Manipulation of Commodity Futures Prices—The Unprosecutable Crime

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The commodity futures market has been beset by large-scale market manipulations since its beginning. This article chronicles these manipulations to show that they threaten the economy and to demonstrate that all attempts to stop these manipulations have failed. Many commentators suggest that a redefinition of "manipulation" is the solution. Markham argues that enforcement of a redefined notion of manipulation would be inefficient and costly, and would ultimately be no more successful than earlier efforts. Instead, Markham argues for a more active Commodity Futures Trading Commission empowered not only to prohibit certain activities which, broadly construed, constitute manipulation, but also to adopt affirmative regulations which will help maintain a "fair and orderly market." This more powerful Commission would require more resources than the current CFTC, but Markham argues that the additional cost would be more than offset by the increased efficiencies of reduced market manipulation.

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Introduction

The Commodity Futures Trading Commission (“CFTC”) was created in
1974 as part of a congressional effort to regulate the trading of commodity
futures contracts more effectively and to prevent the large scale price manipu-

   In brief, a futures contract provides for the buyer (the “long”) to purchase and the seller (the
   “short”) to sell a specified quantity of a specified commodity at a specified future date. Futures contracts
   are standardized, permitting them to be offset on the exchanges. For example, a trader holding a short
   contract could enter into an offsetting long contract and thereby cancel out the initial obligation. To do so,
   however, requires that the offsetting contract provide for delivery in the same delivery month as the initial
   contract. Most futures contracts are settled by offset. Cash settlement may also be used in some futures
   contracts, particularly financial futures contracts on stock indexes. Because futures contracts are standardized,
   the only negotiable term is the price which is set by an auction process on the floor of the futures exchanges.
   See generally Ryder Energy Distribution v. Merrill Lynch Commodities, 748 F.2d 774 (2d Cir. 1990)
   (discussion of futures trading); Katara v. D. E. Jones Commodities, 835 F.2d 966 (2d Cir. 1987) (same);
   Leist v. Simplot, 638 F.2d 283, 286-88 (2d Cir. 1980), aff’d sub nom. Merrill Lynch, Pierce, Fenner &
   975, 93d Cong., 2d Sess. 149 (1974); CFTC, SEC AND FEDERAL RESERVE BOARD, A STUDY OF THE
   EFFECTS ON THE ECONOMY OF TRADING IN FUTURES AND OPTIONS, Ch. II, at 1 (1984) (same); II TREASURY
   DEPARTMENT / FEDERAL RESERVE BOARD STUDY OF TREASURY FUTURES MARKETS, Ch. 1, at 9-14 (1979)
   (description of futures trading), CHICAGO BOARD OF TRADE, COMMODITY TRADING MANUAL 10 (1982)
   (same) [hereinafter COMMODITY TRADING MANUAL; F. HORN & V. FARAH, TRADING IN COMMODITY
   FUTURES 7-9 (1979) (same); P. JOHNSON, COMMODITIES REGULATION § 1.10 (1982) (same) [hereinafter
   COMMODITIES REGULATION].

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The topic of manipulation in commodity futures trading has been a concern for over a century. Congressional concern with price manipulation and abuses did not lessen as a result of the creation of the CFTC. To the contrary, events such as the Silver Crisis of 1980, the Stock Market Crash of 1987 and the battle in the soybean pit in 1989 between Ferruzzi Finaziaria S.P.A. and the Chicago Board of Trade have continued to give rise to concerns that futures markets are susceptible to manipulation and price distortion. These concerns are very real because under present law the crime of manipulation is virtually unprosecutable, and remedies for those injured by price manipulation are difficult to obtain. Moreover, even where a prosecution is successful, the investigation and effort necessary to bring a case will involve years of work, enormous expenditures, as well as an extended trial.

Manipulation in the commodity futures market takes many forms. Prices may be manipulated through rumors or false information conveyed into the marketplace. Prices may also be manipulated through rigged trades or through "capping" or "pegging," by which market prices are set at artificial levels, for margin purposes, price setting and other reasons. But the most significant form of manipulation, and the one of greatest concern, is the market power manipulation. This type of manipulation requires large resources. The trader in such a manipulation is buying so many futures contracts and such large quantities of the underlying commodity that its market power is sufficient to create and sustain a manipulated or artificial price. One type of market power manipulation is the so-called "corner." Here the trader has control of all or virtually all of the available supplies of the commodity that underlie the futures contracts held by the trader. In such a case, the sellers or "shorts" must pay prices dictated by the trader controlling the supply of the commodity. Another form of market power manipulation is the "squeeze" in which the trader acquires

2. As will be discussed below, manipulations may take many forms, but the standard imposed by the government in determining their existence is whether: (1) a trader had the ability to influence market prices; (2) the trader specifically intended to do so; (3) an artificial price resulted; and (4) the trader caused the artificial prices. In re Cox [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,786 (C.F.T.C. 1987).

3. See discussion, infra notes 23-44 and accompanying text.

4. See discussion, infra notes 370-474 and accompanying text.

5. See discussion, infra notes 593-96 and accompanying text.

6. The purpose of this type of manipulation is to move futures prices for a brief period in order to affect the posted opening or closing prices. See Hearings on Russian Grain Transactions, Hearings Before The Senate Permanent Subcommittee on Investigations of the Committee on Government Operations (Part 1), 93d Cong., 1st Sess. 166 (1973) [hereinafter Hearings on Russian Grain Transactions]. It has been stated that this type of manipulation is very difficult to detect and prove. "It involves heavy trading, usually concentrated on the opening or closing of the market." Id.

7. This type of manipulation results in "an unnatural relationship between futures prices and cash prices." Such manipulation also "tends to draw the cash commodity to ... delivery points in unusual amounts" and takes "the commodity out of its normal channels of movement from producer to consumer." This frequently results in an oversupply of the commodity at the exchange delivery point and an undersupply at other points of distribution. Hearings on Russian Grain Transactions, supra note 6, at 164-65.
a large futures position in a situation where there is a shortage of the underlying commodity, thereby moving prices to a level dictated by the squeezer.\footnote{8}

Each type of manipulation, whether market power, rumor, or rigged trading practice, involves a common goal. The trader is seeking to create an artificial price by which he will profit. But here lies the rub: it is virtually impossible to determine what constitutes an artificial price. Prices fluctuate constantly in the futures markets. Indeed, futures contracts are selected for trading on commodities that have volatile prices. There is, therefore, no level of price that can be said to be a typical benchmark, non-artificial or “true” price. Instead, market conditions, which vary daily, or even by the minute, will determine the actual economic price of the commodity. Consequently, the determination of the “true” economic price will turn on an after-the-fact economic analysis of the price a willing buyer and a willing seller would have paid in the absence of the manipulation. But this economic analysis is so complicated and affected by so many factors that it is often impossible to determine what the “true” price was. Further complicating the issue, the government and the courts have engrafted an intent requirement onto the prohibition against manipulation, requiring a showing that the trader intended to create an artificial price. As a result, few prosecutions against manipulators have been brought, despite the fact that this prohibition is the centerpiece of the regulatory scheme. Moreover, even when prosecutions are brought, only rarely are significant sanctions imposed upon those found to have engaged in manipulation.\footnote{9}

This article will argue that if manipulation is to be effectively prevented and prosecuted under the Commodity Exchange Act, the Act must be amended and the CFTC must take a more affirmative role in regulating the futures markets. It must increase its surveillance functions and detect at an early point in time whether traders, either hedgers or speculators, may pose a threat to the market place. If such occurs, the CFTC should move affirmatively to require large traders to reduce their positions or even remove themselves from the market. In contracts where this is a frequent occurrence, the exchanges would then have an incentive to not only consider preventive measures but to also require or allow cash settlement in the contract so that such problems do not become an everyday occurrence.

In addition, the CFTC needs the authority to promulgate regulations that require traders on the floors of the exchanges to maintain a “fair and orderly” market. The CFTC needs to promulgate specific rules declaring certain practices to be manipulative, and it should adopt regulations that assure the goal of a fair

\footnote{8} A squeeze is a lesser form of a corner. Here the manipulating trader does not own the entire supply of a commodity, but he does control enough to create a shortage and thereby “squeeze” prices up. Such a squeeze may be intentionally created or it may result from a natural shortage that traders seek to exploit. The latter event is frequently referred to as “congestion.” See, e.g., REPORT OF THE CHIEF OF THE COMMODITY EXCHANGE ADMINISTRATION 40 (Sept. 25, 1939).

\footnote{9} See Appendix.
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and orderly market. This could include prohibitions against trading practices of short traders that have the effect of "hammering" or "bearing" the market by prolonged and excessive short sales that drive market prices down to artificial levels.\(^\text{10}\) The CFTC also needs to establish requirements governing trading on the exchanges to assure that prices are not being rigged, and it must act more aggressively in detecting those who are spreading false rumors. In addition, the CFTC must be more affirmative in seeking injunctive relief and declaring emergencies where the market is in any way threatened by a trader's activities. More specific regulations should also be adopted so that criminal and civil prosecutions may be more effectively brought.

In particular, Part I of this article will review early commodity price manipulations and early unsuccessful federal legislative efforts to stop manipulations. Part II describes the background of the prohibition against manipulation, and the many subsequent encounters by the government with large traders that have disrupted the markets. This part also examines unsuccessful legislative efforts to deal with manipulation in 1968. Part III reviews the overhaul of the Commodity Exchange Act in 1974, which created the CFTC to deal with manipulation and other disruptive market activities. It then traces the many unsuccessful encounters that the CFTC has with manipulation, and describes how the CFTC has effectively nullified the manipulation prohibition. Part IV examines the various theories of commentators on how to define manipulation in order to make its prohibition effective and why those efforts are inadequate to deal with the problem. Part IV then proposes the adoption of legislation and administrative actions that will require a "fair and orderly" market. Under this proposal the government will be able to prevent manipulative and disruptive trading activities without having to undergo the considerable expense and often fruitless effort to prove what is now a virtually unprovable offense.

I. Historical Manipulation in the Commodity Futures Markets

A. The Growth of Commodity Futures Trading and Its Role

The growth of commodity futures contracts in the last thirty years has been explosive. The Futures Industry Association points out that the volume of futures trading in 1960 was 3.9 million contracts.\(^\text{11}\) By 1970, that volume had increased to 13.6 million contracts and by 1980 to some 92 million contracts.\(^\text{12}\) By 1988, volume had risen to almost 250 million contracts.\(^\text{13}\) This growth was

10. "Hammering" or "bearing" the market means that the market is drawn downward by repeated and heavy short sales.
12. Volume of Futures Trading, supra note 11.
13. This increased volume has carried into 1990. Trading Volume, supra note 11.
due in large measure to changes in monetary policy and inflation during the 1960s and 1970s that caused dramatic increases in commodity prices and which resulted in the development of numerous new financial futures contracts. Trading volume in these financial futures increased to forty-two million contracts in 1982, up from some twenty-nine million contracts a year earlier and only some four million contracts five years before. By 1988, the growth in financial futures trading had expanded even more dramatically to over 180 million contracts. Trading in financial futures has now far outstripped the number of agricultural commodity futures, which traded only some 60 million contracts in 1988.

Although many concerns have been raised about commodity futures trading, futures contracts serve the desirable function of allowing hedging and price discovery. Hedging occurs where, for example, a portfolio manager with a widely diversified portfolio is concerned that the market will drop. He has the alternative of selling his portfolio and avoiding a loss. But to do so would require enormous transaction costs, and large losses may be suffered when other traders realize that a large portfolio is being dumped. Alternatively, the portfolio manager could enter into a futures contract on an S&P stock index which would offset the loss in the portfolio. Should the market drop as expected, the portfolio manager would experience profits in the futures contract that would offset losses on the actual portfolio. Conversely, if the market went up, the portfolio

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would forego any gains because the gains in the increased value of the portfolio would be offset by losses on the futures contract.\textsuperscript{18}

Price discovery is another important function of futures contracts. Price discovery allows investors to know, at any given time, the value of a commodity by simply looking at the prices on a board of trade. This price discovery function has traditionally been quite important in agricultural markets where farmers look at exchange prices to determine the value of their livestock or crops.\textsuperscript{19} Today, financial futures contracts are also serving a price discovery function. That is, the futures contracts are often valuing the underlying financial instruments.\textsuperscript{20}

In order to aid price discovery and hedging functions, the Commodity Exchange Act and the CFTC recognize that speculation and speculators play a valuable role in the market. They provide liquidity to offset hedging risks and bring information into the market to assure that price discovery is efficient.\textsuperscript{21}

The Commodity Exchange Act, however, seeks to curb "excessive" speculation...
and to prevent manipulations that create artificial prices and impair the price discovery and hedging functions of the futures markets.22

B. Early Manipulations

Commodity futures trading has a long history,23 but its development in the United States can be traced to the end of the Civil War when, at the Chicago Board of Trade,24 contracts for the delivery of grain were converted into transferable contracts that often were used to offset each other.25 Speculators soon learned that these contracts offered opportunities to engage in manipulative activities as well as speculation.26 Corners and squeezes became widespread and manipulators became veritable legends as witnessed by the story of Joe Leiter, a Harvard graduate who attempted unsuccessfully to corner the wheat market. His corner was broken when a fleet of boats hired by P. D. Armour

22. Section 3 of the Commodity Exchange Act states that futures transactions are: "affected with a national public interest . . . . The transactions and prices of commodities on such boards of trade are susceptible to excessive speculation and can be manipulated, controlled, cornered or squeezed . . . . rendering regulation of such transactions imperative for the protection of such commerce and the national public interest." 7 U.S.C. § 5. For the background of this provision see, Stassen, Propaganda As Positive Law: Section 3 of the Commodity Exchange Act (A Case Study Of How Economic Facts Can Be Changed by Act of Congress), 58 CHI. KENT L. REV. 635 (1982).

23. Although this article focuses on manipulation issues arising from the futures style trading that developed in the United States in the mid 1860's, problems with manipulation of "actual" or "cash" commodities has had a much longer history. One author has even traced efforts to control cash manipulations back to ancient Rome and Greece. Van Smith, Preventing the Manipulation of Commodity Futures Markets: To Deliver or Not to Deliver?, 32 HASTINGS L.J. 1569, 1571 (1981). During the sixteenth century, England also prohibited certain cash manipulation practices such as "engrossing," which was analogous to a modern corner, and "forestalling," where commodities were purchased and held off the market. Id.; See also, III L. Loss, SECURITIES REGULATION, 1535 note 17 (2d ed. 1961); Mason, Monopoly in Law and Economics, 47 Yale L.J. 34, 34-39 (1937). The latter practice, "forestalling," caused a near crisis during the Revolutionary War in America when goods were held from the market in Philadelphia in order to obtain higher prices from the French when they entered the war. See W. RANDALL, BENEDICT ARNOLD: PATRIOT AND TRAITOR 478 (1990). In fact, the problem became so troubling that George Washington lamented, "Virtue and patriotism are almost extinct. Stock-jobbing, speculating, engrossing seem to be the great business of the multitude." C. HIBBERT, REDCOATS AND REBELS: THE AMERICAN REVOLUTION THROUGH BRITISH EYES 258 (1990) (emphasis supplied).

24. The Chicago Board of Trade plays a significant role in the country's economy. But this has not always been the case. "Organized in 1848 . . . [The Chicago Board of Trade] struggled for existence for several years and among other things it attempted to stimulate attendance by offering a free lunch to members." H. IRWIN, EVOLUTION OF FUTURES TRADING 80 (1954)

25. These contracts, which were first known as "to arrive" or "time" contracts, were used for the delivery of grain to terminal markets such as Chicago. By the 1860s, such contracts were themselves traded on exchanges and became the subject of speculation. These "to arrive" contracts were later replaced by standardized futures contracts on the Chicago Board of Trade. G. HOFFMAN, HEDGING BY DEALING IN GRAIN FUTURES 15 (1925); G. HOFFMAN, FUTURE TRADING UPON ORGANIZED COMMODITY MARKETS IN THE UNITED STATES 29, (1932) [hereinafter ORGANIZED COMMODITY MARKETS]; see also 5 Fed. Trade Comm'n, Report on the Grain Trade 27, 52 (1921) [hereinafter FTC STUDY]; 2 FTC STUDY at 108-109 (1920); T. Hieronymus, Economics of Futures Trading 72-76 (2d ed. 1980) [hereinafter Economics of Futures Trading]; Commodity Exchange Admin., Trading in Commodity Futures 2 (1938) [hereinafter Trading Commodity Futures]; Evolution of Futures Trading, supra note 24, at 70-87.

26. "Speculation in futures contracts reached such vast proportions during the Civil War that the Chicago Board of Trade in 1865 adopted rules recognizing trading in grain futures as a distinct commercial practice." Trading Commodity Futures, supra note 25, at 3.

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broke through the ice on Lake Michigan and flooded the Chicago markets with grain.\(^{27}\) Another even more famous corner of the gold market by Fisk and Gould became a legend in American history.\(^{28}\)

By 1868 there was a corner a month,\(^{29}\) and these manipulations continued into the twentieth century.\(^{30}\) In 1902, for example, James A. Patten made a two million dollar profit in a wheat squeeze in which he pushed prices from $1.00 a bushel to a $1.34.\(^{31}\) Another famous manipulator was Jesse Livermore, whose corners included the purchase of 120,000 bales of cotton in 1908. In order to inflate the value of his purchases, he planted a front page article in a New York newspaper that stated that Livermore had cornered July cotton, causing speculators to rush in and buy cotton in order to jump on his bandwagon. The result was even larger profits for Livermore.\(^{32}\) The market later turned on Livermore, however, and he lost his fortune.\(^{33}\) But “King Jack”

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27. As one report stated with respect to Leiter’s action:
   On paper the market was cornered. Instead of settling contracts at the price Leiter demanded, sellers began to deliver actual wheat. The Northwest scraped its graneries. Russia ate rye and emptied its mill-bins of wheat. Argentine swept the floor .... Armour kept steel-prowed tugs plowing up the ice at the end of the Lakes, and by lake, and rail moved 6,000,000 bushels from Minnesota and the Dakotas to Chicago in mid-winter.


28. M. KLEIN, THE LIFE AND LEGEND OF JAY GOULD 99-115 (1986) (“... the most audacious speculation yet witnessed in Wall Street: an attempt to corner ... the entire gold supply of the nation.”); See H.R. REP. No. 31, 41st Cong., 2d Sess. (1870); K. ACKERMAN, THE GOLD RING (1988). See generally ORGANIZED COMMODITY MARKETS, supra note 25, at 364-65; Paul, The Past and Future of The Commodities Exchanges, 56 AGRIC. HIST. 287, 300, n.7 (1982); Peterson, Futures Trading With Particular Reference to Agricultural Commodities, 7 AGRIC. HIST. 68-9 (1933); The Exchanges And Speculation, supra note 27, at 378-79; PLUNGERS, supra note 27, at 63; Legislation Against “Short” Selling at Home and Abroad, 1st Hist. 1919 Cong. Dis. 290, 290-291 (1932). This was not the only attempt to manipulate the gold market. For example, J. Pierpont Morgan tried to use the “infamous ‘gold room’” on Wall Street to rig the market during the Civil War “by shipping out a large amount of gold on a steamer and earned $160,000 in the process.” R. CHERNOW, THE HOUSE OF MORGAN: AN AMERICAN BANK DYNASTY AND THE RISE OF FINANCE 22 (1990).

29. 1 HISTORY OF BOARD OF TRADE, supra note 27, at 370; ORGANIZED COMMODITY MARKETS, supra note 25, at 31-32 (1932); 2 FTC STUDY, supra note 25, at 110; J. BOYLE, supra note 27, at 64 (1920). These corners began to receive great publicity and were often given names that identified the large traders perpetrating them. One such example was the Chandler oat corner of 1872. 2 HISTORY OF BOARD OF TRADE, supra note 27, at 452-456.


32. Id. at 46-47.

33. Id. at 47. Livermore and Arthur Cutten, another famous manipulator, engaged in a classic battle in the wheat pit in 1924. Cutten won this match by squeezing the price of wheat to over two dollars and
Sturges,34 Benjamin Hutchinson,35 "Crazy Harper"36 and others37 still vied to place themselves in the headlines as "wheat kings," and Chicago became a veritable Valhalla of these anti-heroes.38


34. II HISTORY OF BOARD OF TRADE, supra note 27, at 503-04. Sturges cornered the corn market in July of 1874. He then changed to the short side of the market and was himself caught in a corner of September corn. Sturges refused to meet his obligations, resulting in his expulsion from the Board of Trade. However, he was later reinstated. Id.; J. Lurie, The Chicago Board of Trade 1874-1905, at 41-42 (Mar. 25, 1970) (unpublished dissertation) (available at the University of Wisconsin).

35. Hutchinson was credited with the first important corner in the wheat pit in 1866, and he dominated the wheat market until the late 1880s. PLUNGERS, supra note 27, at 10-12, 48; SPECULATION, supra note 27, at 69; McFarland, The Ingalls Amendment to the Sherman Anti-Trust Bill, 11 KANSAS HIST. Q. 173 (1942) [hereinafter Ingalls Amendment]; 23 CONG. REC. 5983 (1892) (remarks of Sen. Washburn) (Hutchinson was credited with one of the largest trades ever made during the early period of futures trading, i.e., a 1 million bushel sale of wheat); M. Wilson, supra note 30, at 18 (1932). Hutchinson was himself modest about his ability to influence the market, stating that

the market price is the universal price all over the world on any given day, and no man or combination of men can stand up against it. They may take measures to influence it, but they cannot positively control it. It is too mighty, too immense. We can influence the water-power of Niagara; but let us find the man or men who can stop the cataract.

Hutchinson, Speculation in Wheat, 153 N. AM. REV. 414 (1891).

36. Harper, a former sewing machine salesman who became a banker in Cincinnati, backed a group attempting to corner the wheat market. In so doing, he used money that he had obtained illegally from his bank. Wheat prices plummeted after the failure of his corner, and Harper was later sentenced to ten years in prison. M. Wilson, supra note 30, at 18; II HISTORY OF BOARD OF TRADE, supra note 27, at 751-758; PLUNGERS, supra note 27, at 92-108; Ingalls Amendment, supra note 35, at 173.

37. For a description of still other manipulators, see II HISTORY OF BOARD OF TRADE, supra note 27, at 621, 626-627 (description of a "Cincinnati clique"). See also 23 CONG. REC. 5985 (1892) (remarks of Sen. Washburn); Kolb & Spiller, Manipulation of Futures Markets: An Overview 19-26 (Oct. 1990), (unpublished paper presented at a conference on Law, Economics and Public Policy, in Washington, D.C. on Nov. 8-9, 1990); H.R. REP. No. 969, 52d Cong., 1st Sess. 9 (1892) (discussion of Ed Pardridge and "the Chicago bear ring") that "finally succeeded in creating panic throughout the world."); 23 CONG. REC. 6710 (1892) (Pardridge made $500,000 on a single day's trading); CONG. REC. 5983 (1892) (Pardridge reported as being short 10,000,000 bushels of wheat); Chicago Inter-Ocean, Mar. 12, 1892, noted in BOARD OF TRADE AND THE FEDERAL GOVERNMENT, supra note 27, at 112 (Pardridge was "without doubt the heaviest trader on the short side this world has ever seen."); He traded in millions of bushels. Still another great speculator was Leopold Bloom who claimed that "he had made a clean million dollars" before retiring from the business. Id. at 113. Similarly, James A. Patten became famous for his corner of the cotton market. J. BOYLE, supra note 27, at 71-73; see United States v. Patten, 266 U.S. 525 (1930). Patten was accused by Harpers Weekly of being "The Man Who Raised The Price of Bread." HARPERS WEEKLY, May 1, 1909, at 1; Hearings On H.R. 24073 Before the Comm. On Agriculture, 61st Cong., 2d Sess. 20-22 (1910); L. Kendall, supra note 27, at 136-138.

38. "The feats of Leiter, Armour, Patten, and others in cornering the markets are legends of American commerce." L. Kendall, supra note 27, at 204 (author notes, however, that these legends may have grown out of proportion). See also 23 CONG. REC. 5985 (1982) (remarks of Sen. Washburn) ("the recent corner in corn, the Harper corner and the Hutchinson corner, each afford abundant proof that [the commodity exchange] furnishes a market the very reverse of stable, as regard demand or prices; on the contrary, it furnishes a market that is affected by every base rumor, as well as one where fluctuations are abnormally wide, rapid, and frequent, and such as were never dreamed of before").

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These “play boys of speculation” arousing much populist animosity and much congressional ire. Nevertheless, repeated efforts to impose federal controls over futures trading in the late 1800’s and the turn of the century all failed. One such effort, the “Hatch Act,” passed both houses but failed in the Conference Committee. Similarly doomed to failure was an effort to include provisions in the Sherman Anti-Trust Act that would have applied to commodity futures trading. Theodore Roosevelt also sought to curb large short sales that were disrupting the markets. He stated that there “should be measures taken to prevent at least the grosser forms of gambling in securities and commodities, such as making large sales of what men do not possess and

39. “There was a time when the Hutchinsons and the Leiters, and the other so-called ‘playboys’ of speculation, used these public market places as a stage in which to parade their power over prices. They were the market leaders. Their operations churned the markets up and down without regard to fundamental conditions. Followers were attracted by the thousands — suckers, and many uninformed, who made no appraisal of supply and demand, gambled on what the market leaders would be able to do.” Mehl, Federal Regulation of Futures Trading, 4 FED. B.A.J. 195 (1941).

40. Between 1880 and 1920, some 200 bills were introduced to Congress to regulate futures trading. Federal Regulation, supra note 17, at 832 note 46; Organized Commodity Markets, supra note 25, at 365. Congressmen were concerned with the “artificial” prices that were appearing on the exchanges. 23 CONG. REC. 5982, 5984 (July 11, 1892) (remarks of Sen. Washburn). See also 23 CONG. REC. 6710 (July 25, 1892); H.R. REP. No. 969, 52d Cong., 1st Sess. 9 (1892); S. REP. No. 787, 53d Cong., 3d Sess. 103 (1894) (“farm prices of wheat are injuriously affected by the business commonly known as dealing in ‘options and futures.’ This report was also of the view that this business should ‘be abolished and prohibited under heavy penalties. It ought to be made a felony and punished by imprisonment.’”). H.R. REP. No. 975, 93d Cong. 2d Sess. 34 (1974).

41. The Hatch Act was passed by both houses of Congress in the 1890s. But the bills passed by each house varied in their terms. Although the Conference Committee approved a reconciliation, the House did not have time to approve passage of the bill before Congress went into recess. H.R. 7845, 52nd Cong., 1st Sess. (1892). The bill did not achieve passage thereafter. 23 CONG. REC. 2910 (1892); Rainbolt, Regulating the Grain Gambler And His Successors, 6 HOUSTON L. REV. 1, 6 (1977) [hereinafter Regulating The Grain Gambler]; The Chicago Board of Trade, supra note 34, at 105-106, 131-163. See also H.R. REP. No. 845, 53d Cong., 2d Sess. (1894); H.R. REP. No. 969, 52d Cong., 1st Sess. (1892); CONG. REC. 706 (Jan. 20, 1893); H.R. REP. No. 845, 53d Cong., 1st Sess. (1892); C.C. COWING, POPULISTS, FLUNGEES AND PROGRESSIVES 4-6 (1965); J. Lurie, Speculation, Risk and Profits: The Ambivalent Agrarian in The Late Nineteenth Century, 48 AGRIC. HIST. 269 (1972).

'cornering' the market." Over thirty bills were introduced in response to this Presidential message, but none were adopted.

C. The FTC Study Reviews the Issue of Manipulation

At the outbreak of World War I, a short wheat crop resulted in new levels of frenzied speculation and caused widespread concern. The Chicago Board of Trade was forced to adopt emergency measures that stopped all wheat trading in its May wheat contract. Legislation was also adopted to control food prices during the war, and President Wilson was authorized to regulate or prohibit transactions on exchanges. President Wilson and his Commerce Secretary, Herbert Hoover, used that authority to form the Food Administration Grain Corporation. Thereafter, the corporation began buying grain and essentially eliminated the exchanges from this process until the end of the war. Nevertheless, the speculation at the outset of the war resulted in a massive study by the Federal Trade Commission (FTC) of the grain trade. As part of that study, the FTC conducted extensive hearings on the issue of manipulation in the commodity futures markets.

The FTC Study focused principally on the critical period in futures trading when contracts are expiring and futures prices merge into cash market prices. It is at this stage that the greatest danger of price distortion appears because only specified grades of a commodity held in approved exchange warehouses can be used for delivery. In instances where there is a shortage of grain that meets those specifications, and where supplies cannot be brought into the market quickly, traders may stand for delivery and attempt to "squeeze" or

44. L. Kendall, supra note 27, at 134. See also 43 CONG. REC. 1403 (Jan. 26, 1909) (remarks of Sen. Davis) ("this New York Cotton Exchange is one great, big gambling institution"). In 1912, the Democratic Party also sought to prohibit gambling in futures trading. See H.R. REP. No. 681, 62d Cong. 2d Sess. (1912).
45. See, e.g., Our War-Profiteers, LITERARY DIGEST, May 26, 1917 at 1883 ("The Kaiser's Allies In America are the food gamblers . . . ." and "[t]hose who undertake to corner the market . . . . should be put in the same class with the spy and the traitor and share the same fate . . . .")
46. 7 FTC STUDY, supra note 41, at 79. Increases in prices were said to be "unparalleled." Duffus, Government Control of The Wheat Trade in The United States, 8 AMERICAN ECON. REV. 62, 73 (1918); Federal Regulation, supra note 17, at 828 n.28. In fact, food prices had risen by some fifty percent and, it was charged that "[t]he American people are not getting enough to eat," and that "speculators" are "seeking to amass . . . . great fortunes at the expense of the health and happiness of the American people." T. KESSNER, FIORELLO H. LAGUARDIA AND THE MAKING OF MODERN NEW YORK 45 (1989).
47. 7 FTC STUDY, supra note 25, at 260, 382.
48. L. Kendall, supra note 27, at 192-93.
49. 7 FTC STUDY, supra note 25, at 242 note 1; Federal Trade Commission, Hearings On Market Manipulation Of Grain (1922). Unfortunately, these hearings seem to have been lost to history. A search of the Library of Congress, the National Archives, numerous departmental and agency libraries in Washington, as well as public and private libraries across the country has failed to uncover a copy of these hearings.
"corner" the market. The FTC Study found that, if a cornering condition becomes known early in the delivery month, it may be possible to rush large quantities of grain to Chicago to prevent its success. But corners often happen too late in the delivery month for such efforts to work.

