there was free cotton available at the ports and in the

interior which could be delivered by the shorts under deliverer's class rules (Tr. pp. 366, 370-71, 539-41, 770, 774-76).

Respondent Muller testified that the transactions of the firm in the October 1957 future were part of a routine hedging operation against sales commitments of spot cotton; that there was no attempt to manipulate; that the selling price limits which he determined in connection with the sales of October futures on October 14 and 15 were based on what the firm was paying for spot cotton in the interior, and that these price limits were not arbitrary or unreasonable (Tr. pp. 817-29, 838).

Respondent Boedtker testified that he did not act for the purpose or with the intent of manipulating prices; that Volkart Brothers, Inc., was using the futures market as a hedging medium in these transactions; and that he approved of respondent Muller's decision concerning the price limits set by Muller in connection with the sales of October futures on October 14 and 15 (Tr. pp. 798, 802-03, 806-07).

The referee issued a report containing proposed findings of fact, proposed conclusions and a proposed order. In the report the referee recommended that respondents be found to have violated the act as charged in the complaint but he also proposed lesser sanctions than asked by complainant because the price disturbance was "not extreme" and because the short interests "during the period just prior to October 15 practically invited trouble by neglecting to cover their exposed position or by taking steps to have cotton certificated in time for delivery in satisfaction of their contracts." Respondents filed exceptions

to the report. The American Cotton Shippers Association and the New York Cotton Exchange also filed exceptions to the report. The complainant excepted to the referee's statement of reasons for recommending lesser sanctions than sought by complainant. Oral argument was held before the Judicial Officer August 4, 1960, in New York, New York, and following oral argument briefs were filed by the respondents and the intervenors.

In brief outline respondents contend that the evidence does not sustain charges of manipulation, that the trading activities complained of were carried out not for manipulative purposes but for legitimate reasons and that the prices at which the corporate respondent's futures contracts were liquidated were not artificial but normal and reasonable prices. The American Cotton Shippers Association generally supports the position of respondents. The New York Cotton Exchange, while also endorsing the position of respondents, goes further. The Exchange contends that it is permissible under the act, and not manipulation of prices, for a large long at the end of trading to exact a premium from shorts who have "overstayed the market" by not getting out of the market sooner or by not arranging to have deliverable supplies of cotton.

FINDINGS OF FACT

1. Respondent Volkart Brothers, Inc., is a New York corporation with offices and a place of business at 1539 Jackson Avenue, New Orleans 13, Louisiana. The corporation is now and has been at all times material herein engaged in the business of merchandising cotton and other commodities, and at all such times it enjoyed membership privileges on the New York Cotton Exchange and the New Orleans Cotton Exchange.

2. Respondent Volkart Brothers Company is a partnership with offices and a place of business at 120 Wall Street, New York 5, New York. The partnership is now and has been at all times material herein a registered futures commission merchant under the Commodity Exchange Act and a clearing member of the New York Cotton Exchange. At all such times the partnership enjoyed membership trading privileges on the New Orleans Cotton Exchange.

3. Respondents Volkart Brothers, Inc., and Volkart Brothers Company are affiliates of Volkart Brothers of Switzerland, not a respondent herein.

4. Alfred Boedtker is an individual residing at 139 East 39th Street, New York, New York. He is now and has been at all times material herein the president of Volkart Brothers, Inc., a partner in Volkart Brothers Company, a member of the New York Cotton Exchange, a member of the New Orleans Cotton Exchange, and a registered floor broker under the Commodity Exchange Act.

5. Respondent Kurt Muller is an individual residing at 5231 St. Charles Avenue, New Orleans, Louisiana. He is now and has been at all times material herein a vice-president of Volkart Brothers, Inc., a partner in Volkart Brothers Company, and a member of the New Orleans Cotton Exchange.

6. The New York Cotton Exchange and the New Orleans Cotton Exchange are now and have been at all times material herein duly designated contract markets under the Commodity Exchange Act.

7. A cotton futures contract is a contract made on or subject to the rules of the New York Cotton Exchange or the New Orleans Cotton Exchange, in which one party agrees to sell and deliver and the other party agrees to buy and receive a specified quantity of cotton at a specified price in a designated month. The trading unit in cotton futures is one contract, consisting of 50,000 pounds of cotton, plus or minus one percent, contained in about 100 bales of 500 pounds each, more or less. The parties determine the price, number of contracts and month of delivery. All other terms and conditions of the transaction are fixed by the rules of the exchange and are incorporated in every futures contract. When the proper deposits are made, the clearing organization of the exchange is substituted as buyer from the seller and seller to the buyer and each of the contracting parties is thereafter obligated only to the clearing organization. A cotton futures contract must be satisfied by (1) an opposite and offsetting transaction in the future prior to the expiration of trading in the future, or (2) the delivery of cotton by the seller and its receipt by the buyer during the delivery month and in conformity with the rules of the exchange.

8. Under the rules of the New York Cotton Exchange in effect during October 1957, a trader who had a short position which was open on the last trading day was required to instruct

his carrying broker or futures commission merchant (1) to make an offsetting purchase which would liquidate the trader's position, or (2) to issue a notice of intention to deliver against which the trader would deliver cotton. If no instructions were received from the trader, the futures commission merchant had to enter an order for the purchase of futures for execution prior to the termination of trading, which would liquidate the trader's short position.

9. October 15, 1957, was the last day for trading in the October 1957 cotton future on the New York Cotton Exchange and the New Orleans Cotton Exchange, and also the "last notice day," that is, the last day on which a notice of intention to deliver cotton could be issued. October 22, 1957, was the last day on which delivery of cotton on October futures could be made. Short contracts open after the end of trading on October 15, which were not satisfied by delivery on or before October 22, were in default.

10. The class or quality of cotton is determined by its grade and its staple or length of fiber. White cotton of the grade and staple known as "Middling inch" was the contract or basic grade and was deliverable at par on the October 1957 futures contract, that is, without any premium or discount. Other grades and staples were deliverable at premiums or discounts specified by the rules of the exchange.

11. The requirements and procedure for the delivery of cotton in satisfaction of the October 1957 cotton future on the New York Cotton Exchange were as follows:

(a) The cotton must be inspected by the Joint Cotton Inspection Bureau, an organization maintained jointly by the New York Cotton Exchange and the New Orleans Cotton Exchange.

(b) The cotton must be classed and certificated as to grade and staple by the Board of Cotton Examiners of the United States Department of Agriculture.

(c) The grade and staple must be one of the deliverable grades and staples specified by the rules of the Exchange.

(d) The cotton must be stored in a warehouse licensed

by the Exchange located at one of seven delivery points, namely, New York, New York, Charleston, South Carolina, Mobile, Alabama, New Orleans, Louisiana, Savannah, Georgia, Galveston or Houston, Texas.

(e) Five business days prior to the date of delivery, the carrying broker or clearing member must issue and tender to the clearing house a notice of intention to deliver, known as a transferable notice or T/N containing, among other things, information as to the quantity of cotton being delivered, its location, and the Government class, that is, the grade and staple of each bale as shown on the classification certificate of the Board of Cotton Examiners.

