Commodity Futures Trading Commission
CEA CASES

NAME: RAWLIN L. STOVALL AND STOVALL & STOVALL INC.

DOCKET NUMBER: 75-7; 206

DATE: MAY 6, 1977

DOCUMENT TYPE: INITIAL DECISION

NOTE: FORMERLY CEA DOCKET # 206; SUMMARY OF DOCUMENT IS AVAILABLE IN THE CCH COMMODITY FUTURES LAW REPORTER, P20, 420 [1977-1980 TRANSFER BINDER].

UNITED STATES OF AMERICA

BEFORE THE

COMMODITY FUTURES TRADING COMMISSION

In re Rawlin L. Stovall and Stovall & Stovall, Inc., Respondent

CFTC Docket No. 75-7

(Formerly Styled CEA Docket No. 206)

Initial Decision

Preliminary Statement

This is an administrative proceeding under the Commodity Exchange Act, as amended (7 U.S.C. § 1 et. seq., hereafter referred to as the "Act"), initiated by a complaint and notice of hearing filed on January 22, 1973, by the Assistant Secretary of Agriculture. n1

> n1 The Commodity Futures Trading Commission ("the CFTC") is an independent federal regulatory agency which began operation on April 21, 1975, pursuant to the Commodity Futures Trading Commission Act of 1974, Pub. L. 93-463, 88 Stat. 1389 (October 23, 1974). Prior to the 1974 amendments, the Commodity Exchange Act was administered by the Commodity Exchange Authority (the "CEA") of the Department of Agriculture. Futures trading was then regulated in certain specifically-enumerated agricultural commodities, which are the commodities involved in the instant case. The CFTC took jurisdiction of this matter from its predecessor, the CEA, under authority of Sections 411 and 412 of Pub. L. No. 93-463. (Tr. 219)

The complaint charged that on various dates during the period May to December 1972, Rawlin L. Stovall, under the appearance of trading in cash

commodities, solicited and accepted customers' orders for futures transactions without being registered as a futures commission merchant under the Act, in violation of Sections 4 and 4d(1) of the Act (7 U.S.C. §§ 6 and 6(d)(1)). The complaint also charged that Stovall bucketed his customers' orders and entered into fictitious transactions in violation of Sections 4b(D) and 4c(A) of the Act (7 U.S.C.§§ 6b(D) and 6c(A)) and Section 1.38 of the regulations promulgated pursuant to the Act (17 CFR § 1.38).

In addition, the complaint charged that Stovall failed to make his records available for inspection by the Department of Agriculture, in violation of Section 1.35(a) of the regulations promulgated pursuant to the Act (17 CFR §§ 1.35(a)). The corporation of Stovall & Stovall, Inc., of which Stovall was president, was charged with being unfit to engage as a futures commission merchant, as contemplated by Section 8a(3) of the Act (7 U.S.C. § 12a(3)).

Respondents filed an answer on February 7, 1973, which raised certain affirmative defenses, and admitted and denied the material allegations of the complaint. n2

n2 The pleadings were not amended by the parties. At one point in the proceedings respondents moved and were granted leave to amend the answer (Tr. 706-716), however the motion to amend was abandoned (Tr. 811-812).

On January 13, 14 and 15, 1975, the first session of the hearing in this matter was held in Chicago, Illinois. Richard W. Davis, Jr., Esq. appeared on behalf of the Complainant, and Robert P. Howington, Jr., Esq. and J. Gerard Bambrick, Jr., Esq. appeared on behalf of Respondents. On April 27, 1976 and September 20, 21, 22 and 23, 1976 further sessions of the hearing in this matter were held in Chicago, Illinois. Richard A. Levie, Esq. appeared on behalf of the Complainant and Gordon J. Arnett, Esq. appeared on behalf of Respondents. At the conclusion of the hearing the time was set for the filing of briefs. Thereafter oral argument was heard on April 19, 1977. n3 The transcript of hearing consists of 816 pages. During the course of the hearing Complainant called 10 witnesses and Respondent called two witnesses.

n3 Where cited "Tr.", "CX", "RX", "R.A." and "Or" refer, respectively, to the transcript of the hearing, complainant's exhibits, respondent's exhibits, respondent's answer to the complaint, and transcript of oral argument.

Findings of Fact

I. Identity of Parties

1. Rawlin L. Stovall (hereafter referred to as "Stovall"), is an individual, whose business address is 141 West Jackson Boulevard, Chicago, Illinois, with a residence address at 8315 S.W. 72nd Avenue, Miami, Florida. Stovall was at all times material herein n4 a floor broker registered under the Commodity Exchange Act, a member of the Chicago Board of Trade and a member of the Chicago Open Board of Trade(now known as the Mid-America Commodity Exchange). These Boards of Trade are now and were at all times material herein boards of trade and duly designated contract markets under the Act.

n4 The time period material to this case as alleged in the complaint was from May to December 1972.

2. At all times material herein, Stovall was doing business under the name R. L. Stovall, Sole Proprietor, Principal in Cash Commodities. Neither Stovall as an individual nor Stovall doing business under the name, R. L. Stovall, Sole Proprietor, Principal in Cash Commodities, was a futures commission merchant registered under the Act.

3. At all times material herein, Stovall was the president and principal stockholder of Stovall and Stovall, Inc., an Illinois corporation with its principal office and place of business at Room 2014, 141 West Jackson Boulevard, Chicago, Illinois 60604. The corporation was a registered futures commission merchant under the Act.

II. Respondent's Inquiry, Commencement of Investigation, and Refusal to Produce Records

4. Called as a witness by respondent, Clarence Hill, an auditor for complainant, testified that Stovall came to the offices of the CEA in April 1971 and asked if the Commodity Exchange Authority (CEA) "had jurisdiction over the cash grain operation per se." Hill read Stovall Section 4 of the Act and then took Stovall to see Don Smith, Hill's supervisor. Hill felt he lacked sufficient experience in the cash grain field to give Stovall an accurate

response to his inquiry. According to Hill's testimony, Stovall merely stated to Smith that he (Stovall) was going into the cash grain business and wanted to know what he had to do.

To the best of Hill's knowledge, Smith, after listening to Stovall, said "that he did not feel that the cash grain operation as stated was within his jurisdiction. . . ." The witness did not recall any other conversation at that meeting which elaborated on what Stovall meant by "cash grain operation".

5. Subsequently, on December 6, 1972, Daniel Vaccaro came to the CEA offices and spoke with G. Edward Piala, Deputy Director of the Central Region, regarding his trading with Rawlin L. Stovall. Vaccaro explained that he had traded with Stovall in cash commodities for approximately one year and had neither made nor taken delivery of any actual cash commodity. Vaccaro stated that he had no interest in any actual cash commodity or the making or taking of delivery of any actual cash commodity and indicated that his only interest was speculating in cash commodities. Believing Vaccaro's information was not indicative of cash commodity trading, Piala telephoned and then met with Stovall on the same date. At this meeting Stovall stated that his activities were "cash contracts for deferred delivery" and as such beyond the purview of the Commodity Exchange Act. Piala quoted portions of the Act to Stovall and requested Stovall to make available his books and records for examination.

