

**UNITED STATES OF AMERICA**  
**Before the**  
**COMMODITY FUTURES TRADING COMMISSION**

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10:56 am, Jul 30, 2018

**In the Matter of:**

**R.J. O'Brien & Associates LLC**

**Respondent.**

**CFTC DOCKET NO. 18-17**

**ORDER INSTITUTING PROCEEDINGS PURSUANT TO  
SECTION 6(c) AND (d) OF THE COMMODITY EXCHANGE ACT, MAKING  
FINDINGS, AND IMPOSING REMEDIAL SANCTIONS**

**I.**

The Commodity Futures Trading Commission (“Commission”) has reason to believe that R.J. O’Brien & Associates LLC (“RJO” or “Respondent”) violated Section 6(c)(4) of the Commodity Exchange Act (“Act”), 7 U.S.C. § 9(4) (2012), and Commission Regulation (“Regulation”) 166.3, 17 C.F.R. § 166.3 (2017). Therefore, the Commission deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted to determine whether Respondent engaged in the violations set forth herein and to determine whether any order should be issued imposing remedial sanctions.

**II.**

In anticipation of the institution of an administrative proceeding, Respondent has submitted an Offer of Settlement (“Offer”), which the Commission has determined to accept. Without admitting or denying any of the findings or conclusions herein, Respondent consents to the entry of this Order Instituting Proceedings Pursuant to Section 6(c) and (d) of the Commodity Exchange Act, Making Findings, and Imposing Remedial Sanctions (“Order”) and acknowledges service of this Order.<sup>1</sup>

**III.**

The Commission finds the following:

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<sup>1</sup> Respondent consents to the use of these findings of fact and conclusion of law in this Order in this proceeding and in any other proceeding brought by the Commission or to which the Commission is a party or claimant, and agrees that they shall be taken as true and correct and be given preclusive effect therein, without further proof. Respondent does not consent, however, to the use of this Order, or the findings or conclusions herein, as the sole basis for any other proceeding brought by the Commission or to which the Commission is a party or claimant, other than: a proceeding in bankruptcy or receivership; or a proceeding to enforce the terms of this Order. Respondent does not consent to the use of the Offer or this Order, or the findings or conclusions in this Order, by any other party in any other proceeding.

**A. SUMMARY**

Between at least January 2013 and February 2014 (“Relevant Period”), RJO failed to diligently supervise its employees concerning accounts owned or controlled by its client, who was the associated person (“AP”) and founder of a commodity trading advisor (“CTA”) and commodity pool operator (“CPO”). The CTA/CPO’s AP and founder (“Client”) managed commodity futures accounts for numerous individual customers as well as a commodity pool (“Pool”). During the Relevant Period, the Client used RJO’s electronic trading platform to execute bunched orders on behalf of customer and proprietary accounts in a bunched order account held at RJO. The Client used this bunched order account to engage in an unlawful post-execution allocation scheme to the Client’s benefit and to the detriment of certain of the Client’s customers. Despite the presence of red flags indicating that the Client may not have been allocating bunched orders in compliance with Commission regulations, RJO failed to make a reasonable sufficient inquiry into the Client’s allocation practices or take other appropriate action. In addition, RJO failed to adhere to its internal protocols governing the processing of bunched orders, did not employ adequate compliance procedures to monitor, detect, and deter unusual activity concerning bunched orders allocated post-execution, and failed to supervise its employees processing bunched orders.

