

**UNITED STATES OF AMERICA
BEFORE THE
COMMODITY FUTURES TRADING COMMISSION**

In the Matter of:

Excellent USA, Inc.
141 W. Jackson Blvd., Suite 3706
Chicago, Illinois 60604-3201, and

John F. Gallwas
801 S. Plymouth Ct. #L
Chicago, Illinois 60605,

Respondents.

CFTC Docket No: 01-20

Administrative Law Judge
Bruce C. Levine

ORDER MAKING FINDINGS AND IMPOSING REMEDIAL SANCTIONS

I.

On August 20, 2001, the Commission filed a Complaint and Notice of Intent to Condition, Suspend, Revoke, or Restrict Registration and Notice of Hearing Pursuant To Sections 6(c), 6(d) and 8a(4) of the Commodity Exchange Act, as Amended ("Complaint") against Excellent USA, Inc. ("Excellent USA") and John F. Gallwas. Without admitting or denying any of the allegations of the Complaint or the findings herein, Excellent USA and Gallwas acknowledge service of this Order Making Findings and Imposing Remedial Sanctions ("Order"). Excellent USA and Gallwas consent to the use of the findings herein in this proceeding and in any other proceeding brought by the Commission or to which the Commission is a party.¹

¹ Excellent USA and Gallwas do not consent to the use of the Offer or the findings in this Order as the sole basis for any other proceeding brought by the Commission, other than a proceeding brought to enforce the terms of this Order. Excellent USA and Gallwas also do not consent to the use of the Offer or the findings in the Order by any other person or entity in this or any other proceeding. The findings made in the Order are not binding on any other person or entity named as a defendant or respondent in this or any other proceeding.

II.

In order to dispose of the allegations and issues raised in the Complaint as to them, Respondents Excellent USA and Gallwas have each submitted an Offer of Settlement (“Offer”), which the Commission has determined to accept.

III.

The Commission finds that:

A. SUMMARY

Excellent USA, a registered futures commission merchant (“FCM”), and Gallwas, the managing director and registered associated person (“AP”) of Excellent USA, failed to supervise the handling of the foreign customer omnibus accounts of two Japanese firms, Excellent Inc. (“Excellent”) and Core Creation Inc. (“Core”) by Excellent USA’s employees. By such supervisory failures, Excellent USA and Gallwas failed to provide adequate customer protection to foreign retail customers who traded in the U.S. futures markets.

Excellent and Core staff solicited Japanese retail customers to place orders for individual futures trades on a U.S. futures exchange and collected margins for those individual trades. However, Excellent and Core did not transmit the orders as individual orders; instead, they combined different customer and house orders into spreads before relaying them to the U.S. for execution. This reduced the amount of margin they were required to post, and they kept the remaining margin collected from customers for their own uses. The simultaneously transmitted orders included some orders to buy and sell the same spreads. Each day’s orders, when totaled, resulted in each omnibus account being both long and short approximately the same number of futures contracts in each contract month. Such trading results are unusual and should have raised questions concerning the propriety of Excellent’s and Core’s trading. Despite the suspicious

nature of this trading, Excellent USA and its employees never inquired as to the customers' intent or made any inquiry into the trading at issue.

Gallwas, as the managing director of Excellent USA, was responsible for overseeing the day-to-day operation of Excellent USA and, thus, controlled Excellent USA. Gallwas did not establish a systematic and meaningful system for supervising the trading in the Excellent and Core customer omnibus accounts. Gallwas also was aware of the unusual trading by Excellent and Core but never questioned it. Excellent USA and Gallwas also never reconciled information provided by Excellent and Core with their knowledge of Excellent's and Core's business practices.

B. RESPONDENTS

Excellent USA, Inc. is an Illinois corporation that maintained its principal place of business at 141 W. Jackson Blvd., Suite 3706, Chicago, Illinois 60604-3201. Excellent USA has been registered with the Commission as an FCM since July 13, 1990, pursuant to Sections 4d and 4f of the Act. Excellent and Toshio Yokoyama, a Japanese citizen who was the managing director and chief executive officer of Excellent and a part owner of Core, the Japanese firms, are the principals of Excellent USA. Excellent USA ceased operating as an FCM in January 1998.