A "squeeze" is similar to an intentional corner that falls short of being complete. The FTC Study found that a squeeze is generally more successful from a profit standpoint because someone who is cornering the entire market must "bury the corpse." That is, the person must ultimately dispose of the actual grain used in the corner without greatly depressing prices; otherwise, the value of the corner will be lost. Because the cash grain accumulated to offset the corner must generally be disposed of at a sacrifice price much of the profit on the futures side of the corner is dissipated.

The FTC Study noted that traders had found effective methods of burying the corpse. One way is to hold the grain by storing it. However, this tends to increase the difficulty in getting rid of the grain after the effects of the manipulation have dissipated, i.e., grain prices may remain depressed. A more artful method is to render the commodity undeliverable on the futures exchange, as was done in a notorious case of a corner in pork ribs where, prior to being sold, the pieces were cut in such a way as to make them irregular, and therefore unacceptable, for delivery. In other instances, as occurred in several grain corners, the cornering party sold the grain that was taken on delivery in Chicago outside that market, for example, in Buffalo. The trader then provided in its contracts of sale in Buffalo that the grain could not be returned to Chicago.

50. 5 FTC STUDY, supra note 25, at 322. The FTC STUDY stated that a "true" corner occurs where:

. . . some one or more speculators . . . constitute a concentrated interest on the buying side and accumulate more long contracts than they think is possible for the sellers to make delivery on, thus compelling the latter to settle at a price dictated by the cornering interest . . . . In the process of running a corner, the cornerers acquire all or nearly all of the wheat (or corn or oats) that is in storage in regular warehouses in Chicago (or at whatever terminal market may be the scene of their operations) . . . . and thus occupy the position of being the only holders of the actual wheat from whom grain can be bought to meet obligations on the futures contract by delivery.

Id. at 322.

51. Id. at 323.

52. 7 FTC STUDY, supra note 25, at 244.

53. Id. at 244.

54. 7 FTC STUDY, supra note 25, at 244.

55. 5 FTC STUDY, supra note 25, at 327 n.2.

56. 7 FTC STUDY, supra note 25, at 251.

HUBBARD, COTTON AND THE COTTON MARKET 393 (2d ed. 1927), quoted in Trading In Futures, supra note 17, at 239.
The FTC Study found statistical evidence showing that, where corners occur, the price of the grain is "artificially enhanced because it is temporarily in extraordinary demand for the sole and only purpose of using it to meet futures contracts."57 This causes a general loss to the public because the direction, rate, and flow of grain is distorted in a terminal market. The terminal market eventually becomes clogged with grain that is actually needed elsewhere, as traders rush grain to the market to counter the corner or to take advantage of rising prices.58

The FTC Study concluded that a comparison between cash prices when the grain is needed for delivery on futures contracts and when it is not needed for delivery should give some indication of the effect of a particular corner upon the market.59 The presence and effects of a corner also may be revealed by comparison of prices at the close of the delivery month with prices immediately thereafter.60 In addition, a corner may reveal itself through a widening of the price spreads between terminal markets, as between Chicago and Kansas City, for example, if there is a corner in Chicago.61 The existence of a corner may not, however, be completely revealed by this methodology because other markets may reflect to some degree the effects of the corner.62

The FTC Study focused on the fact that there may be "natural" corners and squeezes63—"congestion" in the market that is caused by a natural shortage of supplies.64 The FTC Study found that congestion has price effects nearly as severe as a corner that is deliberately contrived to squeeze the shorts.65 It noted that natural squeezes and corners generally relate to the peculiarities of the futures markets rather than to supply and demand conditions.66

The FTC Study considered claims that a hedger who enters a delivery month seeking delivery actually becomes a speculator because he is wagering on his ability to secure transportation of the grain to the market to make his delivery. The FTC Study was of the view that this claim was like attempting to prevent rear-end railroad collisions by leaving off the rear car. The FTC

57. 5 FTC STUDY, supra note 25, at 232 (emphasis added).
58. Id. at 323.
59. 7 FTC STUDY, supra note 25, at 245.
60. Id. at 245.
61. Id. at 245.
62. Id.
63. Id. at 243. The FTC Study stated that the "Patten corner of 1913" was not really a corner at all. Rather, it was an effort by a trader to exploit natural conditions resulting from a short crop, import limitations and other restrictions. Id. at 244.
64. Id. "Congestion" was later defined by a government agency as:
a condition where one or a few traders control such a large percentage of the open contracts that prices may be unduly influenced by the operations of those traders or where, toward the end of the life of a future, delay of liquidation by longs may cause the maturing future to advance in relation to more distant months and relative to prices of the cash commodity.
65. 7 FTC STUDY, supra note 25, at 243.
66. Id. at 265.

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Study also noted that one grain trader thought that anyone carrying open trades into the delivery month on the long side of the market is evidence of manipulation. The FTC found this notion curious because it assumes that delivery on the futures markets was remote. Similarly, the FTC Study found that there were claims made that merely standing for delivery is manipulation, but the FTC noted that delivery is provided for in futures contracts as a matter of right.

The FTC study examined particular aspects of futures trading that allowed exploitation of short sales by the longs. It found that the "futurity" of the obligation often meant that the seller would not obtain the commodity for delivery at the time of the futures sale. The more leeway the short has, the longer he may postpone acquisition, and "the tighter the position he may be in just before the date of maturity." On the other hand, the "fixed time limit gives the cornerer his opportunity, provided he is able either to foresee or to contrive a conjunction of circumstances that will help him to mulct the shorts." The FTC Study noted that the public and other traders had very little sympathy for short sellers who were caught in corners because there was a widespread belief that short selling of futures depressed prices. The evidence, however, did not support this belief.

The FTC Study discovered a phenomenon known as "tailing on," meaning other speculators were jumping into an ongoing manipulation. The study noted, however, that the presence in the market of a mob of speculators with thin margins and small resources may be an invitation to the bear operator. If a bear can shake outside speculators by a raid, the decline he initiates will be carried further by stop-loss orders and similar sales in sufficient volume to take

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67. Id. at 219. It should be noted that, in fact, delivery is rarely taken on futures contracts. See H.R. REP. No. 975, 93d Cong., 2d Sess. 149 (1974); Comment, Commodities Futures Control: Manipulation Under the Commodity Exchange Act, 57 MINN. L. REV. 1243, 1245 n.10 (1973) [hereinafter Futures Control]; Cargill v. Hardin, 452 F.2d 1154, 1157 (8th Cir. 1971), cert. denied, 406 U.S. 932 (1977). Some futures contracts are now settled in cash. See Katara v. D.E. Jones Commodities, Inc., 835 F.2d 966 (2d Cir. 1987). Historically, delivery was an essential feature of futures trading because: "Despite the fact that most contracts on futures markets are liquidated by offset, it is well settled that a commodity which did not require a short to deliver at maturity and a long to receive a commodity at maturity would be a gambling institution." Volkart Bros., Inc. v. Freeman, 311 F.2d 52 (5th Cir. 1962).

Moreover, delivery plays an important role in pricing:

The basic reason for requiring physical delivery on any futures contract is that it causes futures and cash prices to converge as contract maturity approaches. So long as the seller of a futures contract can substitute physical delivery for the executory contract, the contract's price will converge with the cash market value of the specified product. Thus, one's economic position is maintained so long as he has the right to make or take physical delivery.


68. 7 FTC STUDY, supra note 25, at 269-70.
69. Id. at 251.
70. Id. at 251-52.
71. 5 FTC STUDY, supra note 25, at 327.
72. 7 FTC STUDY, supra note 25, at 239.
73. Id. at 254.
care of his purchases at a profit. However, the FTC Study found that this may be more theory than reality. Rather, “the possibility of successful manipulative shortselling is a matter of the power of large financial resources to win by overawing the market.”

The FTC Study examined the role of intent in manipulation. It noted that, while the public’s interest in manipulations turns on “who did it”, this focus often fails because the intent to manipulate is often not present or cannot be proved, even though there were artificial and injurious price movements. The FTC found that high prices could result from the strength and obstinacy of large buyers, even where there is no conspiracy and no purpose to exploit the market in a monopolistic manner. Moreover, it was not always possible to establish the intention of the big “plungers” who may be “trying out the market” through heavy sales or who may be trying to “feel for the bottom” of the market. Such a trader may have no evil motive, but may trade as if deliberately “hammering” the market. The FTC noted that, whatever the trader’s motive, the effect of such hammering is to lower prices artificially.

The FTC Study reviewed efforts to prevent corners and squeezes. In 1874, Illinois had adopted a statute prohibiting corners, but the statute had little effect. The Chicago Board of Trade also had adopted various rules to prohibit and limit manipulative opportunities. Among other things, it adopted, in 1968, a resolution, which declared corners to be “essentially improper and fraudulent.” The Chicago Board of Trade also required regular trading hours so that the market would not become susceptible to manipulation and rigging late in the day when other traders left the pit. “Curb” trading in hotel barrooms was also prohibited because it allowed manipulation on the opening of trading the next day.

74. Id. at 255. Stop loss orders are often used to protect existing profits or to limit losses by having the broker sell out a position when a particular price level is reached. See Economics of Futures Trading, supra note 25, at 62.

75. 7 FTC STUDY, supra note 25, at 255. This type of activity later became known as “gunning” stop orders, and it is apparently not just a matter of theory. In fact, “gunning” for stop-loss orders has been characterized as one of the “main forms of manipulation.” In re Henner, 30 Agric. Dec. 1151, 1181 n.25 (1971), noted in Redefining the Offense, supra note 17, at 398-99 & n.339.

76. 7 FTC STUDY, supra note 25, at 255.

77. Id. at 243.

78. Id. at 243-44.

79. Id. at 259. The FTC Study noted, for example, that one big trader would sell 100,000 bushels to see how the market took it. If the market took this sale without an undue effect on prices, the trader would then take the opposite side of the market and begin large buying operations. On the other hand, if the market dropped, the trader would not take the long side of the market. Id.

80. 5 FTC STUDY, supra note 25, at 328.

81. 7 FTC STUDY, supra note 25, at 252. This rule was changed at various times by the exchanges. Id. at 252-53 and 5 FTC STUDY, supra note 25, at 179-81. See also Attack on Options and Futures, supra note 30, at 16-17.

82. 5 FTC STUDY, supra note 25, at 145-47.
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Where a corner occurred, Chicago Board of Trade rules allowed a seller to default on contracts, and then claim settlement by arbitration. The first of these rules were adopted in 1869 and 1870. Still another rule was adopted in 1921 that was designed to prohibit "absolutely" any possibility for a squeeze or corner. The FTC Study found that despite these rules, and even under conditions of war-time regulations and restrictions during World War I, there were squeezes in the Chicago futures markets. The study concluded that additional rules should be designed to prevent corners and prevent manipulation and artificial prices.

The FTC Study stated that futures trading should be conducted so that manipulative conditions are checked and their effects on prices are minimized. It suggested that alternate delivery points be designated so that grain could be brought to delivery places other than the terminal market. The study further proposed that consideration should be given to limiting the size, open interest, and number of bushels that may be bought or sold within a particular day by a single individual. The FTC believed that other administrative measures could help prevent artificial prices, for example, the imposition of price limits, which limit the amount of price changes in a given day. It found that such limits, along with other measures, were successful, in relation to the May 1918 trading of oat futures contracts. The FTC suggested that limiting the ability of individual speculators to "bear the market" would be the best way to prevent bear raids.

The FTC Study concluded that, because of the hedging facilities afforded by futures markets, futures trading in grain should not be abolished but should be subject to governmental supervision. It wanted cornering to be treated as a common law crime that would impose liability on anyone purchasing large

83. 7 FTC STUDY, supra note 25, at 253. See also Lurie, Commodities Exchanges as Self-Regulating Organizations in the Late 19th Century: Some Perimeters in the History of American Administrative Law, 28 RUTGERS L. REV. 1107 (1975).
84. 7 FTC STUDY, supra note 25, at 253.
85. Id. at 265.
86. Id. at 271.
87. Id.
88. Id. The Chicago Board of Trade had actually used such methods to break corners in the past by, for example, making additional storage areas "regular" for delivery. Attack on Options and Futures, supra note 30, at 18. As will be discussed below, such position limits became a principal means of regulating the futures markets under subsequent legislation. See infra notes 209, 443-44 and accompanying text; Federal Regulation, supra note 17, at 843.
89. 7 FTC STUDY, supra note 25, at 259. Federal Regulation, supra note 17, at 835-36 n.64. Price limits are still used by the exchanges. See Letter from John M. Damgard, President Futures Indus. Ass'n, to Nicholas Brady 2 (Dec 15, 1987); FUTURES INDUS. ASS'N, AN INTRODUCTION TO THE FUTURES MARKETS 11 (1984); S. KLEINFIELD, THE TRADERS 110-11 (1983); SEC REPORT, supra note 18, at 259.
90. 7 FTC STUDY, supra note 25, at 272.
91. Id. at 279.
quantities of commodities in order to have command of the market. The study stated that, while the Sherman Antitrust Act would be applicable, common law liability would be more appropriate because proof of a conspiracy is not required. The study had found that conspiracies were often not present in manipulations.

D. Early Legislation Fails to Prevent Manipulations

Even before the FTC Study was completed, Congress held hearings to consider legislation that would impose federal controls over commodity futures trading. In the course of those hearings, Commerce Secretary Herbert Hoover testified that large volumes of short selling that were “deliberately intended to depress the price” had caused injury and worked a great injustice on the public and farmers. Another witness testified that manipulation was openly conducted in the Chicago wheat, corn, and oat pits by a few powerful traders, “a piece of audacity having few equals in commercial history.” He stated that it was beyond comprehension why this was permitted and that “doubtless, a few generations hence, the tales of our squeezes and corners and manipulated markets will be read with the same excited interest that we now read of the old buccaneer days.” On the other hand, another witness contended that the Chicago Board of Trade had grown so large that a corner was practically impossible. But he did admit that in earlier days corners had been successfully operated, and that the spectacular publicity which accompanied those activities had kept alive in the public mind the possibility of their recurrence.

Another witness described manipulation as being usually attempted for the purpose of driving prices upward because “[m]anipulators have been inspired by the belief that it would be possible for them to buy a greater quantity of contract grades of grain than could be delivered at the time and place of

94. 15 U.S.C. § 1 (1988). The FTC STUDY cited United States v. Patton, 226 U.S. 525 (1913), where the Sherman Antitrust Act was applied to a cornering operation of the entire cotton market. There, a conviction was obtained on the grounds of conspiracy. 5 FTC STUDY, supra note 25, at 325 n.1.
95. 7 FTC STUDY, supra note 25, at 324-25.
96. The Cotton Futures Act had been adopted previously to set standards for the grading of cotton and pricing based on such grades. PUB. L. 63-174, 38 Stat. 693 (1914). See generally Organized Commodity Markets, supra note 25, at 85-250, 366-67; Federal Regulation, supra note 17, at 832-33. Efforts also were made to standardize grain grading, warehouse receipts, and facilities. See 39 Stat. 46, 482 (1916).
98. Id. at 173.
99. Id.
100. Id. at 669. Nevertheless, the House Committee of Agriculture “agreed and all the witnesses have agreed that the one overshadowing evil that must be eliminated is manipulation. This bill provides, in so far as humanly possible to do so, for the elimination of manipulation upon these grain exchanges.” 61 CONG. REC. H1317 (May 11, 1921) (remarks of Rep. Purnell).
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delivery for which the [futures] contract called. But another witness, Julius H. Barnes, president of the U.S. Grain Corporation during World War I, stated that the futures exchanges could be used "for short selling, that by its own volume and weight becomes manipulative in character . . ." He further stated that, while "it is also true that even though such a price depression must be temporary in character it may, during its period of effectiveness, do substantial injustice by forcing the liquidation of grain held on margin, or by the price tendency thus displayed, frightening owners otherwise confident of the ultimate value of their goods." Congress also heard testimony on the spreading of rumors that were designed to manipulate commodity prices. One example involved a scheme in which it was claimed that "green bugs" that "worked at night" were infesting the wheat harvest. The party pulling this hoax mailed in samples of these bugs and went long the market. Later, after taking his profits and when it was disclosed that the bugs were harmless, they were actually lightning bugs, the manipulator went short the market as prices plunged.

Witnesses testified that intent should be part of any prohibition against manipulation. One stated that simply "because a man does a large volume of trading or is wealthy does not presuppose he has any natural bent toward cornering the market . . ." Various statements were also made in the hearings as to the meaning of manipulation. One witness described manipulation as "the dealing in huge quantities not to cover actual transactions, but to produce unnatural and undue influences either of depression or advance, thus creating a situation which interferes with the free play of prices and introduces into legitimate operations elements of danger, uncertainty, and hazard . . ." A manipulator " . . . is one who suddenly throws upon the market a huge volume of some commodity, and it is an injury to anyone, a hazard to all of us, in the business." Another witness testified: "in a general way I think a manipulator is one who attempts to buy or sell more than the market would be able to take care of, and for the purpose of making it impossible to complete contracts, and therefore force a settlement." The witness continued, "a manipulator is a speculator who through the large quantities of trading attempts "to force

102. Early House Hearings, supra note 101, at 841.
103. Id. at 841-42.
104. Hearings on Future Trading in Grain, supra note 97, at 182. For more on "green-bug plagues" see Cutten & Sparkes, The Story of a Speculator, SAT. EVENING POST, NOV. 19, 1932, at 66.
105. 1921 House Hearings, supra note 101, at 186.
artificial conditions or to exaggerate conditions for his own advantage.'”

Similarly, a Congressman stated that “a manipulator is a speculator or gambler who by reason of his tremendous resources buys or sells grain in such large quantities . . . as to affect the price.” Another congressman stated that manipulation occurs when a trader “endeavors to put down the price of wheat temporarily, in order that he may buy cheaper, or endeavors to put up the price of wheat by long buying, when he knows that is not the real value of the wheat, endeavoring to buy in at the lower price, he is engaging in the manipulation of prices.” It was further noted that it is hard to isolate manipulation because it is often difficult to distinguish the manifestations of legitimate business motives from those which are manipulative: “Moreover, a situation arises frequently in the grain markets where a perfectly legitimate transaction in the beginning develops into a situation before closing of trading that might be considered manipulative.”

In determining what legislation was needed to prevent manipulation, Congress considered, as had been suggested by the FTC Study, the imposition of position limits. Such limits would have limited the size of trading by traders and “foreigners” and therefore limited their ability to manipulate the market. In this connection, Herbert Hoover, the Secretary of Commerce, offered a proposal that would have limited the amount of trading to 200,000 bushels. It was determined, however, that this would be of doubtful effectiveness. Instead, Congress decided that manipulation would be

107. Id. at 446.


109. 61 CONG. REC. 5560 (1921) (remarks of Rep. Mann).

110. Hearings on Futures Trading in Grain, supra note 97, at 25.

111. 61 CONG. REC. 1372 (1921) (remarks of Rep. Tincher). Much concern was expressed over manipulations by foreign traders who allegedly were forcing prices down through futures transactions so that they could buy grain at cheaper prices. See Early House Hearings, supra note 101, at 40, 780, 792, 866-69; 61 CONG. REC. 1372 (1921) (remarks of Rep. Tincher).

112. 1921 House Hearings, supra note 101, at 13. Hoover also stated:

"We have had two forms of manipulation . . . . One was the old-fashioned corner . . . . The second form of manipulation and the one that I feel does at times take place, is the making of a drive on the price by either the sale or the purchase of such quantities as will affect the price by the volume of material coming to the market at that particular time. I would regard those transactions as an attempt to dislocate the normal flow of the law of supply and demand, and any attempt of any individual to dislocate a free market must be against the public interest. I feel it is also against the interest of the individual producer, because a drive on the market that depresses the price must find a considerable number of farmers who, through the fallen price and their outstanding obligations, are compelled to liquidate, and they have been done an injury. Incidentally, the commodity has been brought in the market and an acceleration of the depression has been created."

Early House Hearing, supra note 101, at 911-12.

Hoover further contended that “the wrongful manipulation of the markets is accomplished only by the sale or purchase of very large quantities of grain.” Id. at 896. He stated that in such instances, “grain is brought into the market that would not normally flow there, and thereby such a manipulation has a damaging effect on price and works great injustice.” Id.

113. 1921 House Hearings, supra note 101, at 13.
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prevented by requiring a record to be kept of transactions by large traders. As stated in congressional testimony, it was thought that such records would prevent manipulation because, if a man "is undertaking to 'bear' the market and the whole world's knowing he is doing it, he is the only loser. Secrecy is absolutely necessary to such efforts and that is the reason why the Chicago Board of Trade keeps no records."\(^\text{114}\)

The legislation also sought to prevent manipulation by requiring all futures contracts to be traded on exchanges and then requiring the exchanges to prevent manipulation. If the exchanges failed to do so, they would lose their privilege to conduct futures trading.\(^\text{115}\) It was thought that this legislation would be a mandate to the exchanges that would require them to "drive from their midst the man who is prostituting the machinery of grain market for his own selfish purpose by manipulating the price to his own advantage."\(^\text{116}\) Although one Congressman suggested that the manipulators should be hit with a sledge hammer, it was thought that punitive legislation would not be wise and that exchanges should be permitted to clean their own houses.\(^\text{117}\)

The legislation that was enacted, the Future Trading Act of 1921, was based on the taxation powers of Congress.\(^\text{118}\) It was founded on a Congressional conclusion that futures contracts are susceptible to manipulation and to sudden and unreasonable price fluctuations. It sought to tax out of existence futures transactions that were not conducted on licensed exchanges.\(^\text{119}\) The Supreme Court, however, did not believe that Congress could use its taxation powers in such a method and declared the Futures Trading Act of 1921 unconstitutional shortly after its adoption.\(^\text{120}\)

After the Court's decision, Henry C. Wallace, the Secretary of Agriculture, pointed out to Congress that dramatic and recent fluctuations in the price of wheat had "strengthened the farmer in his belief that prices had been manipulated to his great disadvantage."\(^\text{121}\) A House Report noted that the day after the Supreme Court's decision the price of wheat advanced four cents a bushel. Thereafter, wheat prices declined at a time when there was no reason for them to do so, leading to the conclusion that this was "evidently a straight-out manipulation of the market."\(^\text{122}\)

Congress quickly responded by passing new legislation, the Grain Futures Act of 1922, which substantially resembled the Future Trading Act, except that

\(^{114}\) Id. Compare Id. at 187-88.
\(^{115}\) Id. at 13.
\(^{118}\) 42 Stat. 187 (1921).
\(^{119}\) Id.
\(^{120}\) Hill v. Wallace, 259 U.S. 44 (1922).
it was based on the commerce power of Congress.\footnote{123} The Grain Futures Act was "designed to prevent speculative manipulation of the price of wheat."\footnote{124} As the Supreme Court later noted, its purpose "was to control the evils of manipulation of prices in grain. Such manipulation, Congress found, was effected through dealings in grain futures . . . ."\footnote{125}

Although "[m]any persons had advocated, as a remedy, that all futures trading be abolished,"\footnote{126} the Grain Futures Act established a licensing system pursuant to which commodity exchanges were required to be designated as "contract markets."\footnote{127} All futures trading was required to be conducted on exchanges so designated. The Act required that the exchanges be located near a terminal market where the commodities subject to its futures contracts were sold. In addition, the exchanges had to maintain records of their transactions and they had to allow government representatives to inspect their books and records. The exchanges were also required to prevent their members from disseminating false and misleading crop or market information.\footnote{128}

As a further condition for designation of a contract market, the exchanges were required to prevent their members from engaging in price manipulations.\footnote{129} But, in adopting the Futures Trading Act, the Conference Committee changed the requirement that contract markets provide for the prevention of "undue" or "unfair" manipulations. The words "unfair" and "undue" were struck from the final bill.\footnote{130} Further, a co-sponsor of the Futures Trading Act believed that, since there was no legal definition of manipulation in the Futures Trading Act, it was up to the Secretary of Agriculture to determine the meaning of the term.\footnote{131}

The Grain Futures Act was upheld by the Supreme Court,\footnote{132} and the Seventh Circuit rejected a claim that the Grain Futures Act was void for vagueness because it did not define what was meant by the term "manipulation."\footnote{133} In any event, the statute did not make manipulation a crime.\footnote{134} The Grain Futures Act was "designed to prevent speculative manipulation of the price of wheat."\footnote{124} As the Supreme Court later noted, its purpose "was to control the evils of manipulation of prices in grain. Such manipulation, Congress found, was effected through dealings in grain futures . . . ."\footnote{125}
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Futures Act was administered by a small agency in the Department of Agriculture, the Grain Futures Administration (GFA). The GFA carried out the day-to-day regulatory activities under the statute and was subject to supervision by the Secretary of Agriculture, who was one of three members on a commission that was responsible for overall regulation under the Act. The other two members of this commission were the Secretary of Commerce and the Attorney General of the United States.

In carrying out its functions, the GFA generally deferred to the exchanges. For example, after investigating "erratic and extreme" wheat price fluctuations in 1925, the GFA suggested the "desirability of the exchanges prohibiting the making of new contracts after, say, the 15th of the current delivery month. This . . . would do much toward preventing a squeeze such as occurred in July wheat . . . ." That suggestion had little effect as evidenced by another corner in wheat which occurred in the following year. But, on March 12, 1930, the GFA brought a test case to determine whether trading practices such as "cross trading" and "bucketing" of customer orders after the close of trading could be dealt with under the Grain Futures Act as a form of price manipulation.

The GFA had found some twenty-four persons in Chicago engaging in cross trading and bucketing of orders, and it was found that nine of the fifteen most active clearing members on the Kansas City Board of Trade were engaging in

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Norris, then Chairman of the Senate Agriculture Committee, stated in explaining why Congress did not make manipulation a crime under the Future Trading Act: "These things are various and perhaps impossible of direct definition. I do not know how we would draw a definition to bring it home to the individual." *Future Trading in Grain: Hearings on H.R. 5676 Before the Senate Committee on Agriculture and Forestry, 67th Cong., 1st Sess. 335 (1921)*

Redefining the Offense, supra note 17, at 353 n. 64.

This author also cites another statement in Congress where a futures trader stated in response to a Senator's question: "manipulation" . . . in its use is so broad as to include any operation of the cotton market that does not suit the gentleman who is speaking at the moment." *Cotton Prices: Hearings Before a Subcomm. of the Senate Comm. on Agriculture and Forestry, Pursuant to S. Res. 142, 70th Cong., 1st Sess. 154 (1928)* (cited in Redefining the Offense, supra note 17, at 35 n.67).

135. ORGANIZED COMMODITY MARKETS, supra note 25, at 372-73.
136. 42 Stat. 1000 (1922).
139. To Amend The Grain Futures Act, Hearings Before The Senate Committee On Agriculture And Forestry On H.R. 6772, 74th Cong., 1st Sess. 20 (1936) [hereinafter Amend The Grain Futures Act]. Bucketing means that the customer's order is not sent to the exchange for execution. Instead, the order is held in hopes that the market will move against the customer. When that occurs the individual or firm bucketing the order will profit to the extent of the customer's losses. Commodity Exchange Authority, Administrative Determination No. 200 (May 25, 1966); "Bucketing" and "bucket shops" were intended to be outlawed by the Grain Futures Act. A bucket shop is simply a betting parlor where customers place bets on commodity price changes. S FTC study, supra note 25 at 329. The bucket shop operator, in effect, bets against its customers. Unfortunately, in those rare instances when the customer won the bets, the bucket shop would simply fold up and move elsewhere. J. HILLMAN, GOLDBRICKS OF SPECULATION 39 (1904).
such practices. Among other things, customer orders were filled at the close of trading by using prices from the official trading range during the day. In addition, firms were “scalping” by making cross trades with themselves, which means that the firms would take both the bought and sold sides of the same transaction.

This case, Secretary v. Massey, was reviewed by the Commission that administered the Commodity Exchange Act. The Commission concluded that, while such practices might be detrimental to customers and “may even amount to fraud,” it did not believe that the practices constituted manipulation within the meaning of the Grain Futures Act. The Commission stated that the terms “manipulate” and “manipulation” relate to efforts to stimulate or depress the market price of grain, not “to practices between brokers and their principals where the failure of customers to receive the benefit of full market price grows primarily out of acts which in reality amount to breach of duty imposed by a fiduciary relation.” This decision gave a not-too-subtle hint that the meaning and scope of “manipulation” is uncertain.

The Massey decision underscored the fact, as did several price breaks in the market, that the GFA was an impotent agency that had no effective means of regulating the markets. In fact, it was stated in Congress that the Grain Futures Act had been “almost a complete failure.” It was, as one commentator notes, “thin gruel”. As a result, in 1927 and 1928, legislation was introduced “to limit the amount of a single speculative interest in any one delivery month as a measure to guard against price manipulation.” Another bill “provided for the confiscation of cotton withheld from the market with the intent to manipulate prices.” Neither bill was enacted.

The Grain Futures Administration’s annual reports repeatedly pointed out the ill effects on American grain producers from price manipulations caused

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141. Id. at 7.
142. GFA Dkts 2 & 3 (Nov. 9, 1933), noted in Regulation of Commodity Exchanges, supra note 140, at 69, and Amend The Grain Futures Act, supra note 139, at 20.
143. Amend The Grain Futures Act, supra note 139, at 20. The Commission stated that it believed that “it was the purpose of the Act to restrain influences which tend, through subversive speculative action, to affect artificially general price levels for a particular kind of grain in some particular market or markets.” Secretary v. Massey, slip op. at 5-6 (GFA Dkts. 2-3, Nov. 9, 1933). The Commission further stated that it did "not appear that respondents changed or attempted to change the general level of prices." Id. at 7.
146. Regulating The Grain Gambler, supra note 41, at 8.
147. J. BAER & G. WOODRUFF, COMMODITY EXCHANGES 190 (1929).
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by relentless "grain gamblers." These included a July 1926 squeeze in wheat; a July 1928 squeeze in corn; congestion in the September 1928 corn contract; and a July 1931 corner in corn. In response to a Senate resolution, the Secretary of Agriculture further found that large scale buying and selling operations had completely disrupted the market and the price changes were "felt in every large grain market in the world." The stock market crash of 1929 also resulted in a collapse of commodity prices. This was said to be an "economic catastrophe". Thereafter, on July 10, 1931, President Hoover startled the country by announcing that "certain persons" had been selling short in the wheat market continuously over the prior month. He stated that the sales had "one purpose and that was to depress prices." The President stated that such activity could "destory the return of public confidence. The intention is to take a profit from the loss of other people, even though the effect may be directly depriving many farmers of their rightful income." President Hoover further stated that, if "these gentlemen have that sense of patriotism which outruns immediate profit and desire to see the country recover, they will close up these transactions and desist from their manipulations." The GFA informed Congress that it did not think that under existing legislation it would have had a chance in court if it had brought an action to stop the trading that was of concern to the President.