In addition, during the Relevant Period, the National Futures Association (“NFA”) issued a Member Responsibility Action (“MRA”) against the Client and CTA/CPO prohibiting the Client from soliciting funds or withdrawing money from managed accounts, and ultimately banned the Client from trading for failure to comply with the MRA (together, “NFA Orders”). Despite the NFA Orders, of which RJO compliance and supervisory personnel were aware, the Client was able to open and operate a new account with RJO in the name of the Client’s spouse (“Spouse Account”). RJO’s did not identify that the Client was managing the Spouse Account. RJO processed numerous requests for withdrawals from the Spouse Account despite the prohibition against withdrawals from accounts operated by the Client, and cleared trades executed in the Spouse Account after the Client was banned from trading. RJO’s failure to detect the relationship between the Client and the Spouse Account, which enabled the Client to circumvent the NFA Orders and delayed detection of the Spouse Account by regulators, demonstrated the insufficiency of RJO’s policies and procedures regarding the opening of new accounts and compliance with regulatory actions.

Through these actions, Respondent failed to diligently supervise the handling of its customer accounts, including the processing of bunched orders executed by the Client, in violation of Regulation 166.3, 17 C.F.R. § 166.3 (2017). RJO’s failure to diligently supervise its employees concerning these bunched orders also violated the terms of a prior Commission Order. Consequently, the Commission has the authority under Section 6(c)(4) of the Act, 7 U.S.C. § 9(4) (2012), to bring an action for the violation of such Order.

**B. RESPONDENT**

**R.J. O’Brien & Associates LLC** is Delaware limited liability company with its principal place of business in Chicago, Illinois. At all relevant times, RJO was registered with the Commission as a futures commission merchant (“FCM”).

## C. FACTS

Regulation 1.35(b)(5), 17 C.F.R. § 1.35(b)(5) (2017), permits eligible account managers (“EAMs”), including CTAs, to enter bunched orders on behalf of multiple customers<sup>2</sup> and allocate them to individual or pooled accounts no later than the end of the trading day. To be eligible for post-execution allocation, bunched orders must be allocated as follows: (1) CTAs are required to provide FCMs with allocation instructions “as soon as practicable after the entire transaction is executed, but in any event no later than . . . sufficiently before the end of the day the order is executed to ensure that clearing records identify the ultimate customer for each trade”; (2) allocations must be “fair and equitable,” with no accounts receiving consistently favorable or unfavorable treatment; and (3) the allocation methodology must be “sufficiently objective and specific to permit independent verification of the fairness of the allocations using that methodology.” 17 C.F.R. § 1.35(b)(5)(i)(A), (b)(5)(iv)(A)-(C).

The Client used RJO’s electronic trading platform to execute round-turn trades<sup>3</sup> during the same trading day in E-mini S&P 500 futures contracts on behalf of individual customers, the Pool, and accounts in which the Client or the Client’s associates had a proprietary interest. The Client initially placed these trades in a bunched order account maintained at RJO. At the end of the trading day, after calculating gains and losses on the trades, the Client would send allocation instructions to the AP of an introducing broker (“IB”), who would then forward the instructions to RJO for allocation to accounts managed by the Client. Taking improper advantage of post-execution allocation, the Client disproportionately allocated profitable trades to the accounts in which the Client or the Client’s associates had a proprietary interest, and unprofitable or less profitable trades to the customer accounts or the Pool account.

During the Relevant Period, RJO had an internal protocol for account managers to provide RJO with allocation instructions by 4 p.m. central time so that bunched orders could be processed before the close of the exchange. In addition, RJO had a guideline that account managers allocate retail bunched orders to three or more accounts. RJO’s written procedures also stated that account managers must use a “sufficiently objective and specific” allocation methodology, and required firm personnel with knowledge of improper allocations or other fraudulent or abusive bunched order allocation practices to notify the compliance department. Furthermore, Regulation 1.35(b)(5) places an affirmative obligation on FCMs to monitor for unusual allocation activity and to make a reasonable inquiry into the matter if an FCM has actual or constructive notice of fraudulent allocations. *See* Account Identification for Eligible Bunched Orders, 68 Fed. Reg. 34,790, 34,792 (June 11, 2003); *see also* NFA Notice 9029. Many times, the Client’s allocations did not comply with RJO’s protocols. For example, RJO at times