(f) Five days after issuance of the T/N, the delivering party must deliver to the receiving party all the delivery documents, including warehouse receipts. The warehouse receipts must show on their face the certification by the Board of Cotton Examiners as to the grade and staple of the cotton or, in lieu thereof, there must be attached to the warehouse receipt a "Validated Class Certificate" issued by the Board of Cotton Examiners as hereinafter described.

(g) A deliverer may issue a T/N on the last notice day which does not show the Government class. In lieu thereof, the deliverer may insert in the T/N the grade and staple of the cotton according to his own best knowledge, known as "Deliverer's Class." This may be done only if the Government class certificate has not yet been issued by the Board of Cotton Examiners but the cotton has been inspected and samples are in the custody of the Board, or the cotton can be inspected and samples delivered to the Board in readiness for classification not later than 8 p.m. on the second business day preceding the last delivery day. With respect to the October 1957 future, a delivering party who issued a T/N based on "Deliverer's Class" on Tuesday, October 15,

the last notice day, was required to have the cotton inspected and samples in the hands of the Board of Cotton Examiners not later than 8 p.m., Friday, October 18, 1957.

(h) If on the actual date of delivery the Board of Cotton Examiners has not yet issued a classification certificate, the delivering party may deliver to the receiver a "Validated Class Certificate," consisting of a written notice of the grade and staple according to the deliverer's best knowledge (Deliverer's Class), validated by endorsement by the Board of Cotton Examiners. Such validation by the Board of Cotton Examiners will issue only if the cotton has been inspected and samples are then in the possession of the Board of Cotton Examiners.

12. If cotton delivered under a Validated Class Certificate subsequently fails to meet deliverable grade and staple requirements upon classification by the Board of Cotton Examiners, the delivering party has no right of replacement and is in default.

13. On September 23, 1957, the day before the first notice day in the October 1957 cotton future, respondent Volkart Brothers, Inc., held a long position n3 of 19,700 bales in such future on the New York Cotton Exchange. Between September 24 and October 1, inclusive, respondent corporation sold October 1957 cotton futures and by October 1 had reduced its long position to 12,700 bales. Between October 1 and 11, inclusive, the respondent corporation received 300 bales on delivery but made no sales of October 1957 cotton futures. On October 14 respondent corporation sold 2000 bales of October 1957 cotton futures,

leaving it at the close of business that day with a long position of 10,400 bales in such future on the New York Cotton Exchange. During the above-described period, respondent corporation also traded in October 1957 cotton futures on the New Orleans Cotton Exchange. Between September 23 and October 10 it covered a short position of 1600 bales in the future on the New Orleans Cotton Exchange, and on the latter date it established a long position of 1700 bales, which position it held October 14, 1957.

n3 Unless otherwise stated, references to positions or open interest are as of the close of business on the date indicated.

14. Between October 1 and 14, 1957, inclusive, respondent Volkart Brothers, Inc., entered the following orders through respondent Volkart Brothers Company for the sale of October 1957 cotton futures on the New York Cotton Exchange, the orders to remain in effect until cancelled:

Date of Order	Number of Bales	Price n4
October 1	1000	34.97
October 10	1000	35.02
October 10	1000	35.07
October 10	1000	35.12
October 10	1000	35.17
October 14	1000	35.22
October 14	6400	35.27

n4 All price references are in cents per pound of cotton.

The first execution on the above orders took place October 14, on which date respondent Volkart Brothers Company sold 1000 bales at 34.97 and 1000 bales n5 at 35.02, in accordance with the orders of October 1 and 10, respectively. The remaining orders described above were not executed, but continued in effect until prior to the opening of trading October 15, when they were superseded by the order hereinafter described in Finding of Fact 16. Between October 1 and 14, other traders sold net 17,000 bales of October 1957 cotton futures on the New York Cotton Exchange.

n5 These are the 2000 bales sold October 14, referred to in Finding of Fact 13.

15. At the opening of trading October 15, 1957, the last day for trading in the October 1957 cotton future, the respondent corporation's long position of 10,400 bales in such future on the New York Cotton Exchange represented 89 percent of the open interest in the future on that exchange, and its long position of 1700 bales in such future on the New Orleans Cotton Exchange represented 97 percent of the open interest in the future on that exchange. The trade was aware of the fact that the respondent corporation held such position.

16. On October 15, 1957, prior to the opening of the trading session on the New York Cotton Exchange, respondent Volkart Brothers, Inc., ordered respondent Volkart Brothers Company to liquidate the corporation's long New York position of 10,400 bales in the October future by selling 2000 bales at 35.17 and selling the balance of 8400 bales, less such deliveries as might be received, at 35.27. This order superseded the three unexecuted orders of October 10 to sell at 35.07, 35.12 and

35.17, and the two unexecuted orders of October 14 to sell at 35.22 and 35.27, described in Finding of Fact 14. In accordance with these instructions, during the trading session of October 15, Volkart Brothers Company accepted delivery notices in the amount of 5000 bales and sold for the account of the respondent

corporation 2000 bales of October futures at 35.17 and 3400 bales of October futures at 35.27, liquidating the said respondent's New York position.

17. On October 15, 1957, prior to the opening of the trading session on the New Orleans Cotton Exchange, respondent Volkart Brothers, Inc., ordered its carrying broker in New Orleans to liquidate the respondent corporation's long New Orleans position of 1700 bales in the October future by sales at not less than 35.38, and to take delivery of any part of the position which could not be sold at this price or better. In accordance with these instructions, during the trading session on that day the respondent corporation's broker in New Orleans accepted delivery notices in the amount of 100 bales and sold 1600 bales of October futures for the account of the respondent corporation at prices ranging from 35.40 to 35.48, thereby liquidating the said respondent's New Orleans position.

18. The October 1957 futures transactions described above were managed and supervised by respondent Kurt Muller, and he initiated the orders of October 15 to sell at 35.17 and 35.27 in New York, and at not less than 35.38 in New Orleans. Respondent Muller informed respondent Alfred Boedtker on October 14 that such orders were being entered for execution on the following day, and respondent Boedtker agreed with the action being taken and transmitted the New York orders to the floor clerk of Volkart Brothers Company in New York.

19. The respondent corporation was the only receiver of cotton on the October 1957 future. On October 22, 1957, it took delivery of 5100 bales pursuant to the delivery notices which it had accepted October 15. Prior thereto, on October 4, it had taken delivery of 300 bales. This total of 5400 bales represented all the deliveries in the October 1957 cotton future on the New York and New Orleans Cotton Exchanges. During December 1957, the respondent corporation redelivered 3707 bales of the cotton against short positions in the December future on the New Orleans Cotton Exchange which it had theretofore established by sales of such futures (Complainant's Exhibits 6, 28; Tr. pp. 195-197).

20. As required by the provisions of the Cotton Futures Act (26 U.S.C. § 4863(a)(7)) and the rules of the New York and New Orleans Cotton Exchanges, the October 1957 cotton futures contract called for the delivery of certificated cotton stored in approved warehouses at designated locations. On Tuesday, October 15, 1957, there was in existence a total of 4963 bales of such cotton owned by persons other than the respondent corporation (Complainant's Exhibits 16, 27).