In July of 1932, after the volume of the Chicago Board of Trade increased dramatically, prices sharply declined, leading to the market's close. The decline occurred when a small group of traders dumped their holdings to take profits. Other accounts subsequently had to liquidate their positions in order to stem losses. By October 29, 1932, wheat prices had dropped to a level unseen


149. Grain Prices and The Futures Markets, A 15-Year Survey, 1923-1938, U.S.D.A. Technical Bulletin No. 747 at 66-69 (Jan. 1941). There was also concern that the Soviet Union was manipulating the markets. An investigation by Congress, however, could not determine that such was the case. Id. at 262-66; Report of the Chief of the Grain Futures Administration 6 (June 30, 1931); Peterson, Futures Trading With Particular Reference to Agricultural Commodities, 7 AGRIC. HIST., 68, 78 (Apr. 1933); When the Russian Bear is a Wheat Bear, THE LITERARY DIGEST, Oct. 4, 1930, at 5; H. REP. NO. 1551, 72d Cong., 1st Sess. 2 (1932) (proposed bill would prohibit short selling by foreign traders above a specified level unless for hedging in the United States).

150. Wheat Futures, supra note 138. See also Trading in Grain Futures, Communication from The Secretary of Agriculture in Response to Senate Resolution No. 9, Sen. Doc. 110, 68th Cong., 1st Sess. 1 (Apr. 24, 1924) (investigation of trading in grain futures during 1923 as a result of a Senate resolution which sought to determine whether there had been efforts to "bear the market").


153. Commodity Short Selling, supra Note 152, at 182.

154. Id.

155. Id.

156. Id. at 180-81.

for over 300 years, a bushel of corn cost “less than a package of chewing gum.”

Harry L. Hopkins, Federal Emergency Relief Administrator, came to the market’s rescue and bought wheat for emergency relief. But for his action, prices would have plunged even lower than their already depressed level since a large number of speculative accounts had been liquidated for lack of adequate margin. The exchanges subsequently proposed a twenty percent margin requirement on speculative positions in excess of two million bushels. However, large speculators could still carry large positions since wheat was trading at only one dollar per bushel. In order to restrain speculation, the GFA had, in 1932, obtained the exchanges’ agreements, that the latter would not permit the accumulation of positions greater than five million bushels on the short side of the market. It did not impose any limitation on the long side of the market.

These efforts did not obviate the need for more effective legislation. The collapse of grain prices, the Great Depression and the election of Franklin Roosevelt resulted in a Presidential call for legislation that would establish effective regulation over both commodity and security exchanges. Congress was receptive to that request, and it held hearings in which it was informed that there were some 8 to 16 traders on the Chicago Board of Trade who had been largely responsible for the constant price fluctuations that occurred in periodic raids on the market. “These violent fluctuations had been caused largely

158. Wheat’s Plunge to a 300 Year Low, THE LITERARY DIGEST, NOV. 12, 1932, at 6.
159. Regulation of Grain Exchanges: Hearings Before the House Committee on Agriculture on H.R. 8829, 73d Cong., 2d Sess. 32 (1934).
160. Amend the Grain Futures Act, supra note 139.
162. One author notes:
Wheat prices declined from $1.05 a bushel in 1929 to a paltry 39¢ three years later; cotton went from 17¢ a pound to 6¢; and corn from 81¢ to 33¢ a bushel. Sheriffs endeavoring to foreclose on farms with unpaid mortgages were greeted by hostile armed mobs of farmers. “They are just ready to do anything to get even with the situation,” a Farmer’s Union spokesman told a Senate investigating committee, “I almost hate to express it, but I honestly believe that if some of them could buy airplanes they would come down here to Washington to blow you fellows all up . . . . The farmer is naturally a conservative individual, but you cannot find a conservative farmer today.”

163. President Roosevelt stated that:
The people of this country are, in an overwhelming majority, fully aware of the fact that unregulated speculation in securities and in commodities was one of the most important contributing factors in the artificial and unwarranted “boom” which had so much to do with the terrible conditions of the years following 1929.

164. Regulation of Grain Exchanges, supra note 159, at 282 (1934). See also 79 CONG. REC. 8589 (June 3, 1935) (remarks of Rep. Jones) (“during the last fifteen years about sixteen big traders in grain have from time-to-time taken advantage of unusual conditions to make raids upon the market and to rig the market . . . .”); 78 CONG. REC. 10446 (June 4, 1934) (remarks of Rep. Jones).
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by these big traders, such as Arthur Cutten, who are not interested in any way in the maintenance of the market."165

Cutten was a prominent subject in the Congressional hearings for other reasons.166 In 1932, he had hired a well-known writer, Boyden Sparks, and together they published a series of articles in the Saturday Evening Post that proclaimed the virtues of Arthur Cutten in particular and grain traders in general.167 He also severely criticized the GFA.168 The GFA did not take that criticism lying down. While conducting a survey of the market, it discovered that Cutten had carried a number of accounts in the names of relatives and friends.169 He had lied to the Secretary of Agriculture in claiming that he was only short some 400 contracts at a time when he was really short some 4 million bushels.170 After a two year delay, and in the midst of the hearings on the Commodity Exchange Act, the Grain Futures Administration brought charges against Cutten.171 But the Supreme Court ruled in Wallace v. Cutten172 that the GFA could not bar Cutten from trading on the futures markets because of his false reports concerning the size of his positions and because of his past manipulations. Justice Brandeis, for the court, held that the Grain Futures Act’s sanctioning provisions applied only to on-going offenses and not to prior misconduct. The government had argued that, “since violations of the reporting requirements by very nature cannot be detected during the course of their commission, the literal construction [of the Act] . . . renders it impractical and ineffective as a means of dealing with those persons who violate any provisions of the Act or attempt to manipulate the market price of grain.”173 The Supreme Court, however, rejected this argument on the grounds that the statute would not be rewritten “for the purpose of making

165. Id. (remarks of Rep. Jones). A GFA report had concluded that Cutten had changed his position from short to long numerous times on individual trading days and that he traded in immense proportions. It was found that these operations caused large price changes and unbalanced the whole market. "They can hardly be viewed as other than manipulative and destructive in character." Fluctuations in Wheat Futures, supra note 137, at 5.

166. Cutten was said to be the hated J. P. Morgan of the Grain Exchanges. 78 Cong. Rec. 10447 (1934) (remarks of Rep. May). It was also stated that Cutten had "mined more farmers in this country than any other single man," 78 Cong. Rec. 10448 (1934) (remarks of Rep. Truax), and that a "whisper" that Cutten was buying would cause orders to start rolling in from all over the country. 80 Cong. Rec. 6160 (1936) (remarks of Sen. Pope). Cutten had become particularly well known in the Chicago markets in 1924 when he pushed the price of wheat to over two dollars a bushel for the first time in history. Speculator-King, supra note 31, at 77. Cutten made profits of over five million dollars in this transaction. Id. at 78-79. As a result it has been stated that "Cutten has become one of the most glamorous figures in speculative history." E. DIES, STREET OF ADVENTURE 27-28 (1938).

167. Cutten and Sparks, The Story Of A Speculator, Saturday Evening Post, Nov. 19, 1932, at 3, col. 1; Nov. 26, 1932, at 18, col. 1; Dec. 3, 1932 at 12, col. 1; Dec. 10, 1932, at 24, col. 1; and March 25, 1933, at 14, col. 1.


169. Id.

170. Id.


172. 298 U.S. 229 (1936).

173. Id.
punishable action which, on the face of the statute, is merely to be prevented.\textsuperscript{174}

This decision effectively gutted the Grain Futures Act because the GFA could not finish a case before a manipulation was completed.\textsuperscript{175} The GFA had to face charges that it was politically motivated in that it had delayed two years before bringing its case against Cutten.\textsuperscript{176} The victory for Cutten, however, was not a complete one because the Internal Revenue Service sought to collect taxes in sums aggregating over $1 million as a result of the trading revealed in the accounts discovered by the GFA.\textsuperscript{177}

The Cutten decision was also a significant spur to the adoption of the Commodity Exchange Act.\textsuperscript{178} In the hearings on that legislation, it was stated that speculative trading had resulted in a substantial burden on the wheat and other grain markets because “commissions and gambling profits” were taken out before the farmer was given any payment.\textsuperscript{179} It was charged that “farmers of this country have lost hundreds of millions of dollars through the manipulation of the market on these exchanges. Those manipulators toil not neither do they spin, but they invariably take all of the profit of the farmer’s crop and leave him with the bills to pay.”\textsuperscript{180} Concern was expressed that manipulation had been occurring in the cotton exchange “so as to drive the price down when the farmer is selling and to raise it after his crop is all gone.”\textsuperscript{181}

One Congressman was incensed that “[w]hile the farmer [was] harvesting his wheat or grain, prices [were] hammered down to the extreme low point, but the moment the farmer parts with his grain the speculators start to raise the price and the result is that both the consumers and the farmers are mulcted by a bunch of professional dishonest speculators, . . . [who] sell millions of bushels of wheat, corn, or rye, just for the purpose of artificially lowering the price so that they can buy the grains back at a much lower price.”\textsuperscript{182} He stated that such “dastardly tactics have been followed from day to day and year to year

\begin{itemize}
\item \textsuperscript{174}Id. at 237 (citation omitted).
\item \textsuperscript{175} It was stated in Congress that:
\begin{quote}
As the law now is, a speculator may go into the market, violate the rules of the exchange and of the Government commission, manipulate the trading, make false reports, corner the market on some commodity, and make millions of dollars in profits; and if he gets all that done before a complaint is filed against him he may escape without any penalty.
\end{quote}
\textsuperscript{80} CONG. REC. 6160 (1936) (remarks of Sen. Pope).
\item \textsuperscript{176} H.R. REP. NO. 1522, supra note 171, at 17. \textit{Regulation of Grain Exchanges}, supra note 164, at 133-41, 271-72.
\item \textsuperscript{177} \textit{Amend The Grain Futures Act}, supra note 139, at 262. Cutten had previously been billed as “Chicago’s biggest individual income taxpayer.” \textit{The Grain Trade Doesn’t Think Mr. Cutten is Sentimental}, Business Week, Jan. 28, 1931, at 14, Col. 1.
\item \textsuperscript{179} 78 CONG. REC. 10447 (1934) (remarks of Rep. Boileau).
\item \textsuperscript{180} 78 CONG. REC. 10447 (1934) (remarks of Rep. Rankin).
\item \textsuperscript{181} Id. at 10448.
\item \textsuperscript{182} 78 CONG. REC. 10451 (1934) (remarks of Rep. Sabath).
\end{itemize}
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to the detriment of the growers, legitimate dealers, and the public."

Another Congressman wanted to stop "manipulative short selling; that is the use of the market by the speculator who wishes to depress it, or advance it, as his interest may dictate." 

One legislator informed Congress that speculators who dealt in large quantities were the ones who dominated trading and who cornered the market. These traders were able to control large blocks and "beat the market up or down" through their trading to the detriment of the farmers. Congress was also told that speculative "orgies" on the grain exchanges frequently destroyed commodity prices, and had serious effects upon the incomes of grain producers. Congressmen were appalled that wheat growers in the United States had been regularly victimized by "bear raids," "May squeezes," and "vicious short selling on a huge scale at the hands of big manipulators" who had been in virtual control of the exchanges. One senator asserted that farmers were entitled to protection from price manipulations affecting their incomes.

Congress was advised that concentrated large scale operations resulted in abnormal price movements. For example, at a time when wheat was generally trading for less than $1.25 per bushel, concentrated big-scale speculation caused wheat prices to vary some $.27 in two days. It was thought that legislation was needed to "prevent excessive and abnormal transactions which

183. Id.
188. 80 Cong. Rec. 7863 (1936) (remarks of Sen. Capper). It was stated that "[t]he farmers of this country have lost hundreds of millions of dollars through the manipulation of the market on these exchanges." 78 Cong. Rec. 10447 (1934) (remarks of Rep. Rankin).
189. 80 Cong. Rec. 7857 (1936) (remarks of Sen. Murray). Senator Pope thought that action was needed to prevent manipulation because sanctions under the Grain Futures Act against traders only involved a suspension and that a suspended trader "may very well spend that time cruising in placid waters, enjoy his profits, and be ready for another foray at the end of two years." 80 Cong. Rec. 6160 (1936) (remarks of Sen. Pope). Senator Pope believed that "the prospect of a year in federal prison instead of two years of balmy ocean breezes for such market manipulations might be considerably less attractive." Id.
190. A report by the Chamber of Commerce of the United States was also reviewed by Congress. The report stated that:

The outstanding disturbing influence in some of our commodity-futures markets at the present time is price manipulation by a small group of large-scale traders. Their activities are particularly disturbing because they exercise an artificial influence on the markets. There is no way of telling when they will attempt their manipulations or to what extent they will carry them. There results, therefore, a constant hazard, the force of which may move prices far out of line and, temporarily at least, destroy the hedging value of the futures markets.

Kauffman, supra note 130, at 31.
191. Wheat prices fluctuated wildly in 1933 and 1934, ranging from 60¢ to $1.25. F. Freidel, Roosevelt; A Rendezvous With Destiny 120, 134 (1990).
result in cornering the market, or which result from excessive large-scale transactions.\textsuperscript{193} In one instance, the GFA noted that five traders, acting on the advice of a single individual, had aggregated a 20 million bushel long position and exerted a "disturbing influence" on the market.\textsuperscript{194} In the hearings, it was stated that short sellers were usually large traders and that they would often sell in inordinately large amounts.\textsuperscript{195}

Congress was also concerned with the "sensational price collapse" in the Chicago wheat and corn futures markets on July 19 and 20, 1933, when the exchange was closed. A subsequent investigation by the GFA disclosed that this situation principally was the result of the activities of some traders who controlled fifteen large speculative accounts and who had accumulated an inordinately large holding of wheat and corn. Prices collapsed when a large portion of those positions were suddenly dumped upon the market.\textsuperscript{196} In addition, the GFA noted that another speculator, Thomas Howell, had effected a corner in the July, 1931 corn futures contract. Together with some associates, he accumulated a long interest of over eight million bushels, which totalled some 57% of the total July corn contracts, and he purchased actual corn totalling over 300,000 bushels. This position made it more difficult for others to deliver corn on the futures contracts, and the market was effectively "squeezed." After a price advance in corn during the last three days of trading from $.58 to $.72 per bushel, a large and serious price decline resulted.\textsuperscript{197} An action brought against Howell by the GFA was later thrown out on the same basis as the decision of the Supreme Court in the Cutten case.\textsuperscript{198}

Congress additionally examined a drop of nearly 200 points in cotton futures prices in March of 1935.\textsuperscript{199} It was charged: "That is not supply and demand. That is caused by manipulation."\textsuperscript{200} Congress was also aware that the futures markets were extremely sensitive and that "false or misleading

\textsuperscript{193} Id.
\textsuperscript{194} Regulation of Grain Exchanges, supra note 164, at 21.
\textsuperscript{195} Regulation of Grain Exchanges, supra note 164, at 13, 17. Representative Gilchrist asserted that "[t]he sales from a single source aggregating millions of bushels in the course of an hour exert a very much greater influence upon the price in the same volume of orders originating from widely different sources." 78 CONG. REC. 10449 (1934).
\textsuperscript{196} 80 CONG. REC. 6160 (1936) (remarks of Sen. Pope).
\textsuperscript{197} Id. at 6161.
\textsuperscript{198} See REP. CHIEF GRAIN FUTURES ADMINISTRATION (1935). In another case, Secretary of Agriculture v. Ettinger, similar charges were made and sanctions were entered. Id. at 4. See Note, Prevention of Commodity Futures Manipulation Under the Commodity Exchange Act, 54 HARV. L. REV. 1373, 1377-78 (1941).
\textsuperscript{199} H. R. REP. No. 421, 74th Cong., 1st Sess. 2 (1935).
\textsuperscript{200} Commodity Short Selling, supra note 152, at 304. Representative Rankin stated that: So long as we have a free, and open, and well-regulated exchange, all is well and good, but the last few years, there has developed a practice of manipulating the exchange so as to drive the price down when the farmer is selling and to raise it after his crop is all gone. 78 CONG. REC. 10448 (1934) (remarks of Rep. Rankin). In the midst of the congressional consideration of the Commodity Exchange Act, Congress was forced to pass a resolution directing the Department of Agriculture to investigate a corner in the December 1934 sugar futures contract. See Corner in December Sugar Futures, S. DOC. No. 44, 74th Cong. 1st Sess. (1935).
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statements or fictitious trading might in a few minutes turn thousands of dollars into the pocket of some unscrupulous trader." 201

In determining what legislation was needed to prevent these abuses, members of Congress sought ways to stop "racketeering" by a few large professional traders, 202 and to give the government enough "teeth" to properly regulate the exchanges. 203 One Congressman claimed that the Grain Futures Act had been almost a complete failure, lamenting, "It has no teeth." 204 Specifically, Congress was concerned with price manipulation by a small group of large scale traders who were exercising an "artificial influence on the market" that destabilized prices and destroyed the hedging value of the futures markets. 205

In considering how to prevent this conduct, it was asked in the hearings whether a statute could be framed in order to allow the government to proceed against an individual who had acquired a large amount of wheat for the purpose of either depressing or boosting the market. The response was that this would be a difficult statute to draft. 206 Instead, drafters thought that limitations should be placed on the amount of trading by large traders. Such position limits would prevent transactions that resulted in a cornering of the market or which resulted in an excess of large scale trading. 207 This policy would "prevent upsetting or disturbing the market; in other words . . . prevent manipulation." 208

The Commodity Exchange Act, as adopted, thus not only prohibited manipulation, but it also allowed the government to set position limits. Additionally, it sought to remedy the decision in the Cutten case so that sanctions could be brought against someone who had actually completed a manipulation. 209 In expanding the reach of the prohibition against manipulation, however, Congress did not define the term manipulation. Nor is the legislative history particularly helpful.

201. 80 CONG. REC. 6164 (1936) (remarks of Sen. Murphy).
204. 78 CONG. REC. 10449 (1934) (remarks of Rep. Pierce). The GFA had difficulty explaining to Congress why it had brought so few administrative cases. Amend the Grain Futures Act, supra note 139, at 261-63; Regulation of Grain Exchanges, supra note 164, at 264.
205. Commodity Short Selling, supra note 152, at 201-02.
206. Id. at 120. One participant stated that "the prohibition ought to be based upon the act of manipulation, whether he is actually manipulating the price. That is the thing that you are after." Id.
207. 78 CONG. REC. 10449 (1934) (remarks of Rep. Gilchrist). The FTC STUDY had previously suggested position limits. FTC STUDY, supra note 25, at 259.
209. 7 U.S.C. §§ 6a & 13(b) (1936). See 80 CONG. REC. 7847 (1936) (remarks of Sen. Robinson); 78 CONG. REC. 10451 (1934) (remarks of Rep. Hope) (the purpose of the Commodity Exchange Act is "to make a broader market, one which is not manipulated, and a better market in which legitimate hedging transactions can be carried on"); 79 CONG. REC. 8589 (1935) (remarks of Rep. Jones) (the Commodity Exchange Act sought to "check manipulation of markets by certain big traders").
There are two brief snippets of legislative history that have been used by the courts and agencies to discern what is meant by manipulation. The first of these was a statement by Arthur Marsh in hearings held on cotton price fluctuations. There, Marsh stated that manipulation, “is any and every operation or transaction or practice, the purpose of which is not primarily to facilitate the movement of the commodity at prices freely responsive to the forces of supply and demand; but, on the contrary, is calculated to produce a price distortion of any kind in any market either in itself or in its relation to other markets.”

Marsh stated that manipulators use “devices by which the prices of contracts . . . may be higher than they would be if only the forces of supply and demand were operative; or [use] . . . devices by means of which the price or prices . . . in a given market may be made lower than they would be if they were freely responsive to the forces of supply and demand.” He also stated that “[a]ny and every operation, transaction, device, employed to produce those abnormalities of price relationship in the futures markets, is manipulation.”

The other statement was made by Senator Pope who defined a “squeeze” or “congestion” in the market as “a condition in maturing futures where sellers (hedgers or speculators), having waited too long to close their trades, find there are no new sellers from whom they can buy.” He stated that another aspect of a squeeze or congestion is that “[d]eliverable stocks are low, and it is too late to procure the actual commodity elsewhere to settle by delivery. Under such circumstances, and though the market is not cornered in the ordinary sense, traders who are long hold out for an arbitrary price.”

Legislators treated the lack of a definition of manipulation with some evasion and levity in the hearings on the Commodity Exchange Act. But the GFA also noted that “it is practically impossible, merely because a man sells, to prove that he is doing it in order to manipulate the market.”

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210. See infra notes 276, 278, 287 & 484 and accompanying text.
211. Cotton Prices, Hearings Before a Subcommittee of the Senate Committee on Agriculture And Forestry, 70th Cong., 1st Sess. 201-03 (1928) [hereinafter Cotton Prices]. It has been asserted that Marsh’s statement does not provide much guidance in defining manipulation. Redefining the Offense, supra note 17, at 360-63. As one commentator noted, “The difficulty with this definition is that it appears to impose an obligation not to act in one’s own best interest.” Id. at 372.
212. Cotton Prices, supra note 211, at 201-03.
213. 80 CONG. REC. 8089 (1936).
214. Id.
215. Mr. Heffelfinger. . . . What is a corner on the market?
Senator Murphy: Oh, I guess we all have pretty general ideas about what a corner on the market is, haven’t we?
Senator Murphy: You asked me what a corner is, Do you know what a corner is? You are arguing against this provision here in relation to a corner. Obviously, you have some knowledge about what a corner is. What is it?
Senator Norris: Mr. Chairman, the American people for many years have been hunting a corner that they could get around [laughter] and find the other side of it. Amend the Grain Futures Act, supra note 139, at 124.
216. Commodity Short Selling, supra note 152, at 181.

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difficulty should have forewarned Congress of the effects of its undefined prohibition against manipulation.

II. The Commodity Exchange Act Proves to be Ineffective in Dealing with Manipulation

A. The Commodity Exchange Authority Unsuccessfully Struggles with Manipulation

Because the Commodity Exchange Act did not define manipulation, the task of interpretation was left to the courts and to another small agency within the Department of Agriculture—the Commodity Exchange Authority ("CEA")—which administered the statute under the direction of the Secretary of Agriculture and a Commodity Exchange Commission composed of the Secretaries of Agriculture and Commerce and the Attorney General.\(^\text{217}\) During its nearly 40 year existence, the CEA continually faced concerns of congestion and manipulation, which it often sought to resolve by deferring to the exchanges. In fact, problems began almost immediately for the CEA. It found congestion also in rye and corn in the May 1936 contracts, and it was concerned with the December 1936 corn contract on the Chicago Board of Trade.\(^\text{218}\) The CEA soon encountered problems in potatoes as well,\(^\text{219}\) and congestion occurred later still in the September 1937 corn futures contract, which ultimately resulted in suspension of trading by the Chicago Board of Trade. Investigations revealed that the market had been substantially controlled by one long trader and two short traders who had fought each other out in the pit: "The result was a stubborn struggle between the opposing interests. They refused to settle their contracts except on profitable terms."\(^\text{220}\) In 1939, problems with congestion occurred three times in the cotton market because of the operations of a few traders.\(^\text{221}\)

Early in its existence, the CEA also brought an action against Cargill Inc., ("Cargill"), a Cargill subsidiary, and certain of its officers. The CEA alleged that these respondents were operating a corner in the 1937 September corn futures contract and that they manipulated the December 1937 corn futures contract on the Chicago Board of Trade by short selling some ten million


\(^{218}\) REPORT OF THE SEC. OF AGRIC. 75 (1937); REPORT CHIEF COMMODITY EXCH. ADMIN., 16 (1937).

\(^{219}\) Id. at 16-17.

\(^{220}\) REP. OF THE SEC. OF AGRIC., supra note 218.

The CEA also charged the respondents with engaging in wash sales for the purpose of creating a false impression of market activity and stimulating public participation.

In March of 1940, the CEA denied trading privileges to Cargill’s president, but stopped short of subjecting Cargill itself to a trading prohibition. This action did not prove to be much of a deterrent. In 1951 Cargill manipulated the price of oat futures, and it was then barred from trading. Still later, the CEA found Cargill guilty of manipulating the May 1963 wheat contract on the Chicago Board of Trade. Cargill’s ongoing activity in the face of CEA sanctions provides a case in point for the ineffectiveness of the Act’s prohibition against manipulation.

The CEA faced several other market emergencies in its early years. For example, in 1939, congestion in the cotton market threatened to create serious price disturbances on three occasions. The loss of the European markets under Nazi conquest began to depress grain prices. The exchanges were asked to report to the CEA on measures to prevent unwarranted speculation as the result of the war, but the exchanges did not provide many useful proposals. The CEA brought manipulation charges in connection with trading in the October 1940 wool top (long fibers combed from wool) and other markets.

When the European War broke out the commodity markets behaved like “yo yo’s” and the “smart money went into wheat.” However, after the attack on Pearl Harbor, the CEA made efforts to prevent panic trading and implemented several measures, including price ceilings to stabilize prices.

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222. Cargill had been expelled from the Chicago Board of Trade for its activities in the corn market during this period. Cargill complained to the CEA that the Board of Trade’s action was improper. The CEA later dismissed the complaint. REPORT CHIEF COMMODITY EXCH. ADMIN. 17 (1938). REPORT CHIEF COMMODITY EXCH. ADMIN. 39-40 (1939).

223. Supra note 198, at 1378. The CEA charged Cargill with manipulating the December corn future by selling futures contracts that covered ten million bushels of corn. At the same time, Cargill was seeking to corner the September corn future, all in an effort to create artificial prices. REPORT CHIEF COMMODITY EXCH. ADMIN. (1940). The trading suspension for the Cargill president was lifted in 1942. See In re Cargill, CEA Docket No. 11, Order of June 25, 1942, COMMODITY EXCHANGE AUTHORITY U.S.D.A. DEPT. OF AGRIC., SUMMARY OF ADMIN. & JUDIC. PROC. UNDER THE COMMODITY EXCHANGE ACT (1942).


226. REPORT CHIEF COMMODITY EXCH. ADMIN. 40 (1939).

227. REPORT CHIEF COMMODITY EXCH. ADMIN. 2 (1941).

228. Id. at 7-8.

229. Id. at 13.


231. See REP. ADMINISTRATOR, AGRICULTURAL MARKETING ADMIN. 68-69 (1942); Agriculture Department Appropriation Bill for 1943, Hearings Before a Subcommittee of the House Committee on
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The CEA also asked the exchanges to increase their margin requirements voluntarily in order to curtail speculation. The Secretary of Agriculture further asked that futures trading be suspended in grain futures at specified price levels, and the exchanges agreed to this arrangement.

Nevertheless, manipulation continued. The CEA charged Daniel Rice and General Foods Corporation with attempting to corner the 1944 Chicago rye futures market. For two years, General Foods had purchased Chicago rye futures and took delivery of rye. Other respondents engaged in heavy purchasing and sold the rye to General Foods at locations outside the delivery system in Chicago. In addition, they took delivery of Canadian rye for the alleged purpose of keeping the rye out of the Chicago market and thereby increasing prices. The CEA found that this conduct violated the manipulation provisions of the Commodity Exchange Act. The Seventh Circuit dismissed the case, however, holding that these activities were simply efforts designed to stabilize prices and not to manipulate them. The CEA continued to believe, however, that pegging or stabilizing of prices constituted manipulation just as much as a manipulation designed to increase or decrease prices.