6. Following Piala's meeting with Stovall on December 6, 1972, Henry Matecki, a CEA auditor-investigator, went to Stovall's office and received from Stovall copies of a customer agreement, trading authorization, management contract and statement of salesman presentation used by Stovall in his business (CX5). The "sales agreement" provided, inter alia, that the customer would deposit with Stovall such monies as Stovall might demand. The "trading authorization' gave the trading agent complete discretion to

make all trades for a customer and to buy or sell contracts on margin. The "management contract" noted the customer's desire to buy and sell "cash contracts for deferred delivery" and the customer's deposit of monies to open an account with Stovall.

7. Stovall having agreed on December 6 to provide records which would prove that his business did not come within the jurisdiction of the CEA, Matecki and another CEA auditor, William Pollack, later visited Stovall's office on December 8 to obtain such records. At the meeting Stovall produced copies of customer statements for two individuals, Rutherford and Gerber. The Rutherford file revealed that a delivery might have been made but Stovall was unable to produce warehouse receipts or similar documentation to substantiate delivery. Matecki requested the production of additional customer data to determine the number of customers who made or took delivery of any commodities but the additional data was not furnished.

During this December 8 meeting Stovall stated that he solicited and obtained accounts through referrals and advertising and was on the opposite side of all his customers' transactions. Stovall also told Matecki that he solicited money from customers.

8. After receiving a letter dated December 6, 1972 from Stovall indicating that he was no longer in the cash commodity business as of that date (CX2), Robert Clark, Director of the CEA Central Region, met with Stovall on December 14, 1972, orally requested access to Stovall's records, and handed Stovall a letter (CX3) making a similar request for records. On December 18, 1972, another letter by Clark requesting production of Stovall's books and records was delivered to Stovall (CX4).

9. On December 19, 1972 Stovall and his attorney, David Romoser, Esq., met with Piala and produced for Piala's inspection, purchase and sale statements

("P&S") of Stovall's personal futures trading accounts. These records were not material to Piala's inquiry and he so informed Stovall and his counsel. The following day Piala wrote a letter to Stovall and his attorney again seeking production of all books and records relating to Stovall's "cash commodities" business.

10. No records were produced by Stovall following the December 19 meeting. The books and records requested for production were considered essential by CEA personnel to determine whether Stovall's business was a true cash commodities business or in reality futures trading.

Stovall was informed of the statutory authority for requesting production of his "cash commodities" business records orally by Piala and in the letters sent Stovall by Piala and Clark.

11. The investigation by CEA personnel of approximately 25 to 30 of Stovall's customers revealed an absence of delivery of the cash commodities purportedly traded in Stovall's program, a lack of any interest in delivery of the actual commodity because the persons in the program were not in the business of merchandising the actual commodities, and a lack of intention to make or take delivery of the actual commodities. With the qualified exception of Mr. Rutherford (discussed more fully, findings 20 and 21 infra.) none of the records of Stovall's customers examined by CEA personnel showed the making or taking of delivery of any cash commodity. Prior to the filing of the complaint in this proceeding, Matecki did not have a list of all of Stovall's salesmen, or a list of all of Stovall's customers.

III. Promotion of Stovall's Program

12. Between May and December 1972 Stovall employed salesmen also known as "independent contractors" to solicit business and accounts from the public. After responding to an advertisement in the Wall Street Journal Douglas Newkirk became a salesman for Stovall. Newkirk then hired one of his friends, Vernon Henrichs to work for Stovall. Once affiliated with Stovall the salesmen were paid a commission for securing new business and customers. The salesmens' duties included talking with prospective customers, obtaining money from the prospective customers obstensibly to be used as deposits for trading in cash commodities for deferred delivery, and forwarding the money and customer agreements to Stovall.

13. To facilitate the acquisition of new customers Stovall provided his salesmen with written promotional materials for dissemination to prospective customers. A salient feature of the promotional materials and customer agreements was the repetition of the speculative nature of investing in Stovall's program. In his sales agreement (CX5) Stovall noted that the "client fully understands the high leverage speculative potential for profits and/or losses from the ownership of cash commodities." In a promotional brochure (CX8) it was stated that: "cash commodities by their

nature, can properly be called a speculative medium . . ." A similar representation regarding the speculative nature of cash commodities was found in yet another brochure (CX 51).

The promotional materials also listed the commodities in which Stovall claimed he traded, the amount of deposits required, the handling fees, and sample P&S statements (CX 53, 54, 55). In addition such materials stressed the existence of a trading plan, based on an analysis of a variety of factors, which offered high profit potential and the attraction of avoiding payment of taxes on profits for 2 years, because profits could not be withdrawn from the customers' account (CX 8, 51). Absent from these promotional materials and customer agreements was a clear explanation of Stovall's function as a principal or any

clear disclosure that Stovall was on the opposite side of the transactions into which the customers purportedly entered.

14. When Newkirk first contemplated employment as a salesman for Stovall they met in Chicago where Stovall took Newkirk onto the trading floor of the Chicago Board of Trade ("CBT") and spoke of selling accounts for investment or speculation in cash commodities. As a result of his conversations with Stovall, Newkirk believed that the cash commodities were traded by Stovall on the floor of the CBT. Moreover, as a result of his conversations with Stovall, Newkirk understood that Stovall managed the money on the CBT and controlled the trading.

Following commencement of his activities as a client of and salesman for Stovall, Newkirk solicited and obtained 12 customers for Stovall's operation. Most of the customers Newkirk obtained were personal friends, and he maintained close contact with these customers and their business conducted with Stovall.

15. Like Newkirk, Henrichs contracted prospective customers, explained the type of trading, and obtained a signed contract for Stovall with a check payable to Stovall. Henrichs obtained 7 customers, in addition to himself, for Stovall's operation.

16. In mid-1972 Stovall met with Henrichs, Newkirk and several present and prospective customers at Newkirk's home in Michigan. At that meeting Stovall stated that he would buy and sell contracts in cash commodities for deferred delivery in the name of the various clients, that he would be doing the trading, and that he would report to the clients the trades made and any resulting profit or loss. Stovall explained that at no time would the clients be expected to receive or make delivery of any of the commodities. He stated further that arrangements for delivery of a specific commodity could be arranged if the customer desired but that the normal operation of the business did not involve taking or making deliveries of the commodities.

IV. Delivery of Commodities n5

n5 See also: findings 26, 27, 28, infra.

17. Consistent with his understanding of the program as explained by Stovall, Newkirk never took or made delivery of any cash commodity nor was he engaged in a business requiring the use of any of the cash commodities purportedly traded by Stovall. Because most of the persons Newkirk obtained for Stovall's program were his personal friends with whom he maintained close contact, Newkirk testified that to the best of his knowledge none of these individuals ever took or made delivery of any cash commodity. Similarly none of the persons recruited by Newkirk had any need for the cash commodities purportedly traded by Stovall and none ever told Newkirk that they were interested in receiving delivery of any commodity.

18. Between May and December 1972, Newkirk received by mail copies of P&S statments sent by Stovall to the customers recruited by Newkirk. The P&S statements showed: transaction date, quantity bought or sold, shipment dates, grade and type of commodity, place of delivery, trade price, handling fees, opening and closing balances, and open positions on previous transactions.

These statements were used to confirm the purported execution of customer trades and to show open positions. Examination of the P&S statements (CX 15, 16) corroborates Newkirk's testimony that neither he nor the persons he recruited for Stovall's program made or took delivery of any cash commodity. All purchases were closed out by offsetting sales and any sales were terminated by offsetting purchases.