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<sup>2</sup> *See* Customer Clearing Documentation, Timing of Acceptance for Clearing, and Clearing Member Risk Management, 77 Fed. Reg. 21,278, 21,286 (Apr. 9, 2012); *see also* Adaptation of Regulations to Incorporate Swaps, 77 Fed. Reg. 66,288, 66,311 (Nov. 2, 2012) (discussing purpose of Regulation 1.35 with respect to bunched orders). Under Regulation 1.35(b)(5), EAMs placing orders for a single account must still provide that account number at the time of order entry. *See* NATIONAL FUTURES ASS’N, NFA Interpretive Notice 9029, *NFA Compliance with Rule 2-10: The Allocation of Bunched Orders for Multiple Accounts* (“NFA Notice 9029”), n.3, <https://www.nfa.futures.org/rulebook/rules.aspx?RuleID=9029&Section=9>.

<sup>3</sup> A round-turn trade is a completed transaction involving both a purchase and a liquidating sale, or a sale followed by a covering purchase.

received the Client's allocation instructions after 4 p.m. central time, and the Client routinely allocated bunched orders to a single account.

On September 4, 2013, NFA issued an MRA against the Client and the CTA/CPO for conduct unrelated to the allocation scheme. This MRA prohibited the Client and the CTA/CPO from soliciting funds from customers, or disbursing funds from any account they owned or controlled, without NFA approval. RJO compliance and supervisory personnel received notice of this MRA and were directed to immediately notify NFA if the Client attempted to withdraw funds from any account the Client managed or controlled. A few weeks later, the Client opened the Spouse Account with RJO—an account that the Client managed and controlled, and was therefore subject to the terms of the MRA. RJO did not receive a power of attorney from the owner of the Spouse Account to allow the Client to exercise discretion over this account, and therefore RJO was not aware of the relationship between the two accounts. In turn, at the request of the IB, RJO permitted the Client to allocate trades to the Spouse Account. In addition, despite an obligation to notify NFA if the Client sought to withdraw money from any account the Client controlled, for approximately four months after the MRA was issued, RJO permitted the Client to withdraw funds from the Spouse Account. Over the life of the Spouse Account, the Client deposited only \$5,000, yet withdrew a total of \$270,000. Not only was the Client able to make these withdrawals in violation of the MRA, but the Spouse Account's significant return on investment was a red flag that the Client may have been engaging in an unlawful allocation scheme.

On January 16, 2014, NFA issued an order permanently banning the Client and the CTA/CPO from placing trades for any pools they operated or accounts that they owned or controlled, except for the liquidation of existing positions. RJO compliance and supervisory personnel also received notice of this order. Nonetheless, RJO cleared trades in the Spouse Account for nearly a month, which were placed in violation of the trading ban.<sup>4</sup>

Notably, in January 2013, RJO settled a case with the Commission for failing to supervise the handling of certain customer orders in violation of Regulation 166.3, 17 C.F.R. § 166.3 (2017). The Commission charged RJO with failure to supervise its employees in their processing of certain bunched orders, including the failure to employ adequate procedures to monitor, detect, and deter unusual activity concerning trades allocated post-execution. This settlement culminated in RJO updating its policies regarding the post-execution allocation of bunched orders. However, RJO did not detect the Client's improper allocation activity for over a year after entering into the January 2013 settlement with the Commission, demonstrating that RJO's revised policies remained insufficient to detect unusual allocation activity.<sup>5</sup>

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<sup>4</sup> RJO issues trader IDs, such as Tag 50 IDs, to clients. RJO did not immediately deactivate the Client's Tag 50 ID after being notified of the trading ban, which allowed the Client to execute trades in the Spouse Account following the ban.

<sup>5</sup> Since the Relevant Period, RJO has taken remedial steps, including improving and enhancing its policies, procedures and practices.