At the end of World War II, numerous problems arose in the commodity futures markets. For example, the lifting of price ceilings in cotton caused a tremendous rise in prices and a later collapse that "constituted one of the most rapid and extensive price movements in the history of the cotton markets." A select committee of Congress undertook a massive investigation of trading in the markets between July 1, 1946 and June 30, 1948. Among other things, the committee found that two concerns may have been attempting to corner the cotton seed market. It also found that there had been a leak of...
confidential information concerning government commodity buying policies and that there had been a large amount of speculation in lard prior to an official announcement.\textsuperscript{240} For example, there was unusual trading in lard by a small company that had never traded before.\textsuperscript{241} Two former high government officials had also traded.\textsuperscript{242}

The select committee further found that speculation in commodities on the futures markets had reached a tremendous volume in 1947. It urged the Congress to watch commodity speculation closely and, if necessary, "enact legislation to eliminate rigging and manipulation on the exchanges."\textsuperscript{243} It noted, however, that speculators had "developed highly complex techniques for concealing the nature of their buying and selling activities and the sources of information upon which they conducted their operations."\textsuperscript{244}

Of particular concern was speculation that occurred in the Chicago wheat market in February and March 1947.\textsuperscript{245} The Secretary of Agriculture noted that on February 4, 1947, at a time when a sharp break in wheat prices was occurring, one speculator had sold short approximately one million bushels of July wheat and made a then staggering profit of several hundred thousand dollars.\textsuperscript{246} President Truman then requested the grain exchanges to increase their margin requirements in order to curb speculation.\textsuperscript{247}

Following a large break in grain prices occurring in February 1949, there was a large price break in wool tops on March 16 and 17, 1949.\textsuperscript{248} The

\begin{thebibliography}{9}
\bibitem{240} Id. at 12.
\bibitem{241} Id. at 15.
\bibitem{242} Id. at 16. \textit{see also}, H.R. REP. No. 2449, 80th Cong., 2d Sess. 5-6 (1948). The CEA later brought a lard manipulation case. \textit{See Moore v. Brannan}, 191 F.2d 775 (D.C. Cir.), \textit{cert. denied}, 342 U.S. 860 (1951). \textit{See also} H.R. REP. No. 2462, 80th Cong., 2d Sess. 27 (1948) (concern expressed that government grain purchase price changes may have been leaked to traders); T. Szulc, \textit{Then and Now: How the World Has Changed Since WW II} 98 (1990) (description of massive government grain exports for relief of Europe after war).
\bibitem{243} H.R. Rep. No. 2472, \textit{supra} note 238, at 17.
\bibitem{244} \textit{Id.} at 17. To Amend the Commodity Exchange Act, \textit{Hearings Before the Subcommittee on Domestic Marketing and Consumer Relations of the House Committee on Agriculture on H.R. 11788}, 89th Cong., 2d Sess. 191-92 (1966). The CEA also later observed a phenomenon of manipulation through the "group action" of speculators which it described as:

\textit{Manipulative activity by the group technique involves a number of closely associated speculators whose combined activities are large enough to manipulate the price, although no one of the group may have holdings large enough to exert an apparent price effect. In order to prove manipulation in such instances it may be necessary to establish collusion or common understanding among members of the group. Usually this is difficult, and must be based largely on circumstantial evidence, since the members of the group are not likely to admit collusive action, and the contacts between the various participants are not ordinarily committed to writing.}
\bibitem{245} \textit{H.R. Report No. 2472, supra} note 238, at 17.
\bibitem{246} \textit{Id.} at 17. To Amend the Commodity Exchange Act, \textit{Hearings Before the Subcommittee on Domestic Marketing and Consumer Relations of the House Committee on Agriculture on H.R. 11788}, 89th Cong., 2d Sess. 191-92 (1966). The CEA also later observed a phenomenon of manipulation through the "group action" of speculators which it described as:

\textit{Manipulative activity by the group technique involves a number of closely associated speculators whose combined activities are large enough to manipulate the price, although no one of the group may have holdings large enough to exert an apparent price effect. In order to prove manipulation in such instances it may be necessary to establish collusion or common understanding among members of the group. Usually this is difficult, and must be based largely on circumstantial evidence, since the members of the group are not likely to admit collusive action, and the contacts between the various participants are not ordinarily committed to writing.}
\bibitem{248} \textit{Margin Requirements on Commodity Exchanges Hearings on S1881 Before the Senate Comm. on Agric. and Forestry, 80th Cong., 2d Sess. 3, 5, 20} (1948). This trader, E.T. Maynard, was a floor trader in Chicago. \textit{Id.} at 6.
\bibitem{249} \textit{Report Admin. of the Commodity Exch. Auth. 4-5} (1947).
\bibitem{250} \textit{Report of the Admin. Commodity Exch. Auth. 4-5} (1949).
\end{thebibliography}
outbreak of the Korean War also led to speculative trading of an "almost frenzied character." President Truman again unsuccessfully requested Congress to authorize federal control of margins and to curb speculation in agricultural commodities.

The CEA found additional manipulation in the egg market. In Great Western Food Distrib. v. Brannan, the CEA charged that Great Western Food Distributors Inc. had manipulated the December 1947 egg future on the Chicago Mercantile Exchange. It had acquired a large cash position in deliverable eggs, and it stood for delivery on its futures contracts. The Seventh Circuit later found that Great Western had cornered the market. The court stated that the intent of the parties is a determinative element in establishing a corner, and that it must make a determination as to whether prices were artificial. The court found that the combination of a controlling interest in the cash supply and futures resulted in abnormal prices. It made this determination from an extensive economic analysis of the historical relationship of egg prices with the futures contract in question. With respect to the requirement of intent, the court also stated that all that needed to be proven was that the trading program was intentionally undertaken. The company's trading privileges

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249. See also CEA, CURRENT SPECULATION IN COMMODITY FUTURES, (July 31, 1950); Lahey, Fattening On Futures, NEW REPUBLIC, May 21, 1951, at 11.
250. R. DONOVAN, CONFLICT AND CRISIS 349 (1977) (stating Truman's opposition to speculation); Federal Regulation, supra note 17, at 822, n. 2. One politician, Fiorello LaGuardia, urged President Truman to "put every dabbling grain exchange out of business." T. KESSNER, supra note 45, at 584. But Congress did not act.
251. 201 F.2d 476 (7th Cir.), cert. denied, 345 U.S. 997 (1973). Great Western distributors had previously been accused of price manipulation by the CEA and had been suspended from trading for a period of 10 days after it admitted a "violation." REPORT CHIEF COMMODITY EXCH. ADMIN. 13 (1941).
252. 201 F.2d at 484.
253. Id. at 482-84.
254. Id. at 483.
255. The court disagreed with some of the economic analysis of the government. It noted that it had not been provided with the October and November 1947 egg prices and therefore there was nothing in the record to show that the December prices were abnormally high in relation to the preceding months. The court stated that the fact that December 1946 prices were considerably lower than those prevailing in December 1947 was not alone sufficient to show abnormal prices. The court had not been told of anything concerning the comparative market conditions prevailing in those two years. The government did show that there was an abnormal difference between the December 1947 and January 1948 futures contract prices. Some years, however, had to be excluded because of price controls and it was also claimed that certain years were "depression" years that had abnormal differences as well. Nevertheless, it was still found that the spread and prices at issue were abnormal. Id. at 482-83.
256. Id. at 484. The court defined a corner as:

[A]n executed plan of manipulation of prices of a given commodity whereby a trader or group of traders gains control of the supply or the future demand of a commodity and requires the shorts to settle their obligations, either by the purchase of deliverable quantities of the supply or offsetting long contracts, at an arbitrary, abnormal and dictated price imposed by the cornerer. This manipulation may be effected by a creation of an artificial demand through purchases of long contracts in excess of the known deliverable supply . . . . or by the purchase of all the available cash supply . . . or by a combination of both, as charged in this complaint.

201 F.2d at 478-79 (citations omitted).
were suspended for one year.\textsuperscript{257} The company later became the subject of a rare criminal action under the Commodity Exchange Act for trying to manipulate the October 1949 egg futures contract on the Chicago Mercantile Exchange.\textsuperscript{258}

Similarly, in \textit{G.H. Miller & Co. v. United States},\textsuperscript{259} the Seventh Circuit held that the respondents "had a corner; that they knew it and had the shorts on their knees and at their mercy."\textsuperscript{260} Nevertheless, the court did note that corners can develop unintentionally and that it is difficult to prove by direct evidence that transactions by traders are undertaken pursuant to an agreement or understanding to act collectively. Such evidence must be circumstantial unless one of the respondents confesses, which is unlikely. Here, the chain of circumstances established \textit{prima facie} that respondents acted "with the intent that their combined acquisitions would cause an artificial price increase and enable them by pressure to unjustly liquidate their holdings at a profit."\textsuperscript{261}

This proved to be but another in a long series of egg manipulation cases.\textsuperscript{262}

Perhaps the most manipulated market of all was onions. For example, in \textit{Vincent W. Kosuga},\textsuperscript{263} the CEA charged that onion prices had been manipu-

\begin{quotation}
\textsuperscript{257} 201 F.2d at 477-78. Charges were dismissed against two respondents. \textit{REPORT OF THE ADMIN. COMMODITY EXCH. AUTH. 25-26} (1953).
\textsuperscript{258} Upon a plea of \textit{nolo contendere}, Great Western Food Distributors Inc. was fined $21,200 and five other defendants were fined a total of $10,800. \textit{CEA, FUTURES TRADING UNDER THE COMMODITY EXCH. ACT 1946-1954 35} (1954); \textit{REPORT ADMIN. OF THE COMMODITY EXCH. AUTH. 15-16} (1950).
\textsuperscript{259} 260 F.2d 286 (7th Cir. 1958), cert. denied, 359 U.S. 907 (1958).
\textsuperscript{260} 260 F.2d at 289.
\textsuperscript{261} Id. at 290.
\textsuperscript{263} In David G. Henner, 30 Agric. Dec. 1151 (1971) manipulation of the November 1968 shell egg futures contract was found to have occurred on the Chicago Mercantile Exchange in the last few seconds of trading. The hearing officer there wrote a lengthy opinion. Among other things, he made an extensive examination of various definitions of the terms manipulations, corners and squeezes, including the following: ‘Manipulation’ is a vague term used in a wide and inclusive manner, possessing varying shades of meaning, and almost always conveying the idea of blame-worthiness deserving of censure. There is usually also an implication of artificiality and of skillful and ingenious management. In its most common use it has reference to a speculator, or to a group of speculators who buy or sell produce, in such a way as to give outsiders the impression that such buying or selling is the result of natural forces. Hence the term includes excessive speculation, the spreading of false rumors, the working of syndicates to increase or depress prices, ‘wash sales,’ ‘matched orders,’ and ‘corners.’ \textit{Id.} at 1226 (quoting SMITH, \textit{ORGANIZED PRODUCE MARKETS 109-110} (1922)).
\textsuperscript{264} 19 Agric. Dec. 603 (1960).
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lated upward and then downward. The respondent, Kosuga, had taken delivery on cash onions and removed them from delivery channels. Sales of onions were made, but then Kosuga agreed not to make further sales in order to strengthen the market price of onions. However, Kosuga began selling short futures contracts on the Chicago Mercantile Exchange and began making large deliveries on that market. The judicial officer noted that "[d]rawing a line between legitimate trading and trading with manipulative intent is sometimes a very difficult task."264 Upward manipulation was found in the agreement with onion growers to remove onions from the delivery channels.265 Although this may have been an attempt to stabilize prices, the CEA, unlike the court in General Foods Corp. v. Brannan,266 believed that this was an improper motive and that it caused prices to move to an artificial level.267 A short manipulation was also found in the selling of the futures contracts and deliveries in Chicago. An artificial price was found when prices were compared with onion prices of preceding years.268

Numerous other instances of wild onion price fluctuations occurred in the Chicago market.269 Congress later found that onion futures had been manipulated by a small number of individuals. In one instance, to their surprise, these individuals had received several carloads of onions that had been shipped to Chicago. Onions in Chicago then sold for less than the cost of the bags in which they were contained, and it resulted in "a terrible waste" of the onions in Chicago, and caused a scarcity of the product in other locales. It also resulted in waste of transportation facilities to bring the onions to Chicago.270 As a result of all this, Congress prohibited trading in onions. It remains banned even today.271

Onions were not the only problems encountered by the CEA during the 1950s. In fact, price manipulations were "attempted on a large scale in several

264. Id. at 615.
265. Id. at 616.
266. 170 F.2d 220 (7th Cir. 1948).
268. 19 Agric. Dec. 619-624. Cf. Kelly v. Kosuga, 358 U.S. 516 (1959) (agreement between Kosuga and purchaser of onions that was designed to keep onions off the market was an enforceable contract once the sale of the onions was completed).
269. Department of Agriculture Appropriations for 1959: Hearings Before A Subcommittee Of The House Comm. on Appropriations, 85th Cong., 2d Sess. (Part II) 1057-1058 (1958); B. TAMARKIN, supra note 33, at 29 ("[h]ardly a day passed, it seemed, without somebody trying to corner the onion market or squeeze prices higher or push them lower").
271. 7 U.S.C. §2, Pub. L. 85-839, (1958). This legislation apparently resulted from a March, 1953, attempt to corner the onion market. The CEA, however, had advised Congress that it was the peculiar nature of onions, which are highly perishable, that made them susceptible to large price swings. S. REP. NO. 766, 84th Cong., 1st Sess. 2 (1955).
commodities including eggs, soybeans, oats and potatoes. For example, in In re Landon v. Butler, the respondents were found to have controlled the soybean market in Chicago during June and July 1954. Among other things, they sold soybeans under terms and conditions which rendered the soybeans unavailable for delivery on futures, and large quantities of soybeans were shipped out of Chicago under uneconomic conditions. Respondents entered orders on the exchange that were designed to increase prices. Respondents also circulated false information concerning large shipments of deliverable soybeans out of Chicago.

Cotton posed other problems. In Volkart Brothers v. Freeman, the Fifth Circuit considered CEA charges in which it was claimed that Volkart Brothers had manipulated the October 1956 cotton futures contract on the New York and New Orleans Cotton Exchanges by a controlling long position in futures contracts. It was charged by the CEA that this position had been used to exploit the fact that there was an insufficient supply of cotton that was eligible for delivery. In considering these charges, the Fifth Circuit took note of the earlier Congressional testimony of Arthur R. Marsh as a means of providing guidance on what constitutes manipulation. The court concluded from that testimony that the term manipulation means more than the charging of what someone may consider to be an unreasonably high price. Rather, there must be an intent to create prices that are not responsive to the forces of supply and demand. Manipulative conduct must be calculated to produce a price distortion. A squeeze not planned or intentionally brought about by a trader would not be actionable under the Commodity Exchange Act.

The court also relied upon Senator Pope’s description of what constituted a squeeze in the debates on the Commodity Exchange Act. Here, too, the court noted that some squeezes are the result of natural forces and not illegal activities. Consequently, the intent of the parties would be a determinative element in establishing a violation of the manipulation prohibitions of the Commodity Exchange Act. Therefore, in order to establish a violation it must be shown not only that the respondent profited from the squeeze but also that

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274. Butler, who lived in the Graceland mansion that Elvis Presley later purchased, was convicted of fraud in connection with his soybean operations. It was found he was selling soybeans that he did not own. Laing, Still Full of Beans, BARON’s April 30, 1990.

275. 311 F.2d 52 (5th Cir. 1962).

276. Id. at 58. This testimony is described supra at notes 211-212 and accompanying text.

277. 311 F.2d at 58-59, citing FTC STUDY, supra note 25.

278. 311 F.2d at 58 note 10. Senator Pope’s statement is set forth supra at notes 213-14 and accompanying text.
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it intentionally brought about the manipulation by planned action. Generally this will require that the trader effectively controlled the spot commodity so that it could use a dominant long futures position to squeeze or corner the market.\(^\text{279}\)

In this case, there were millions of bales of cotton available for delivery around the country. The cotton had not been certificated formerly for delivery by the required delivery date, but the court concluded that the shorts had had adequate opportunity to have done so. The court stated that the shorts were required to exercise “due diligence” to assure that they had available supplies for delivery.\(^\text{280}\) The respondents had no duty to assume that the short traders would not meet their delivery obligations by obtaining certificated cotton in time for the delivery period.\(^\text{281}\)

This decision proved particularly troubling for the CEA because it concluded that natural corners and squeezes will occur and that, as such, they are not actionable under the Commodity Exchange Act, even where a trader is exploiting the situation.\(^\text{282}\) Further, the Court imposed an obligation upon the shorts to assure that they had adequate deliverable supplies on hand should they choose to stay in the market as delivery approached. The decision, therefore, gave long traders a license to exploit congested markets, provided that they did not intentionally attempt to create an artificial price. As might be expected, this decision was not accepted by the CEA.\(^\text{283}\)

The Volkart decision must also be contrasted with a subsequent decision of the Eighth Circuit in Cargill Inc. v. Hardin.\(^\text{284}\) There it was charged that Cargill and others had manipulated wheat futures prices. Cargill had owned the bulk of deliverable wheat in Chicago, and the futures contract could not be liquidated in an orderly fashion when the Spanish government announced it would be purchasing wheat. The court rejected the claim that a trader must profit from a manipulation or that it must commit an “uneconomic act” in order to violate the Commodity Exchange Act, noting that manipulations through rumors does not involve an uneconomic act.\(^\text{285}\) The court found that Cargill

\(^{279}\) 311 F.2d at 59.
\(^{280}\) Id. at 60.
\(^{281}\) Id.
\(^{282}\) Id. at 58-59.
\(^{284}\) 452 F.2d 1154 (8th Cir. 1971), cert. denied, 406 U.S. 932 (1972).
\(^{285}\) 452 F.2d at 1163. The court stated that:

We think the test of manipulation must largely be a practical one if the purposes of the Commodity Exchange Act are to be accomplished. The methods and techniques of manipulation are limited only by the ingenuity of man. The aim must be therefore to discover whether conduct has been intentionally engaged in which has resulted in a price which does not reflect basic forces of supply and demand. In such an inquiry, the question of whether an alleged manipulator has made a profit is largely irrelevant, for the economic harm done by manipulation is just as great whether there has been a profit or a loss in the operation. . . . And it may be pointed out that one of the most common manipulative devices, the floating of false rumors which affect futures prices, does not involve the commission of an 'uneconomic act.' Thus we must reject Cargill's
had acquired a dominant position in the futures contract and that there was an insufficient supply of wheat available from other sources for the opposite sellers to deliver. Although there were supplies of wheat in surrounding areas that could have been shipped to Chicago, it was of a different grade and no premium was allowed for its delivery. In addition, the cost of shipping the wheat into Chicago was an economic impediment that made it cheaper to pay a premium to Cargill than to pay those charges.286

The court conducted an economic analysis to determine whether the prices were artificial.287 Futures prices over the preceding nine years were compared with those that occurred in the contract at issue. It was found that Cargill’s trading resulted in a record rise in the futures prices in the last two days of trading that was not comparable to any movements of the past nine years. Other price relationships were also of greater magnitude than had been seen in prior years.288

The Cargill court refused to adopt the Volkart decision.289 But the decision in Cargill was a somewhat mixed victory for the CEA. Sanctions were suspended because the action had taken so long.290 Consequently, the CEA received no more than what it viewed to be a favorable decision to offset the effects of the Fifth Circuit’s decision in Volkart.

The CEA encountered other problems during the 1960s. For example, the CEA found excessive speculation occurring in sugar futures contracts on the New York Coffee and Sugar Exchange that contributed to a large price increase and a subsequent sharp drop in prices on that exchange.291 Wild price fluctuations occurred in the May 1964 wheat futures contract, and sharp

contention that manipulation under the Commodity Exchange Act must include the commission of an ‘uneconomic act.’

452 F.2d at 1163.

Several years later, one commentator suggested that the test advocated by Cargill, i.e., the existence of an uneconomic act, should be the basis for imposing liability for manipulation cases. Redefining the Offense, supra note 17 at 393.

286. 452 F.2d at 1164-67.

287. Id. at 1167. In determining the elements of manipulation, the court relied upon Senator Pope’s statement in the hearings on the Commodity Exchange Act. Id. at 1161. Senator Pope’s statement is set forth supra at notes 213-214 and accompanying text. The court stated that squeezes are prohibited where prices are ‘intentionally’ manipulated. It also noted that many squeezes do not involve intentional manipulation of futures prices but are caused by natural market forces such as unusual weather conditions. Id. at 1161-62.

288. Id. at 1167-70.

289. Id. at 1172-73.

290. Id. at 1156. The Cargill case was not the only problem in wheat encountered by the CEA. See Continental Grain, 17 Agric. Dec. 854 (1958) (consent order determining that respondent manipulated March 1955 and September 1957 wheat futures contracts); Henry Kate, 18 Agric. Dec. 884 (1959) (respondents manipulated March and May 1959 wheat futures contract on Chicago Board of Trade; order entered by consent).

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increases occurred in Maine potato futures. Problems in cotton and wool on the New York markets also required extensive investigation, as did shell egg futures, spot eggs in Chicago and New York, flaxseed futures and cottonseed oil futures. A wool manipulation was charged in the May 1962 wool future on the New York Cotton Exchange, and problems were encountered in the September 1961 rye futures contract.

B. The 1968 Amendments Seek to Address the Manipulation Issue

In 1966, the CEA sought legislation that was designed to overturn the Volkart decision and enhance its ability to deter manipulation on the commodity futures markets. The proposed legislation contained a definition of manipulation, and it required the government to prove at least three factors. First, a price deviation between cash and futures prices must be shown. Second, the effect of such a deviation must be "to impair the effectuation of the declared purposes of the Act." Finally, a direct and demonstrable relationship between the alleged actions of the accused and an artificial or abnormal price must be proven.

The proposed bill further sought to grant the Secretary of Agriculture authority to raise margin requirements where there was a danger of manipulation, sudden or unreasonable fluctuations or unwarranted changes in the price of any commodity, excessive speculation, or any other activity expected to restrain trade. The legislation sought to restrict judicial review of CEA proceedings so as to prevent the courts from overturning CEA decisions as the court did in the Volkart case. The bill provided for increasing the penalties for manipulation by making such violations a felony, and it sought to grant the

293. Id.
296. To Amend the Commodity Exchange Act. Hearings on H.R. 11788 Before The Subcomm. on Domestic Marketing and Consumer Relations of the House Comm. on Agric., 89th Cong., 2d Sess. 16 (1966) [hereinafter 1966 Hearings]. Specifically, the proposed legislation defined manipulation as:

...the exacting, causing or maintaining of an abnormal or artificial price by any action or course of action which raises, depresses, fixes, pegs, or stabilizes the price at or to a level different than that which would otherwise prevail. Any such exacting, causing, or maintaining of an abnormal or artificial price shall constitute manipulation irrespective of any acts or omissions by the holders of futures contracts adversely affected thereby.

H.R. 11788, 89th Cong., 1st Sess. § 1 (d) (1965).
297. 1966 Hearings, supra note 296, at 3. This was not the first effort by the CEA to obtain authority from Congress to allow it to define the term manipulation. Such a request had been rejected in 1949. REPORT ADMIN. COMMODITY EXCH. AUTH. 9-10 (1949), noted in 1 L. LOSS, SECURITIES REGULATION 1168 n. 10 (2d ed. 1961); H.R. 4685, 81st Cong., 1st Sess. § 1 (1949) ("The word 'manipulate' shall mean to cause or maintain an artificial price by planned action."); S. 2807, 86th Cong., 2d Sess. § 1 (1960) ("The word 'manipulate' shall be construed to include the causing or maintenance of an artificial price by action intended for that purpose."); S. 1980, 87th Cong., 1st Sess. § 1 (1961) (same but definition is not "limited to" such action); S. 402, 88th Cong., 1st Sess. § 1 (1963) (same).
298. 1966 Hearings, supra note 296, at 5.
Secretary of Agriculture authority to seek injunctive relief against persons who were about to engage in violations of the Commodity Exchange Act.\textsuperscript{299} Moreover, the bill would have allowed the Secretary to suspend the registration of persons engaging in actions having the effect of restraining trade, which the department likened to provisions in the Sherman Antitrust Act.\textsuperscript{300} This power could be used even in the absence of evidence of price manipulation if there was evidence that a trader had sufficient control of a futures market to effectively restrain the trading in one or more commodities on that market.\textsuperscript{301}

Opposition to this proposed legislation was vigorous and sustained. Although the Department denied that its proposals were designed to overturn the \textit{Volkart} decision,\textsuperscript{302} the Exchanges, and at least Congressman Dole, were clearly of the view that exactly the opposite was the case.\textsuperscript{303} An industry witness charged that the Department of Agriculture was seeking to eliminate any requirement of intent from the statute. This was objectionable because it could make even legitimate conduct a crime. The witness pointed out that the CEA had proposed a definition of manipulation a few years earlier in which intent was included as an element. The witness claimed that this reversal demonstrated that Congress could not effectively define manipulation. Instead, the witness suggested that the development of a definition should be left to the courts.\textsuperscript{304}

The industry was equally insistent that the government should not be given the other powers it sought. The strongest opposition was to the proposal that the Department of Agriculture should be given the authority to control margins. Since margins were a means to control losses on the part of brokerage firms and exchanges and not a means to limit credit, the setting of margins should be left to those authorities. These leaders noted that Congress had earlier concluded that the idea that controlling margins could control commodity price

\textsuperscript{299} Id. at 7.
\textsuperscript{301} 1966 \textit{Hearings}, supra note 296, at 15.
\textsuperscript{302} Id. at 23.
\textsuperscript{303} Id. at 44, 53, 78, 92, 102.
\textsuperscript{304} Id. at 102-03.
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advances had "no foundation in fact." The examples cited by the Department of Agriculture as instances where it could have used such authority were also found to be unpersuasive.

As a result of this opposition, Congress did not adopt the proposed legislation. Nevertheless, the Department sought new legislation in 1967. This time, however, it did not seek power to control margins or the authority to define manipulation, the two elements of its 1966 proposal that had raised the most opposition. In support of these new proposals, an Assistant Secretary of the Department testified that there had been a long history of manipulation, fraud and dishonesty on the commodity exchanges. He cited an instance where a speculator was apprehended for falsifying records. At that time, the trader stated that he was going to sell out his long grain position on the United States futures markets and go back to Canada. In fact, he had a short position and the purpose of his announcement was to depress prices so that he could buy in his short position at a profit. In another case, a large company sold oat futures heavily in Chicago with offsetting purchases on the Winnipeg Grain

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308. Id. at 42. One matter that was not mentioned by the CEA in the hearings was "one of the most notorious financial scandals of our time" in which some $1.6 billion pounds of salad oil disappeared and losses of over $200 million were sustained. Miller v. New York Produce Exchange, 550 F.2d 762, 764-765 (2d Cir. 1977). This was the famous Salad Oil Swindle in which Anthony DeAngelis, through his Allied Crude Vegetable Oil Refining Corporation, purchased over ninety percent of the cottonseed oil futures contract on the New York Produce Exchange in order to inflate prices. When the market, nevertheless, turned against DeAngelis, he could not meet his margin calls. It was then discovered that he had used many millions of dollars in fake warehouse receipts as security for loans. One large New York Stock Exchange firm was forced to go out of business and the New York Produce Exchange failed. See In re Ira Haupt & Co., 234 F. Supp. 167 (S.D.N.Y. 1964), aff'd, 343 F.2d 726 (2d Cir. 1965), cert. denied, 382 U.S. 890 (1965); American Express Warehousing Ltd. v. TransAmerica Ins. Co., 380 F.2d 277 (2d Cir. 1967); N. MILLER, THE GREAT SALAD OIL SWINDLE (1965); Vogelson, Tightened Regulation For Commodity Exchanges, 55 A.B.A. J. 858 (1969).

One court noted in connection with a large position held by DeAngelis on the New York Produce Exchange that:

a concentration in the long interest like that achieved by Allied is fraught with potential danger to the market, inasmuch as it reduces liquidity, lessens price stability, heightens the risk of a disorderly liquidation of contracts . . . and in general threatens the maintenance of an orderly market.

Exchange. The company then moved cash oats from Winnipeg to Chicago to depress Chicago prices in relation to Winnipeg, all for the purpose of manipulating prices. In still another case, a speculator lost heavily in a manipulative attempt that was partially financed by warehouse receipts on soybeans. But the elevators where the soybeans were supposed to be kept were empty when his creditors tried to redeem the receipts. The Assistant Secretary stated that the hedging function of the markets and its liquidity were not being “served by massive speculation in which powerful interests slug it out to make the market go the way that will best serve their own speculative positions.”

The most vital of the amendments that the government was seeking was injunctive authority that could be used to stop manipulative activities before irreparable damage was done. Under existing standards, the Department had to undertake protracted administrative or criminal proceedings before a final order could be issued or a conviction obtained. The Assistant Secretary of Agriculture, Dr. George Mehren, testified, “Often irreparable damage is done, especially where continued fraud or manipulation is occurring. We can cite cases, large and small.” The Administrator of the CEA testified that there had been six specific cases involving manipulation where injunctive authority was needed and was not available.

The Department of Agriculture further sought to make manipulation a felony, as well as to obtain cease and desist administrative authority. The government sought authority to limit the power of a court of appeals to overturn the findings of the CEA. This was a renewed effort to avoid another decision such as that in Volkart where the court had found that the evidence did not support the CEA’s determinations.

The industry was, once again, vociferous in its opposition to the Department’s proposals. One industry witness, Robert V. Parrott, opposed the authority being sought to issue cease and desist orders and injunctive relief, stating that such powers were “fundamentally at odds with the realities of futures market trading.” He stated that a finding of manipulation requires a determination that there is an “unwarranted or unreasonable price change” and he did not believe that the Secretary possessed the necessary clairvoyance to identify whether a particular price change is unwarranted or unreasonable unless it was done through an after-the-fact analysis. Even then, “most futures price changes are seen to have been warranted by the emergence of new information. Because new information emerges randomly, however, it is

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309. 1967 Hearings, supra note 307, at 43.
310. Id. at 46.
311. Id. at 80-81.
312. Id. at 5.
313. Id. at 89-90, 102-103.
314. Id. at 27.
315. Id.
impossible to say what price change is unreasonable or unwarranted as it occurs." The witness also believed that a provision making manipulation a felony should be stricken from the bill because it would pose a grave threat to effective operation of contract markets. The witness further charged that the CEA proceedings were unfair because no respondent had ever prevailed in a proceeding that went to a decision by the Secretary, while the decisions of the Secretary had often been reversed by the court of appeals. In response, the Department of Agriculture stated that there had been a total of some fourteen administrative cases which were appealed to the federal courts and one criminal case (this apparently included all CEA cases and not just manipulation cases). In only three such cases had the Secretary of Agriculture been reversed.

The Chicago Board of Trade was even more strident in its opposition to the request for injunctive power. The Chairman of the Board of Trade, who would later become a CFTC Commissioner, stated that the use of injunctive power as the Department of Agriculture had suggested would be like making a "surgical incision with a meat axe." He stated that the Department of Agriculture had not proved that it was able to determine whether manipulation was actually occurring. In that regard, the witness noted that in cases on appeal to the circuit courts where charges of manipulation were at issue, the Department had been reversed three out of six times. The Chicago Board of Trade also stated that the mere existence of injunctive power could have a significant adverse effect on the markets. This was because the commodity markets have unique characteristics that distinguish them from markets regulated by other federal agencies where injunctive authority had been used for years.

As a result of this opposition, Congress declined to enact the requested authority for injunctive relief, stating that there was an insufficient showing that the Department of Agriculture needed such sweeping authority. Congress also rejected a change in the review standards for the courts of appeals. Nevertheless, a committee report found that the commodity markets were playing an increasingly important role in the economy and that those markets had been the scene of "economic struggles by powerful opposing groups." One Congressman stated that these economic "slug fests" had disrupted normal operations of the market, and that Congress was concerned that the "basi-
cally speculative feature of the markets, on occasions, leads to attempts—sometimes successful—to artificially influence prices.\textsuperscript{327} Congress therefore granted the Department of Agriculture authority to issue cease and desist orders, and made manipulation a felony.\textsuperscript{328}

C. The 1968 Amendments Prove to be Ineffective

The 1968 amendments did not prove effective in stopping price manipulations on the futures markets. This was due in part to the fact that, like the GFA, the CEA generally deferred to the exchanges. Its record in prosecuting manipulations also proved to be less than spectacular. By its own admission, only three criminal actions and some thirty administrative proceedings involving manipulation were brought throughout the thirty-eight year history of the CEA.\textsuperscript{329} The sanctions in its administrative proceedings were also remarkably lenient. The table included at the end of this Article lists the actions brought by the CEA and sets forth the sanctions in those cases, as well as the time that was necessary for decision.\textsuperscript{330} It seems clear from a review of this table that administrative action by the CEA should not have been a deterrent to anyone bent on breaking the law.