John F. Gallwas resides at 801 S. Plymouth Ct. #L, Chicago, Illinois 60605. He has been registered with the Commission as an AP pursuant to Section 4k(1) of the Act since at least 1982. During the relevant period of time, Gallwas was registered as an AP of Excellent USA and was the managing director of Excellent USA. Gallwas is currently registered as an AP of Striker Securities Inc.

C. FACTS

Excellent and Core were Japanese corporations with common ownership that were formed in 1987 and 1994, respectively. The two firms acted as brokerage firms offering trading opportunities in the U.S. commodities markets to retail customers in Japan. Excellent and Core solicited Japanese customers to place orders to buy or sell outright positions in futures contracts traded on the U.S. markets. Both firms collected margins from its customers for outright trades, representing to their customers that the firms had to send the full margin to the U.S. However, Excellent and Core combined their customers' orders into spreads before relaying them to the U.S. for execution, in order to minimize the amounts of money they were required to send to their clearing firm to margin the trades. Excellent and Core kept the balance in Japan and used the funds to pay the firms' operating expenses and to support the extravagant lifestyle of Yokoyama, the common owner. By February 29, 2000, Japanese criminal authorities had convicted and sentenced the principals of Core, including Yokoyama, of cheating unsophisticated customers by churning their accounts, setting up false trades against the trades ordered by customers and misappropriating customer margin funds.

Excellent, at the suggestion of Gallwas, established Excellent USA as a non-clearing FCM in the U.S. to process its orders through an omnibus account in July 1990. From 1994 until January 1998, Excellent USA cleared the Excellent and Core accounts through Lincco Futures Group (Lincco") and its successor, LFG, L.L.C. ("LFG"). Between March 1994 and January 1998, Excellent and Core placed their orders by faxing an order sheet to Excellent USA overnight instructing it to place orders to buy or sell spreads in the Chicago Board of Trade ("CBOT") grain contracts. Each morning, Excellent USA staff retrieved the overnight orders

from their fax machine, recorded the orders on office tickets and called the orders to the LFG desk on the floor of the CBOT. A floor broker, who was an officer of Excellent USA, filled the Excellent and Core orders on most trading days.

Both Excellent and Core regularly entered various spread orders, including simultaneously entered orders to buy or sell the same spread, that resulted in both omnibus accounts holding almost equal and offsetting positions in each futures month. Excellent USA accepted these orders from Excellent and Core without seeking any clarification of the customers' intent.

Excellent USA received a daily equity run showing that the omnibus accounts held almost equal and offsetting open positions in each futures month. Excellent USA staff reviewed the daily equity run every day for accuracy, but never questioned Excellent or Core about the almost equal and offsetting open positions in each futures month in the omnibus accounts even though the trading had the appearance of wash sales.

Gallwas, as managing director of Excellent USA, was responsible for supervising the employees of Excellent USA. Excellent USA staff reported to Gallwas. He was responsible for hiring staff, and all of the staff he hired were his children or their spouses. Gallwas was ultimately responsible for all regulatory compliance. He failed to maintain an internal system to monitor the trading in the Excellent and Core omnibus accounts. The Excellent and Core accounts constituted most of the business handled by Excellent USA, and Gallwas was aware of the trading in those accounts. Nevertheless, Excellent USA and Gallwas failed to question the trading and had no system in place whereby Excellent USA employees could monitor the trading in the omnibus accounts.

The full extent of Excellent USA's supervision of the trading in the omnibus accounts consisted of a compliance questionnaire which Gallwas and Excellent USA, at irregular intervals, sent to Excellent and Core to obtain information about their customers and business operations. The compliance questionnaire never asked Excellent or Core about the rationale for the trading that resulted in the omnibus accounts of both firms holding almost equal and offsetting open positions in each futures month. Excellent USA and Gallwas never reconciled the apparent discrepancies between the questionnaire responses and their knowledge of Excellent's and Core's business practices. For instance, Gallwas and Excellent USA failed to question Excellent's July 1997 questionnaire response reporting that it had only two customer complaints. This response was suspect because, in March 1997, Yokoyama told Gallwas that customer complaints at Excellent were worse than he expected and that he intended to "wind down" Excellent and "wind up" Core.