21. The notices of delivery which were issued October 15, 1957, in the aggregate of 5100 bales (Complainant's Exhibit 4; Findings of Fact 16, 17), included notices covering 1192 bales tendered as "Deliverer's Class." These notices were issued in varying quantities by six different delivering parties. In each instance the delivering party was a cotton merchant, and in each instance the cotton covered by such notice was owned by such merchant on or prior to October 14, 1957, and had either been certificated or was in the process of certification when the delivery notice was issued October 15 (Complainant's Exhibits 17-23B).

22. A trader who was short in the October 1957 cotton future October 15, 1957, and who did not have certificated cotton in his possession on that date, would not have sufficient time in which to locate and procure cotton and have it inspected and certificated by October 22, the last delivery day. If such trader issued a "Deliverer's Class" T/N October 15 and delivered a "Validated Class" certificate October 22, he would be in default with respect to any cotton covered by such certificate which failed to meet deliverable grade and staple requirements.

23. The price of a cotton future in the delivery month reflects the current spot price of Middling inch cotton, the contract or basic grade. The cost of delivering against the future is approximately 100 points, and under normal

market conditions the price of the future in the delivery month exceeds the spot price of Middling inch cotton by the cost of delivery (Complainant's Exhibits 2, 3; Tr. pp. 181-182, 543). On October 11, 1957, the closing price of the October future on the New York Exchange exceeded the Middling inch spot price n6 by 139 points, and on the New Orleans Exchange this

spread or differential was 120 points. On October 14 and 15, 1957, the following business days, these spreads widened because of the increases in the price of the future, and at the close of trading October 15, the last trading day, the spread was 192 points in New York and 213 points in New Orleans. These spreads were greater than any other October future spot cotton price spread which prevailed on the respective exchanges on the last trading day in the October future during the 11-year period from 1948 through 1958, and more than twice as great as the majority of such other spreads.

n6 Calculated as the average of the prevailing spot prices for Middling inch at the Gulf ports of New Orleans, Houston and Galveston, the three principal delivery points (Complainant's Exhibits 7, 8).

24. On October 11, 1957, the closing price of the October future on the New York Exchange exceeded the closing price of the December future by 56 points and in New Orleans this spread or differential was 39 points. At the expiration of the October future on October 15, owing principally to increases in the price of the October future on both exchanges, these spreads had widened to 92 points in New York and 112 points in New Orleans, and were greater than any other October-December futures price spreads which prevailed on the respective exchanges at the expiration of the October future during the 11-year period from 1948 through 1958.

25. Prevailing prices of spot cotton are published daily by the United States Department of Agriculture. These prices are based upon actual transactions in spot cotton, as ascertained and reported by Spot Cotton Quotation Committees which function under the supervision of the Secretary of Agriculture, pursuant to the provisions of the Cotton Futures Act (26 U.S.C. § 4851 *et seq.),* and the rules and regulations there under (7 CFR 27.93 *et seq.),* in each of 14 spot cotton markets designated by the Secretary of Agriculture. Included among these 14 markets are the Gulf ports of New Orleans, Houston and Galveston. These three markets are also the principal delivery points for cotton delivered on futures sold on the New York or New Orleans Cotton Exchanges. On each day between October 4 and 15, inclusive, the price of Middling inch spot cotton, determined as above described, remained unchanged at 33.25 in New Orleans and 33.40 in Houston and Galveston. In Memphis, Tennessee, which is also one of the 14 designated spot cotton markets but which is not a delivery point for futures, the price of Middling inch spot cotton remained unchanged at 33.50 during the entire month of October 1957.

26. During the last two weeks in September and throughout October 1957, Anderson, Clayton and Company, a large cotton merchandising firm, purchased 150,437 bales of cotton in the Memphis, New Orleans, and Houston territories, based upon maximum prices which it was offering to pay for Middling inch cotton delivered at those points. During the same period, the company had in effect maximum offering prices in the Galveston territory for Middling inch cotton delivered at Galveston. The company's offering prices in such territories, the spot quotation for Middling inch cotton at those points, and the differences between such offering prices and the spot quotations, for each business day in the above period, were as follows:

	MEMPHIS			NEW ORLEANS		
Date	Spot	Buying	Buying Price over (+) or under (-)	Spot	Buying	Buying Price over (+) or under (-)

(1957)	Quotation	Price	Spot Quotation	Quotation	Price	Spot Quotation
Sept.						
17	33.00	32.80	-20	33.20	33.10	-10
18	"	"	"	"	"	-10
19	"	"	"	33.15	"	-5
20	"	"	"	"	"	-5
23	"	"	"	"	"	-5
24	"	"	"	33.05	"	+5
25	"	"	"	33.00	"	+10
26	33.50	"	-70	33.10	"	
27	"	"	"	"	"	
30	"	"	"	"	"	
Oct.	33.50	32.80	-70	33.10	33.10	
1	"	"	"	"	"	
2	"	"	"	33.15	"	-5
3	"	"	"	33.25	"	-15
4	"	"	"	"	"	"
7	"	"	"	"	"	"
8	"	"	"	"	"	"
9	"	"	"	"	"	"
10	"	"	"	"	"	+25
11	"	33.20	-30	"	33.50	"
14	"	"	"	"	"	"
15	"	"	"	"	"	"
16	"	"	"	"	"	"
17	"	"	"	"	"	"
18	"	"	"	"	"	"
21	"	"	"	"	"	"
22	"	"	"	"	"	"

	MEMPHIS			NEW ORLEANS		
Date (1957)	Spot Quotation	Buying Price	Buying Price over (+) or under (-) Spot Quotation	Spot Quotation	Buying Price	Buying Price over (+) or under (-) Spot Quotation
23	33.50	33.20	-30	33.35	33.50	+15
24	"	"	"	"	"	"
25	"	"	"	33.60	"	-10
28	"	"	"	33.75	"	-25
29	"	"	"	"	"	"
30	"	"	"	"	"	"
31	"	"	"	"	"	"

	HOUSTON			GALVESTON		
Date (1957)	Spot Quotation	Buying Price	Buying Price over (+) or under (-) Spot Quotation	Spot Quotation	Buying Price	Buying Price over (+) or under (-) Spot Quotation
Sept.						
17	33.00	33.10	+10	33.00	33.10	+10
18	"	"	"	"	"	"
19	32.75	"	+35	"	"	"
20	33.00	"	+10	32.85	"	+25
23	"	"	"	32.90	"	+20
24	"	"	"	32.95	"	+15
25	"	"	"	33.00	"	+10
26	33.25	"	-15	"	"	+10
27	33.50	"	-40	33.20	"	-10
30	33.40	"	-30	33.30	"	-20