Apparently, in only two of the CEA cases was a total trading prohibition ordered.\textsuperscript{331} In the rest, suspensions of one year or less were generally imposed.\textsuperscript{332} However, various firms had their licenses to act as futures commission merchants revoked and other firms had their licenses suspended.\textsuperscript{333} In addition, a few floor brokers had their licenses revoked and several were suspended.\textsuperscript{334} However, these sanctions simply meant that these traders could not execute customer orders. They were free to trade for their own accounts after the short periods of suspension of their trading privileges. Consequently, if the purpose of the Commodity Exchange Act in prohibiting manipulation and making it a crime was to exclude individuals from the market who engaged in

\textsuperscript{327} S. REP. NO. 947, 90th Cong., 2d Sess. 3 (1968).
\textsuperscript{329} 1966 Hearings, supra note 296, at 88; 1967 Hearings, supra note 307, at 20-21.
\textsuperscript{330} See Appendix.
\textsuperscript{331} Even then the prohibitions were entered only upon the consent of the respondents or by default. See In re Winn & Lovett Grocery Company, 14 Agric. Dec. 561 (1955) (consent agreement pursuant to which sanctions were dropped against parent company of other respondents); In re Landon Butler, 14 Agric. Dec. 429 (1955).
\textsuperscript{332} See Appendix.
\textsuperscript{333} Id.
\textsuperscript{334} Id.
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such activities, the cases that were brought and sanctions that were imposed did not have that result and did not represent any meaningful deterrent.\textsuperscript{335} The CEA also faced other problems after the 1968 amendments. It simply had insufficient resources and jurisdiction to regulate the futures markets, which exploded as record inflation caused investors to rush into unregulated precious metals and other commodities such as coffee and sugar where there was a virtual price "bubble".\textsuperscript{336} People were concerned that speculation and manipulation on the commodity exchanges were fueling these rapid price increases.\textsuperscript{337}

Some of these price changes were unbelievable. Soybeans, for example, increased by over eight dollars a bushel in a period of some five months.\textsuperscript{338} This resulted in chaotic trading in soybeans futures contracts during the spring and summer of 1973. By early March the long side of the market was largely concentrated in the hands of a relatively small number of traders. On one day, more than ninety percent of all the long contracts on soybeans on the Chicago Board of Trade were held by only four traders.\textsuperscript{339} Between May 23, and June 27, 1973, the price of soybeans on the Chicago Board of Trade soared to the previously unheard of level of $12.90 per bushel. Ten months earlier, soybeans had been selling for $3.31 a bushel. Some charged that this cornering of the market by a handful of traders made it possible for the price of soybeans to go

\textsuperscript{335} Perhaps the most severe remedies were imposed in G.H. Miller & Co. v. United States, 260 F.2d 286 (7th Cir. 1958), cert. denied, 359 U.S. 907 (1959), where the registration of the company as a futures commission merchant was revoked and the registration of an individual floor broker was revoked. Their trading privileges were also denied for one year and trading privileges as to other respondents were denied for periods ranging from sixty days to one year. There were some fifteen respondents in that case.


\textsuperscript{337} Representative Sullivan stated that:

The incredible increases which have occurred in food prices since August of 1971, when the price control authority of the Economic Stabilization Act was first put into effect, can be attributed only in part to the excessive speculation in commodity futures trading, but excessive speculation in futures has been a significant part of the problem of food price inflation. Basically, the soaring food price index reflected the failure of the Administration from the very beginning of the controls program to impose price ceilings on any raw agricultural commodities. Coupled with an unrestricted export program, including the manner in which the Russian wheat deal was negotiated and allowed to take effect, the lack of controls over farmer prices and the inadequate controls over commodity futures speculation in farm commodities have resulted in price increases at the retail level which have hurt the American family grievously, and particularly the lower income families and those on fixed incomes. Speculation in non-food futures has contributed significantly to the increases in other living costs.

\textsuperscript{338} Id.

\textsuperscript{339} 20 CONG. REC. 30465 (1974) (remarks of Sen. Hart). One Senator stated that there were some "amazing things" going on in soybeans that were causing the "skyrocketing" of prices. Russian Grain Transactions, supra note 6 at 85 (1976) (remarks of Sen. Jackson); CFTC Role, supra note 305, at 716 (market reacted with "mob hysteria"). See also Smith, Commodity Futures Trading, 25 DRAKE L. REV. 1 (1975) (discussion of price runups) [hereinafter Commodity Futures Trading]. See also Case & Co. v. Board of Trade of City of Chicago, 523 F.2d 355 (7th Cir. 1975) (Chicago Board of Trade removed position limits on soybeans because rapid price increases did not allow shorts to cover their positions under existing Board of Trade price limits); In re Hugh P. King, [1975-1977 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 20,211 (C.F.T.C. 1976) (manipulation of July 1972 oat futures contract on the Chicago Board of Trade).

beyond any level justified by supply and demand. Consequently, the shorts were at the mercy of those who held the long contracts.\textsuperscript{340}

There was also concern with the 1973 cotton futures markets. In the fall of 1973, one trader on the New York Cotton Exchange held sixty-seven percent of all long contracts. The July 1973 corn futures also posed serious problems after it was discovered that there was no transportation available for the delivery of grain to Chicago, the delivery point for the contract. Consequently, traders on the long side of the market were able to demand as much as a dollar-thirty per bushel more for the contracts than the corn would have cost if it could have been delivered. There was adequate corn in Iowa, but it simply could not be brought into Chicago in time for delivery.\textsuperscript{341}

Several other critical events focused attention on the inadequacy of the CEA. Perhaps the most important was the so-called great "Grain Robbery" in which the Soviet Union made huge purchases of grain in the United States and drove grain prices to new levels.\textsuperscript{342} These purchases were not announced publicly for some months, during which time hedgers and others traded on the markets with knowledge of the sales. Apparently, the Soviets were secretly buying large futures positions as well as large amounts of cash grain. The rising futures prices caused by their purchases of cash grain were said to give the Soviets substantial profits, while consumers paid higher prices.\textsuperscript{343}

\begin{itemize}
\item \textsuperscript{342} D. MORGAN, MERCHANTS OF GRAIN 121 (1979) ("The 'Grain Robbery' of 1972 was one of those economic events that, like the OPEC Oil Embargo . . . , can truly be said to have changed the world."); H. R. REP. No. 975, 93d Cong., 2d Sess. 47-48 (1974); B. TAMARKIN, supra note 33 at 46-48.
\item \textsuperscript{343} Representative Adams stated that Our experiences with the Soviet wheat deal demonstrates the disastrous effects which unfair trading practices can have on farmers and consumers alike. Major grain exporting companies speculate freely on the commodities exchanges, and it appears that their manipulation of the trading allowed them to buy wheat cheap and keep it secret from other traders, later they sold it at higher prices to the Russians. We have all seen the results in high food prices and short grain supplies. Without new controls there is nothing to prevent foreign nations from manipulating commodity futures. 120 CONG. REC. 10741 (1974) (remarks of Rep. Adams). See also CFTC Role, supra note 305, at 747; Valdez, Modernizing The Regulation of the Commodity Futures Markets, 13 HARV. J. LEG. 35 (1975). On June 11, 1971, President Nixon announced that sales of grain to the Soviet Union and the People's Republic of China would no longer be subject to validated licensing provisions of the Export Control Act. He also announced that he was rescinding the American flag shipping provision that had been in effect for some eight years on United States grain exports. That provision had required fifty percent of United States grain to be transported in American-flagged vessels. Thereafter, in November of 1971, the Soviet Union purchased some three million tons of United States feed grains. Hearings on Russian Grain Transactions,
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It was further claimed that the closing price on the Kansas City Board of Trade had been raised in order to affect the U.S.D.A. subsidized program in connection with those sales. The CEA initially deferred to an exchange investigation to determine if there had been such a manipulation. The Exchange found no misconduct. However, the CEA later conducted its own investigation and found that the market had been manipulated on the close for several days, resulting in payments of millions of dollars in additional foreign export subsidies. This matter was referred to the Justice Department.344

III. The CFTC is Created in Order to Deal with the Issue of Manipulation and Market Disruption

A. The 1974 Amendments

These problems in the commodities markets, as well as a series of articles in the Des Moines Register, 345 which attacked the CEA as being an ineffective regulator, led to a series of Congressional hearings in which new legislation was proposed. 346 A Senate report noted that there had been a major shift in the United States to a "market-oriented" economy since the 1968 amendments to the Commodity Exchange Act, bringing the general public into the futures markets in growing numbers. 347 As a result, futures were "playing an increasingly important role in the pricing and marketing of the nation's commodities." The consumer was also becoming "increasingly aware that futures markets were

supra note 6, at 8. It was charged that this constituted some twenty-five percent of the United States wheat crop and that these purchases pyramidied into higher costs for feeding poultry and livestock, and eventually into large increases in prices to consumers, through higher cost of meats, eggs, poultry, butter and other commodities. Id. at 3.

344. H.R. Rep. No. 975, 93d Cong., 2d Sess. 47-48 (1974). It was claimed that the increased agricultural export subsidy that occurred as a result of the Soviet grain sales had cost taxpayers over three hundred million dollars. Hearings on Russian Grain Transactions, supra note 6, at 3. Later, the Continental Grain Company was charged with filing incomplete and inaccurate reports with respect to its cash positions in various commodities. Apparently no other action was taken. Id. at 168. This was not the first time that this company was subject of CEA inquiry. See Continental Grain Co., 17 Agric. Dec. 854 (1958). Its subsidiary was also later charged with manipulating the silver market in 1979 and 1980. See In the Matter of Hunt, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,296 (C.F.T.C. 1986); H.R. Rep. No. 395, 97th Cong., 1st Sess. (1981).


having a direct effect on such matters as his grocery bills and the cost of his home." The report stated that properly operating futures markets helped to hold down consumer prices by "reducing middleman costs." On the other hand, improperly operating futures markets could have the opposite result.348 "If individual speculators or groups operating in concert obtain control of the futures markets, price manipulation, corners and squeezes can occur, with adverse effects on producers and consumers alike."349 It seemed clear that additional regulation was needed, particularly since it appeared that the importance of the futures markets to the general public and to the nation was equal to that of the securities markets.350

Among other things, Congress now viewed injunctive authority as a "desperately needed"351 means of preventing market price disruptions and protecting market users.352 Senator Hart stated that this injunctive authority could be used to "prevent inflationary prices which do not reflect supply and demand -- but which are the result of speculation, manipulation of the markets, or some other force."353 Some in Congress thought that injunctive authority was needed "to stop a trader from maintaining a position in the market that is causing the market to be disrupted or causing an abnormal price movement."354

Congress determined that the problems in the commodity futures industry had brought about a crisis of public confidence, and it was determined that CEA resources were "totally inadequate to police the industry."355 Congress found that self-regulation by the exchanges had not been effective in stopping abusive trading.356 Further, many futures contracts were completely unregulated because the Commodity Exchange Act had not kept pace with developments in the industry. These contracts included silver, gold, coffee, sugar, cocoa and plywood and foreign currencies. There were also plans to expand futures trading to such things as home mortgages, all of which would be unregulated under the existing regulatory scheme.357

348. Id.
349. Id.
350. Id. at 19.
352. Id. at 68.
353. 120 CONG. REC. 30465 (1974).
355. Id. at 37. One Senator was particularly skeptical of the CEA, stating that he was intrigued by their utter lack of discipline, authority and capability: "[i]f there ever was a need for reform, it is in this area." Hearings on Russian Grain Transactions, supra note 6, at 86.
356. H.R. REP. No. 975, 93d Cong., 2d Sess. 38 (1974). It was stated that 'brokers, customers, and, eventually, the American economy suffers [sic] in this atmosphere of so-called 'self-regulation' where tradition and self-interest has [sic] been allowed to displacethe public interest." Id. at 38. See also S. REP. No. 1131, 93d Cong. 2d Sess. 19 (1974).
357. Id.
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To remedy this concern, Congress passed the Commodity Futures Trading Commission Act of 1974.\textsuperscript{358} It substantially amended the Commodity Exchange Act by creating a new federal regulatory commission to regulate the CEA.\textsuperscript{359} This agency, the Commodity Futures Trading Commission (CFTC), was designed to be comparable to the Securities and Exchange Commission.\textsuperscript{360} The CFTC was given expanded powers under the Commodity Exchange Act, including injunctive authority, and was given exclusive jurisdiction over all futures trading.\textsuperscript{361} A significant provision that was enacted as a means of preventing violations gave authority to the CFTC to declare a market emergency.\textsuperscript{362} Whenever it had reason to believe that an emergency existed, the amendment allowed the CFTC to direct a contract market to take such action as the CFTC believed necessary to maintain or restore orderly trading in, or liquidation, of any futures contract. Such emergencies would include “threatened or actual market manipulation and corners,” any act of the United States or a foreign government that would affect a commodity, or any “major market disturbance which prevents the market from accurately reflecting the forces of supply and demand for such commodity.”\textsuperscript{363} Exchanges were also authorized to take emergency action.\textsuperscript{364}

The CFTC was given authority to designate additional delivery points on a contract market.\textsuperscript{365} It was thought that this would allow the CFTC to relieve pressure on contracts when, for transportation or other reasons, shortages of

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\bibitem{358} PUB. L. NO. 93-463, 88 Stat. 1389.
\bibitem{359} Id. It was thought that this legislation would: “significantly strengthen the regulation of commodities trading, protect the investor, and assure the consumer, the farmer, the commodity user, and the public at large that price manipulations and trading abuses on futures exchanges will not be tolerated.” 120 CONG. REC. 34999 (1974) (remarks of Sen. Clark). In the process of congressional debate on the creation of the CFTC, it was initially thought that the Commission should be composed of a part-time panel of members. But the argument was successfully made that a full time commission was needed to respond to squeezes and manipulations that could occur so fast that a part-time panel would be unable to cope with them. 120 CONG. REC. 10762 (1974) (remarks of Rep. Smith).
\bibitem{361} 7 U.S.C. § 13a-1 (Supp. I 1990). Among other things, registration categories were expanded to include commodity pool operators and commodity trading advisors. 7 U.S.C. §§ 6m and 6o. Such authority had been sought at least since 1949. See H.R. 4685, 81st Cong., 1st Sess. (1949).
\bibitem{362} 7 U.S.C. § 12a(9).
\bibitem{363} Id.
\bibitem{364} Id. \textit{See also} 17 C.F.R. § 1.41.
\bibitem{365} 7 U.S.C. § 7a(10). The exchanges were already required to extend delivery periods where to do so would prevent “‘squeezes’ and market congestion.” 7 U.S.C. § 7a(4). \textit{See generally, REPORT CHIEF COMMODITY EXCH. ADMIN. 14 (1938) (discussion of order of Secretary of Agriculture requiring extended delivery period). The CFTC later worked with the Chicago Board of Trade to add two additional delivery points for the corn contract. This followed a series of congested market problems that resulted from a growth of corn trading without an increase in storage capacity in Chicago. Toledo and St. Louis were added as delivery points. \textit{Extend Commodity Exchange Act: Hearings on H.R. 10285 Before the Subcommittee on Conservation and Credit of the Committee on Agriculture, 95th Cong., 2d Sess. 20 (1978) [hereinafter 1978 House Hearings To Extend Commodity Exchange Act]. See also Reauthorization of the Commodity Futures Trading Commission: Hearings Before the Subcommittee on Agricultural Research and General Legislation of the Committee on Agriculture, Nutrition and Forestry, 95th Cong., 2d Sess., pt. 2. 253 (1978) (discussion of adding delivery points) [hereinafter 1978 Senate Reauthorization Hearings].}
supplies would occur at present delivery points and thereby make the contract susceptible to squeezes or corners. Additional delivery points would assure greater access to transportation facilities and make a corner or squeeze that much more difficult.  In addition, the CFTC was granted the authority to impose civil penalties of up to $100,000 for each violation of the Commodity Exchange Act, and criminal penalties for manipulations were increased from $10,000 to $100,000. The Commodity Exchange Act, however, was not amended to define manipulation, nor did it designate certain practices as constituting manipulation. Consequently, the new agency was saddled with the same problems that had stymied the Commodity Exchange Authority for so many years.

B. The CFTC’s New Powers Prove to be Ineffective

The first real test for the CFTC and its new powers for preventing and punishing manipulation occurred in connection with a default in the May 1976 Maine potato futures contract traded on the New York Mercantile Exchange. As that contract approached maturity, the CFTC’s market

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surveillance discovered that a relatively large number of traders held short positions. On the last trading day, one individual raised his long position by 2500 contracts for a total of over 4000 contracts. Other traders hearing rumors of this activity acquired additional long contracts in order to take advantage of the situation. But the deliverable supply of Maine potatoes was inadequate to cover the number of open positions, and the shorts were unable to deliver because the longs had tied up all available railroad cars. The long positions holders had in effect cornered the market, and the shorts defaulted about two weeks after the last trading date in the contract. A default of this size was virtually unprecedented in the commodity markets and it shocked the markets and market participants more than any other single event in recent years.

As one court stated, this was a "gross" violation of the prohibition against manipulation in the Commodity Exchange Act "of the very type against which Congress has been legislating for half a century." The CFTC expended a great deal of resources in investigating this case. It issued over 170 subpoenas and it questioned some two hundred people about the defaults. Some 140 witnesses were interrogated under oath. The default raised such animosity that Senator Frank Church introduced a bill to ban all trading in potato futures contracts.

The CFTC used its new emergency powers prior to the potato default by ordering the New York Mercantile Exchange to increase potato futures margins one hundred percent and to trade for liquidation only. But the CFTC's use of emergency power did not prevent the manipulation that resulted. Never-

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375. Id.


378. H.R. Rep. No. 565, 97th Cong., 2d Sess. pt. 1, at 58 (1982). Even this belated action was criticized by the industry as an improper interference with the market place:

The emergency powers allow the C.F.T.C. to interfere in trading on an exchange when it deems that the markets have become "disorderly." However, it is the very nature of price discovery that what appears to be disorder is [sic] in fact legitimate market processes at work. Allowing the Commission to interfere with markets at its discretion actually creates more uncertainty and more disruption of the price discovery process than what even the most "erratic" of markets.

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theless, the CFTC later charged both the shorts and longs with manipulation.379 This was the first time that the CFTC commenced a manipulation proceeding. The CFTC imposed sanctions against most of the shorts in an order issued on March 7, 1978. Pursuant to a settlement agreement, Peter J. Taggares and John R. Simplot, the two great “potato barons,” along with their companions, were barred from trading on contract markets for periods of four and six years, respectively.380 Although these sanctions were not minor ones, their severity was greatly mitigated by the fact that this was the second manipulation of the potato market by Messrs. Taggares and Simplot.381

The potato default became the subject of a complicated web of private litigation.382 The Supreme Court considered the default and held that there was a private right of action under the Commodity Exchange Act for those injured by this activity.383 The circuit court also reviewed the conduct. It

The authority to exercise emergency powers carries with it the danger that out of fear of misfeasance, the C.F.T.C. will feel obliged to use the powers frequently until its use will become the automatic ‘solution’ even to the most minor of problems . . . . To continue to give the C.F.T.C. the authority to take this type of action in light of their proven lack of expertise and understanding, could well lead to the destruction of the market. This power should be completely removed from the C.F.T.C. and not placed in the hands of any other agency.


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noted that Simplot processed approximately fifty percent of all Idaho potato products sold in the United States, while Taggares processed approximately thirty percent of all Washington potatoes. Simplot and Taggares were also partners in a large potato farm in the State of Washington. The complaint before the court charged that Simplot and Taggares, their companies, and others engaged in a conspiracy to depress the price of the May 1976 Maine potato futures contract. In aid of the alleged conspiracy, Simplot made $1 million available to engage in futures trading. It was asserted that Simplot and Taggares also had shipped large quantities of Idaho potatoes to Maine in order to depress prices there, even though they had no buyers. The complaint charged that there was a second group of Eastern conspirators who thought that they could beat the Western producers, Taggares and Simplot, at their own game. This “long” group allegedly purchased May contracts and maneuvered the tight cash potato market so that the shorts could not make delivery. They did this by tying up all of the rail cars of the Bangor & Aroostook Railroad, which was the only railroad able to deliver potatoes to satisfy the May futures contract. According to the complaint, this was accomplished by using the cars for phony export shipments and leaving them loaded or only partially unloaded when they reached their destinations. Neither side flinched in this fatal game of “chicken.”

384 The Supreme Court stated that some 1.5 million pounds of potatoes rotted because they could not be shipped out of Maine.

This did not end the CFTC’s problems with potato futures. In 1979, another severe market disruption occurred when 90% of the potatoes tendered for delivery for the March 1979 contract did not meet contract requirements. At that point, the Exchange took emergency action and voted to liquidate the positions. This led to further litigation.

The CFTC used its emergency powers again in a situation involving the December 1977 coffee futures contract on the New York Coffee and Sugar Exchange. This emergency arose after a severe frost struck the coffee

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386. See CFTC, The First Ten Years, supra note 373, at 29; see also Sam Wong & Son v. New York Mercantile Exch., 735 F.2d 653 (2d Cir. 1984). The court held that there was no private right of action for failure of an exchange to amend the terms of its futures contracts to correct defect in delivery provisions. However, a private right of action could be brought against an exchange for failing to maintain an orderly market by not enforcing its rules if the exchange acted in bad faith.


387. H.R. Rep. No. 565, 97th Cong., 2d Sess. pt.1, at 58-59 (1982). In fact, a concern raised by Congress when it was creating the CFTC was the prevention of a price “bubble” such as had been
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growing regions of Brazil on July 17, 1975. There were also floods in Columbia, an earthquake in Guatamala, and civil war in Angola, where the largest amount of coffee was produced. This led to expectations that coffee would be in short supply. In fact, coffee prices rose from $0.55 per pound in July of 1975 to a peak of $3.55 in April 1977, after which prices began declining due to organized consumer resistance. On November 23, 1977, the CFTC declared an emergency and ordered liquidation of the December contract. The exchange took similar emergency action. \textsuperscript{388} As one court said: “This action was taken amid reports that some coffee producing nations were attempting to drive coffee prices up.” \textsuperscript{389} A group of foreign traders then unsuccessfully challenged the CFTC’s action in court. \textsuperscript{390}

Later, in \textit{In re Compania Salvadorena de Cafe}, \textsuperscript{391} the CFTC charged that a group of coffee growers in Colombia, Mexico and Brazil had entered into an agreement to support coffee prices on the futures markets. Salvadorena had entered futures orders pursuant to an agreement that was designed to increase coffee prices. Although the CFTC had earlier warned Salvadorena that its actions could significantly affect prices, Salvadorena maintained its dominant long position, taking delivery on about 84\% of all July contract deliveries. \textsuperscript{392} A CFTC Administrative Law Judge (“AL”) concluded that an artificial price resulted from these activities because the July contract prices exceeded the International Coffee Organization indicator prices for coffee of equivalent grade and contemporaneous prices for the September 1977 contracts. The ALJ noted that Salvadorena did not need cash coffee but it stood for delivery anyway. \textsuperscript{393}

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\textsuperscript{388} CFTC, \textsc{First Ten Years}, supra note 374, at 16-17 (1985); see also H.R. \textsc{Rep.} No. 1181, 95th Cong., 2d Sess. 102 (1978).

\textsuperscript{389} Compania de Salvadorena v. CFTC, 446 F.Supp. 687, 689 (S.D.N.Y. 1978). The New York Times reported that agents of Brazil and El Salvador were attempting to artificially inflate coffee prices by a $100 million commitment. This scheme was called “operation Central Park.” \textsc{Jensen, U.S. Studying Whether Two Nations Act To Keep Coffee Prices, N.Y. Times, Dec. 30, 1977, at 1, col. 2}.


\textsuperscript{392} \textit{Id.} at 27,813-18.

\textsuperscript{393} \textit{Id.} at 27,816. It was found that the respondents had engaged in trades that were designed to “make the market go up” and to “make the market strong”. \textit{Id.} at 27,813. Salvadorena also took delivery on about 84 percent of all deliveries on the July contract, and it engaged in wash trading in a further effort to
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A $200,000 civil penalty was imposed on one trader by default, and he was prohibited from trading on United States contract markets. But the penalty apparently meant little since the trader was outside the CFTC's jurisdiction. Salvarec's company was prohibited from speculative trading on U.S. markets, but this also was a meaningless penalty since the company represented large scale hedging interests. Charges against several other respondents were dismissed by the CFTC. The CFTC was heavily criticized for its lack of prompt action in the runup of coffee prices.

This did not end the CFTC's problems with coffee. The following year, it encountered concerns with another foreign entity that was trading on behalf of others. The CFTC attempted to find out on whose behalf the company was trading, but the company, located in Switzerland, refused to provide the information, contending that it was not disclosable under Swiss law. The CFTC rejected this defense and imposed sanctions against the firm, but the Second Circuit reversed because the CFTC had not given proper notice before demanding the information at issue.

The next use of emergency power by the CFTC involved the March 1979 wheat futures contract on the Chicago Board of Trade. The problems that precipitated this use of emergency power had their origin in the extremely small 1978 wheat crop. This shortage, combined with transportation problems and other factors, caused prices for earlier-maturing contracts on the Chicago market to exceed those for later-maturing contracts, the converse of normal action. This occurred throughout the 1978 and 1979 wheat marketing years. The first real problems appeared when the December contract neared maturity. At that time, two traders from a single firm held over 60% of the long position for the four
days before the contract was due to mature. The price of the contract increased
by $0.25 during the last three days of trading.\textsuperscript{401}

The March 1979 wheat futures contract posed additional problems as it
neared maturity. Traders on the floor of the exchange held 80% of the long
positions four days before trading was to end. Their trades exceeded three
times the available deliverable supplies of wheat. Two of the traders were from the
same firm and had been involved in what appeared to have been a manipulation
of the December 1978 Chicago wheat contract. Transportation problems and
limitations on elevator space prevented substantial quantities of wheat from
being brought to Chicago and Toledo, the delivery points. The Board of Trade
and the CFTC sought assurances from traders that the liquidation would be
orderly. There was no solid evidence that the traders were acting together but
they were "in a position to squeeze the market, if they [chose] to do so."\textsuperscript{402}

There was room to believe that prices were being distorted as there was a
highly unusual 36-1/4 cent premium for the March futures contract. The prices
in that contract increased with no corresponding increase in related wheat prices
at other locations. It also appeared that demand for wheat in Chicago and
Toledo was solely based on the need for delivery on the futures contracts rather
than for commercial use. It was found that the cash price declined and the
normal premium for soft wheat over hard wheat returned after the closing

\textsuperscript{401} CFTC Reauthorization, Hearings on H.R. 5447 Before the Subcomm. on Conservation, Credit,
[hereinafter CFTC Reauthorization on H.R. 5447]. See also March Wheat Futures Trading on the Chicago
Board of Trade, Hearing Before The Subcomm. on Conservation and Credit of The House Comm. on
Agriculture, 96th Cong., 2d Sess. 5-9 (1979).

\textsuperscript{402} CFTC Reauthorization on H.R. 5447, supra note 401 at 721-22. Interestingly, the injunctive
authority originally proposed for the CFTC would have allowed it to seek an injunction against a trader
or traders that were "in a position" to effectuate a squeeze or corner. H.R. REP. NO. 13113, 93d Cong., 2d
Sess., 14 at § 211 (1974). The Senate Committee, however, concluded that such "unprecedented" language
should not be adopted because it believed that the mere fact that a person had the ability to manipulate the
market would not be appropriate basis for injunctive relief, since the person may not have any intention
language was therefore stricken from the bill. The injunctive authority as adopted allowed the CFTC to seek
an injunction where a person was "about to engage" in violations. But Congress also thought that this should
be narrowly limited to those "rare instances" where a person intended to proceed with his plans despite an
agency's challenge. \textit{Id. See also} 120 CONG. REC. 10741 (1974). In contrast, the House Report, which had
proposed the broader language for injunctive relief, stated that:

Injunctive authority could also be used to stop a trader from maintaining a position in the market
that is causing the market to be disrupted or causing an abnormal price movement. For example,
in June 1972, CEA became concerned about the large percent of the outstanding futures contracts
held by a trader in the July 1972 oat future. Without injunctive authority CEA could only advise
the trader that it was concerned and would investigate his trading if there was any indication of
price manipulation or price artificiality. The trader persisted in maintaining his dominant position
in the futures contract and upon the completion of its investigation CEA issued a complaint
Rep. (CCH) ¶ 20,211 (1976).]} With injunctive authority, CEA may have been able to stop the
trader from maintaining his dominant position.