IV.

LEGAL DISCUSSION

Commission Regulation 166.3 imposes on registrants an affirmative duty to "diligently supervise the handling by its ... officers, employees and agents (or persons occupying a similar status or performing a similar function) ... of all commodity interest accounts carried, operated, advised or introduced by the registrant and all other activities of its ... employees and agents ... relating to its business as a Commission registrant." "Failure to supervise is an independent and primary violation of the Commission's rules." *In re Paragon Futures Assn.*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,266 (CFTC April 1, 1992). One can violate Regulation 166.3 even if there is no underlying violation of the Act. *In re First National Trading Corporation ("FNTC")*, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH)

¶ 26,142 at 41,786 (CFTC July 20, 1994) (“In appropriate circumstances, proof of an independent substantive violation is not a necessary element to establish a breach of the duty imposed by Rule 166.3”), *aff’d without op.*, *Pick v. CFTC*, No. 95-3761 (6th Cir. Oct. 26, 1996).

Gallwas was a controlling person of Excellent USA pursuant to Section 13(b) of the Act. As such, he may be held liable for the violations attributable to Excellent USA. Controlling person liability exists pursuant to Section 13(b) of the Act for one who directly or indirectly controls any person who has violated any provision of the Act (or the regulations promulgated thereunder) and who either acted with a lack of good faith or knowingly induced the acts that constitute the violation. Gallwas is liable as a controlling person because he controlled Excellent USA and acted with a lack of good faith. *Monieson v. CFTC*, 996 F.2d 852, 859 (7th Cir. 1993).

A controlling person acts with a lack of good faith if he fails to maintain a reasonably adequate system of internal supervision and control or fails to enforce that system with reasonable diligence. *Monieson v. CFTC*, 996 F.2d at 860. Gallwas’ lack of good faith is evidenced by both his failure to put an adequate system of supervision in place and his lack of diligence in following up on the information he had about Excellent’s and Core’s business practices.

Excellent USA and Gallwas, individually and as a controlling person, failed to supervise the handling of the Excellent and Core commodity accounts by Excellent USA employees in that Excellent USA employees routinely accepted simultaneous orders from the two customers making up the vast majority of the firm’s business without making any inquiry about the intent of the ultimate customer. This unusual trading pattern occurred virtually every trading day between July 1996 and January 1998. An employee of Excellent USA filled the simultaneously entered orders at the CBOT and reported the filled trades to Excellent and Core each day.

An FCM has a duty not to accept or transmit orders for transactions that demonstrate an intent to avoid a bona fide market position. *In re Three Eight Corporation*, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,749 at 40,445 (CFTC June 16, 1993). In *Three Eight*, the Commission found that the receipt of paired orders for matching executions demanded clarification before execution. *Id.* at 40,446. The Commission recently reaffirmed this principle in *In re Piasio*, [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 28,276 at 50,689 (CFTC September 29, 2000) (account executive has a duty to inquire about customer's intent when he receives simultaneous orders to buy and sell the same spread). While both *Three Eight* and *Piasio* dealt with liability for wash sales, they also set out a standard that is applicable in evaluating FCM supervision of other improper trade practices. In this case, the orders were sufficiently unusual that Excellent USA and Gallwas should have sought clarification from Excellent and Core regarding the intent or rationale behind the trades.

Excellent USA and Gallwas also missed or disregarded other red flags suggesting a problem with the trading by Excellent and Core. Excellent USA and Gallwas failed to reconcile information reported by Excellent and Core in the compliance questionnaires with their knowledge of Excellent's and Core's business. By disregarding the red flags raised by the information available to it, Excellent USA and Gallwas failed to provide meaningful customer protection to foreign retail customers and thereby violated Regulation 166.3. As previously discussed, Gallwas is liable for this failure to supervise both individually and as a control person of Excellent USA.

V.