19. As with Newkirk, when Stovall executed a transaction for a customer recruited by Henrichs, Henrichs received a copy of the P&S statement for the transaction. Based upon the P&S statements sent by Stovall to the customers he recruited, Henrichs testified that there was no indication that any of these persons made or received delivery of any cash commodities. Further none of these persons ever informed Henrichs that they had made or received delivery of any cash commodities.

Henrichs stated that he had no use for any cash commodities or any desire to make or take delivery of the cash commodities in which he thought he was trading in Stovall's program. To Henrich's knowledge neither he nor any of the persons he recruited made or received payment for taking or making delivery of any cash commodities. The only payment made was the original deposit sent to Stovall. Examination of the P&S statements (CX 15, 16) corroborates Henrich's testimony that neither he nor the persons he recruited for Stovall's program made or took delivery of any cash commodity.

20. Donald Rutherford, called as a witness by respondents testified that in 1971 he was a farmer and commenced dealing in cash commodities with Stovall in 1970. Complainant's exhibits 18-48 were identified by Rutherford as P&S statements of cash commodity contracts for deferred delivery between himself and Stovall. To the best of Rutherford's knowledge CX 18-48 represented all confirmations and P&S statements received by him from Stovall.

21. Counsel for both parties stipulated that CX 18-48 were prepared by or under the control of Stovall, were sent through the mail, received by Rutherford, and that the contents of those exhibits were true, correct and accurate.

Using all of Rutherford's P&S statements of cash commodity transactions for deferred delivery with Stovall, Matecki computed the percentage of transactions which were settled by offset and those settled by delivery. Of the 18 total purchases made by Rutherford from Stovall, all the transactions were settled by offset (100%) and none settled by deliver); of the 22 total sales by Rutherford to Stovall 6 (27.3%) were settled by delivery and 16 (72.7%) were settled by offset. (CX 56 A&B)

V. Mechanics of Stovall's Trading

22. As a result of his conversations with Stovall, Newkirk understood that Stovall controlled all the trading in the program, and Stovall

was the only one authorized to trade for Newkirk. In addition, Newkirk did not know who was the opposite party in the trades in which Stovall purportedly engaged on Newkirk's behalf. Likewise Stovall told Henrichs that he (Stovall) would control the trading, and Henrichs never placed an order with Stovall or any person to buy or sell any cash commodities. Generally the customers did not know what trades were made for their accounts until they received their P&S statements.

The contracts and agreements signed by customers entering Stovall's program gave a trading agent authority to act on the customers' behalf in all transactions (CXS). One item of promotional literature (CX 51, P5) refers to Stovall acting as trading agent for the customer to "buy and sell orders". The management contract employed by Stovall specifically gave the "agent power and authority to place orders for the buying and selling of cash commodity contracts for deferred delivery for clients' account . . ." (CX 5, management contract, paragraph 2).

23. In approximately July 1972 Stovall approached Frank Hackbarth regarding the employment of Hackbarth as a trading agent for Stovall's customers. He told Hackbarth he wanted to interject a third person who would trade with Stovall on

behalf of Stovall's customers. Frank Hackbarth was a stockholder and president of International S.C.O.P.E.S.,

a company which provided Stovall with computer services. Upon receipt of source data from Stovall, such as customer and trade information, the company produced computerized P&S statements (CX 15, 16).

From the commencement of his duties as trading agent in July 1972 until September 1973, Hackbarth in his individual capacity received no compensation from Stovall for acting as trading agent. Hackbarth's company, International S.C.O.P.E.S., received compensation for producing the computerized P&S statements. At the time Hackbarth assumed his duties as trading agent he had had some prior experience trading futures contracts on the Chicago Open Board of Trade. With respect to cash commodities, Hackbarth's background consisted of only what he had received as a youngster back on the farm in Iowa.

24. In order for Hackbarth to function as trading agent Stovall or his salesmen obtained a signed trading authorization (CX5) from the customer and presented it to Hackbarth for his signature. Because of a physical disability which made signing the authorizations difficult, Hackbarth in August, 1972 gave Stovall's wife written "power of attorney" to sign his name to the trading authorization (CX 11). Although the document was dated January 15, 1972, Hackbarth testified

that he signed it in July or August 1972.

25. In his capacity as trading agent Hackbarth had no contact or consultation with the customers he represented prior to a trade and did not receive any compensation from the customers for his services as a trading agent. To initiate a trade, either Stovall or Hackbarth would call the other and propose a trade of a specific commodity at a specific price with a specified delivery month. The party receiving the proposition had the option of accepting or declining it.

Hackbarth traded, not for individual accounts, but rather for groups or sub-groups of customers composed of persons who commenced dealing with Stovall during specific time periods and through specific salesmen. The volume traded in any transaction was determined by specifying a volume or "quantity as so much per 'X' number of dollars in the customer's margin account." The individual customer would get a pro-rata portion of the total volume traded.

26. Based on data supplied by Stovall the International S.C.O.P.E.S. computer was programmed by Hackbarth to show specific delivery periods and specific delivery points, the latter being determined by the commodity involved. For example, the computer was programmed to show a trade of # 3 soybean oil as having a delivery point in Decatur, Illinois. Also based on

data from Stovall the computer was programmed to show delivery periods depending upon whether the initiating party proposed a sale or purchase of a commodity. Thus it was only necessary during "negotiations" between Hackbarth and Stovall for the initiating party to refer to a specific month such as July and the computer was programmed to show a specific delivery period.

Although Stovall supplied the source data or raw data for the printouts and the computer was programmed to show deliveries, Stovall never provided computer input to show actual deliveries of any commodities during the time period material to this proceeding.

27. In his capacity as trading agent Hackbarth never intended for his clients to make or take delivery of any cash commodity without the direct order of the client.

28. The typical transaction during July to December 1972, in which period Hackbarth engaged as trading agent with Stovall, was closed out by offsetting trades instead of delivery of the actual commodity. If the persons Hackbarth represented made money on a trade, Stovall, as the opposite party, lost money.

29. While Hackbarth functioned as trading agent, his company, International S.C.O.P.E.S., continued to print-out computerized P&S statements for Stovall and his program. The P&S statements were prepared on a weekly basis and left for Stovall to pick up. Once the P&S statements were picked up, Stovall, who operated from Chicago, mailed them to salesmen and customers such as Newkirk and Henrichs in Michigan.

VI. Characterization of Stovall's Operation as Dealings in Futures Contracts

A. Based Upon Investigation

30. Matecki testified that his investigation revealed that Stovall's contracts contained the elements of futures contracts, an agreement to buy or sell a specified commodity at a specified price at some future date. He also found that the contract had not been entered into for the purpose of merchandising the particular commodity and there was no actual delivery made of the commodity. Examination of the customer statements received from Stovall by Newkirk and Henrichs (CX 15, 16) showed Matecki that the transactions, containing terms similar to those of futures contracts, were probably futures transactions.

Matecki testified that the investigation disclosed that Stovall solicited or accepted orders for the purchase or sale of commodities for future deliver)' on or subject to the rules of the contract markets on which

these futures transactions should have been executed. However he found no evidence that these futures transactions had, in fact, been executed on any contract market.