The House Committee, however, cautioned that the CFTC should use injunctive authority only where
other remedies were inadequate or not realistic. \textit{Id.} at 30.
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period on the March 1979 futures contract. However, price increases were only gradual and the evidence of price distortion was not very strong in light of other fundamental factors. Nevertheless, the long traders were in a substantial position to exert control over the future in its last few days of trading.\footnote{403}

The CFTC asked the Chicago Board of Trade to take emergency action on the March 1979 wheat futures contract, but the Board of Trade refused to take any action that the Commission believed was appropriate.\footnote{404} As a result, the CFTC declared its own market emergency and ordered a one-day suspension of trading to allow the exchange to take further action. The exchange again refused to do so, and the CFTC then ordered the exchange to suspend all further trading in the March contract and to settle any contracts at the prevailing settlement price of the future.\footnote{405} The Chicago Board of Trade, over a weekend, obtained a preliminary injunction in federal district court against the emergency declared by the CFTC, and the contract was settled without the CFTC's liquidating measures.\footnote{406}

The Seventh Circuit subsequently reversed the district court, but that reversal came after the settlement of the contract.\footnote{407} In its decision, the Seventh Circuit held that the CFTC emergency was basically unreviewable in court.\footnote{408} The statute was subsequently changed to allow judicial review under limited circumstances.\footnote{409} Thus, instead of broadening the CFTC's authority as the result of this frustrating episode, Congress actually reduced its powers. This was because of concern that suspension or early termination of a futures contract could have "serious long-term implications for the viability of the market." In particular, it was feared that governmental intervention "introduces a type of uncertainty that traders are ill-equipped to handle."\footnote{410} This effec-

\footnote{403. CFTC Reauthorization on H.R. 5447, supra note 401, at 722-23.}
\footnote{404. Id.}
\footnote{407. Board of Trade v. CFTC, 605 F.2d 1016 (7th Cir. 1979), cert. denied, 446 U.S. 928 (1980).}
\footnote{408. 605 F.2d at 1023-1025.}
\footnote{410. CFTC Reauthorization on H.R. 5447, supra note 401, at 727. It was contended that [halting trading is an extremely powerful emergency tool for the CFTC, but one that is fraught with dangers. It can impose great inconvenience and unexpected losses upon the innocent as well as the guilty. It introduces difficult problems in determining fair settlements and tends over the long run to undermine confidence in and usefulness of the market. Consequently, less drastic measures which prevent traders from acquiring or holding manipulative positions during the delivery periods are to be preferred. In particular, regularly prescribed position limits which force traders to reduce their large positions as the contract markets are recommended. Provisions for tightening these limits in emergencies also appear to be needed. \textit{Id.} at 733. Nevertheless, it was stated in Congressional hearings that the CFTC should have explicit emergency authority to require large traders to reduce their positions when they had the ability to control price. It was asserted that this should be the primary emergency measure for dealing with threatened manipulation that arises during the delivery period. \textit{Id.} at 737.}
tively ended any effort by the CFTC to use its emergency authority to prevent price manipulations. In fact, the CFTC has stated that it uses its emergency authority only as a "last resort", that it expects the exchanges to take action first, and that it prefers market participants to comply voluntarily with CFTC and exchange requests to take steps to avert an emergency situation.

The CFTC's injunctive powers proved to be equally ineffective as a means of preventing market threats. In 1977, in an action against the Hunt family of Dallas, Texas, the CFTC charged that the Hunts were collectively exceeding the amount of soybean futures contracts that a speculator could hold at any one time. Soybean prices had increased by four dollars and prices continued to increase as delivery approached on the May futures contract. The CFTC was concerned that the Hunts were taking advantage of tight supplies in the Chicago market.

The Hunts held soybean futures contracts covering over twenty million bushels of soybeans. They also held contracts for May delivery that amounted to some eight million bushels of soybeans, while there was only some ten million bushels on hand in Chicago. The evidence against the Hunts was overwhelming. The CFTC had charged that they were acting in concert to exceed the maximum amount of three million bushels of soybeans that could be traded by any one trader or group of traders acting together. The Hunts contended that they were acting separately. But the Seventh Circuit found that Nelson Bunker Hunt and William Herbert Hunt were brothers and that they were the principal family figures in these transactions. The two Hunts entered the soybean market, and by August each brother held a long position...
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at the three million bushel limit. "Through a series of purchases—the date, timing, and size of which were virtually identical, each brother, by January 1977 held a three million bushel position in March 1977 soybeans."417 In addition, over the following weeks the "Hunt brothers entered into eight transactions—on the same days using the same broker, involving virtually identical quantities and prices."418 One of their employees also "prepared commodity position statements for the brothers reflecting their combined holdings and unrealized profits and losses."419 The CFTC was unsuccessful in obtaining an injunction before the contract expired, but the Seventh Circuit later concluded that the Hunts were acting together in violation of CFTC speculative limits. It enjoined the Hunts from further such activities in the soybean market.420 This was apparently the only time that the CFTC ever sought to use its injunctive authority to prevent a market disruption.421

In one of its more severe market crises, the CFTC neither took emergency action nor sought injunctive relief. This was the so-called "Silver Crisis" that occurred after the price of silver increased from less than $9 an ounce in 1979 to a peak of approximately $50 dollars an ounce in January of 1980.422 On March 18, 1980, silver prices dropped thirty-three percent in twenty-four hours. Silver was then trading at $10.80 an ounce—off from $39.50 the day before.423 The Hunt family then failed to meet hundreds of millions of dollars in margin calls, which threatened the financial stability of Wall Street.424

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417. 591 F.2d, at 1218-19.
418. 591 F.2d, at 1219.
419. Id. See also H. Hurt, Texas Rich, 364-65, 1978 Senate Reauthorization Hearings, supra note 365, at 216. The Hunts were later fined five hundred thousand dollars for their foray into the soybean market in CFTC administrative proceedings. Knight, Hunt Family Fined $500,000 For Soybean Deals, Wash. Post, July 22, 1981, at A1, col. 1.
The SEC suspended trading in the stock of various major Wall Street firms in response to reports that these firms were suffering heavy losses because of the Hunts’ failure to meet margin calls. The CFTC Chairman was of the view that the entire “financial fabric of the United States was endangered” as a result of the Hunts’ activities. Although this proved to be overblown, it was truly an emergency situation that required the combined force of numerous senior government officials to deal with and monitor. The Silver Crisis had a serious impact on other financial markets regulated by those entities, and the tremendous amounts of credit extended for the Hunt silver purchases adversely affected commercial productivity and individual users of silver, and affected monetary policy, causing the Federal Reserve to ask the banks not to extend loans for speculative trading. Nevertheless, “[f]aced with dramatic and disorderly market conditions, the CFTC took none of the specific preventive or emergency actions allowed under the Commodity Exchange Act, although it had both the statutory duty to act and the requisite information.” A Congressional Committee asserted that the CFTC could have alleviated the situation by declaring a market emergency but did not do so.

on Agriculture and Forestry, 93d Cong., 2d Sess. 478-87 (1974).
426. Id. at 24.
427. A SEC investigation determined that:
For six days late in March 1980 it appeared to government officials, Wall Street and the public at large that a default by a single family on its obligations in the plummeting silver market might seriously disrupt the U.S. financial system. Various broker-dealers carrying Hunt accounts, among the largest firms in the securities industry, faced the possibility of very substantial losses if this group of customers had failed to make good on its obligations. The potential failure of even one of these firms threatened a financial chain reaction that would have jeopardized commodity clearinghouses and their members, other broker-dealers and their customers and banks, public companies and their stockholders. Although financial catastrophe was ultimately averted, the silver crisis provides a valuable lesson in the fragility and interdependence of the financial structure, and challenges both the private sector and government to respond.
429. Id. at 4.
430. Id. at 19. Nevertheless, the Federal Reserve later gave tacit approval to a 1.1 billion dollar loan to the Hunts to pay their margin calls and other silver-related obligations. Id. at 7; H. HURT, supra note 419, at 14-15; Noble, supra note 424.
431. H.R. REP. No. 395, 97th Cong., 1st Sess. 5 (1981). The committee also noted that the large concentrated trading of the Hunts and others had created a “disorderly” market by the end of 1979 in which orderly and efficient trading was disrupted and price fluctuations were accentuated by exchange actions, which further destabilized silver trading. Id.
432. Id. The Chairman of the Federal Reserve Board was more restrained. He stated that:
In the end, the best defense against that type of behavior must be the discipline of the market itself. History is replete with efforts at ‘cornering’ that failed. I hope the recent silver experience has had a chastening influence. But memories are short; human greed leads to temptation and an attempt to corner, successful or not, can be extremely damaging, not just to the speculator, but to all those who count on the stability of markets and financial institutions.
Silver Prices, supra note 422, at 21l.
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A subsequent CFTC investigation found that the Hunts had at least three billion dollars in silver futures contracts at the exchanges. The Hunts were trading in large amounts through a company they owned jointly with two Arab Sheiks. The CFTC also determined that the Hunts were acting with a group of foreign traders who also held huge silver positions. Several years later the CFTC charged the Hunts and those foreign traders with manipulation. Several of these respondents consented to sanctions, and in 1989 Nelson Bunker Hunt and his brother, Herbert Hunt, agreed to a permanent bar from trading on all commodity exchanges. They also each agreed to pay a ten million dollar civil penalty. But those sanctions were all but meaningless. The Hunt brothers were insolvent and only $1.5 million was allowable as a claim in their bankruptcies, along with hundreds of millions of dollars of claims by other creditors.

The Hunts and others were the subject of several private actions in which it was claimed that their trading activities had caused damages. The most significant of these was the case Minpeco, S.A. v. ContiCommodity Serv. There it was claimed that a government agency in Peru had suffered sharp losses from its speculations in the silver futures markets during the time the Hunts were trading. After years of discovery, the case was tried for several months in the Southern District of New York. On September 1, 1988, a judg-

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433. H. R. REP. NO. 395, 97th Cong., 1st Sess. 48 (1981). At one point, January 17, 1980, the Hunt positions were valued at more than $9.8 billion. Silver Crisis, supra note 424.
434. H. R. REP. NO. 395, 97th Cong., 1st Sess. 43 (1981). It was charged that, by late December, 1979, the Hunts held 43.6 percent of the open interest in silver on the Comex and that another group operating in parallel with the Hunts owned 53 percent of the certificated silver stocks on the Comex and almost 70 percent of the certificated silver in Chicago, i.e., silver that was certified for delivery. Id. at 11.
435. Id. at 43-46. It was asserted that a trader from this group had just recently cornered the orange juice market after the Florida freeze of 1977. Id. at 46.
436. See In re Hunt, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,296 and 23,244 (C.F.T.C. 1987). The CFTC investigation was delayed for several years by the sheer volume of the trading and by the fact that the traders involved were located around the world, causing delays in gathering information. In addition, a Swiss bank that had conducted the trading for several of the larger traders abroad refused to disclose their identity on the grounds that the CFTC lacked jurisdiction and on the grounds that Swiss law prohibited such disclosure. In re Banque Populaire Suisse, [1980-1982 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,255 (1981). The CFTC also had trouble obtaining service on a large trader who lived in Brazil because the Court of Appeals for the District of Columbia Circuit held that the CFTC could not enforce an investigative subpoena served on a foreign citizen in a foreign nation. CFTC v. Nahas, 738 F.2d 487 (D.C. Cir. 1984). See Blaitis, Shielding Non-Resident Aliens From the Reach of Administrative Subpoenas Under the Commodity Exchange Act, 10 ASILS, Int'l L.J. 39 (1986). Later, however, the Commodity Exchange Act was amended to broaden the CFTC's authority to serve subpoenas abroad. See H.R. REP. NO. 995, 99th Cong., 2d Sess. 21-22 (1986).
ment in the amount of $132 million was entered against the Hunts and others. The jury found that they had violated the Commodity Exchange Act, federal antitrust statutes, New York common law fraud and the Racketeer Influenced and Corrupt Organizations Act. However, the Hunts subsequently filed bankruptcy which made collection doubtful. Minpeco did obtain substantial settlements from various brokerage firms which had handled the Hunt and other accounts.

The CFTC was called to account in Congress for the Silver Crisis. The CFTC's stated justification for not taking emergency measures on the futures exchange was that it was concerned that its actions might themselves be a destructive force in the larger worldwide market. The CFTC was of the view that its emergency powers were to be used only for threatened or actual market manipulations or corners that occur in the context of very short-term emergencies that last only a few days or weeks and only require specific and limited remedial action. In the Silver Crisis, the Commission was concerned it would have to administer the exchanges' price procedures over longer prolonged periods. Since the CFTC did not have speculative limits for silver, and it believed it could not adopt them retroactively, it was dependent upon the exchanges for adopting such limits. Later, after the crisis, the CFTC adopted a regulation that required each contract market to have speculative position limits for its contracts.

The Silver Crisis and the events that led to its declaration of prior emergencies were not the only market problems encountered by the CFTC during its

443. 1982 Senate Hearings, supra note 366, at 44.
444. Id. at 104-05; H.R. REP. No. 565, 97th Cong., 2d Sess., pt 2, at 33 (1982); 17 C.F.R. § 1.61 (1990). The Commodity Exchange Act was amended in 1982 to make violations of exchange position limit rules a violation of the Commodity Exchange Act itself. 7 U.S.C. § 6a, amended by Futures Trading Act of 1982, Pub. L. No. 97-444, § 204, 96 Stat. 2294. However, the criminal provisions of the Commodity Exchange Act apply to such violations only when a person knowingly violates an exchange's limits. Id. In that connection, the Conference Committee rejected a Senate proposal that would have allowed criminal prosecution only where the violative activity was in connection with an attempt to manipulate, corner or squeeze a market. H.R. REP. No. 964, 97th Cong., 2d Sess., 39 (1982). See also S. REP. No. 484, 97th Cong., 2d Sess. 44-45 (1982).
fifteen years of existence. To the contrary, its annual reports contain a litany of market congestion and concerns with large traders and turbulent markets. For example, in 1979, in addition to the problems with silver, coffee and the March wheat blowup discussed above, the CFTC encountered problems in lumber because of lack of available supplies and the existence of some large traders in the market. This precipitated potential liquidation problems, and the Chicago Mercantile Exchange took emergency action to reduce position limits during the delivery month. Problems were also encountered in the June 1979 ninety day Treasury Bill future on the Chicago Mercantile Exchange and volatility was encountered in gold.445 In fact, 1979 seemed to have been a banner year for manipulation in that there were five reported instances of such activity.446

In 1982, problems were encountered in the feeder cattle contract on the Chicago Mercantile Exchange and the exchange declared a market emergency; congestion threatened the pork belly market on the Chicago Mercantile Exchange; and problems were encountered in coffee.447 The Futures Trading Act also required the CFTC to conduct a two-year study of the use of futures markets by large hedgers in cattle, hogs and pork bellies because of Congressional concern with “unwarranted price pressures by large hedgers.” In that study, the CFTC noted that hedgers were exempt from position limits and that they could therefore establish larger futures positions than could speculators. The study concluded consequently that “hedgers have the potential of acquiring greater market power than individual speculators and a greater capacity to affect—and possibly distort—futures prices.”448

In 1983, problems were encountered in the July 1983 corn futures contract. Problems also arose in the liquidation of the 1983 pork belly futures contract, and it was rumored that a squeeze was developing. This caused a market emergency to be declared by the Chicago Mercantile Exchange.449 In 1985, problems were encountered in cocoa, stock index futures and a number of grain futures contracts.450 In 1986, problems were encountered in cattle, stock index futures and cotton.451 In 1987 and 1988, in addition to the Stock Market Crash, a drought caused much concern in the grain markets and there were problems in orange juice and copper.452

The most noteworthy of these events was the Stock Market Crash of 1987. Those events have been well documented in numerous government studies and

447. CFTC ANNUAL REPORT 64-65 (1982).
450. CFTC ANNUAL REPORT 48 (1985).
articles. In brief, the Dow Jones Industrial Average dropped nearly thirty-three percent in less than a week. This “precipitous” drop began on October 14, 1987, as a result of news that there was a larger trade deficit than had been expected and because a House Committee had proposed to eliminate tax benefits associated with corporate take-overs. The market dropped some ninety-five points on October 14 and this plunge continued on October 15 with another drop of some fifty-seven points. Thereafter, the market continued to free-fall and on “Black Monday”, October 19, 1987, the Dow Jones Industrial Average fell over five hundred points on trading volume of over six hundred million shares. Trading was halted in many stocks because of the massive volume of trading, which included two billion dollars of shares that were traded in the first thirty minutes on that day. October 20, 1987, also saw further confusion in the market-place but the markets recovered after several corporations announced stock purchase programs to take advantage of the reduced security prices. Nevertheless, it was found that the financial markets had “approached breakdown” on October 20 because of the disconnection between the futures and stock markets. But the CFTC did not declare an emergency in the course of these incredible events. Rather, it deferred to the exchanges and allowed them to handle the crisis.

A Presidential commission was appointed to study what occurred in the markets, and the Securities Exchange Commission, the CFTC and other bodies


454. BRADY REPORT, supra note 18, at 15.
455. Id. at 17, 21.
456. On October, 16, 1987, the market dropped another 108 points, the largest single day drop to that point. Id. at 25.
457. Id. at 36.
458. Id. at 30. The BRADY REPORT stated that October 19 was “perhaps the worst day in the history of U.S. equity markets.” Id. at 36.
459. Id. at 41. The commodity exchanges did take emergency action by imposing price fluctuation limits on the stock index contracts that were the center of this event. CFTC Final Report, supra note 453, at 182-85.
460. CFTC Final Report, supra note 453, at 182-85. In its report following the October crash, the CFTC asserted that its regulatory system had been successful. Id. at 190.
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filed voluminous reports. The Presidential commission -- the Brady Commission -- suggested, among other things, that "circuit breakers," such as trading halts in times of market volatility, were necessary to prevent the chaos that occurred in October, 1987. Concern was also raised that manipulation had occurred in the market index futures contract on the Chicago Board of Trade. This controversy arose out of trading on October 20, 1987, in the Major Market Index Maxi ("MMI") futures contract. On October 20, the November MMI futures contract opened up some 23 points higher than the prior day's close, and the market continued to rise for forty-five minutes after the opening. It then began to decline, dropping 104 points. During the day, several other exchanges halted trading in index futures contracts because more than two hundred stocks underlying the index contracts had experienced delayed openings at the New York Stock Exchange, due to large sell order imbalances. Nevertheless, the Chicago Board of Trade decided to keep the MMI contract open, leaving it as the only stock index futures contract trading between 11:35 a.m. and 12:05 p.m. During this period, the November MMI rose approximately 80 points before declining, and its price was out of line with the stocks underlying the index. There was also concern that the market had been manipulated during this period. The CFTC examined all of the trading in the market but could not conclude that any of the activities had been manipulative. The CFTC staff stated that manipulation required a demonstration that the alleged manipulators had "the ability to influence market prices, a specific intention to do so, and the existence and causation of artificial prices." This finding, however,

461. See supra note 453. The Stock Market Crash of 1987 gave rise to the concern that low margins on futures contracts had contributed materially to the events triggering the crash and that exotic trading mechanisms such as program trading, portfolio insurance, index arbitrage and other aspects of futures trading threatened the stability of the securities markets, as institutional traders poured billions of dollars in investments into this new form of trading. See, Markham & Stephanz, The Stock Market Crash of 1987 - The United States Looks at New Recommendations, 76 Geo. L.J. 1993 (1988). The significance of the Stock Market Crash of 1987 may be shown by the fact that the market plunge caused a loss of equity in excess of one trillion dollars. BRADY REPORT supra note 18, Executive Summary at V. Moreover, on October 16, 1987 alone, nearly one billion dollars in commodity margin calls were issued and over eleven billion dollars in margin calls were issued for the next four trading days. On October 19, 1987, alone, some $3.6 billion in margin was demanded, and on the next three days an additional eight billion dollars were requested, causing a liquidity crisis in the financial markets. SEC Report, supra note 18, at 5-12, 5-13.

462. Id. at 66-69. In brief, these circuit breakers would involve the establishment of price limits on trading that would effectively halt trading when prices had fluctuated a specified amount. It was also suggested that trading halts could be considered as a means of cooling the market off when it became overheated. Id.


465. Id. at 7, n. 11. The MMI Report stated that it did not find: any reasonable indication that price manipulation occurred in the MMI contract on October 20. The trading of two of the three largest buyers occurred prior to the major price advance. The third largest buyer's transactions occurred almost entirely just after the high of the rally and consisted in total of just three purchases all at the same price, which were later offset at a substantial loss. . . . If a trader
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proved to be controversial after it was charged that an exchange had given incorrect data to the CFTC, and that the CFTC had reached its conclusions before even beginning an inquiry.\textsuperscript{466}

Most recently, an SEC staff report concluded that a large market break in October of 1989 was fueled by speculative trading as well as index arbitrage and other program selling. The report found that “[o]n October 13, 1989, the nation’s securities markets experienced extraordinary price volatility, losing $190 billion in value, $160 billion of which was lost in 90 minutes.” The report concluded that, under current regulations, there was no assurance that such extraordinary volatility will not be repeated or exceeded in the future.\textsuperscript{467} A CFTC report on the same issue, however, found that there had been no manipulation or intermarket futures activity such as index arbitrage or program trading that caused the market break.\textsuperscript{468}

Another recent market controversy involved trading by Ferruzzi Finaziaria S.P.A., an Italian company that held a dominant position in the July 1989 soybean futures contract on the Chicago Board of Trade. Problems with the July soybean contract had begun with the drought of 1988. The small harvest resulted in total stocks of soybeans in July 1989, of only one hundred and twenty-five million bushels compared to the over three hundred million bushels in July 1988. While outstanding July futures contracts on the Chicago Board of Trade on July 10, 1989, called for the delivery of 40.3 million bushels of soybeans, there were only about 12.5 million bushels of deliverable grade soybeans at the Chicago/Toledo warehouses. A substantial portion of both the

had been attempting artificially to raise the MMI price, he or she probably would have entered several incremental orders in succession, with each order to have been filled at progressively higher prices. There was no evidence of this pattern of purchases.

The Division’s analysis also indicates more selling than buying pressure by the most active traders during the focus period. Equally significant, the trading during the focus period is dispersed among numerous traders and there is no evidence of any group of traders trading in concert.

\textit{Id.} at 14-15. Interestingly, the only manipulation case that arose from the Stock Market Crash of 1987 was brought by the Securities and Exchange Commission. \textit{See Hass, Official is Sentenced,} N.Y. Times, Feb. 28, 1990, at C1, col. 4.


\textsuperscript{468} \textit{CFTC Division of Economic Analysis, Report on Stock Index Futures and Cash Market Activity During October 1989} (1990). The chairman of the CFTC also charged that the SEC’s report on the mini-crash was “misleading” and selectively omitted critical data. Salwen, \textit{CFTC Rakes the SEC’s Findings on Mini-Crash as Turf War Flares,} Wall St. J., June 28, 1990, at C1, col. 5. The SEC chairman responded in kind, asserting that action is needed ‘to eliminate the unsafe practices and rampant speculation in the futures market.’ \textit{SEC Chief Accuses CFTC of Distortion in Mini-Crash Probe,} Wall St. J., June 29, 1990, at C16, col. 6. Clearly, these two agencies have different regulatory perspectives. \textit{See generally 2 Comm. Fut. L. Rep.} (CCH) \textit{¶ 24,890} (July 1990) (General Accounting Office Report commenting on the SEC and CFTC reports).
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long side of the July futures and the deliverable supply of soybeans were held by Ferruzzi.469

Ferruzzi's position was so large that the Board of Trade declared a market emergency under its rules and ordered Ferruzzi to liquidate over twenty million bushels of soybean futures contracts.470 This action sent prices falling and charges and countercharges were made between Ferruzzi and the Chicago Board of Trade.471 Among other things, it was claimed that six Chicago Board of Trade directors held short positions while the Exchange was ordering Ferruzzi to liquidate. The CFTC found no conflict, and it concluded that the exchange's emergency action was necessary to avoid disorder in the soybean market as the July contract expired.472 The CFTC, however, did not itself take any action. A CFTC Commissioner noted, with respect to the Ferruzzi crisis, that other than "jawboning" and imposing trading limits, the CFTC was not willing to exercise its power to deter squeezes.473 It was also pointed out that the CFTC had brought only a few price manipulation cases in its fifteen year history and that the CFTC had adopted such a narrow interpretation of price manipulation that


A charge that the emergency action by the Chicago Board of Trade was itself a market manipulation was later dismissed by a district court. Court Throws Out Main Charge in Suit Filed Against CBOT, Wall St. J., April 27, 1990, at C15, col. 3. But see Burns, Big Grain Trader Takes on CBOT, Chicago Sun Times, Sept. 13, 1990.

473. Ingensoll, As Congress Returns, Will CFTC Feel The Squeeze On Soybean Flap?, Wall St. J., Aug. 22, 1989, at C1, col. 5. Another Commissioner stated with respect to the Ferruzzi crisis that any decision to take emergency action is a difficult one to make, particularly since his instinct as a regulator is to "let the market work if it can." Minutes of a CFTC Agricultural Advisory Committee 10 (Aug. 28, 1989) (available from the CFTC's Freedom of Information Officer).
it was difficult for it to find manipulation. As one CFTC Commissioner stated: "Hell, it's virtually impossible."\textsuperscript{474}

C. CFTC Manipulation Decisions Nullify the Manipulation Prohibition

The CFTC literally inherited the CEA's administrative cases, and its frustrated attempts to define manipulation. Several CEA cases were still pending when the CFTC was created, and the CFTC took responsibility for those cases.\textsuperscript{475} The CFTC also faced the conflicting precedent of the \textit{Cargill} and \textit{Volkart} cases.

One of the pending cases, \textit{In re Hohenberg Bros.},\textsuperscript{476} concerned a charge that the December 1971 cotton futures contract had been manipulated by a large cotton merchandising firm and its president, Julien Hohenberg. The company, Hohenberg Brothers, owned or had commitments to purchase a net amount of some 290,000 bales of cotton. The company had partially hedged that position on the New York Cotton Exchange through short futures cotton sales. The price of that futures contract had been declining from 33.67 cents a pound to 29.33 cents a pound. This caused the company to begin to sell its cash cotton and increase its short hedge on the futures exchange to the point that its contracts constituted about 46% of the short open interest by November 23, 1971, the first delivery notice date. The CEA had charged that the company was attempting a short manipulation by driving the prices of cotton down.\textsuperscript{477}

The CFTC concluded that, in order to sustain a manipulation charge, there must be a finding that a party engaged in market conduct with the intention of affecting the market prices of a commodity and that such conduct created an artificial price. An attempted manipulation merely requires an intent to affect market prices artificially and some overt act in furtherance of that intent. Intent may be inferred from objective facts since it would be a rare case where the manipulator's state of mind could be ascertained. The CFTC stated that a profit motive was not a necessary element of manipulation.\textsuperscript{478}

\textsuperscript{474} Ingersoll, \textit{As Congress Returns, Will CFTC Feel The Squeeze On Soybean Flap?}, Wall St. J., Aug. 22, 1989, at C1, col. 5. This Commissioner, Fowler West, stated that "Whether you call it a squeeze or a corner, you are talking about someone jerking the market around . . . . We need to find a way to move earlier." \textit{Id.} at C14, col. 6. Institutionally, the CFTC has made a more limited concession: "[c]ases involving suspected manipulations are among the most difficult for the Commission to pursue." Stoller, 2 Comm. Fut. L. Rep. (CCH) ¶ 24, 834, at 36, 927 n.10 (C.F.T.C. 1990).


\textsuperscript{475} Pursuant to Section 412 of the Commodity Futures Trading Commission Act of 1974, pending proceedings of the CEA were not to be abated. Rather, they were to be disposed of pursuant to the amended provisions of the Commodity Exchange Act by the CFTC. Pub. L. No. 93-463, § 412, 88 Stat. 1389, 1414 (1974).


\textsuperscript{477} \textit{Id.} at 21,473-74.

\textsuperscript{478} \textit{Id.} at 21,477-78.
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The CFTC could not find evidence in In re Hohenberg Bros. that the company was attempting to depress prices artificially. The evidence indicated that the company knew that there were “strong hands” that would accept its delivery notices.\(^{479}\) This indicated that the company did not expect prices to be depressed since the strong hands would absorb the delivery of the cotton without an undue effect on the market. This case signaled an inauspicious start for CFTC manipulation cases under the Commodity Exchange Act.\(^{480}\)

In In re Indiana Farm Bureau Coop. Ass’n,\(^{481}\) the CFTC resolved another CEA instituted proceeding by concluding that manipulation had not occurred. This case involved the July 1973 corn futures contract on the Chicago Board of Trade.\(^{482}\) Corn prices had increased rapidly as the result of a shortage, and the respondent was charged with manipulating prices by standing for delivery on its corn futures contracts, which were asserted to be four times the available deliverable supply of corn.\(^{483}\) In this case, the CFTC set forth its views on manipulation in greater detail. It rejected any negligence or general intent requirement as being sufficient to establish the requisite intent for manipulation. Rather, the CFTC ruled that there must be a specific intent to engage in conduct for the purpose of manipulating prices to artificial levels. The respondent must be shown to have acted with the purpose or conscious objective of causing an artificial price. The CFTC stated that, if a market participant intentionally and significantly reduced available deliverable supplies, an inference could be drawn that such conduct was done with the intent to manipulate prices. On the other hand, where traders are simply attempting to seek the best price for a commodity even in a congested market, a finding of manipulation will not follow. A trader who builds up a large interest in the cash market approaching a corner and a large long interest in the futures market has laid the basis for a squeeze. However, if a congested futures market arises from natural causes such as a low deliverable supply, manipulative intent will not be inferred if the trader simply seeks the best price from the situation and does not exacerbate

\(^{479}\) The term “strong hands” means that there was a party in the market place who was well-financed and able to take delivery on the futures contract. CFTC, THE CFTC GLOSSARY: A LAYMAN’S GUIDE TO THE LANGUAGE OF THE FUTURES INDUSTRY 50 (1990).

\(^{480}\) Hohenberg Bros., [1975-1977 Transfer Binder] Comm. Fut. L. Rep. (CCH) § 20,271 at 21,478. The CFTC stated that, “[e]ven though respondents’ activities may have involved a ‘profit motive,’ absent a finding of manipulative intent, trading with the purpose of obtaining the best price for one’s cotton does not constitute, in itself, a violation of the Commodity Exchange Act.” Id. at 21,478.