OFFER OF SETTLEMENT

Excellent USA and Gallwas have each submitted an Offer of Settlement in which they neither admit nor deny the findings in the Order. Subject to the foregoing, Excellent USA and Gallwas: acknowledge service of this Order and admit the jurisdiction of the Commission with respect to the matters set forth in this Order; waive (1) a hearing and all post-hearing procedures, (2) judicial review by any court, (3) any objection to the staff's participation in the Commission's consideration of the Offer, (4) all claims that they may possess under the Equal Access to Justice Act, 5 U.S.C. § 504 (1994) and 28 U.S.C. § 2412 (1994), as amended by Pub. L. No. 104-121, §§ 231-232, 110 Stat. 862-63, and Part 148 of the Commission's Regulations, 17 C.F.R. §§ 148.1, et seq. (2001), relating to, or arising from this action, and (5) any claim of double jeopardy based upon the institution of this proceeding or the entry in this proceeding of any order imposing a civil monetary penalty or any other relief.

Excellent USA and Gallwas stipulate that the record basis on which the Order is entered consists of the Order and the findings in the Order consented to in the Offer. Excellent USA and Gallwas consent to the Commission's issuance of this Order, which makes findings as set forth herein and orders that: (1) Excellent USA comply with its undertaking as set forth in the Offer and incorporated in this Order²; and (2) Gallwas cease and desist from violating Commission Regulation 166.3, that his registration as an associated person be suspended for a period of six (6) months, that he pay a civil monetary penalty of \$65,000, and that he comply with his undertaking as set forth in the Offer and incorporated in this Order.

² Because an Order is being entered *in In re Excellent USA, Inc.*, Docket No. SD 01-01 on this same date, revoking Excellent USA's registration as an FCM, no other remedial sanctions are being entered against Excellent USA in this matter.

VI.

FINDING OF VIOLATIONS

Solely on the basis of respondents' consent, as evidenced by the Offer, and prior to any adjudication on the merits, the Commission finds that Excellent USA and Gallwas violated Commission Regulation 166.3, 17 C.F.R. § 166.3 (2001).

VII.

ORDER

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

1. Gallwas shall cease and desist from violating Commission Regulation 166.3;
2. Gallwas' registration with the Commission as an AP shall be suspended for a period of six months commencing on the third Monday after the date of this Order;
3. Gallwas shall pay a civil monetary penalty ("CMP") in the amount of \$65,000 within ten (10) business days of the date of this Order. Gallwas may make such payment by electronic funds transfer to the account of the Commission at the United States Treasury or by certified check or bank cashier's check made payable to the Commodity Futures Trading Commission and addressed to Dennese Posey, or her successor, Division of Trading and Markets, Commodity Futures Trading Commission, 1155 21st Street, N.W., Washington, D.C. 20581, under cover of a letter that identifies Gallwas and the name and docket number of this proceeding. A copy of the cover letter and of the form of payment shall be simultaneously transmitted to Director, Division of Enforcement, Commodity Futures Trading Commission, 1155 21st St., N.W. Washington, D.C. 20581. In accordance with Section 6(e)(2) of the Act, 7 U.S.C. § 9a(2), if Respondent fails to make payment of his penalty within fifteen (15) days of the due date, he shall be automatically prohibited from trading on or subject to the rules of any

registered entity as defined in Section 1a(29) of the Act, 7 U.S.C. § 1a(29), and his registration suspended, until he shows to the satisfaction of the Commission that payment of the full amount of the penalty with interest thereon to the date of payment has been made; and

4. Neither Excellent USA, Gallwas nor any of their agents or employees acting under their authority or control shall take any action or make any public statement denying, directly or indirectly, any allegation of the Complaint, finding or conclusion in the Order, or creating or tending to create the impression that the Order is without a factual basis; provided, however, that nothing in this provision affects (i) the testimonial obligations of Excellent USA or Gallwas, their employees or agents; or (ii) their right to take legal positions in other proceedings to which the Commission is not a party.

The provisions of this Order shall be effective on this date, unless otherwise specified.

By the Commission:

Jean A. Webb
Secretary to the Commission
Commodity Futures Trading Commission

Dated: February 4, 2002