A chart received by Newkirk from Stovall to show prospective customers (CX 55) was utilized by Matecki to compare aspects of Stovall's operation with normal futures trading. The comparison disclosed that 15 of the 24 commodities listed on Stovall's chart had contract sizes and handling fees identical to those traded on the corresponding contract markets (Tr. 755-760). The remaining 9 commodities listed, which Stovall purported to trade were not regulated in 1972 and thus not part of this proceeding.

B. Based Upon Expert Testimony

31. Russell F. McDonald, a Ph.D. in Agricultural Economics (Marketing), is employed as an economist with the Commodity Futures Trading Commission and qualified as an expert witness as an individual with "knowledge in agriculture and marketing sufficient to distinguish between futures trading and cash commodities."

Dr. McDonald testified about the distinguishing features and characteristics of cash commodity contracts and futures contracts; his testimony in this regard is best demonstrated by the following summary chart contained in complainant's proposed finding 76:

Characteristic	Cash Contracts	Futures Contracts
Mode of Settlement	Delivery of Actual Commodity (Tr. 289)	Usually by Offsetting Transactions (Tr. 289)
Intended Use	Obtain quantity of	Transfer risk of owner-

Characteristic	Cash Contracts	Futures Contracts
	actual commodity (Tr. 290, 320-321)	ship (Tr. 293, 320-321, 329)
Price	Negotiated between buyer and seller (Tr. 290)	Determined at public auction (Tr. 290)
Contracts Terms		
(a) Quantity	Negotiated between buyer and seller (Tr. 290)	Standardized by exchange contract (Tr. 290)
(b) Quality (grade)	Negotiated between buyer and seller (Tr. 291)	Standardized by exchange contract (Tr. 291)
(c) Delivery Points	Negotiated between buyer and seller (Tr. 291)	Standardized by exchange contract (Tr. 291)
(d) Delivery Period	Negotiated between buyer and seller (Tr. 291)	Standardized by exchange contract (Tr. 291)
(e) Delivery Date	Negotiated between buyer and seller (Tr. 291-292)	Standardized by exchange contract (Tr. 291-292)

32. Dr. McDonald examined the complaint in this action, Annex A to the complaint (CX 10, a summary of approximately 177 transactions in regulated commodities for 14 accounts from May to December 1972) and the transcript of the hearing in this proceeding held in January 1975. n6 As a result of examining these documents, Dr. McDonald was of the opinion that the operation of Stovall paralleled and was identifiable with "the type of activities one would expect to see if one were involved in the futures market". In elaborating on his opinion, Dr. McDonald testified that the quantities bought and sold in Stovall's operation paralleled quantities that were typical of futures contracts and that the characteristic manner of settlement in futures contracts is by offset. He also relied on the fact that the customers who testified in January 1975 stated that they did not intend to take delivery (Tr. 296-300).

n6 The hearing in January 1975 included the testimony of Newkirk and Henrichs concerning their accounts and those of their customers, plus the testimony of CEA personnel regarding statements made to them by Stovall and other Stovall customers.

In delineating some qualities of a cash contract Dr. McDonald said that "the bulk of the cash contract between buyer and seller usually results in the buyer taking delivery of the actual" (Tr. 301). In emphasizing this point Dr. McDonald later stated that seldom in a cash commodity transaction "do we find the buyer not wanting a commodity after the purchase" (Tr. 321).

33. As a result of examining the documents noted above (Complaint, CX 10, and January 1975 transcript), Dr. McDonald stated that Stovall's transactions represented in Annex A (CX 10), if executed, could have been used for: hedging transactions in interstate commerce in the commodities or by products of the commodities set forth in Annex A, determining the price bases of transactions in interstate commerce in those commodities and delivering such commodities sold, shipped or received in interstate commerce for the fulfillment thereof.

34. Michael Maduff, the managing partner of Maduff & Sons, a firm actively engaged in futures and cash transactions, testified about his experience in futures contracts and cash commodities and was qualified as an expert in futures contracts and cash commodities.

Given a hypothetical question which assumed that: (a) the information in Annex A (CX 10) was representative of transactions that occured between two principals, (b) the customers specified in Annex A were not in a business requiring the use of the commodities listed as bought, and sold in Annex A, (c) the customers specified in Annex A signed a contract stating an intention to make or take delivery but that there was testimony to the effect that there was no intention in fact by these customers to make or take delivery, (d) no deliveries of the commodities were made and (e) the

customers listed in Annex A placed an initial deposit with Stovall, Maduff testified that the factual situation presented had "far more characteristics of a futures transaction than of a cash transaction" (Tr. 389-390, 392-393).

In explaining his opinion Maduff noted that all of the transactions represented in Annex A were settled by offsetting or opposing transactions on the same day or within a few days of the initial transaction. To Maduff this was significant because in the cash market an offset without delivery would be extremely rare requiring "special circumstances", and "for such unusual circumstances to occur would require a much greater length of time than is indicated by (Annex A) . . ." (Tr. 393-394). Although he acknowledged a dim recollection of specific transactions in 1972, according to Maduff's "recollection of the general methods and business of cash transactions going back for the last 15 years, there is nothing that stands out as one year any different from any other in this respect, and that is that of all the cash transactions that (he had) been involved in or witnessed, an infinitesimal percentage, certainly less than two or three percent, were not, in fact, settled by physical delivery" (Tr. 396).

35. In distinguishing between the intended uses of futures and cash commodity contracts Maduff noted that persons entering the futures market do so with the intent of profiting by price fluctuation or, in the case of one in the industry, with the intent of profiting or not losing as a result of price fluctuations. Conversely, Maduff testified that one goes into the cash market "with the intent of obtaining or getting rid of specific merchandise for specific reasons . . . ." (Tr. 398-399).

36. Maduff's opinion that Stovall's operations bore the characteristics of futures transactions did not change when the facts in the hypothetical set forth in finding 34, supra. were changed to provide for deliveries of the actual commodities (Tr. 429).

37. In response to questions by Stovall, Maduff stated that in a cash sale the "contract size" is "practically never right on the pound" (Tr. 404). Maduff also testified that a buyer and seller in a cash commodity transaction generally initiate negotiations by telephone conversations and negotiate all terms of the contract (Tr. 403-405).

38. With respect to the quality or grades of commodities, Maduff agreed with Dr. McDonald that the trade does not recognize a grade of number 3 pork bellies as was found on Stovall's P&S statements. (Tr. 316, 397, CX 10, 15, 16).

39. As an expert, qualified in the nature of futures trading G. Edward Piala, on the basis of the CEA investigation of Stovall, opined that the transactions which Stovall purported to execute were futures transactions and not transactions in cash commodities.

He defined a futures contract as one "in which one person agrees to buy and another to sell a specified commodity for delivery during a specified period in the future, which ordinarily is entered into for the purpose of assuming or shifting the risk of price change without assuming or transferring title to the

cash commodity, and is, or is of the character of, a contract of sale for future delivery as commonly conducted on a board of trade" (Tr. 31).

In addition he testified that "(t)he principal distinguishing feature between a futures contract and a cash contract is that a futures contract is ordinarily intended to be satisfied by offset against another futures contract; whereas a cash commodity contract is ordinarily intended to be satisfied by actual deliver)' of the commodity" (Tr. 32, 192).