## IV.

### LEGAL DISCUSSION

#### A. Failure to Supervise

Regulation 166.3, 17 C.F.R. § 166.3 (2017), requires that every Commission registrant (except APs who have no supervisory duties) “diligently supervise the handling by its partners, officers, employees and agents” of all activities relating to its business as a registrant. Regulation 166.3 imposes upon a registrant an affirmative duty to diligently supervise its employees and agents by establishing, implementing and executing an adequate supervisory structure and compliance program. *In re Collins*, CFTC No. 94-13, 1997 WL 761927, at \*10 (Dec. 10, 1997); *see also In re Vision Fin. Mkts.*, CFTC No. 13-36, 2013 WL 5376144, at \*2 (Sept. 24, 2013) (consent order). For a registrant to fulfill its duties under Regulation 166.3, it must both design an adequate program of supervision and ensure that the program is followed. *In re GNP Commodities, Inc.*, CFTC No. 89-1, 1992 WL 201158, at \*17-19 (Aug. 11, 1992), *aff’d sub nom. Monieson v. CFTC*, 996 F.2d 852 (7th Cir. 1993).

A violation of Regulation 166.3 is an independent violation for which no underlying violation is necessary. *In re First Nat’l Trading Corp.*, CFTC No. 92-17, 1994 WL 378010, at \*10 (July 20, 1994) (citing *In re Paragon Futures Ass’n*, CFTC No. 88-18, 1992 WL 74261, at \*13 (Apr. 1, 1992)); *GNP Commodities*, 1992 WL 201158, at \* 17 n.11; *see, e.g., In re FCStone, LLC*, 2015 WL 2066891, at \*3 (May 1, 2015). Consequently, a violation of Regulation 166.3 is established by showing either that: (1) the registrant’s supervisory system was generally inadequate, or (2) the registrant failed to perform its supervisory duties diligently. *FCStone*, 2015 WL 2066891, at \*3 (citing *In re Murlas Commodities*, CFTC No. 85-29, 1995 WL 523563 (Sept. 1, 1995)); *Paragon*, 1992 WL 74261, at \*14 (concluding that the “focus of any proceeding to determine whether Rule 166.3 has been violated will be on whether [a] review [has] occurred and, if it did, whether it was ‘diligent’”); *GNP Commodities*, 1992 WL 201158, at \*19 (holding that Regulation 166.3 is violated if the supervisory system is not diligently enforced). Thus, a registrant’s failure to develop proper procedures for the detection of wrongdoing, standing alone, can evidence the lack of an adequate supervisory system. *See CFTC v. Sidoti*, 178 F.3d 1132, 1137 (11th Cir. 1999). Whether a registrant has met its supervisory duties is a fact-intensive determination. *See, e.g., GNP Commodities*, 1992 WL 201158, at \*17. Evidence of violations that “should be detected by a diligent system of supervision, either because of the nature of the violations or because the violations have occurred repeatedly” is probative of a failure to supervise. *Sidoti*, 178 F.3d at 1137.

Finally, CTAs are permitted to engage in post-execution allocation only if the conditions of Regulation 1.35(b)(5) are met. *See* 17 C.F.R. § 1.35(b)(5)(i)(A), (b)(5)(iv)(A)-(C) (2017). In addition, CTAs must have written investment discretion over all accounts participating in post-execution allocation. 17 C.F.R. § 1.35(b)(5)(i). FCMs that execute or clear trades for CTAs using post-execution allocation have a “responsibility to monitor for unusual allocation activity.” NFA Notice 9029.

At all relevant times, RJO was registered as an FCM with the Commission. As such, RJO had a duty to monitor the Client’s accounts for unusual allocation activity. During the

Relevant Period, the Client submitted allocation instructions after 4 p.m. central time, frequently allocated orders to only one account, and did not have written investment discretion over the Spouse Account, to which the Client allocated trades on a post-execution basis. Despite these red flags, RJO did not undertake a reasonable inquiry into this unusual allocation activity, nor did it sufficiently instruct its allocation personnel regarding how to recognize and report such red flags.