Date (1957)	MEMPHIS Spot Quotation	Buying Price	Buying Price over (+) or under (-) Spot Quotation	NEW ORLEANS Spot Quotation	Buying Price	Buying Price over (+) or under (-) Spot Quotation
Oct.						
1	33.50	33.10	-40	33.25	33.10	-15
2	"	"	"	33.30	"	-20
3	33.40	"	-30	33.40	"	-30
4	"	"	"	"	"	"
7	"	"	"	"	"	"
8	"	"	"	"	"	"
9	"	"	"	"	"	"
10	"	"	"	"	"	"
11	"	33.25	-15	"	33.25	-15
14	"	"	"	"	"	"
15	"	"	"	"	"	"
16	33.50	"	-25	33.50	"	-25
17	"	"	"	"	"	"
18	"	"	"	"	"	"
21	"	"	"	"	"	"
22	"	"	"	"	"	"

Date (1957)	HOUSTON Spot Quotation	Buying Price	Buying Price over (+) or under (-) Spot Quotation	GALVESTON Spot Quotation	Buying Price	Buying Price over (+) or under (-) Spot Quotation
23	33.60	"	-35	33.65	"	-40
24	33.50	"	-25	33.60	"	-35
25	33.65	"	-40	33.75	"	-50
28	33.50	"	-25	"	"	"
29	33.65	"	-40	"	"	"
30	"	"	"	"	"	"
31	33.60	"	-35	33.65	"	-40

27. On October 14, 1957, respondent Volkart Brothers, Inc., submitted bids for 740 bales of cotton of various grades and staples located at Memphis, Tennessee, and offered for sale by the Commodity Credit Corporation for unrestricted use under its program NO-C-5. It was the purpose of the respondent corporation to use such cotton in its merchandising operations. The weighted average of the bid prices submitted by the respondent corporation, adjusted for differences in grade and staple, was 33.31 for Middling inch. The spot price quotation for Middling inch cotton at Memphis on October 14, 1957, was 33.50.

28. At the close of business October 10, 1957, respondent Volkart Brothers, Inc., had 31,235 bales of cotton in inventory or under purchase, earmarked for domestic use, as against domestic sales commitments through February 1958 in the amount of 30,900 bales. On the same date, the respondent corporation had a total inventory, including purchases, of 112,675 bales as against total sales commitments through October 1958 of 78,965 bales. On October 11, 1957, the respondent corporation's domestic inventory including purchases increased to 33,291 bales without any change in its domestic commitments, and its total inventory including purchases increased to 114,531 bales while its total commitments through October 1958 increased to 79,561 bales.

29. On October 14, 1957, respondent Volkart Brothers, Inc., further increased its total inventory including purchases by about 7700 bales, and its total commitments by 2000 bales. At the close of business on that day it had 41,000 bales of cotton in inventory or on purchase earmarked for domestic use, as against domestic sales commitments through April 1958 in

the amount of 39,900 bales, or an excess of domestic inventory over domestic requirements for the next six and a half months of 1100 bales. At the same time, its total inventory including purchases was 121,498 bales as against total sales commitments through October 1958 of 79,565 bales, or an excess of total inventory over total requirements for the next 11 1/2 months of 41,933 bales.

30. On October 15, 1957, respondent Volkart Brothers, Inc., received notices of delivery in the amount of 5100 bales as described in Findings of Fact 16 and 17, and made purchases of spot cotton in addition thereto. At the close of business on that day it had, exclusive of the cotton covered by such delivery notices, a domestic inventory of 44,269 bales as against domestic sales commitments through April 1958 of 39,900 bales, or an excess of domestic inventory over domestic requirements for the next six and a half months of 4369 bales, exclusive of cotton received on delivery. At the same time its total inventory, exclusive of such deliveries, was 124,748 bales as against total commitments through October 1958 of 65,919 bales, or an excess of total inventory over total requirements for the next 11 1/2 months of 58,829 bales. Out of the respondent corporation's total inventory of 124,748 bales of cotton on October 11, 1957, approximately 78,000 bales had not been classified as to grade and staple.

31. Respondent Volkart Brothers, Inc., continued to acquire spot cotton after October 15, 1957. At the close of business October 22, 1957, excluding deliveries which the respondent corporation had received on the October future, it had a domestic inventory of 61,904 bales as against domestic sales commitments through October 1958 of 54,306 bales, and a total inventory of 139,382 bales as against total commitments through October 1958 of 85,316 bales. The respondent corporation thus had, at the close of business October 22, 1957, an excess of inventory over requirements for approximately the next full year of 6598 bales on a domestic basis and 54,066 bales on an over-all basis, exclusive of the 5100 bales which it had received October 15, 1957.

32. At all times between October 10 and 15, 1957, inclusive, respondent Volkart Brothers, Inc., had on hand or under purchase, earmarked for domestic use, sufficient spot cotton to fulfill its domestic requirements at least four and a half

months in advance. At all times during this period respondent Volkart Brothers, Inc., had on hand or under purchase at least 34,000 bales of spot cotton in excess of the quantity needed to fulfill all existing requirements, export and domestic, for approximately one year in advance.

33. A purchaser who buys cotton from the Commodity Credit Corporation under its export program has an export obligation with respect to such cotton with the right of free substitution -- that is, the purchaser may sell such cotton in the domestic market provided he later exports an equal quantity of cotton of any grade or staple from domestic stocks. During October 1957, respondent Volkart Brothers, Inc., and other cotton merchants took advantage of this right of substitution by selling in the domestic market export cotton acquired from the Commodity Credit Corporation.

34. A fixed price purchase or fixed price sale is a purchase or sale of spot cotton in which the price has been agreed upon by the buyer and seller. A cotton merchant's fixed price position consists of his total inventory plus fixed price purchases of spot cotton minus fixed price sales of spot cotton. If the inventory plus such purchases exceeds such sales, the merchant has a long fixed price position, and if the reverse is true he has a short fixed price position. If a cotton merchant wishes to hedge, he trades in the futures market in an amount which is approximately equal in quantity but opposite in direction to the position he wishes to hedge.

35. The respondent corporation's trading in cotton futures during October 1957 did not constitute hedging. At all times between September 23 and October 8, 1957, it had a long fixed price position and also a long futures position. Such positions constituted speculation in spot cotton and futures. Between October 9 and 22, it had a short futures position against a portion of its long fixed price position, but its short futures position was at all times substantially less than its long fixed price position, and the changes in its short futures position varied erratically from changes in its long futures position and did not indicate a pattern characteristic of a hedging operation. The corporation's fixed price position, its futures position, and the daily net changes in each of such positions, for each business day within such period, were as follows (Complainant's Exhibit 52):

Date	Long Fixed Price	Net	Net Futures Position		Net Change	
1957	Position	Change	Long	Short	Long	Short
9-23	10,792		4,300			
9-24	11,173	+381	4,300			
9-25	8,094	-3,079	4,300			
9-26	8,795	+701	2,800		-1,500	
9-27	9,232	+437	1,000		-1,800	
9-30	10,600	+1,368	1,700		+700	
10-1	13,108	+2,508	2,200		+500	
10-2	15,451	+2,343	2,200			
10-3	15,755	+304	2,200			
10-4	14,067	-1,688	2,500		+300	
10-7	16,481	+2,414	2,500			
10-8	18,491	+2,010	100		-2,400	
10-9	20,894	+2,403		5,500		+5,500
10-10	22,635	+1,741		3,500		-2,000
10-11	24,691	+2,056		3,500		
10-14	31,999	+7,308		8,100		+4,600
10-15	40,369	+8,370		26,800		+18,700
10-16	41,389	+1,020		33,800		+7,000
10-17	41,251	-138		34,300		+500
10-18	43,917	+2,666		34,300		
10-21	51,927	+8,010		35,800		+1,500
10-22	54,798	+2,871		37,500		+1,700

36. The New York selling prices of 35.17 and 35.27, and the New Orleans selling price of 35.38 or better, set and obtained by respondent Volkart Brothers, Inc., on October 15 as the minimum prices for its October futures, did not reflect market conditions but were fixed and arbitrarily high, and out of line with prevailing prices of spot cotton. Such selling prices were also out of line with prevailing prices of December 1957 cotton futures. Respondent Volkart Brothers, Inc., was able to demand and receive the prices which it set October 15 because of its controlling long position in the October future and the limited supply of certificated cotton available on that day. This situation resulted in a "squeeze" in the October 1957 cotton future which was intentionally carried out by respondents.