Another distinguishing feature, according to Piala, is that one dealing in a cash contract usually has a use for the commodity he is buying and is in the business, whereas if one wanted to speculate he would go into the futures market. The witness acknowledged that a buyer of a cash commodity lacking storage facilities might defer delivery but stated that this does not make it a futures contract. Piala also noted the standardized aspects of a futures contract, the lack of title transfer with futures contracts and the manner of settlement by offset.

VII. Perjury Conviction of Stovall

40. On the basis of a plea of guilty, Stovall, as an individual, stands convicted of a felony (perjury before a federal grand jury) in Case No. 73 Cr 679 (United States District Court for the Northern District of Illinois) (CX 12).

Opinion

The foregoing findings and the conclusions which follow have been made after full consideration of the entire record. All contentions raised by the parties have been considered, whether or not specifically mentioned. All motions, objections, proposed findings and arguments presented by the parties which are inconsistent with this decision are denied or found to be without merit.

Jurisdiction

Any doubts regarding Jurisdiction are easily resolved by reference to the language of Sections 6(b) and 6(c) of the Act (7 U.S.C. § 9, 13b) which authorizes the Secretary of Agriculture (now the Commission) to proceed against any person whom the Secretary has reason to believe is violating or has violated any of the provisions of the Act, or rules and regulations. Section 8a(3) of the Act (7 U.S.C. 12a(3))incorporates by reference the procedures "in paragraph (b) of section 6 of this Act." The provisions of the Act and regulations which the Secretary had reason to believe were violated by respondents were enumerated in the complaint and will be discussed in detail below.

Stovall's Program

In our consideration of the merits of this proceeding we must conclude that complainant has sustained its burden of proof and that the allegations of the complaint are supported by a preponderance of the record evidence.

The Stovall transactions which were the subject of this proceeding were not as respondent maintains, transactions in cash commodities for deferred delivery, but instead were transactions in futures contracts in commodities subject to regulation under Section 2 of the Act (7 U.S.C. 2), which transactions are commonly conducted on boards of trade and subject to the rules of the boards of trade.

During oral argument in this proceeding (Or. 2-3) attorney for complainant compared the Stovall program to a game of monopoly - - "a game made possible by Mr. Stovall being able to enlist the aid and assistance of innocent and

unbuspecting people - - who thought they were actually engaging in some business transactions, when in fact there were no business transactions".

By further analogy one might compare the Stovall operation to a board of trade or exchange operated privately by Stovall in which fictitous trades were solicited and bucketed.

Although cash and futures contracts have characteristics which are to a degree similar and dissimilar, an examination of generally recognized characteristics of each (findings 30-39) as applied to the facts in this case lead to the inescapable conclusion that the purported transactions were futures contracts.

Two primary characteristics which distinguish cash contracts from futures contracts are the intended use and the method of settling such contracts. With respect to use, the cash contract is a merchandising contract while the futures contract is a speculative or hedging contract. In regard to method of settlement, the cash contract is ordinarily settled by delivery of the actual commodity whereas futures contracts are ordinarily settled by offsetting transactions. In this regard see pages 9-10, 12 of respondents' answer.

Regarding these characteristics, the testimony of Piala, McDonald and Maduff representing views of a regulatory agency, academia and the industry, is very persuasive and entitled to much weight. This testimony as well as the facts adduced concerning the operation of Stovall's program demonstrate that Stovall's alleged transactions were futures transactions and not cash commodity transactions. Most significant is the fact that all of Stovall's transactions, with the qualified exception of Rutherford, were

settled by offset in lieu of delivery and that none of the persons involved with Stovall, again with the qualified exception of Rutherford, had any use for any of the commodities they thought they purchased or sold. Further, none of these persons had any intention to make or take delivery of the actual commodity. Analyzing Stovall's business in terms of the reasons customers became associated with him undeniably leads to the conclusion that Stovall's customers were seeking a speculative investment vehicle.

Although the cash contract is recognized as a vehicle for merchandising a cash commodity, Stovall's customers were not employing the cash commodity contracts as such vehicle. Even though there was testimony that two customers thought they were dealing in cash commodities, neither these customers nor any others had any business use for the commodities traded. In this regard it is highly significant that of 177 transactions in 14 accounts there was not a single delivery of the actual cash commodity (Annex A - CX 10.). The absence of any use for merchandising the actual commodities is inconsistent with the purpose and use of real cash commodity contracts.

The only testimony adduced at the hearing regarding the merchandising aspect with cash contracts was that of Donald Rutherford, a

contracts signed by Stovall's customers contained a clause that the customer intended to make or take delivery (CX 5 - sales agreement), the customer testimony at the hearing and the documentary evidence introduced showed that none of the customers, with the very limited exception of Rutherford, terminated their contracts by delivery. When Stovall simultaneously acted as trading agent and principal for customers such as Newkirk and Henrichs, the record reflects only offsetting transactions. Hackbarth spoke only in terms of executing transactions and not mutual recission for those persons on whose behalf he acted as trading agent. Although Stovall supplied the source data or raw data for the computerized P&S statements and the computer was programmed to show deliveries,

Stovall never provided input regarding deliveries during the time period material to this case. This is further indication that the transactions were closed out by offset in lieu of delivery. There was likewise no testimony from Rutherford that he and Stovall mutually agreed to non-delivery of the actual commodities; rather, Rutherford's trading record (CX 18-48, 56A & 56B) indicates either delivery in a very small percentage of the total purchases and sales or, more frequently, an offsetting transaction.

Respondents, at various places in their briefs, argue that evidence concerning the Terms of Purchases and/or Sales Agreement (CX 5) and the intention of Stovall's customers to make or take delivery of the actual cash commodity is inadmissible, as violative of the parol evidence rule and the Illinois Uniform Commercial Code. This agrument, while perhaps applicable to the parties to the agreement, is of no merit here

in a disciplinary proceeding, where the subject of the agreement lies within the control of Congress to regulate. Cf: Wallace v. Hudson-Duncan & Co., 98 F.2d 985, 991-992 (9th Cir., 1938).

Further paragraph 3 of the Terms of Purchase (CX 5) states that:

"CLIENT agrees that any and all purchasee and/or sales with STOVALL contemplate actual delivery and/or receipt of the (actual) commodities . . . ."

A reading of this paragraph reveals that "contemplate" involves a mental process subject to various interpretations and that the relationship was intended to be an on going one. During the hearing testimony was presented by Stovall's customers. Their testimony was clear and unambiguous - they did not contemplate making or taking delivery of the actual commodities. This testimony explained the parties' understanding of an ambiguous term in the document, and demonstrated the true intention of the parties to the agreement and the circumstances surrounding the formulation of the agreement. Indeed, an examination of those transactions (CX 10, 56 A&B) where Stovall was the purchaser shows a settlement, almost exclusively, by offset instead of delivery. Thus, even where Stovall as purchaser should have taken delivery, according to his construction of the Agreement, he did not take delivery. Thus Stovall's actions, in fact, were consistent with the customer's belief and intention.

Other characteristic differences between cash and futures contracts and the manner in which futures contracts are traded provide additional support for the conclusion that Stovall's transactions involved futures contracts. With futures contracts, the contract written by the exchange contains provisions that are standardized with respect to all terms (quantity, quality, place of delivery) except month of delivery and price. In cash transactions all terms are subject to negotiation between the parties. Analysis of Stovall's operation in light of contract terms shows it was one involving futures contracts.