Furthermore, RJO did not have adequate procedures or systems in place concerning the processing of bunched orders allocated post-execution, the opening and closing of client accounts, or the monitoring of accounts owned or operated by clients subject to regulatory actions. And in certain instances, RJO did not follow internal protocols regarding the processing of bunched orders. RJO's failure to detect the Client's unusual allocation activity and recognize that the Spouse Account was being operated by the Client—and was therefore subject to the NFA Orders—delayed discovery of the Client's scheme, which resulted in unjust gains to the Client and losses to customers.

Collectively, these deficiencies evidence RJO's failure to diligently supervise the handling by its employees of its business as a Commission registrant, in violation of Regulation 166.3.

**B. Failure to Comply with Commission Order**

On January 2, 2013, RJO voluntarily consented to a Commission Order prohibiting it from violating Regulation 166.3, relating to the supervision of its employees' processing of certain bunched orders ("January 2, 2013 Order"). *See In re R.J. O'Brien, LLC*, CFTC No. 13-10, 2013 WL 55701, at \*3 (Jan. 2, 2013). The Commission has the authority under Section 6(c)(4) of the Act, 7 U.S.C. § 9(4) (2012), to bring an action for violation of this Order.

As described herein, during the Relevant Period, RJO failed to diligently supervise the handling of its customer accounts by failing to employ adequate compliance procedures to monitor, detect, and deter unusual activity concerning bunched orders, or follow internal protocols concerning the allocation of bunched orders. By this conduct, RJO violated the January 2, 2013 Order.

**V.**

**FINDINGS OF VIOLATION**

Based on the foregoing, the Commission finds that, during the Relevant Period, Respondent violated Section 6(c)(4) of the Act, 7 U.S.C. § 9(4) (2012), and Regulation 166.3, 17 C.F.R. § 166.3 (2017).

**VI.**

**OFFER OF SETTLEMENT**

Respondent has submitted the Offer in which it, without admitting or denying the findings and conclusions herein:

- A. Acknowledges service of this Order;
- B. Admits the jurisdiction of the Commission with respect to all matters set forth in this Order and for any action or proceeding brought or authorized by the Commission based on violation of or enforcement of this Order;
- C. Waives:
  - 1. The filing and service of a complaint and notice of hearing;
  - 2. A hearing;
  - 3. All post-hearing procedures;
  - 4. Judicial review by any court;
  - 5. Any and all objections to the participation by any member of the Commission's staff in the Commission's consideration of the Offer;
  - 6. Any and all claims that it may possess under the Equal Access to Justice Act, 5 U.S.C. § 504 (2012) and 28 U.S.C. § 2412 (2012), and/or the rules promulgated by the Commission in conformity therewith, Part 148 of the Commission's Regulations, 17 C.F.R. pt. 148 (2017), relating to, or arising from, this proceeding;
  - 7. Any and all claims that it may possess under the Small Business Regulatory Enforcement Fairness Act of 1996, Pub. L. No. 104-121, §§ 201-53, 110 Stat. 847, 857-74 (codified as amended in scattered sections of 5 U.S.C. and 15 U.S.C.), relating to, or arising from, this proceeding; and
  - 8. Any claims of Double Jeopardy based on the institution of this proceeding or the entry in this proceeding of any order imposing a civil monetary penalty or any other relief, including this Order;
- D. Stipulates that the record basis on which this Order is entered shall consist solely of the findings contained in this Order to which Respondent has consented in the Offer;
- E. Consents, solely on the basis of the Offer, to the Commission's entry of this Order that:
  - 1. Makes findings by the Commission that Respondent violated Section 6(c)(4) of the Act, 7 U.S.C. § 9(c)(4) (2012), and Regulation 166.3, 17 C.F.R. § 166.3 (2017);
  - 2. Orders Respondent to cease and desist from violating Regulation 166.3;
  - 3. Orders Respondent to pay a civil monetary penalty of six-hundred thousand dollars (\$600,000) plus post-judgment interest;
  - 4. Orders Respondent and its successors and assigns to comply with the conditions consented to in the Offer and as set forth in Part VII of this Order.