37. Respondents, by their trading operations, described above, on the last few days of trading in the October 1957 cotton future on the New York Cotton Exchange and the New Orleans Cotton Exchange sought to raise October future prices on such exchanges.

CONCLUSIONS

I

The basic facts, or most of them, are not in dispute. It is conceded that the respondent corporation carried long positions in the October 1957 cotton future on the New York and New Orleans Cotton Exchanges into the last trading

day October 15, 1957, that at such time the corporation had 89 percent of the long contracts on the New York Cotton Exchange and had practically all the long contracts on the New Orleans Cotton Exchange, that it was the only long to receive deliveries on either exchange in the October 1957 future, that the corporation's long position was over twice the size of the supply of certificated cotton, that it fixed liquidating price limits for October 15, 1957, the last day of trading at which it sold out its contracts upon which deliveries were not made and that these liquidating prices were higher than the previous day's prices on the two exchanges.

Nevertheless there is a lengthy record consisting of both evidence and argument as to whether or not respondents manipulated October 1957 cotton futures prices. We proceed then to examine the issues in the light of the record with the preliminary observation, however, that there seems to be a good deal of material that is perhaps peripheral rather than central to the controlling issues.

It is not uncommon for futures prices on an exchange to advance toward the end of trading, particularly on the last day, not because of any change in supply or demand factors for the actual or spot commodity but solely because of the technical condition within the futures market itself of a shortage of readily available supplies for delivery by shorts who must then buy futures in order to get out of the market. Such a technical condition may or may not be manipulative in violation of the act, and is variously described as "congestion," "technical situation" or "squeeze." For example, Technical Bulletin No. 747 (January 1941), United States Department of Agriculture, *Grain Prices and the Futures Market,* has a summary on page 70 of the portion of the bulletin under the heading (p. 60) "The Delivery Problem." The summary is as follows:

"Futures contracts, as now drawn, give to every buyer the right to demand and to every seller the right to make fulfillment by actual delivery. This right or privilege is socially desirable so long as deliverable supplies prove adequate to meet maturing futures contracts. But from time to time in the past this balance between deliverable supplies and maturing contracts has not been maintained and forced movements of supplies and prices have resulted. The elements present in most of these cases of congestion are:

1. A small deliverable supply (relative to other years).

2. One or a few interests have large commitments open on the long side of the maturing future.

3. These leading longs make no indication of any kind that they are going to sell out their positions.

4. The short interests observe a steadily decreasing period of time in which to acquire supplies to fulfill their contracts.

5. To offset their commitments in the maturing future, the short interests may bid against one another in attempting to cover their positions.

6. As an alternative, the short interests may bid against one another for available supplies of cash grain in order to fulfill their sales by delivery.

"A setting of this kind may cause prices to advance materially but finally end with all contracts fulfilled either by offset or delivery, constituting a squeeze. Or the long interest or interests may stand for delivery, with the shorts unable to deliver in full, with still higher and more uncertain prices, constituting a corner. In either case the net effect is artificial spot and current futures prices causing harmful diversion of supplies, sales and shipments in the cash-grain trade with an equally harmful effect upon the speculative trade, encouraging reckless guesswork at the expense of intelligent forecasting."

Similarly, in one of the standard works on futures trading,

Hoffman, *Future Trading Upon Organized Commodity Markets in the United States* (Univ. Pa. 1932), Chapter XVI, entitled, "Deliverable Cash Supplies and Futures Prices," under the heading (p. 313), "3. Artificial Factors Causing Abnormal Conditions" the following appears (p. 315):

"The Threat of Taking Delivery. Having greater possibilities of success and much more common is the threat of taking delivery. Here the long interests attempt to profit at the expense of the 'shorts.' By continuing long up to and into the delivery month, speculative short sellers find it increasingly difficult to buy in their contracts. The short interest, it will be recalled, has the option of choosing the day during the delivery month when the actual commodity will be delivered. This option only serves to postpone the time when an ultimate settlement will have to be made. With the hope that prices will break or that the long interest will take the initiative and liquidate, they may carry along their position well into the delivery month with little thought of acquiring the necessary supplies. At the end of the month when delivery must be made supplies may be scarce and, in a frantic effort to close out their position, the current future advances rapidly. This process may or may not be accompanied by any manipulative intent but in any event it is an artificial situation producing a temporary derangement in prices."

See also *Report of the Federal Trade Commission on the Grain Trade,* Vol. VII (1926), p. 284; Baer and Saxon, *Commodity Exchanges and Futures Trading* (Harper, 1949), p. 83.

III

We shall first attempt to ascertain whether there was any "congestion" or "squeeze" on October 15, 1957, on the two exchanges, *prescinding at this stage of our deliberations from the issue as to whether the respondents intended to push futures prices upward by the corporation's trading.*

The closing prices of the October 1957 cotton future on October 14, 1957, on the New York Cotton Exchange were *34.91* bid and *35.03* asked and on the New Orleans Cotton

Exchange the closing price was *34.60* bid. The closing prices *at the end of trading in the future on October 15, 1957, were 35.27 in New York and 35.48 in New Orleans.* October 1957 futures prices in October 1957 (October 1-14) had ranged in price on the New York exchange from a low of 34.25 October 1 to a high of 34.87 October 9 and 10, and on the New Orleans exchange from a low of 34.27 October 1 to a high of 34.70 October 11.

It is seen that October futures prices rose October 15, 1957, on both exchanges to levels higher than prices prevailing on October 14, 1957, and prior thereto in the month of October. Why did this happen? The answer is inescapable. A concentrated long position -- more than twice the size of the certificated cotton -- stood for delivery or for its liquidating price limits which were higher than previously existing prices.

At the opening of the trading session October 15, 1957, the total open interest on both exchanges was 13,400 bales, *i.e.,* there were unliquidated futures in that amount held by shorts against the same quantity held by longs. On the long side Volkart had 12,100 bales and other longs had 1300 bales. On the short side the 13,400 bales had to be covered before the end of trading October 15, 1957, by the purchase of futures or the delivery of certificated cotton or cotton which was in the process of certification. There were only about 5000 bales of certificated cotton owned by persons other than Volkart. Consequently there were available, without recourse to Volkart, only about 5000 bales of certificated cotton and 1300 bales of long contracts to meet the demand

by the shorts of 13,400 bales. The remaining demand of 7100 bales had to be met out of Volkart's supply of long contracts and out of whatever cotton was in the process of certification.