To initiate a futures transaction one need only be concerned with price and delivery month. To initiate a trade in Stovall's program, either Stovall or Hackbarth would call the other and propose a trade of a specific commodity at a specific price with a specified delivery month. The party receiving the proposition had the option of accepting or declining it. Based on data supplied by Stovall the International S.C.O.P.E.S. computer was already programmed by Hackbarth, pursuant to Stovall's instructions, to show specific delivery periods and specific delivery points, the latter being determined by the commodity involved. Also based on data from Stovall the computer was programmed to show delivery periods according to whether the initiating party proposed a sale or purchase of a commodity.

It was only necessary during the telephone conversations for the initiating party to refer to a specific month such as July and the computer was programmed to show a specific delivery period. Thus in Stovall's program everything was standardized and programmed in the computer except the delivery month and price. This is hardly consistent with the concept of term by term negotiation in legitimate cash commodity contracts.

The overwhelming evidence, including the records of Rutherford, support complainant's contention that Stovall's program involved futures transactions. Regardless of what Stovall chose to call his operation, his "program" involved futures contracts and not true cash commodity contracts. Such futures transactions, if executed, could have been used for: hedging transactions in interstate commerce in the commodities or byproducts set forth in CX 10, determining the price bases of transactions in interstate commerce in those commodities, and delivering such commodities sold, shipped or received in interstate commerce for the fulfillment thereof.

Respondents' argument, paragraphs 4 and 5 of their Supplemental Brief and at oral argument (Or. 50-51), that certain exhibits were inaccurate and false is without merit and ignores the testimony adduced at the hearing. Annex A (CX 10) and supporting documents (CX 15, 16) represented transactions between Stovall and the Michigan customers, such as

Newkirk and Henrich (Tr. 81, 87, 104-105, 171-176, 558-561, 570-579, 724-726). The thrust of respondents' argument here is that in Stovall's "negotiations" with Hackbarth the computer was always programmed to show Stovall's purchase of a # 1 grade and a sale of a # 3 grade, which was inconsistent with some of the grades in complainant's exhibits.

However since Hackbarth never acted as trading agent for those customers, Stovall's allegations as to the accuracy of CX 10, 15 and 16 appear frivolous. Conceding for purpose of argument the presence of typographical errors in CX 10, does not destroy its efficacy as a summary of 177 transactions from 14 Stovall accounts from May to December 1972, all of which were settled by offsetting transactions and not by delivery of the actual commodity. Moreover, the fact that the computer was programmed according to Stovall's instructions to show standardized data for everything but price and delivery month is indicative of futures transactions.

Respondents argue estoppel and claim that the sample of customers upon which this action is predicated is insufficient. With respect to the latter contention respondents claim that the complainant rests its case on the trades of 25 to 30 customers whereas Stovall's program involved about 4,000 customers. Matecki testified that 25 to 30 customers were interviewed (Tr. 73). Hackbarth testified that there were 50 to 70 customers starting in June 1972, which number increased to about 3,300 in September 1973. Hackbarth did not know the number of customers in

December 1972 (Tr. 464, 480-481). Stovall, of course, had the only complete customer list, which he refused to turn over to CEA investigators (Tr. 20-21, 24, 26-29,69-70, 149-152, 732-733; CX 1, 3,4), and Stovall did not testify on his own behalf or in response to questions by Complainant's counsel at the hearing. The subpoena issued by the CEA to obtain customer information was not honored and the enforcement action was delayed by the criminal investigation of Stovall's activities (Tr. 160-161, 165A-167). In these circumstances, we believe that the Complainant's sample of Stovall's customers is adequate and representative. Indicative of its adequacy is the fact that Rutherford, the sole witness to testify on Stovall's behalf about actual deliveries, was the sole customer complainant, in the early stages of the hearing, believed might have made delivery (Tr. 75, 176, 178, 181).

Regarding respondents' estoppel argument, Stovall contends that his program was approved by employees of the CEA and that complainant is now estopped from prosecuting this matter. When Stovall met with CEA employees Hill and Smith in April 1971 he inquired whether the CEA had jurisdiction over a "cash grain operation per se". According to the testimony at the hearing Stovall did not elaborate on the details of his proposed operation. At that time it might well have appeared that

Stovall was proposing a legitimate cash merchandising operation. The skeletal information offered by Stovall was certainly inadequate to bind the complainant to approval of his program. Moreover Stovall's refusal to give pertinent records to CEA investigators is inconsistent with his claim of earlier good faith attempts to obtain CEA approval of his program.

Finally respondents contend (Brief page 8) that trading a contract on a contract market is what makes it a futures contract. Respondents further argue that if Stovall's transactions were futures contracts they were not subject to the Commodity Exchange Act because they were not traded on a board of trade. However the requirement that a futures contract be executed on a designated contract market is what makes the contract legal, and not what makes it a futures contract. To permit execution other than on a contract market would invite bucket shops and other fraudulent and non-regulated activities to the detriment of the public and in contravention of the history of commodity regulation, which was designed to insure honest dealings and protection of the public.

All tradings in futures contracts must be done on a contract market designated by the Secretary of Agriculture, now the CFTC. See: Cargill, supra, at 1156; In re: Louis Romoff, 31 Agric. Dec. 158, 162 (31 A.D. 158, 162) (1972);

In re David G. Henner, supra. at 1156.

Viewed in this light, it is evident that the statutory language contained in various provisions, "on or subject to the rules of any contract market", means that a futures contract must be executed on a designated contract market to be legal. Cf. In re: Henry S. Sicinski, 25 Agric. Dec. 302, 306 (25 A.D. 302, 306) (1966); Secretary of Agriculture v. Ray E. Stuart, 1 Agric. Dec. 359, 361 (1 A.D. 359, 361) (1942 consent). To construe the statute in any other way would be to ignore its remedial nature and to render meaningless the requirement that contract markets be designated in accordance with the Act. n7 In addition, the requirement that futures contracts be executed on a designated contract market to be legal is consistent with the statutory provisions prohibiting bucketing and fictitious transactions. To require less would invite the proliferation of bucket shops and operations similar to that of Stovall.

> n7 In order to obtain designation as a contract market for trading in a particular commodity, a board of trade must meet rigid requirements (see Section 5 of the Act, 7 U.S.C. § 7), and must continue, after designation, to maintain specific standards. (See Section 5a of the Act, 7 U.S.C. § 7a).

Because the trades Stovall purportedly executed were futures transactions, they should have been executed on a designated contract market.

Violations of the Act

1. Section 4 of the Act:

Section 4 of the Act (7 U.S.C. § 6) provides, in part that:

"It shall be unlawful for any person to deliver for transmission through the mails or in interstate commerce by telegraph, telephone, wireless, or other means of communication any offer to make or execute, or any confirmation of the execution of, or any quotation or report of the price of, any contract of sale of any commodity for future delivery on or subject to the rules of any board of trade in the United States, or for any person to make or execute such contract of sale, which is or may be used for (a) hedging any transaction in interstate commerce in any commodity or the products of byproducts thereof, or (b) determining the price basis of any such transaction in interstate commerce, or (c) delivering any commodity sold, shipped, or received in interstate commerce for the fulfillment thereof, except, in any of the foregoing cases, where such contract is made by or through a member of a board of trade which has been designated by the Secretary of Agriculture (Commission) as a 'contract market' . . ."