\(^{482}\) See supra note 341 and accompanying text for a discussion of the Congressional concern with this contract during hearings on the creation of the CFTC.

the congestion.484 Here it was found that the respondent did not deplete the local cash commodity; it did not establish a large position when it held virtually all the cash commodity; and it did not increase its long position in the last day of trading when it could have squeezed the market. The CFTC found that the shorts had also not behaved responsibly by making sure there were sufficient available supplies.485 This view appeared to signal that the CFTC, unlike the CEA, was adopting, and even extending, the Volkart decision.486

In another carry-over CEA case, In re Cox,487 the CFTC sought to determine whether an illegal manipulation had occurred in the May 1971 wheat futures contract.488 In conducting its analysis of whether manipulation had occurred, the CFTC had to consider available deliverable supplies. It concluded that supplies that were committed to delivery at points other than the terminal market could not be included in available supplies for determining whether a manipulated price was present. Nevertheless, since the traders were unaware of these commitments, the CFTC determined that this should not be marked against them.489 It also stated again that the shorts had an obligation to maintain supplies adequate to meet their delivery obligations. The CFTC focused on the fact that the respondents could not foreclose the delivery option and thus lacked the ability to influence prices. In other words, if the short traders could have obtained supplies from any source to meet their delivery obligations, they had an obligation to do so. If there was such an availability, there would be no basis for charging manipulation.490 The CFTC also determined the historical price comparisons were of less probative value than data from related contemporaneous markets, including the cash markets, for the underlying commodity.491 This too seems to divert from the analysis in Cargill492 and

484. Id. at 27,282-283. Campbell, supra note 17, at 242. The CFTC also relied upon Senator Pope's statement in the legislative history to the Commodity Exchange Act, which defined a squeeze. See, supra notes 213-214 and accompanying text. The CFTC stated that Senator Pope's definition described a congested futures market and that he then defined what would turn a congested market into an unlawful manipulation. He concluded that the essence of manipulative activity is the creation of an artificial price by planned action. The CFTC also relied upon the FTC Study. Indiana Farm Bureau Ass'n, supra note 483, at 27,284-285. See 7 FTC STUDY, supra note 25, at 284-85.

485. Indiana Farm Bureau Ass'n, supra, note 483, at 27, 285-87.

486. The CFTC later at least tacitly acknowledged that it was extending Volkart to its broadest reading. See In re Frey, 2 Comm. Fut. L. Rep. (CCH) ¶ 24,578, at 36,502, note 12 (C.F.T.C. 1990).


488. In a later aspect of this case, the CFTC noted that manipulation of May wheat had plagued the commodities industry since the early 1920s. See In re Frey, 2 Comm. Fut. L. Rep. (CCH) ¶ 24,578, at 36,501 (C.F.T.C. 1990). The CFTC quoted from hearings before Congress in 1922 that, "the same thing happens year after year at almost exactly the same time, becoming so familiar that the 'May squeeze' is marked on Chicago's calendar as methodically as Easter or Decoration Day." Grain Futures Hearings on H.R. 11843 Before the Senate Committee on Agriculture and Forestry, 67th Cong., 2d Sess. 37 (1922). Complaints of "May squeezes" were also raised in the hearings on the Commodity Exchange Act in 1936. 80 CONG. ROLL. 7863 (1936) (remarks of Sen. Capper). See also Wheat Futures, supra note 138.


490. Id. at 34,066-068.

491. Id. at 34,065. See also Defining Manipulation, supra note 93, at 212 (price comparisons have limited utility).
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adopt the approach of Volkart.\textsuperscript{493} In fact, several Commissioners of the CFTC have stated that the CFTC’s position is even broader than that indicated by the Volkart decision.\textsuperscript{494}

Following the decision in Cox, the CFTC’s Division of Enforcement was left with an almost impossible burden of proof in proving manipulation. Nevertheless, it brought a case, In re Abrams,\textsuperscript{495} in which it charged that an individual speculator had attempted to manipulate the September 1986 orange juice market.\textsuperscript{496} Abrams’ brokerage firm, Drexel Burnham, Lambert, Inc., was charged with aiding and abetting that attempt by loaning him funds to take delivery on his position. However, the trader had acquired a large long position well before the delivery date, and he did not substantially increase that position. He had strongly expressed his views that there was a shortage of orange juice, that it was underpriced and that he was, therefore, standing for delivery. An ALJ rejected a claim that the trader should have taken “EFPs” by swapping his futures contracts for uncertified orange juice supplies.\textsuperscript{497} The trader had argued that it was not necessary to take EFPs because he wanted certified deliverable stocks that he could retender through the exchange once the prices had adjusted in a manner that he believed supply and demand dictated.\textsuperscript{498} The ALJ dismissed this case on summary judgment, and the CFTC refused to grant interlocutory review.\textsuperscript{499} The CFTC thereafter settled the case against the brokerage firm respondent, dropping the manipulation charges and taking sanctions on minor recordkeeping issues. An appeal is now pending as to the other respondents.\textsuperscript{500}

\begin{itemize}
\item \textsuperscript{492} See supra notes 284-90 and accompanying text.
\item \textsuperscript{493} See supra notes 275-83 and accompanying text.
\item \textsuperscript{494} In re Frey, 2 Comm. Fut. L. Rep. (CCH) ¶ 24,578 at 36,502 n. 12 (C.F.T.C. 1990).
\item \textsuperscript{496} Apparently, the CFTC Staff had charged attempted manipulation in the Abrams case as a means of avoiding the difficulty of proving that the prices were in fact artificial, a long costly process that had failed in the Cox decision. Compare, Apex Oil Company v. Di Mauro, 822 F.2d 246 (2d Cir. 1987), on remand, 713 F. Supp. 587 (S.D.N.Y. 1989) (rejection of conspiracy claims for manipulation liability).
\item \textsuperscript{497} For a discussion of “EFPs” see, U.S. Dept. of Agric., Hedging in Grain Futures, Circular No. 151 28-30 (June 1931); Ryder Energy Distribution Corp. v. Merrill Lynch Commodities Inc., 748 F.2d 774 (2d Cir. 1988); CFTC, DIVISION OF TRADING & MARKETS, REPORT ON EXCHANGES OF FUTURES FOR PHYSICALS (Oct. 1, 1987).
\item \textsuperscript{498} 2 Comm. Fut. L. Rep. (CCH) ¶ 24,408 at 35,783. The ALJ considering this case also noted that the shorts had failed to “drum up” orange juice in time for delivery, i.e., the shorts failed to place orange juice in drums as required by exchange delivery requirements. Id. at 35,783-784.
\item \textsuperscript{499} 2 Comm. Fut. L. Rep. (CCH) ¶ 24,577 (C.F.T.C. 1989).
\end{itemize}
D. The CFTC Has Not Been Successful in Its Efforts to Prevent and Punish Manipulation

Since its creation, the CFTC has rendered some six decisions in cases that were initially brought by the CEA. In three of those cases, the charges were settled by consent. Penalties ranged from trading suspensions of sixty days to one year and a civil penalty in one case of ten thousand dollars. The three remaining cases were contested, but were dismissed. One of those actions took sixteen years to resolve, while the other two actions each took approximately five years. The CFTC also brought eight manipulation cases of its own. Three of those cases were contested, and manipulation charges were eventually dismissed in all three. Sanctions against respondents in the remaining cases were the result of default or settlement, and they ranged from prohibitions against trading on the markets to civil penalties of varying amounts.

The small number of cases brought and the very small number of respondents who have been subject to significant sanctions, particularly in contested cases, suggest that manipulation is virtually an unprosecutable crime. This is due to the difficulty of meeting the standards of manipulation articulated by the CFTC. The government is required to devote an incredible amount of investigative resources to meet those standards. It must review all available cash supplies, fundamentals of the market, the actions of the shorts in assuming delivery, the role of other traders in the market place, and the complicated price relationships between the various futures months. It must then attempt to delve into the mind of the manipulator to prove that there was an intent to manipulate.


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the market. Even where a gross manipulation occurs, the government is still faced with the imposing burden of proving that the price was artificial and that the trader was attempting to create an artificial price rather than exploiting a market situation based upon natural forces.\textsuperscript{505} All of this has proved to be a daunting, indeed impossible, task for the CFTC staff. Consequently, it is no surprise that the CFTC has brought so few manipulation cases.

The CFTC’s other efforts to prevent manipulation have met with equally little success. Its jawboning efforts have, it is true, often been sufficient to persuade traders to liquidate their positions.\textsuperscript{506} However, that jawboning has certainly not been successful with traders who are determined to maintain their positions in the markets. Nor has the CFTC’s use of its injunctive power, a power that had been so stridently sought by the CEA, proved effective in acting as a deterrent to market manipulation, and that authority has not been used effectively in stopping manipulations or market disruption. As shown above, the only time this injunctive action was used in an action involving a potential threat to the market was the action brought against the Hunts in the soybean futures market. There, the CFTC expended great resources and energy requiring the Hunts to liquidate their soybean positions. Although the CFTC was ultimately successful, victory came long after the delivery period in the soybean futures contract and only after a considerable fight with the Hunts.\textsuperscript{507}

The CFTC’s use of emergency powers, which was thought to be another needed tool in preventing manipulations, has also been of limited effectiveness. As already noted, the CFTC has declared an emergency where manipulation was threatened on only three occasions in its fifteen year history. In none of those instances did the use of that authority appear to have been very successful.

The CFTC’s emergency action in the 1976 Maine potato futures contract did not stop the manipulation and subsequent default. The outcome of its administrative action against the traders involved in that debacle was also of doubtful utility. The large traders, Simplot and Taggares, had already been the subject of a CEA manipulation case, but they were only given limited bars from

\textsuperscript{505} To illustrate, the CEA’s proceeding against Cargill took six years to complete; the trial required thirty-two days, a four thousand-seven hundred page record, fifty witnesses and over two hundred exhibits; and the hearing examiner wrote a one hundred-twelve page opinion. 29 Agric. Dec. 880 (1970), noted in, Preventing Manipulation, supra note 400 at 1581-88; Futures Control, supra note 67 at 1244. The potato case in 1976 similarly required a massive amount of resources just to investigate and the litigation continued for years. See supra notes 373-83 and accompanying text.

\textsuperscript{506} See generally, Hieronymus, Manipulation of Commodity Futures Trading: Toward a Definition, 6 Hofstra L. Rev. 42, 52-53 (1977); Abuses in The Commodity Markets, supra note 17, at 762 (the CEA attempted to identify unhealthy market activity and take preventative measures). The CFTC has, in the past, depended almost entirely on “jawboning” either the exchanges or traders to reduce their positions. See CFTC, 1985 Annual Report 48-49 (1986), and CFTC, 1983 Annual Report 58-59 (1984). Although this may be useful in many situations, it hardly constitutes an effective deterrent to someone bent on manipulating the market.

\textsuperscript{507} See supra notes 413-21 and accompanying text.
trading in both cases. The CFTC's emergency action in the coffee contract does not seem to have been successful since it later had to bring a manipulation action there as well. The result of that action was the default of one individual, who was heavily sanctioned. Those sanctions were meaningless, however, since the trader was outside the CFTC's jurisdiction. A successor to the principal firm involved was also relieved of any meaningful sanctions. With respect to the emergency in the March 1979 wheat futures contract, no manipulation action was ever brought, and the CFTC was enjoined from implementing its emergency action. Although the CFTC ultimately prevailed in that litigation, it was only after once again being thwarted at the most critical moment.

The FTC study authors, Congress and the Grain Futures Administration, thought that position limits would be the best way to prevent manipulation. Although the CFTC had been given authority to regulate silver futures contracts by the 1974 amendments, it did not adopt position limits for silver before the advent of the silver crisis, and it did not believe that it could impose them retroactively. Consequently, it was dependent upon the exchanges to impose rules. The CFTC has since acted to require all exchanges to adopt speculative limits. Those limits, however, are not generally applicable to hedgers. The result is to leave a gaping hole in the effective application of position limits, for hedgers are the largest players in the markets and have been the most frequent type of traders involved in major manipulation cases. Consequently, position limits have not served as an effective deterrent.

IV. A Better Methodology Is Needed to Prevent and Attack Manipulation and Disruptive Market Activities

A. A Better Definition of Manipulation Is Not a Cure

Commentators who have considered the problems faced by the government in proving manipulation have focused on the difficulty of defining manipulation. They have proposed various alternatives to the definition applied by
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the courts, the CEA and the CFTC. For example, one author, taking a lead from the FTC study, suggested that the common law principal of “prevention or hindrance” should be applied to preclude manipulation. This common law doctrine prohibits someone from preventing or hindering another party from fulfilling his contractual obligations. The author believed that a trader buying up the cash commodity and preventing the shorts from delivering would be engaging in such an act.518

Another commentator would establish a presumption that traders who do not offset their contracts before delivery are guilty of manipulation.519 Still another author has argued that manipulation should include some aspect of fraud or deceit.520 An economics professor would, on the other hand, basically leave it to the markets to decide whether acts were economic and therefore manipulative,521 which may be what the CFTC has done. More recently, a law school professor has asserted that the definition of manipulation should be changed and that the courts should focus on whether “uneconomic” acts have been committed.522

Each of these author’s efforts to define manipulation and establish a workable framework for prosecution of the offense suffers from the same flaws as the CFTC approach. Even if the definition of manipulation is altered to the form suggested by commentators, courts and the agencies will still be saddled with determining whether there has been a real “hindrance” or whether particular acts are “uneconomic,” “fraudulent,” etc. The burden and difficulties of proof remain. Moreover, simply defining manipulation will not correct the problem because, whatever the definition, the same issues and concerns will

519. Preventing Manipulation, supra note 400, at 1605-06.
521. Hieronymus, supra note 505, at 52-53 (1977). Compare, Harrington, supra note 446, at 266-75 (criticizing the Hieronymus approach and suggesting that the issue be left to the courts).
522. Redefining the Offense, supra note 17. One district court recently seemed to have adopted a similar test. See Transnor (Bermuda) Ltd. v. BP North America Petroleum, 2 Comm. Fut. L. Rep. (CCH) ¶ 24,829 at 36,910 (S.D.N.Y. 1990) (where a trader acts with a legitimate investment or commercial purpose, no manipulative intent can be found.”). See also Apex Oil Co. v. Dimauro, 822 F.2d 246 (2d Cir. 1990), on remand, 713 F. Supp. 587 (S.D.N.Y. 1989) (market dominance required).

The full force of academia is still being brought to bear on the issue of how to identify whether a manipulation has occurred. Most recently, Professor Richard Friedman at the University of Michigan has suggested a two part approach for determining whether a squeeze has occurred. This approach would be an alternative to the “classical” requirements of market dominance, artificial price, causation and intent. See Friedman, Stalking the Squeeze: Understanding Commodities Manipulation, 89 Mich. L. Rev. 30 (1990).
arise that have arisen in the context of CFTC, CEA and judicial decisions. The result will predictably be the same as that reached by the CFTC because no one wants to stifle trading and the competitiveness of the markets by punishing traders who may unintentionally affect market prices in some adverse manner.

On the other hand, by simply prohibiting manipulation without defining the term, Congress sought to cover all types of conduct that could be formulated by someone seeking to affect market prices "artificially." In taking that approach, Congress instituted a prohibition so vague and broad that it can impede legitimate conduct if it is not carefully circumscribed by burdensome standards such as those adopted by the courts and the CFTC.

Moreover, any effort to correct the manipulation definition would appear to lie now with the Congress, rather than the courts or the CFTC. A recent Supreme Court case is instructive. In Reves v. Ernst & Young, the Supreme Court noted that Congress had taken an approach founded on economic reality rather than establishing a set of per se rules in determining what constitutes a security under the Securities Exchange Act of 1934. The Court noted that while this approach might result in confusion, it has the advantage of preventing individuals from escaping the coverage of the Act by creating new instruments that would not be covered by a more determinative definition. The Court stated that "[o]ne could question whether, at the expense of the goal of clarity, Congress over valued the goal of avoiding manipulation by the clever and dishonest. If Congress erred, however, it is for that body, not this Court, to correct its mistake."

The approach taken by the Congress under the federal securities laws in the Reves case may actually have been the wiser course for purposes of securities registration. But, in the case of the Commodity Exchange Act, it seems beyond peradventure that the government and the courts have overvalued the concern that clever and dishonest traders will avoid a manipulation prohibition that is definitive and simple. The result has been to overcomplicate the issue and nullify the prohibition.

In order to prevent the market disruptions that occur most frequently, such as those during delivery periods, more definite standards are needed to obviate the need for delving into questions such as intent and artificial pricing and to reduce the possibility that some other manipulator will escape regulation

525. 110 S. Ct at 950, n.2.
526. See also, Memorandum from Mark Powers to CFTC, Nov. 16, 1976, attaching paper of Dr. A.C. Johnson, Economic Analysis of Price Manipulation Under The Commodity Exchange Act, 1945-1974 at 92 (rejecting efforts to catalogue manipulative practices because "crafty" traders could evade the prohibitions); Cargill, Inc. v. Hardin, 452 F.2d 1154, 1163 (8th Cir. 1971), cert. denied, 406 U.S. 932 (1972) ("The method and techniques of manipulation are limited only by the ingenuity of man. The aim must be therefore to discover whether conduct has been intentionally engaged in which has resulted in a price which does not reflect basic forces of supply and demand.").
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through a narrow definition or an undefined legal term. Most importantly, a completely different regulatory approach is needed to attack the concerns raised by manipulation and congestion. This is not to suggest that a broad prohibition against manipulation is not needed. Indeed, it may be appropriate to maintain a residual—broad prohibition against manipulation that will sweep up unusual or novel manipulation techniques.

B. More Effective Regulation Is Needed in the Form of Requirements that Seek to Attain the Goal of a "Fair and Orderly" Market

The principal weakness in the CFTC's regulatory efforts has been a desire to avoid interference with market mechanisms even where price distortions and chaos are threatened. In almost every case where the CFTC has declared an emergency, the declaration came too late to have any effect. Its use of injunctions has been so limited that it is unclear whether they could be an effective remedy. The CFTC's failure or inability to adopt a mechanism for controlling hedger positions also raises grave concerns about its ability to prevent manipulation.

The CFTC's extreme reluctance to intervene in the markets even during times of grave crisis is due, at least in part, to the fact that the commodity futures industry has prided itself on being the last bastion of free enterprise relatively unrestrained by governmental regulation. The industry has staunchly resisted any action that would restrict its unregulated atmosphere. That freedom, however, has not resulted in market mechanisms that are self-correcting, or even effectively self-regulating.

Undoubtedly, the lack of regulation in the futures industry has allowed rapid growth and innovation in the market. But those very valuable attributes must be balanced against the fact that the futures exchanges are now playing a major role in our financial markets and, as in the case of the Stock Market Crash of 1987 and the Silver Crisis of 1980, these markets can seriously disrupt or even threaten the entire economy.

The value of a more affirmative approach seems to be proven by the experience of the SEC. In contrast to the CFTC, manipulation is an important part of the enforcement program at the SEC. The federal securities laws attack manipulation in a number of ways. These include specific prohibitions, grants of rule making authority to the SEC and a general prohibition against trading for a manipulative purpose. Although price artificially may be

529. See Pitt & Shapiro, Securities Regulation by Enforcement: A Look Ahead at the Next Decade, 7 YALE J. ON REG. 149, 256-59 (1990).
required to establish a violation under the securities laws, the SEC gives much less cognizance to a requirement of illegal purpose. Further, while the securities laws do not specifically define manipulation, they do prohibit certain specified types of conduct which, in effect, constitute manipulation. The effect of these prohibitions is very much the same as defining the term manipulation, and "it is, of course, important in attempting to prevent or punish a manipulation to be able to point to a specific statutory provision which describes the conduct in question." But it is doubtful that the specificity of the provisions of the Securities Exchange Act alone have resulted in the SEC bringing more manipulation cases than the CFTC. The SEC is simply more aggressive in this area. For example, in a typical year, the SEC initiated 13 cases involving market manipulation, almost as many as the CFTC has brought in its 15 year history.

351. Id. at 992; N. Wolfson, R. Phillips & T. Russo, Regulation of Brokers, Dealers and Securities Markets § 2.13, at 2-68 (1977) (nevertheless, manipulation cases remain "exceedingly complex." Id. at 2-7). See also Santa Fe Indus. v. Green, 430 U.S. 462, 477 (1977) (the prohibition against manipulative devices in the federal securities laws is a term of art but "[n]o doubt Congress meant to prohibit the full range of ingenious devices that might be used to manipulate securities prices"); Schreiber v. Burlington Northern, Inc. 472 U.S. 1 (1985) (intentional conduct required to establish securities manipulation). See also Crane Co. v. Westinghouse Air Brake Co., 419 F.2d 787, 792-96 (2d Cir. 1969), cert. denied, 400 U.S. 822 (1970); Chris-Craft Indus. v. Piper Aircraft Corp., 480 F.2d 341, 383 (2d Cir. 1973), cert. denied sub nom. First Boston Corp. v. Chris-Craft Indus., 414 U.S. 910 (1973); Thornton v. SEC, 171 F.2d 702, 703 (2d Cir. 1948).


354. 1966 Hearings, supra note 296, at 33 (testimony of Philip A. Loomis, Jr., General Counsel, SEC). Another witness at the hearings when this statement was made testified that commodity manipulation is inherently difficult to define and virtually impossible to anticipate in advance. Id. at 70 (testimony of Dr. Roger W. Gray, Professor at Stanford University). Indeed, one exchange official thought that manipulation should not be made a felony because "there is too much doubt about what it means." Id. at 77 (statement of F. Marion Rhodes, President, New York Cotton Exchange).

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If manipulation is to be prevented and manipulative practices are to be prosecuted, the CFTC must play a much more affirmative role in the market place. It must simplify prosecutions, and its goal must be to assure a "fair and orderly market." The CFTC must be prepared to intervene actively to assure that this goal is reached.\(^{536}\) The concept of a fair and orderly market far transcends traditional concerns with "manipulation." Market disruption should not need to approach a crisis atmosphere before preventive action is taken. In fact, it has been stated that the markets are susceptible to "little manipulations" as well as very large manipulations.\(^{537}\) The CFTC must also seek to rid the market, or at least lessen the effects, of congestion or other so-called natural corners or squeezes that do not involve intentional plots to manipulate the futures markets.

The concept of a fair and orderly market would lead to an overall approach of prevention, intervention and prosecution. For example, the SEC is given broad authority under the Securities and Exchange Act of 1934 to adopt regulations necessary "to maintain fair and orderly markets."\(^{538}\) In this regard, the Securities and Exchange Commission imposes "market maker" obligations on participants in the securities industry.\(^{539}\) Those obligations are designed, in large measure, to assure a fair and orderly market and to prevent disorderly trading. A market maker in the securities industry, one who buys and sells for his own account, is required to assist in "maintaining a stable market" through transactions designed to fill temporary gaps in public supply and demand.\(^{540}\) Exchange rules may also require that trades be "reasonably calculated to contribute to the maintenance of a fair and orderly market".\(^{541}\)

Any affirmative price stabilization or price maintenance requirements would undoubtedly be anathema to the commodity futures industry and to other opponents of government regulation, with good reason.\(^{542}\) Nevertheless,
market maker obligations do not seem to fall within these categories. Indeed, the Chicago Board of Trade has proposed a market maker mechanism to supplement the present auction process, requiring a market maker to quote a minimum size, maximum bid-offer spread for a two sided market. But such market makers would be used only to stimulate a new contract and would be phased out as volume increased.\textsuperscript{543} The Chicago Mercantile Exchange has also proposed a market maker obligation for its proposed "Globex" worldwide computerized trading system.\textsuperscript{544}

It also does not seem that there is any obstacle or justification that would preclude the CFTC from preventing activity that results in a market that is not fair and orderly. Nevertheless, one author has asserted that it would be simpler and more effective directly to prevent disorderly trading by exchange rules that limit maximum price changes in a particular trading session.\textsuperscript{545} The author then asserts that, if the goal of price limits is to stabilize prices, it is at fundamental odds with the basic price-setting function of a futures market.\textsuperscript{546} However, price limits and other efforts to assure a more fair and orderly market merely act as circuit breakers to allow time for decisions to be made and margin funds to be acquired. Price limits allow market operators to obtain a more objective perspective on the underlying factors which have precipitated the heavy fluctuations, to prevent panic among either buyers or sellers, to permit the exchange commission houses as well as the clearing house itself to prepare additional calls for market variation margins, and to enable exchange traders to prepare to meet such calls.\textsuperscript{547}

The purpose of maintaining an orderly market is to assure that prices reflect actual conditions and are not the result of disruptive trading by powerful market forces that have the wherewithal to unduly affect prices. The requirement of a fair and orderly market reflects a social judgment that large traders should not be permitted to abuse these markets by causing disruptions affecting consumers and the economy in general. It also reflects the difficulty and frustration of attempting to prove purposeful conduct and artificiality of prices.

\textit{The Good and Evil in Organized Speculation}, Lit. Dig., Aug. 5, 1922, at 64. Unfortunately this advice was not followed.\textsuperscript{543} Letter from Karsten Mahlmann, Chairman, Chicago Board of Trade, to Robert C. Bower, Merrill Lynch Government Securities, Inc. (Mar. 28, 1990).\textsuperscript{544} Chicago Mercantile Exchange Inc. proposed rule 581.\textsuperscript{545} Redefining the Offense, supra note 17, at 389. For a discussion of price limits see supra note 90 and accompanying text.\textsuperscript{546} Redefining The Offense, supra note 17, at 389.\textsuperscript{547} Campbell, supra note 17, at 226 n. 58 (quoting) BAER & SAXON, COMMODITY EXCHANGES AND FUTURES TRADING, 157 (1949)). See also B. TAMARKIN, supra note 33, at 28; SEC REPORT, supra note 18. 364
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As stated in a related context, "you cannot tell at exactly what stage a kitten becomes a cat in determining whether a man bought or sold on the market for the purpose of raising or depressing the price . . . ."548

This more active regulatory approach would require the establishment of more effective surveillance systems. Day-to-day surveillance of the markets is already the backbone of CFTC preventative activity in the markets. Over twenty-five percent of the CFTC staff is assigned to the function of looking for inordinate market power, possible manipulation and delivery congestion.549 Nevertheless, it has been long recommended that the CFTC upgrade its surveillance programs.550 Indeed, the CFTC staff admitted that in at least one instance it could not establish that a floor broker had caused a large price increase because of the lack of precise trade timing information.551 Recent grand jury investigations in Chicago have also exposed gaps in the audit trail of orders, which is often vital to determining whether improper trading has been conducted.552 Further, while large traders must now report their positions on a daily basis,553 the CFTC focuses its surveillance activities on contracts that are approaching the delivery period.554 The CFTC should conduct surveillance throughout the life of the contract to see if large traders are affecting prices through their trades and whether these positions are so large that they should be required to liquidate well before the delivery period. This would also assure that large traders are not trying to "bull" or "bear" the market or to engage in manipulative trades or any other number of abuses such as "frontrunning".555

The CFTC must also broaden its surveillance role over the cash market.556 In instances where there is a shortage of supplies, the CFTC must recognize that the market may become "congested." In such instances, it must adopt a much more active regulatory framework for limiting the effects of large traders. This could include the adoption of a regulation allowing the CFTC to declare


549. 1978 Senate Reauthorization Hearings, supra note 365, at 223.

550. See COMPTROLLER GENERAL, REPORT TO THE CONGRESS, COMMODITY FUTURES REGULATION: CURRENT STATUS AND UNRESOLVED PROBLEMS (July 15, 1982); Commodity Futures Trading, supra note 338, at 24.


554. Although it does review the entire life of futures contracts, the CFTC focuses on the last thirty days because that is when manipulation is most likely to occur. 1978 Senate Reauthorization Hearings, supra note 365, at 402.


556. See 17 C.F.R. § 19.00-.01 (1990) (reports on cash portions of certain ledgers).
a market "subject to congestion." In such a case, the CFTC would affirmatively
take action to restrict the size of trading by large traders, whether they were
hedgers or speculators. The CFTC would simply order large traders to liquidate
or reduce their positions without requiring that there be a market "emergency"
or that an actual manipulation be threatened. This would assure that traders do
not exploit congested market situations and cause abnormal disruptive price
changes.

It is often stated that the delivery requirement should be maintained in order
to assure that futures prices remain connected to the underlying commodity
prices. Nevertheless, the concept of a fair and orderly market will also require
the CFTC to prohibit traders from standing for delivery in a market that is
subject to congestion. The CFTC could do this by either ordering liquidation
prior to a delivery period or, possibly, declaring that particular contracts will
be settled by cash settlement. In either case, large traders would be
prevented from either taking advantage of short traders or causing disturbances
in the markets by forcing emergency efforts to bring additional supplies to a
market simply to meet delivery obligations.

This will, of course, require some social judgments. By preventing delivery,
it can be argued that the CFTC is taking a policy position in favor of the shorts
by allowing them to escape their delivery obligations. But that is exactly the
type of decision that must be made if regulation is to be effective. Even if the
decision is to allow the shorts to get "off the hook," that decision is being made
not to benefit the shorts but to benefit the market place as a whole. There is
nothing to be gained by requiring shorts to bring additional supplies to a
delivery point that does not need those supplies for anything other than delivery
on a futures contract. The fact that the longs are prevented from profiting
because of a congested market situation does not seem to have much social
detriment. Of course it might also be argued that these trading restrictions will
decrease demand and thereby themselves distort prices. But that should serve
as a motivation for the exchanges to act by providing sufficient delivery points,
or cash settlement, so that the threat of a congested market is reduced.

This is not to suggest that disruptive trading practices of short traders should
be ignored. Short traders should not be allowed to "hammer" or "bear" the
market by repeated large short sales at descending price levels. A "tick" test
is used in the securities industry to restrict short sales when a market is trading

557. See generally, McDermott, supra note 93, at 218-19; Futures Control, supra note 67, at 1246 n.11
(while delivery is an infrequent occurrence in a futures contract, the requirement remains essential because
it maintains a true price relation between the cash market and the futures market); Illusory Bar, supra note
17, at 174.