Respondents, several of their witnesses and the intervenors point to the large stocks of uncertificated cotton in existence October 15, 1957, and seem to take the position that the mere existence of these stocks is proof that there was no artificiality in October cotton futures prices on October 15, 1957, on the New York and New Orleans exchanges. The existence of these large stocks does not negate artificiality in October 15 cotton futures prices. The evidence amply demonstrates that uncertificated cotton was not *readily available* to the shorts, particularly non-merchant shorts, on the last day of trading. Every

delivery by means of a deliverer's class certificate on the October 1957 future on both exchanges was by a merchant short who had possession of the cotton on or prior to October 14, 1957 (Finding of Fact 21). There was no practicable alternative for a short on October 15, 1957, who did not have cotton, but to pay the price to get out. This meant for most shorts who did not have cotton to deliver not less than the price fixed by the concentrated controlling long interest with the consequence that prices advanced. That this was the situation on October 15, 1957, on both exchanges seems to be self-evident n7 but in any event is amply demonstrated by the evidence. See the testimony of witnesses Lawrence E. Richmond (Tr. pp. 6-48), Charles Layton Merrill, Jr. (Tr. pp. 119-28), Charles Layton Merrill, Sr. (Tr. p. 143), Dan T. Manget (Tr. pp. 73-119), and James Eblen (Tr. pp. 887-92). The testimony of Edward Modet (Tr. pp. 5-49) and Eli Watson Tullis (Tr. pp. 129-39) who were brokers for the sale of some of the few outstanding long contracts on the New York Cotton Exchange not held by the corporate respondent is very illuminating. The orders were to sell for E. F. Hutton & Company's house account 400 bales of long futures at a point or two below Volkart's first selling order. Thus it is seen that professional traders recognized the obvious fact that a concentrated long would make or determine market prices for cotton futures on that day. Respondents' witness Kohlmeyer admitted that he had told investigators for complainant that Volkart had control of the market for October futures on October 15 and that October futures prices had thereby become artificially inflated (Tr. pp. 447-55). Too, respondents' witnesses connected with the New York Cotton Exchange who testified that there was no illegal squeeze or manipulation nevertheless asserted that whenever congestion threatens in the way of longs standing for delivery on the last day with apparently inadequate deliveries

to be made and the longs holding out for excessive prices the Exchange notifies cotton merchants and "prods" them into making a profit going short and delivering upon their short contracts. n8 If uncertificated cotton is readily available to *existing* non-merchant shorts on the last day of trading, and therefore there is no price-enhancing factor in a shortage of certificated cotton relative to outstanding long contracts, why would it be necessary to alert the cotton merchants who have cotton suitable for certification to come into the market at the last minute as *new* shorts?

n7 Cf. Garside (then Economist of the New York Cotton Exchange), **Cotton Goes To Market** (Stokes 1935), p. 269:

"When the current futures delivery on a futures exchange, that is to say, the maturing futures contract, advances substantially above the next future delivery, it is said that there is a squeeze in the current month.' Squeezes sometimes occur in tight supply situations, due to buyers of future deliveries holding them for premiums, or refusing to sell them at all and insisting on taking delivery of the cotton contracted for. * * * If the merchant is not in a position to deliver his hedged spot cotton on the futures contract, he must either bid up the price of the maturing future delivery to find someone who will sell an offsetting future delivery to him or he must go into a spot market and purchase other cotton for

delivery on the contract. **Such action raises the price of the current future delivery on the futures exchange** and of cotton for immediate delivery in spot markets. * * *" [Emphasis supplied.]

n8 See e.g., the testimony of Thomas F. Russell, Jr., chairman of the New York Cotton Exchange Control Committee, who testified that if Volkart's liquidating price limits had been a cent higher the Exchange would have gone to spot houses and asked them to sell four or five thousand bales and to deliver upon their short contracts (Tr. p. 599).

Respondents and intervenors defend cotton futures prices on the two exchanges on October 15, 1957, as not being artificially high. Considerable statistical data as to cotton futures prices over some months including periods subsequent to October 15, 1957, were introduced to support the defense that cotton futures prices had been distorted on the low side and that futures prices on October 15 were *natural* rises. The justification is advanced too that the official spot prices of the Spot Quotation Committees were too low and did not represent the actual market prices for Middling inch cotton.

We are concerned here with cotton futures prices on both exchanges on October 15, 1957, and the reason for the price advances on that day. By a wide margin respondents' evidence fails to establish any reason for the advance other than a concentrated long interest -- twice the size of certificated stocks -- holding out for delivery or for its liquidating price limits. Respondents and intervenors attack the official spot price quotations as being too low but cotton futures prices October 15, 1957, went up by virtue of the "congestion" or "squeeze" of a concentrated long interest standing for delivery or its liquidating price limits. The futures prices were therefore artificial as brought about by technical factors within the futures market itself and not by any supply or demand factors for cotton generally or by *free* trading opinion as to such factors. *This is true regardless of what spot cotton prices were.* Moreover, as is seen from our discussion below under heading IV on the issue as to whether prices were manipulated, respondents fail to impeach the announced spot prices of the Spot Quotation

Committees and respondents do not succeed in substituting higher prices as the true market prices for Middling inch cotton. The intimation by intervenor New York Cotton Exchange that supply and demand for *futures contracts* as distinguished from actual cotton should be considered legitimate price-making factors for futures prices is patently lacking in merit. Such a position would justify as valid corners, "squeezes" and all kinds of manipulation both up and down.

The artificiality of the October 15 futures prices is reflected in the spread between October futures prices and December futures prices on October 15 (Finding of Fact 24). On October 15 the *October future* advanced 30 points in New York and 88 points in New Orleans. The *December future* advanced five points in New York and six points in New Orleans. As a result of these advances, on October 15 the October future closed 92 points over the December future in New York and 112 points over the December future in New Orleans. These spreads were substantially in excess of the spreads between these two futures which had theretofore prevailed on the respective exchanges during that month, and greater than any similar spread at the close of the October future during the 11-year period 1948 through 1958.

Too, the price of a cotton future at maturity should reflect the price of Middling inch spot cotton, the contract grade, plus the cost of delivery which is about one cent or 100 points. Accordingly, the price of the October future at the termination of trading October 15, 1957, should have been approximately equal to the price of Middling inch spot cotton plus one cent. This was not the fact, however. The closing price of the future in New York was 192 points over the Middling inch spot price, and in New Orleans it was 213 points over the Middling inch spot price. These spreads were greater than any other which had theretofore prevailed during October 1957, and substantially in excess of

similar spreads at the close of the October future on either exchange during the 11-year period 1948 through 1958.