Stovall violated this statutory provision by using the mails to transmit to his customers confirmations of the purported transactions and to quote the prices of the transactions, since such transactions had not been executed on a designated contract market. See: In re Sicinski, supra. Stovall's purported transactions were in reality futures

transactions and, as such, subject to the rules of a board of trade.

2. Section 4d of the Act:

Section 4d of the Act (7 U.S.C. § 6d) provides in part that:

"It shall be unlawful for any person to engage as futures commission merchant in soliciting orders or accepting orders for the purchase or sale of any commodity for future delivery, or involving any contracts of sale of any commodity for future delivery, on or subject to the rules of any contract market unless -

(1) such person shall have registered under this Act, with the Secretary of Agriculture (Commission) as such futures commission merchant and such registration shall not have expired nor been suspended nor revoked;. . . "

In addition Section 2a of the Act (7 U.S.C. § 2) defines "futures commission merchant" to:

"mean and include individuals, associations, partnerships, corporations, and trusts engaged in soliciting or in accepting orders for the purchase or sale of any commodity for future delivery on or subject to the rules of any contract market and that, in or in connection with such solicitation or acceptance of orders, accepts any money, securities, or property (or extends credit in lieu thereof) to margin, guarantee, or secure any trades or contracts that result or may result therefrom. "

Although Stovall's activities fell within the statutory definition of a futures commission merchant (FCM) he, as an individual or as R. L. Stovall, Sole Proprietor in Cash Commodities, was never registered as an

FCM.

In the case of In re David L. Hofer, 29 Agric. Dec. 1334 (29 A.D. 1334) (1970), the Judicial Officer, on facts similar to those here, concluded that the respondent was acting as an unregistered FCM. Hofer solicited and obtained from his customers a "Power of Attorney and Agency Agreement . . which authorized him, as agent and attorney-in-fact, to buy, sell, and trade in commodities or contracts relating thereto", 29 Agric. Dec. at 1338-1339 (29 A.D. at 1338-1339). The agreement gave respondent open-ended discretion with respect to all trades and required the customer to place a sum of money as a deposit with Hofer. The agreement in Hofer was found to be an "order" within the definition of an FCM

and Hofer's conduct qualified him as an FCM. 29 Agric. Dec. at 1339-1342 (29 A.D. at 1339-1342). See also: In re J. M. Leak, 7 Agric. Dec. 528, 530-531 (7 A.D. 528, 530-531) (1948, Default).

It is clear that Stovall's conduct was such that his business involved the solicitation and acceptance of orders to buy or sell futures contracts and the acceptance of money to margin those trades. As in Hofer, Stovall's trading authorization and management contract (CX 5) gave the trading agent (Stovall and later Hackbarth) complete and open discretion concerning trades, provided for the customer to authorize the trading agent to buy and sell contracts on "margin" (CX 5 - Trading Authorization) and called for the customer to give Stovall a "deposit" for the purpose of

trading (CX 5 - management contract). Moreover Stovall admitted to Matecki that he solicited accounts and money from customers (Tr. 158, 171). Stovall's conduct and activities bring him within the statutory definition of an FCM. Stovall's lack of registration as an FCM is undisputed and violative of Section 4d of the Act (7 U.S.C. § 6d).

3. Section 4b(D) of the Act; Section 1.38 of the Regulations Section 4b of the Act (7 U.S.C. § 6b) prohibits bucketing n8 by making it unlawful:

"(1) for any member of a contract market, or for any correspondent; agent, or employee of any member, in or in connection with any order to make, or the making of any contract of sale of any commodity in interstate commerce, made, or to be made, on or subject to the rules of any contract market, for or on behalf of any other person, or (2) for any person, in or in connection with any order to make, or the making of, any contract of sale of any commodity for future delivery, made, or to be made, on or subject to the rules of any contract market, for or on behalf of any other person if such contract for future delivery is or may be used for (a) hedging any transaction in interstate commerce in such commodity or the products or by products thereof, or (b) determining the price basis of any transaction in interstate commerce in such commodity, or (c) delivering any such commodity sold, shipped, or received in interstate commerce for the fulfillment thereof. . . .

(D) to bucket such order, or to fill such order by offset against the order or orders of any other person or willfully and knowingly and without the prior consent of such person to become the buyer in respect to any selling order of such person, or become the seller in respect to any buying order of such person."

n8 Bucketing is the practice of taking the opposite side of a customer's trade instead of executing it in the open market. Campbell, Trading in Futures Under The Commodity Exchange Act, 26 Geo. Wash. L. Rev. 215, 232.

The danger of bucket shops has long been recognized. Hoffman states that: n9

"Their intent is to defraud their patrons. To accomplish this, they encourage their customers to enter into contracts promising profit if prices advance. However, these contracts may be handled, whether nominally executed upon a recognized exchange or not, the house assumes an opposite position to the customer gaining if the customer loses and losing if the customer gains. They must have quotations from some source to operate. If they are to remain in business, (1) their trade must either include both buying and selling customers which offset each other thus permitting the house to profit from commissions without the costs of execution or the risk of the market or (2) the market must so move, where they are forced to take an opposite position to their customers, that they will gain and their customers lose."

n9 Hoffman, Futures Trading Upon Organzied Commodity Markets In the United States (1932), pp. 357-358, (referred to as "one of the standard works on futures trading", In re Cargill, Incorporated 29 Agric. Dec. 880, 907 (29 A.D. 880, 907))

In purporting to execute transactions for customers such as Newkirk and Henrichs, Stovall took the opposite side of a customer's order when acting as agent for the customer on the one hand and as the principal for his own account on the other. Further, such transactions were not executed in accordance with the rules of a contract market. In part this situation changed in approximately July 1972 when Hackbarth became trading agent for some of the Stovall customers. The substitution of Hackbarth, however, did not detract from Stovall's practice of taking the opposite side of a customer's trade. After Hackbarth began acting as trading agent, Stovall or his salesmen continued to obtain customers and new accounts. Hackbarth played no role in the solicitation of business and had no personal contact with the persons on whose behalf he traded. Each time Hackbarth "executed" a trade, Stovall benefited by a gain in the transaction or collection of a handling fee (Respondent's proposed finding 76). Regardless of who held the trading authorization, the account owners were Stovall's customers. Stovall thus retained an interest in the account against which he purported to trade.

Stovall's admission to Matecki on December 8, 1972 that he was on the opposite side of each of his customers' transactions (Tr. 772) demonstrates a clear violation of Section 4b of the Act as well as

Section 1.38 of the regulations (17 CFR § 1.38) which requires execution of trades "openly and competitively". See e.g., In re: Julian M. Marks, 22 Agric. Dec. 761, 776 (22 A.D. 761, 776) (1963); In re: Raymond A. Gerstenberg, 26 Agric. Dec. 816, 822 (26 A.D. 816, 822) (Consent 1967); In re: Charles Vojtek, 7 Agric. Dec. 386, 388-389 (7 A.D. 386, 388-389) (Default 1948); Secretary of Agriculture v. Stuart, 1 Agric. Dec. 359, 361 (1 A.D. 359, 361) (Consent 1942).

4. Section 4c(A) of the Act

Section 4c(A) of the Act (7 U.S.C. § 6c(A)) prohibits fictitious transactions. Under that Section it is:

"unlawful for any person to offer to enter into, enter into, or confirm the execution of, any transaction involving any commodity, which . . . .