Upon consideration, the Commission has determined to accept the Offer.

## VII.

### ORDER

#### Accordingly, IT IS HEREBY ORDERED THAT:

- A. Respondent shall cease and desist from violating Regulation 166.3, 17 C.F.R. § 166.3 (2017).
- B. Respondent shall pay a civil monetary penalty of six-hundred thousand dollars (\$600,000) (“CMP Obligation”) within ten (10) days of the date of entry of this Order. If the CMP Obligation is not paid in full within ten (10) days of the date of entry of this Order, then post-judgment interest shall accrue on the CMP Obligation beginning on the date of entry of this Order and shall be determined by using the Treasury Bill rate prevailing on the date of entry of this Order pursuant to 28 U.S.C. § 1961 (2012).

Respondent shall pay the CMP Obligation and any post-judgment interest by electronic funds transfer, U.S. postal money order, certified check, bank cashier’s check, or bank money order. If payment is to be made other than by electronic funds transfer, then the payment shall be made payable to the Commodity Futures Trading Commission and sent to the address below:

MMAC/ESC/AMK326  
Commodity Futures Trading Commission  
Division of Enforcement  
6500 S. MacArthur Blvd.  
Oklahoma City, OK 73169  
(405) 954-6569 office  
(405) 954-1620 fax  
9-AMC-AR-CFTC@faa.gov

If payment is to be made by electronic funds transfer, Respondent shall contact Marie Thorne or her successor at the above address to receive payment instructions and shall fully comply with those instructions. Respondent shall accompany payment of the CMP Obligation with a cover letter that identifies the paying Respondent and the name and docket number of this proceeding. The paying Respondent shall simultaneously transmit copies of the cover letter and the form of payment to the Chief Financial Officer, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, D.C. 20581.

- C. Respondent and its successors and assigns shall comply with the following conditions and undertakings set forth in the Offer:
  - 1. Public Statements: Respondent agrees that neither it nor any of its successors and assigns, agents or employees under its authority or control, shall take any action or make any public statement denying, directly or indirectly, any findings or

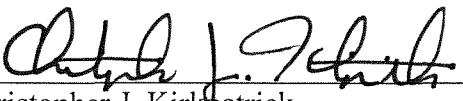


conclusions in this Order or creating, or tending to create, the impression that this Order is without a factual basis; provided, however, that nothing in this provision shall affect Respondent's: (i) testimonial obligations; or (ii) right to take legal positions in other proceedings to which the Commission is not a party. Respondent and its successors and assigns shall undertake all steps necessary to ensure that all of its agents and/or employees under its authority or control understand and comply with this agreement.

2. Cooperation with the Commission: Respondent shall cooperate fully and expeditiously with the Commission, including the Commission's Division of Enforcement, and any other governmental agency in this action, and in any investigation, civil litigation, or administrative matter related to the subject matter of this action or any current or future Commission investigation related thereto.
3. Partial Satisfaction: Respondent understands and agrees that any acceptance by the Commission of any partial payment of Respondent's CMP Obligation shall not be deemed a waiver of its obligation to make further payments pursuant to this Order, or a waiver of the Commission's right to seek to compel payment of any remaining balance.
4. Change of Address/Phone: Until such time as Respondent satisfies in full its CMP Obligation as set forth in this Order, Respondent shall provide written notice to the Commission by certified mail of any change to its telephone number and mailing address within ten (10) calendar days of the change.

**The provisions of this Order shall be effective as of this date.**

By the Commission.

  
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Christopher J. Kirkpatrick  
Secretary of the Commission  
Commodity Futures Trading Commission

Dated: July 30, 2018.