The movement of the prices of the October future and spot cotton is further evidence of artificiality in the price of the October future (Finding of Fact 25). The closing price of the October future on October 15 advanced approximately 30 points n9

in New York and 88 points in New Orleans without any movement in spot cotton prices. Spot quotations on that date remained stationary at 33.25 in New Orleans, 33.40 in Houston and Galveston, and 33.50 in Memphis, and had not changed since October 4 in New Orleans, October 3 in Houston and Galveston, and September 26 in Memphis.

n9 Calculated with reference to the midpoint (34.97). of the 34.91 bid and 35.03 asked at the close October 14 (Complainant's Exhibit 7).

IV

We shall consider next the question as to whether we should conclude that respondents intended to maintain and to employ Volkart's controlling long position for the purpose of influencing cotton futures prices upward on October 15, 1957, on both exchanges.

The size of the certificated stocks was of course public knowledge and yet Volkart's long contracts amounting to more than twice the size of the stocks of certificated cotton and constituting almost all the long position on the New York exchange and practically the entire position on the New Orleans exchange were carried into the last trading day. Obviously Volkart was in a commanding position and could set prices for its futures reflecting its monopoly. Respondents "estabished" liquidating prices October 15 above prevailing previous prices and these became the futures prices for the day on the New York Cotton Exchange and the floor for prices on the New Orleans Cotton Exchange.

Respondents contend that Volkart "originally" purchased the long contracts as hedges, that Volkart retained the long position because it desired cotton for merchandising purposes, n10 that the cheapest spot cotton available was by delivery upon the futures market, that it preferred delivery of spot cotton upon all its futures rather than liquidation by sales and that it established liquidating price limits October 15 at the suggestion of New York Cotton Exchange officials and at levels representing what it was paying for spot cotton.

n10 See p. 284, Vol. VII, Report of the Federal Trade Commission on the Grain Trade, **supra,** which says, "A large long interest may exist which has not been built up for manipulative or even speculative purposes, but as a hedge, and may be a hedge on which the buyer expects to take delivery to meet cash grain commitments."

By orders of October 1 and 10, 1957, 5000 bales of the corporate respondent's futures were offered for sale at a five-point scale-up per thousand bales ranging from 34.97 October 1 to

35.17 October 10. Offers of sales of futures ahead of market prices and by means of a scale-up in prices do not indicate use of long contracts for procurement purposes. Furthermore, Respondents' Exhibit 6-D showing the corporation's purchases of spot cotton over the period September 15 - October 29, reveals that practically all the cotton it bought was of a staple length longer than one inch and some of it was of a higher grade than Middling. The basis for the futures contract is Middling one-inch with deliveries permitted at 29/32 inch and with no premium for staple length exceeding 1-1/16 inches. The

respondent corporation deals in hundreds of thousands of bales of cotton annually and there were only 5000 bales of certificated cotton October 15. Too, Findings of Fact 28-32 reveal that Volkart had sufficient cotton to meet existing sales commitments. Respondents' explanation that Volkart held its October long contracts into October 15 for delivery of cotton because it was experiencing difficulty in getting the higher quality spot cotton it wanted and sought to get it through deliveries on its futures contracts is simply not credible.

Respondents urge too that Volkart sought merely to get for its futures the prices which it was paying for spot cotton and that futures prices were less than actual spot cotton prices at the time. They dismiss the official published prices of the Spot Quotation Committees as too low and invoke evidence submitted by them, or on behalf of them, in this proceeding as demonstrating that October 15, 1957, cotton futures prices were not excessive or manipulated in the light of the alleged prices paid for spot cotton.

Much of the evidence and much of the written and oral argument in the record deal with such matters as whether the corporate respondent was hedging and whether the corporation needed the cotton represented by its long contracts for merchandising purposes. Whatever the original purpose for the corporation's going long, we are concerned with respondents' activities in October 1957 futures in October 1957 and particularly at the end of trading in these futures. The corporate respondent was not engaged in so-called *bona fide* hedging under the act or in any discernible variation thereof incident to merchandising cotton (Findings of Fact 34 and 35). If this were not so, manipulative motive would not necessarily be ruled out. Even hedging may be used for manipulative purposes.

What respondents emphasize as the motivation for going

into the last day of trading with their dominant and controling large long position is the desire to obtain spot cotton for merchandising through deliveries by the shorts. This is repeated throughout the proceeding beginning with their answer to the complaint. They claim that they would have preferred delivery upon *all* the corporation's long contracts but established liquidating price limits on the last day at the suggestion of the New York Cotton Exchange n11 and they assert that these liquidating prices were set at what the corporation was paying for spot cotton.

n11 According to the testimony of Thomas F. Russell, Jr., chairman of the Control Committee, he was informed of the corporate respondent's liquidating price limits on October 14, 1957, and did not suggest or request that Volkart liquidate (Tr. pp. 582, 583, 594, 597, 598).

First of all we should observe that apparently no other cotton merchant believed that in the latter days of trading in the October future cotton futures prices were less than spot cotton prices plus the cost of delivery on the future. It is extremely unlikely that if such were the case other cotton merchants would not also have been long and stayed long on a sizeable scale. Volkart was practically the sole long on the last day. Respondents' Exhibit 6-D purporting to show Volkart's costs for cotton on a Middling inch basis is represented to have been made up from Volkart's buyers' reports and on the buyers' descriptions of grade and staple. But the original invoices to the producers or sellers were never made available to complainant for examination by the complainant and for the testing of the exhibit. Too, the conversion factors used in the exhibit were the differentials under Commodity Credit Corporation's cotton loan program, whereas the official Spot Quotation Committee differentials for staple lengths and grades above Middling inch actually used in the trade during the period were higher than Commodity Credit loan differentials (Complainant's Exhibit 42) which would result in lower prices paid by Volkart for its cotton purchases on a Middling inch basis than computed by respondents on their exhibit.

Testimony given by other merchants for respondents does not establish that they paid the prices for Middling inch cotton claimed for Volkart. These merchants testified as to computed average prices on a Middling inch basis but for the most part they bought grades and staples other than Middling inch, some on the buyer's appraisal, and they used their own differentials

to get from the grades and staples they purchased to a Middling inch basis. We are dealing here with not too wide a margin of futures prices over spot prices and, depending upon what conversion factors are used, several spot prices for Middling inch basis may be calculated. The official Spot Quotation Committee prices are not shown to be inaccurately low by respondents' evidence. Volkart's bid on October 14, 1957, for Commodity Credit Corporation cotton (Finding of Fact 27) was 33.31 for Middling inch as compared to the Memphis spot quotation of 33.50. Creekmore's bid for the same cotton said by respondents to have been 35.73 on a Middling inch basis turns out as 33.83 when adjusted to Middling inch cotton on the Spot Quotation Committee's differentials instead of the 35.73 computed on the New York Cotton Exchange contract differences. The basis buying sheets of Anderson, Clayton and Company (Finding of Fact 26) were generally below spot quotations and the respondents' characterization of these sheets as containing *minimum* prices and not buying guides or *maximum* prices is incorrect.