(A) if such transaction is, is of the character of, or is commonly known to the trade as, a 'wash sale', 'cross trade', or 'accommodation trade', or is a fictitious sale; "

"The essential and identifying characteristic of a 'wash sale' seems to be the intent not to make a genuine, bona fide trading transaction in stocks or commodities. A wash sale is a form of fictitious transaction". The fictitious sale provision of the statute was intended "to outlaw insofar as possible all schemes of trading that are artificial and are not the result of arms-length trading on the basis of supply and demand factors and trading opinion of these factors." In re: Jean Goldwurm, 7 Agric. Dec. 265, 274-276 (7 A.D. 265, 274-276) (1948). As noted above, Stovall bucketed the "trades" in his program and none of the transactions were ever actually executed in a bona

The Sanction

The complaint and notice of hearing filed in this proceeding alleges willful violations of the Act and reads:

". . . At such hearing, the respondents will have the right to appear and show cause, if any there be, why an appropriate order should not be issued in accordance with the Commodity Exchange Act, (1) suspending or revoking the

registration of respondent Rawlin L. Stovall as a floor broker, (2) suspending or revoking the registration of respondent Stovall and Stovall, Inc. as a futures commission merchant (at pages 27 and 28 of the brief in support of proposed findings and conclusions, complainant seeks revocation of the finds registration), (3) prohibiting respondent Stovall from trading on or subject to the rules of any contract market, and directing that all contract markets refuse all trading privileges to respondent Stovall for such period of time as may be determined and (4) directing that respondent Stovall shall cease and desist from violating the Act in the manner alleged herein."

Under the Administrative Procedure Act (5 U.S.C. § 558), a revocation or suspension order may be issued without prior notice only if the violation was willful. Assuming that this section is applicable, the violations by respondent, Stovall, were willful.

The respondent is an experienced trader. Stovall, during the period material to this proceeding, was a registered floor broker and his firm, Stovall and Stovall, Inc., was a registered futures commission merchant,which necessitated familiarity with the Act and Regulations. Hence the inference is inescapable that Stovall willfully violated the

Act and Regulations in the manner described above.

A violation is willful, within the meaning of the term in a regulatory statute, if the violator "1) intentionally does an act which is prohibited, -- irrespective of evil motive or reliance on erroneous advice, or 2) acts with careless disregard of statutory requirements" Goodman v. Benson, 286 F.2d 896, 900 (7th Cir., 1961) .

Because the activities of R. L. Stovall, Sole Proprietor, Principal in Cash Commodities, were flagrant violations of the Act, fraudulent misrepresentations to the public, and a source of gain to Stovall, the sanction imposed is severe and consistent with that recommended in the complaint, viz.:

a. Revocation of the floor broker registration;

b. Two year denial of trading privileges; and

c. An order to cease and desist.

In addition the registration of Stovall & Stovall, Inc., a registered futures commission merchant during 1972, is revoked as being unfit to continue as a futures commission merchant, since Stovall as an officer (President) and principal stockholder of the firm, engaged in practices prohibited by the Act, and was convicted of a felony (perjury)

in a federal court (finding 40). Such revocation is in accord with Section 8a(2) (B) (1) and 8a(3) of the Act (7 U.S.C. § 12a(2)(B)(1) and 12a(3)).

CONCLUSIONS OF LAW

1. The CEA (now CFTC) has jurisdiction over the persons and subject matter of this action by virtue of Sections 6(b), 6(c) and 8a(3) of the Act (7 U.S.C. §§ 9, 13b, 12a(3)).

2. The business in which Stovall engaged involved the offer to make and the purported entering into of purchases and sales of commodities for future delivery which were subject to the rules of contract markets.

3. By soliciting and accepting orders for the purchase and sale of commodities for future delivery on or subject to the rules of any contract market,and accepting money deposits to margin such orders, Stovall engaged in business as a futures commission merchant.

4. Because Stovall was not registered with the Secretary of Agriculture in 1972 as a futures commission merchant, Stovall violated Section 4d of the Act (7 U.S.C. § 6d).

5. By using the mails to transmit confirmations of the purported executions and quotations or reports of prices of contracts of sale of commodities for future delivery on or subject to the rules of

any board of trade, which were not executed by or through a member of a board of trade which has been designated as a contract market, Stovall violated Section 4 of the Act (7 U.S.C. § 6).

6. Because Stovall was on the opposite side of all his customers' transactions which were not subject to bona fide execution in accordance with the rules of a contract market and because such transactions were not executed openly and competitively by open outcry or posting of bids and offers or by other equally open and competitive methods in a place provided by a contract market, Stovall violated Section 4b(D) of the Act and Section 1.38(a) of the Regulations (7 U.S.C. § 6b(D) and 17 CFR § 1.38(a)).

7. In reporting and confirming a trade to customers as having been executed, when in fact no bona fide execution had occurred, Stovall engaged in fictitious transactions and violated Section 4c(A) of the Act (7 U.S.C. § 6c(A)).

8. Stovall's failure and refusal to make available for inspection by representatives of the CEA and Secretary of Agriculture his books and records regarding his business violated Section 1.35(a) of the regulations (17 CFR § 1.35(a)).

9. Because Rawlin L. Stovall, an officer of Stovall and Stovall, Inc. violated the Act and was convicted of a felony, the corporation is unfit to engage in the business as a futures commission merchant.

ORDER

1. The respondent, Rawlin L. Stovall, is prohibited from trading on or subject to the rules of any contract market for a period of 2 years, and all contract markets shall refuse all trading privileges to him during said period. Such prohibition and refusal shall apply to all trading done and all positions held directly, or indirectly, whether for his account, or for the account of any other person.

2. The registration of respondent, Rawlin L. Stovall, as a registered floor broker under the Act, is revoked.

3. The registration of respondent Stovall and Stovall, Inc., as a futures commission merchant under the Act, is revoked.

4. Respondent, Rawlin L. Stovall, shall cease and desist from:

a. Engaging as a futures commission merchant without being registered as required by the Act and the regulations thereunder;

b. Using the mails to transmit confirmations of purported executions and quotations or reports of prices of contracts of sale of commodities for future delivery, on or subject to the rules of any

board of trade, which are not executed by or through a member of a board of trade which has been designated as a contract market;

c. Entering into, or offering to enter into, any futures transaction subject to the Act if such transaction is, is of the character of, or is commonly known to the trade as, a "wash sale," or is a fictitious sale; and

d. Executing any futures transaction subject to the Act if such transaction is bucketed or if such transaction is not executed openly and competitively in accordance with section 1.38 of the regulations issued under the Act (17 CFR 1.38).

5. Paragraphs 1, 2, and 3 of this Order shall be effective on the twentieth day after this Decision and Order become final. Paragraph 4 shall be effective on the date this Decision and Order become final.

6. Pursuant to the Rules of Practice governing proceedings under the Act, this Decision and Order shall become final 30 days after service thereof, unless appealed to the Commodity Futures Trading Commission

by a party to this proceeding, or otherwise acted upon by the Commission. (17 CFR § 10.84(c), 10.102)

7. Copies hereof shall be served upon each party and on each contract market.

Done at Washington, D.C.

6 MAY 1977

[SEE SIGNATURE IN ORIGINAL]

John A. Campbell

Administrative Law Judge

LOAD-DATE: August 6, 2008