V

We have concluded that respondents intended to advance prices by means of Volkart's monopolistic control of the long interest which Volkart had October 15 and that this was accomplished, but not by a drastically large rise. The New York Cotton Exchange argues that because the price rise was not greater than it was the price was not manipulated. The reasoning in support of this proposition is that a controlling long interest cannot manipulate the price even though certificated stocks of cotton are short relative to the outstanding long contracts because if the long interest holds out for too high a price, cotton merchants will be alerted by the exchange to the profits to be made by going short on the last day and by delivering cotton upon their short contracts. Until the price gets up to this point, the so-called "bother" price, the long or longs have the right to exact a premium from the shorts who have "overstayed" the market by not previously selling out or arranging to have deliverable supplies.

It seems elementary and beyond controversy that the deliberate pressuring of futures prices upward by a "squeeze" technique resulting in artificial or fictitious prices intentionally

brought about constitutes manipulation of prices. n12 It is no answer to say that prices were not *substantially, unreasonably* or *excessively* raised. What we have to decide is not whether October 15 futures prices were excessive or unreasonable but whether they were manipulated. Small manipulations as well as large manipulations are prohibited by the act.

n12 Manipulation is, "any and every operation or transaction or practice * * * calculated to produce a price distortion of any kind in any market either in itself or in relation to other markets. If a firm is engaged in manipulation it will be found using devices by which the prices of contracts for some one month in some one market may be higher than they would be if only the forces of supply and demand were operative * * *. Any and every operation, transaction [or] device, employed to produce these abnormalities of price relationship in the futures markets, is manipulation." (Testimony of Arthur R. Marsh, former president of the New York Cotton Exchange, Cotton Prices. Hearings Before a Subcommittee of the Committee on Agriculture and Forestry, U. S. Senate, 70th Cong., 1st Sess., pp. 201-02.)

Respondents and intervenors argue too that in other court cases finding manipulated prices in violation of the act there was present control over deliverable stocks of the commodity or a substantial part of such stocks. They contend that respondents here had no ownership or control of the certificated cotton or cotton supplies generally and that, therefore, the respondents did not attempt to, and did not in fact, manipulate cotton futures prices. In view of the relative sizes of Volkart's long holdings and the certificated stock there was no need for respondents to control the certificated stock in order to accomplish their purpose. It is plain too that futures prices may be manipulated upward or downward or kept from going up or down by numerous and diverse methods n13 and if such prices may be intentionally raised artificially under some circumstances without the necessity of monopoly of the deliverable spot commodity or control over a substantial part of the deliverable supply, we know of no principle of law to the effect that the prices are not manipulated. n14 See, *e.g., Great Western Food Distributors, Inc.* v. *Brannan,* 201 F.2d 476, 478-79 (7th Cir. 1953), *cert. denied,* 345 U.S. 997 (1953).

n13 Respondents' witness W. K. Love, Jr., president of the New York Cotton Exchange, explained (Tr. p. 408): "I would say a squeeze can occur under two sets of circumstances: one where the long interest, whether it be one party or a number of parties holding same, is in excess of the available supply of cotton **that can be tendered on contract;** the other would be where the available supply of cotton is controlled by the long interest." [Emphasis supplied.]

n14 See Campbell, Trading In Futures Under The Commodity Exchange Act, 26 George Washington Law Review 215 (Jan. 1958).

VI

Respondents seek at this stage of the proceeding a review of the referee's ruling denying their motion to dismiss filed after the introduction of the complainant's case-in-chief. Complainant contends that respondents waived any review of the ruling by proceeding to put on their case, citing *court* decisions on *court* proceedings. Respondents claim that in this *administrative* proceeding they are now entitled to such a review and that such review shall be limited to the evidence before the referee when he made his ruling.

We have some doubt as to whether a respondent in an administrative proceeding of this kind is entitled as a matter of due process of law to a ruling upon the question as to whether the complainant makes out a *prima facie* case on its main presentation as distinguished from a ruling on the merits when the hearing record is closed. We have some doubt too as to whether respondents are also due a review of such ruling, after they put in their evidence, that is restricted to examination of complainant's case-in-chief. And it is a difficult task at the end of the proceeding for the deciding officer to close his eyes to some of the record and make a ruling limited to part of the record. But, at any rate, we agree with the referee that the complainant made out a *prima facie* case. Respondents stress an entire lack of evidence as to participation by the individual respondents but these respondents were president and vice-president, respectively, of the corporate respondent, as well as being partners in Volkart Bros., the partnership respondent, and these admitted facts were enough to deny the motion to dismiss as to them. Cf. *United States* v. *Dotterweich,* 320 U.S. 277 (1943).

Respondents and intervenors attack the series of physical acts by respondents cited in the complaint and in the evidence, such as the corporate respondent's staying long on such a relatively large scale into the last day, and maintain that each activity was legitimate in itself and should not be considered as an indication of, or as evidence of, manipulative intent. They insist that a long has a legal right to stand on his contract and demand delivery. Certainly he

has such right in general. But there are circumstances such as inadequate deliverable supplies relative to his long interest in which his standing for delivery to push prices up constitutes manipulation of prices in violation of the act. Actions otherwise licit may amount to manipulation when the manipulative motivation is present. Both individual respondents denied at the hearing that they intended

to "manipulate" prices. But it is not an essential ingredient of violation of the act in this respect that a respondent intend to commit what he knows to be a prohibited act. It is enough that he intends to do what he did. We have found and concluded on the evidence that respondents intended to move futures prices up by their activities and that this was accomplished. Intervenors see a grave threat to the continued existence of futures trading if we reach such a result, because, they say, no long can stand for delivery without the danger of being accused of manipulation, etc. What we hold here is reached upon a careful study of the evidence and the applicable law. Other facts or circumstances may or may not end in the same conclusions.

The referee proposed lesser sanctions than sought by complainant because (1) the futures prices were not drastically raised by the manipulation and (2) the shorts were somewhat to blame by not getting out or arranging to have deliverable cotton prior to October 15, 1957. Complainant excepts to the latter ground as erroneous and immaterial in the evaluation of appropriate sanctions. We share the view of complainant in this respect. Respondents and intervenors repeatedly urge that a short has either to deliver upon his short contracts or pay the price to get out. A short has the option to deliver or to liquidate by purchasing futures. But this does not mean that a long has the right to require shorts to pay manipulated prices in order to get out. While we disavow the referee's reference to the so-called negligence of the shorts, we conclude, upon all the facts and circumstances of the case, that the sanctions proposed by the referee be adopted.

All objections, exceptions, suggested findings, etc., inconsistent with this decision and order are overruled or denied. Of course since we decide that respondents manipulated futures prices it necessarily follows that respondents also attempted to manipulate such prices as also charged in the complaint.

ORDER

Effective May 22, 1961, the registration of Volkart Brothers Company as a futures commission merchant and the registration of Alfred Boedtker as a floor broker are suspended for a period of 15 days.

Effective May 22, 1961, all contract markets shall refuse all

trading privileges to Volkart Brothers, Inc., Volkart Brothers Company, Alfred Boedtker and Kurt Muller, for a period of 15 days, such refusal to apply to all trading done and positions held directly by any of the said persons or firms, and also to all trading done and positions held indirectly through persons owned or controlled by them, or any of them, or otherwise.

A copy of this decision and order shall be served on each of the respondents and on each contract market.

LOAD-DATE: June 8, 2008