(advoctating cash settlement to prevent squeezes and corners).
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down.\textsuperscript{559} Such a test may not be inappropriate for the commodity markets. Short selling practices such as “gunning stops,”\textsuperscript{560} selling that unduly depresses prices, and even selling that unnecessarily results in a free fall in commodity prices, should be prohibited.\textsuperscript{561} Much of this type of trading is done on the floor of the exchange by traders in the pits or large institutional traders with direct access to the floor. Because of the time and place advantage they enjoy, it is often possible for them to engage in selling sprees, usually of a short duration, that drive prices down. Recent events also suggest the need for short sale controls. On July 26, 1990, it was reported that short sales of some two thousand contracts caused a sharp drop in the cocoa market. The orders were apparently placed by someone misrepresenting their identity.\textsuperscript{562}

The CFTC must establish a body of rules that includes a prohibition against sustained short sales in a dropping market and a prohibition against rigged trades made at the closing or opening of trading with the purpose of setting prices for one reason or another.\textsuperscript{563} This type of trading could be restricted,

\begin{itemize}
\item \textsuperscript{559} 17 C.F.R. § 240.10(a)(1) (1988). See Macey, Mitchell & Metter, Restrictions on Short Sales: An Analysis of the Uptick Rule and Its Role in View of the October 1987 Stock Market Crash, 74 CORNELL L. REV. 799 (1989); SEC REPORT, supra note 18, at 3-24 through 3-26 (SEC concludes that the extension of short sale restriction to derivative markets such as futures is not feasible); Power & Sal., SEC Is Warning Index Traders On Uptick Rule, Wall St. J., April 26, 1990, at C1, col. 3 (SEC curtails use of exemption from tick test for index arbitrage).
\item \textsuperscript{560} Compare Evolution of Futures Trading, supra note 24, at 63 (suggesting use of an SEC tick test for short sales in the futures markets during periods of sharp decline) with 1978 Senate Reauthorization Hearings, supra note 365, at 302-03, 306 (short selling restrictions could impair use of commodity markets).
\item \textsuperscript{561} See supra note 74 and accompanying text. Recently, the Secretary of the Treasury has stated that: For over 50 years the securities laws have restricted bear raiders like the 1920's Jessie Livermore from selling short in declining markets. The purpose of these restrictions is to prevent “gunning” the market, which drives down the market and confuses the small investor. However, a concerted selling effort in the futures market can completely undermine the short selling restriction—and in fact, because of low futures margins, can accelerate the stock market downdraft and increase public confusion.
Letter from Nicholas F. Brady, Secretary of the Treasury, to Senator Patrick Leahy, Chairman, Senate Committee on Agriculture Nutrition and Forestry, Secretary of the Treasury (May 8, 1990). See also, Note, Manipulation of the Stock Markets Under the Securities Laws, 99 U. PA. L. REV. 651, 674 (1951) (“Stop-loss orders have been condemned because they produce "terrific breaks in stocks.").
\item \textsuperscript{562} It was suggested long ago that restrictions on short sales were needed: Opposition to the bill in the form in which it first came before the committee developed mainly on the power vested in the Secretary of Agriculture to fix a short-selling limit and to prohibit short selling entirely when found necessary. It was contended that this was too much power to place in the hands of any one person. This objection is met in the present bill, which gives this power to the commission named in the grain futures act instead of the Secretary of Agriculture. Since the exchanges themselves have authority to limit or prohibit short selling, but have not the will to exercise it, it would seem that so long as these markets are to be regarded as public markets there can be no objection to lodging the same power in a tribunal such as that provided for. The records of the past few years provide ample evidence that further control over speculative activity in the commodities markets is urgently necessary.
\item \textsuperscript{563} In Zenith-Godley Co., 6 AGRIC. DEC. 800 (1947), the CEA had discovered that the Dairymen’s League Cooperatives Association of New York had manipulated spot butter prices in order to increase fluid milk prices, which were set on the basis of Grade A butter prices under the Agricultural Marketing
\end{itemize}
for example, by imposing limits on the amount of short trading that any one trader can engage in on a given day. The CFTC presently has the authority to restrict the size of daily trading for speculators. Early in its existence, however, the CFTC Advisory Committee on the Role of Contract Markets recommended that the CFTC shift its regulatory emphasis away from strict speculative limits. It did so because it believed such limits provide little control over hedgers and virtually no control during delivery months. The committee recommended instead that daily limits be replaced by improved monitoring and surveillance programs. Pursuant to that recommendation, the CFTC eliminated its daily trading limits. That decision should be revisited.

A fair and orderly market would include more definite prohibitions against wash sales or other trades, such as frontrunning, that could set artificial prices in the market place. The CFTC should impose specific obligations on traders on the floors of the exchanges, requiring them to refrain from acts that disrupt the market. This would mean that traders have an affirmative obligation not to enter into trades that would tend to disrupt the market. For example, during delivery periods, the CFTC should prohibit traders from executing orders that are large enough to increase existing contracts beyond available deliverable supplies. Such action is needed because even critics of government intervention admit that a line cannot be drawn between manipulation and aggressive trading. Prohibitions against disruptive aggressive trading are also needed to prevent small squeezes which are less obvious and perhaps more frequent than large ones. The CFTC has also noted that if

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Agreement Act, 7 U.S.C. § 601. The respondents had bought ninety-seven percent of the butter sold on the exchange during a five day period, and its trading effectively pegged the price of butter at eighty-four cents, up from eighty-two and a half cents. After the League stopped its trading, prices dropped to seventy-four cents. The trading substantially increased price differences between Chicago and New York butter, causing butter to be sent to New York from Chicago. *Id.* see also Randolph, 21 AORIC. Dec. 219 (1962) (manipulation of egg prices in order to value cash market transaction); Polonyi Co., CFTC Doc. No. 82-38 (complaint) (filed Apr. 26, 1983).


567. 7 U.S.C. § 6(c) (Supp. I 1990). What constitutes a wash sale has been left in doubt as a result of the dismissal by the Second Circuit of a CFTC case in which a trader seeking to better his position for purposes of delivery entered into simultaneous buy and sell transactions. Stoller v. CFTC, 834 F.2d 262 (2d Cir. 1987) (case arising out of May 1976 Maine potato futures manipulation case). See also, In the Matter of Gilchrist, 2 Comm. Fut. L. Rep. (CCH) ¶ 24, 993 (C.F.T.C. 1991) (dismissal of wash trading claim).

568. See supra note 555. The House of Representatives has approved legislation that would prohibit front running. H.R. REP. No. 236, supra note 552, at 11.


570. It has been stated that:

Obviously, there is a great deal of risk in attempting a squeeze. And if the squeeze is successful, so that price is markedly affected, the squeezer will likely be prosecuted by the CFTC. This implies that a would-be manipulator had better attempt only a relatively small squeeze, where detection of price distortion is difficult or impossible. Some people have suggested that such small squeezes are common in the futures markets.
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a trader is attempting to artificially raise prices during the day, "he or she more probably would have entered several incremental orders in succession, with each order to have been filled at progressively higher prices." Caution should be used in restricting such activities, however, because traders often use "scale" orders—purchase orders at progressively higher prices or sell orders at progressively lower prices—in order to assure that they are following, not over-bidding or under-offering, the market.

The concept of a fair and orderly market will require that the CFTC be given additional authority to impose greater restrictions on hedge traders. This seems to be one of the more critical needs since hedge traders are usually both the largest traders in the market and the ones most frequently involved in market disruption and manipulation. Indeed, it was noted in Congress in 1978 that "five of the eight most recent market manipulation cases brought under the Commodity Exchange Act were against commercial operators with hedging exemptions" from speculative prohibition limits, while "8 of the 11 market manipulation complaints issued under the Commodity Exchange Act since 1971 were at least in part against commercial operators" acting as hedgers.

These would be difficult rules to draft. But the CFTC has found that there are indicia of what may constitute particular types of manipulation. For example, it has found three general trading activities that are indicative of short term manipulation: "(1) purchases made substantially above the market price, or bidding above existing offers in the pit; (2) rapid purchases at increasingly higher prices; and (3) extremely large purchases relative to the market." Specific prohibitions against such practices are needed. For example, in the Silver Crisis it was charged that one trader had conducted trading on the floor of the Comex in a manner calculated to raise the price of silver.

But care should be taken here so that the "manipulation" trap does not descend once again. Requirements of specific intent to create artificial prices or to disrupt the market should be eschewed. Rather, these prohibitions should be objective. If the trader is determined to have engaged in specified prohibited practices that have disrupted the market, a violation of the CFTC regulation would occur. The trader's intent and justification could then be weighed in determining the appropriate penalty.

Regulation for hedgers could also be in the form of position limits that will restrict the abilities of hedgers to take on large positions as the delivery periods

CFTC Reauthorization on H.R. 5447, supra note 401, at 720.

571. MMI REPORT, supra note 454, at 14.

572. See CFTC, THE CFTC GLOSSARY, supra note 479, at 52 (description of scale orders).


574. MMI REPORT, supra note 464, at 7.

approach and require them to liquidate positions where the CFTC determines that a market is subject to congestion. Such an effort was made in the aftermath of the coffee crisis, when the CFTC proposed a rule that was designed to prevent hedgers and other large traders from causing market congestion or engaging in manipulation in the market place. This proposed rule would have required each exchange to limit positions of traders in maturing futures contracts to no more than twenty-five percent of the open interest in that future, unless the exchange affirmatively determined that the position was not a threat to orderly trading. The proposal was designed to limit large positions during a maturing future without having the CFTC declare an emergency.\(^7\) The proposed rule would have applied to all traders, regardless of whether their positions constituted bona fide hedging positions or speculation.\(^7\)

The proposed rule was not designed to require automatic divestiture of a position in excess of twenty-five percent. Rather, it was designed to serve as a standard by which the exchanges would be required to analyze the probable effects of a large position on the futures market. Only if an exchange determined that the position could result in price manipulation or market congestion would it then notify the holder of the position and direct the holder to take whatever action was necessary to prevent congestion or manipulation.\(^5\)

The CFTC advised Congress that most market manipulation cases had been brought against commercial operators with hedging exemptions. For that reason, the CFTC thought that its position limits could not provide a sufficiently strong defense against market abuses because position limits apply only to speculators.\(^5\) The historical reason for not applying position limits to hedgers was the belief that hedgers are not price conscious.\(^5\) But this has not proved to be the case. Hedgers also have advantages over speculators. Hedgers have

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578. 43 Fed. Reg. 15,438 (April 13, 1978). The CFTC further stated that it wanted to consider whether there should be a provision in the rule that would allow persons who anticipated holding major positions during the last days of trading to seek an advisory determination from the exchange in advance that would allow the trader to have as much time as possible to liquidate his position, if it appeared that the position was a problem. 43 Fed. Reg. 15,438 (Apr. 13, 1978).


580. See Note, supra note 198, at 1377 n.29.
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considerably lower margins and can obtain financing for their trading more easily.581 The industry strongly opposed the adoption of limiting large positions, and the rule was not adopted by the CFTC.582 Among other things, the exchanges asserted that they could not identify the positions of large traders, and claimed that they would have difficulty aggregating the positions of traders acting together.583 It was also noted by the CFTC staff that there were other major problems that could arise from the proposed rule, which presumed that the exchanges could determine "what are orderly markets and what is orderly trading. In that connection, there are definitional problems with the terms 'price manipulation' and 'market congestion.'"584 This appears to be a startling admission that neither the exchanges nor the CFTC knows what constitutes price manipulation or market congestion, and it underscores the need for affirmative regulation in this area.

The grounds for not adopting the proposed rule also seem to be less than convincing. Large traders are required to report their positions every day to the CFTC,585 and each exchange must determine its open interest each day.586 It is a simple matter to identify those positions that constitute a significant percentage of the open interest. That information can then be coupled with available deliverable supplies and other fundamental information to determine

581. Valdez, supra note 343, at 67-68 (CFTC could interpret its mandate to require that hedgers trade in an "orderly manner").

582. See, e.g., Letter from John M. Schobel, Jr., supra note 576 ("I think it is probably one of the worst regulations that the Commission has proposed . . .."); Letter from David H. Morgan, President, MidAmerica Commodity Exchange, to CFTC Secretariat (July 17, 1978) ("The proposed Regulation is unworkable and can be expected to result in unnecessary litigation, foreclosure of the use of futures markets by many hedgers and speculators, and a deterioration of confidence in such markets."); Letter from Clayton Yeutter, President, Chicago Mercantile Exchange, to Office of the CFTC Secretariat, (July 21, 1978) ("The proposed regulation grossly expands the statutory requirement to include all persons regardless of market's control over them, and to include 'market congestion' in addition to price manipulation. To the extent that the proposed regulation goes beyond the statute it raises serious legal and conceptual problems which will inevitably be troublesome both to the Commission and the industry."); Letter from John J. Conheeney, Director, Commodity Division, Merrill Lynch, Pierce, Fenner & Smith Inc., to Secretariat CFTC (June 26, 1978) ("Different contract markets will be impacted to different extents by the proposed rule since it is more likely that the smaller exchanges will have an individual with a position requiring the determination. This we think is unfair to those exchanges and puts them under a greater burden than the larger exchanges."); Letter from Robert K. Wilmouth, President, Chicago Board of Trade, to Secretariat CFTC (undated) ("rule is totally unworkable. . . . wholly arbitrary and is without any factual basis") (Letters available from the CFTC Freedom of Information Act officer). More recently, large money managers have claimed that existing position limits for speculative trading are "archaic" and unduly restrictive. Angrist, Archaic Limits on Futures Vex Managers, Wall St. J., Sept. 6, 1990, at C1, col. 3.

583. See Draft Memorandum from the CFTC Division of Economics and Education to the CFTC 6-15 (available from the CFTC Freedom of Information Act officer). Some of the exchanges did not have surveillance systems that allowed them to determine whether they were large traders in their markets. This seems to be incredible, if it is assumed that the exchanges have any role in seeking to prevent or punish manipulation.

584. Id. at 26. Concern was also expressed that the exchanges would intervene in the market unnecessarily in order to avoid liability under the rule. No Squeezing, supra note 517, at 944 n.119.


whether a position in any way poses a threat of congestion or disruption.\footnote{587} If it does, the position should be reduced to a safe level.\footnote{588} This will mean, of course, that a hedger may be placed in a difficult situation. If the hedger is required to liquidate the futures position, his position in the cash market will be exposed, subjecting him to a risk he may not want to incur. On the other hand, this type of restriction would impose an obligation on the hedger to assure himself that his risk position and hedges do not get so large that a contract market might view them to be a threat. This would, in effect, be a self-policing incentive.

Other approaches also may be taken. During the Stock Market Crash of 1987, the concept of “bracket rationing” appeared under Chicago Mercantile Exchange rules limiting the size of trading by hedgers and arbitrageurs. Initially, such traders could obtain retroactive permission to exceed those limits when they demonstrated that their positions were based on business need, financial ability and market liquidity. On October 20, 1987, however, the Exchange limited requests by major traders for higher limits and, took emergency action requiring prior approval for traders to exceed their hedge limits. It also required large traders to “bracket ration” by spreading their transactions out over time brackets during the trading day.\footnote{589} This reduced the concentration of sell orders and had the effect of imposing position limits on hedges as well as speculators. From that experience, it would appear that a workable methodology for controlling and lessening the effect of large hedging positions on the market can be effectuated.\footnote{590}

Additional surveillance of hedgers should be undertaken to assure that they are not speculating in the markets, an inquiry that is rarely undertaken by the CFTC or the exchanges. This issue appeared in the Ferruzzi crisis because there was concern that the Ferruzzi position was so large that it was, at least in part, speculative.\footnote{591} The House of Representatives has since approved a measure that would require greater exchange surveillance in this area.\footnote{592} The CFTC, however, must become more involved and play a more affirmative role.

\footnote{587} It should be noted that the use of large trader information acquired by the CFTC must be maintained as confidential, and the CFTC is sharply restricted in the use it may make of such information. The CFTC, however, may share this information with the exchanges under specified circumstances. To the extent those circumstances are not sufficient to allow the exchanges to have every day access to this information, the statute should be changed. \textit{See} 7 U.S.C. § 12(a)(6) (1990).

\footnote{588} \textit{See} No Squeezing, supra note 517, at 945 \textit{et seq.}


\footnote{590} In the Ferruzzi crisis, the Ferruzzi’s hedging exemption was revoked which required it to liquidate all of its May futures position in excess of the three million bushel speculative trading limit. This action, however, was not strong enough because Ferruzzi simply rolled its position over into the next futures month. \textit{CBT Emergency Action, supra} note 27, at 9.

\footnote{591} \textit{Id.} at 13.

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The CFTC must broaden its efforts to prevent manipulation through rumors. Commodity futures prices are affected by unfounded rumors in the market place. Such rumors include the "green bugs" with which Congress was concerned before adopting the Commodity Exchange Act.\(^{593}\) false rumors of Presidential deaths, cancer threats or drought scares, and also more sophisticated practices, such as economic announcements that are designed to affect market prices or to aid traders who have advance knowledge.\(^{594}\) Only recently, false rumors concerning Iraqi troop movement after the Kuwait invasion resulted in price increases of some 10 percent on the New York Mercantile Exchange, a worldwide barometer of oil prices.\(^{595}\) But very few manipulation cases have ever been brought for the spreading of rumors or false information.\(^{596}\)

Controlling rumors will require the CFTC to monitor news reports and market rumors more closely. The CFTC also should follow prices closely when they rise or fall sharply; it should find out what caused the aberration and assure that erroneous information is not being manufactured, and that trading activities are not improper. It is only through these and other efforts that the CFTC will effectively cleanse the markets of manipulative and fraudulent practices.

Another measure needed to contribute to a fair and orderly market in the commodity futures industry is the development of an automatic order execution system for small orders. The securities exchanges have already developed such systems. For example, the New York Stock Exchange has a "designated order turnabout system" ("DOT," later called "Super DOT"). This system and other systems used by other exchanges allow orders of up to 2000 shares to be electronically routed to a specialist desk. For over-the-counter trading,

593. See supra note 104 and accompanying text.
595. Belton, Anxiety Fed Rumor Mill Causes Wall St. Tremors, USA Today, Sept. 18, 1990, at B1, col. 3. See also, Wald, Oil-Price Role Defended by Futures Exchanges, N.Y. Times, Nov. 12, 1989, at D 2, col. 5 (futures exchange blamed for volatile oil prices during Gulf crisis); Potts & Lippman, Is this Anyway to Set Oil Prices? Wash. Post, Jan. 12, 1991, at Al, col. 4 (rumor that Iraqi leader Saddam Hussein had dreamed that the prophet Muhammad advised him to withdraw from Kuwait causes prices to drop on futures exchange).
NASDAQ has a small order execution system that allows orders of up to 1000 shares to be automatically executed at the best market price. However, these order systems do not always operate well in times of stress, as demonstrated during the stock market crash of 1987.

The commodity futures industry has made little effort to provide for automatic execution on the floors. Hopefully, the development of commodities electronic trading systems such as the one that is now going forward in a joint effort between the Chicago Board of Trade and the Chicago Mercantile Exchange, which will allow electronic trading after regular exchange hours, will alleviate or change that situation. Although both this system, "Globex," and a proposal for a hand-held computer order entry system are as of yet untried and untested, their ultimate design should allow maximum electronic order execution, particularly for small orders, so that a flood of paper work does not disrupt trading. Such a system hopefully could obviate the widespread petty thefts that seem to occur with some frequency on the floors of the commodity exchanges in connection with the execution of small orders.

Large block orders also have been subject to special provisions in the securities industry that limit possible disruptive effects. The commodity futures industry, however, has no such provisions; indeed, the CFTC has asserted that they are barred by statute. Nevertheless, the commodity exchanges are now experimenting with provisions that control large orders. This effort should go forward as rapidly as possible.

All of these efforts must be coupled with an effective program of prosecution. This program must provide for both criminal and civil penalties. If CFTC regulations are sufficiently pointed in attacking particular practices, prosecution can be quick and effective, or at least it can be conducted without the squandering of resources that traditionally has been required for prosecution of a "manipulation" case. Traders secretly acting together, "conspiring" or acting in "concert" to trade in a manner that threatens the market, must be subject to

598. BRADY REPORT, supra note 18, at 34; SEC REPORT, supra note 18, at 9-12 through 9-15.
600. In 1989, the FBI conducted a sting operation on the floor of the Chicago commodity exchanges. As a result, 48 brokers were indicted on multiple counts of prearranging customer trades in a non-competitive manner that allowed the traders to defraud customers of small amounts on numerous trades. See discussion infra note 605 and accompanying text.
601. Committee on Futures Regulation of the Association of the Bar of the City of New York, Large Order Execution in the Futures 44 Bus. Law. 1335 (1989) [hereinafter Large Order Executions].
602. Id.
603. Id. See Crawford & Gaines, Merc Moves Would Go to Core of Trading, Chicago Tribune, April 21, 1989, § 3 at 1, col. 2; Berg, Chicago Merc to Allow Some Trading Off Floor, N.Y. Times, Sept. 22, 1989, at D1, col. 4. Institutions should also be given broader latitude in their ability to execute trades in the over-the-counter market. See generally Markham, Regulation of Hybrid Instruments Under the Commodity Exchange Act: A Call for Alternatives, 1990 COLUM. BUS. L. REV. 1.

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effective regulations that will prohibit such practices. In the past, traders only rarely have been prosecuted criminally for activities that disrupt the markets.\textsuperscript{604} Recently, the Justice Department has undertaken a broad scale effort to enforce the Commodity Exchange Act. The now famous sting operations in Chicago led to the creation of task forces in U.S. Attorney offices around the country to bring commodity-related prosecutions. The Chicago sting operations have already resulted in the indictment of some forty-eight traders.\textsuperscript{605} But only a few minor charges were proven in the first of the government trials arising from those charges.\textsuperscript{606} Joint efforts between the CFTC and the Justice Department are needed to prosecute those who engage in activities that would disrupt these very important and vital markets.

Finally, a cost-benefit analysis is needed to determine whether a framework that seeks to create a “fair and orderly market” is more appropriate than a more laissez-faire system. The greatest danger from more affirmative regulation is that it might strangle the markets and stifle innovation. Most political campaigns in recent years and public opinion in general have shunned increased governmental regulation because it has been thought that “overregulation” by the government has been impairing our economy.\textsuperscript{607} Undoubtedly, those concerns are very real ones, and particular care should be taken with the highly innovative and still-growing futures industry. Nevertheless, more affirmative regulation is required in these markets if they are to enjoy the confidence of the public. The alternative is to declare that the manipulation of commodity prices is an unpunishable crime in which traders may engage with no regard for the effect upon the consumer and the economy in general.

Although a cost-benefit analysis cannot be an exact one, strong arguments could be made that the benefits of a fair and orderly market far outweigh the costs of decreased market efficiency from manipulations and market disruptions. The cost of enacting legislation, adopting needed rules, and adding CFTC staff members to enforce those rules, pales in comparison to the vast expenditures of resources that have been applied to manipulation investigations. The litigation and societal costs that result from a manipulated artificial price are also significant. By preventing circumstances that lead to price artificiality, and by assuring that there is a level playing field on which trading can be conducted

\textsuperscript{604} As noted above, the CEA asserted that only three criminal prosecutions have ever been brought for price manipulation under the Commodity Exchange Act. See supra note 329 and accompanying text. The author, however, has been able to discover only two such actions. See supra note 258 and accompanying text; United States v. Bauer, 72 Crim. Ct. 186 (N.Y. Sup. Ct. 1972).


\textsuperscript{607} See, e.g., Easterbrook, supra note 520; Silver Prices, supra note 422, at 211.

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in a "fair and orderly manner," it would seem that a cost-benefit analysis would weigh heavily in favor of more affirmative regulation.

Conclusion

The history of manipulation in the commodity futures industry dramatically underscores the fact that regulatory efforts on the part of the federal government have been unsuccessful. The "wheat kings" were almost entirely unregulated until the 1920's, when the Grain Futures Act was adopted. That legislation, however, proved unsuccessful. Thereafter, the Stock Market Crash of 1929 and the precipitous decline in commodity prices resulted in the adoption of the Commodity Exchange Act of 1936. This regulation also proved to be lacking in effective regulatory measures to prevent manipulation. Among other things, it failed to define manipulation, and it failed to prohibit particular manipulative practices that could easily be prosecuted.

Because of these shortcomings, complicated investigations and extended litigation were necessary to prove manipulation. As a result, cases were often settled with de minimus sanctions; and, when a matter was litigated, the government's proof or theories were often found lacking. The split in the circuits between Volkart and Cargill caused further confusion, and efforts by the government to eliminate that confusion through legislation proved to be unsuccessful. The limited legislation adopted in 1968 to give the government additional powers also proved ineffective.

Later, with the explosion of commodity prices in the early 1970's, Congress created the CFTC and granted it what appeared to be broad powers to deal with market misconduct. This included the authority to impose civil penalties of up to $100,000 and the authority to take emergency action. Those powers, however, proved to be ineffective. This is well illustrated by such events as the potato default, the assault on the soybean market by the Hunts, the silver crisis of 1988, the stock market crash of 1987, and other episodes described above. The CFTC also inherited the existing difficulty of proving a manipulation case. As a result, it has only brought a limited number of cases, often with limited success.

Everyone seems to agree that prosecuting of manipulations is central to the regulatory scheme. But the courts and the federal agencies that have strug-

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608. See Hearings on Russian Grain Transactions, supra note 6, at 164 (CEA Administrator asserts that "price manipulation is the most serious violation of the Commodity Exchange Act" and that it can destroy the entire marketing structure); 1978 Senate Reauthorization Hearings, supra note 365, at 280 (Chairman of the CFTC asserts that one of the primary responsibilities of the CFTC is to detect and prevent price manipulation); 1978 House Hearings To Extend Commodity Exchange Act, supra note 365, at 113 (primary reason for the existence of the CFTC is to prevent manipulation); U.S.D.A., FARMERS USE OF FORWARD CONTRACTS AND FUTURES MARKETS 7 (March 1976) ("The abuse probably of most concern is price manipulation . . . ."); Taylor, Trading In Commodity Futures -- A New Standard of Legality, 43 Yale L.J. 639 note 131 (1939) (even the Grain Futures Act sought the prevention of manipulation as its
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gled with the issue of manipulation have been unable to formulate a methodology that would permit effective prosecution. Instead, they have become bogged down on the elements of intent and economic determinations of whether price artificiality has been achieved by the trading activities of a particular individual or firm. This approach has resulted in complicated trials, and discovery proceedings that often require eight or more years to resolve at enormous cost. These costs obviate any deterrence factor that the law may be seeking to achieve.

The courts and federal agencies do not want to adopt a standard that inhibits aggressive price competition in the commodity future market. As a result, they have adopted an intent test: a defendant must have the intent to create a "artificial" price. The establishment of such intent and price artificiality raises complex and difficult economic questions. Many fundamental factors may be cited to justify any particular trading activity. Several commentators have sought to resolve this conundrum by proposing new definitions of manipulation. Those definitions, however, do not lessen the complicated nature of a price manipulation prosecution.

Congress is also now considering whether to move at least part of the CFTC's jurisdiction to the SEC or even to merge the two agencies.609 These jurisdictional battles have been waged for several years.610 The stock market crash of 1987, however, exacerbated the situation. Now it appears that the CFTC faces some danger that it could lose some of its jurisdiction. Whatever happens, however, the eventual regulator will face the same issue. How are these commodity markets to be effectively regulated so as to prevent congestion, market manipulation and crises brought about by large traders? A simple

primary intention).


prohibition against manipulation has been proven ineffective. Consequently, more affirmative regulation such as that recommended in this article will be required by the agency that ultimately retains or assumes authority over futures trading, unless it too wishes to continue the never ending succession of crises that have plagued the futures industry virtually from its inception.611

In sum, if manipulation is to be effectively prevented and prosecuted under the Commodity Exchange Act, the Act must be amended, and the government must take a more affirmative role in regulating the futures markets. As it is, we are left with the words of the FTC study when it observed over seventy years ago that "[t]hough the evil is specific and is a peculiar result of future trading technique, effective remedies for corners are not found in the present law; at least as it is actually enforced."612

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611. Recent legislation authorizes the SEC to act to prevent the manipulation of equity securities prices that are likely to affect market volatility. The SEC could thus prohibit or constrain any act or practice during times of extraordinary volatility when the SEC determined that those acts or practices contribute to extraordinary levels of volatility which affect the maintenance of fair and orderly markets. Similar authority could be used to impose a fair and orderly market during market disruptions. See H.R. 3657, 101st Cong., 2d Sess. (1990); Pub. L. No. 101-432, 104 Stat. 963; S. REP. No. 524, 101st Cong., 2d Sess. 43-44 (1990); Salwen, House Approves Measure Giving SEC Power to Act Against Program Trading, Wall St. J., Oct. 1, 1990, at C10, col. 5; Asides, Wall St. J., Oct. 17, 1990, at A14 (legislation has been enacted to require CFTC to report to Congress annually on its efforts to protect market integrity).

612. FTC STUDY, supra note 25, at 21.
Appendix:
Table of Manipulation Cases Brought
By the CEA and CFTC
<table>
<thead>
<tr>
<th>Case Name</th>
<th>Commodity At Issue</th>
<th>Date and Type of Alleged Manipulation</th>
<th>Date of Decision</th>
<th>Time Required For Resolution</th>
<th>Sanctions or Damage</th>
</tr>
</thead>
<tbody>
<tr>
<td>In Re Cargill, Inc. CEA Doc No. 11 (1940).</td>
<td>September and December 1937 corn futures contracts on Chicago Board of Trade.</td>
<td>Sep. to Dec. 1937. Market Power.</td>
<td>CEA decision rendered March 6, 1940 and modified on June 25, 1942.</td>
<td>Approximately 2-1/4 years.</td>
<td>President and subsidiary denied trading privileges until further notice. President’s suspension lifted approximately two years later.</td>
</tr>
<tr>
<td>Nichols &amp; Co. et al. Rep. of C.E.A. at 13 (1941) and 131 F.2d 651 (1st Cir. 1942) on rehearing, 136 F.2d 503 (1st Cir. 1943).</td>
<td>Oct. 1940 wool top futures on N.Y. Wool Top Exchange.</td>
<td>Market power and rigged trades.</td>
<td>1943.</td>
<td>Approximately 3 years.</td>
<td>No manipulation found in hearing before Dept. of Ag. and no rigged trading.</td>
</tr>
</tbody>
</table>
### Manipulation of Commodity Futures Prices

<table>
<thead>
<tr>
<th>Case</th>
<th>Respondents</th>
<th>Allegations</th>
<th>Result</th>
</tr>
</thead>
</table>

For a more detailed description of the cases and respondents, please refer to the table above.
<table>
<thead>
<tr>
<th>Case Name</th>
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<tbody>
<tr>
<td>Case</td>
<td>Description</td>
<td>Start Date</td>
<td>End Date</td>
<td>Duration</td>
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<td></td>
<td>contracts on the Chicago Mercantile Exchange; Jan. and Feb. 1956 downward</td>
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<td></td>
<td>manipulation of March onion futures contracts on the Chicago Mercantile</td>
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<td></td>
<td>Exchange and cash onions.</td>
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<td></td>
<td>Orleans Cotton Exchange.</td>
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</tbody>
</table>

Upward manipulation charges dismissed; floor broker registration of respondent revoked and his trading privileges suspended for 10 months; trading privileges of two other respondents suspended for 10 months.

Registration of 2 individuals as floor brokers suspended for 30 days; 5 respondents' trading privileges suspended for 30 days, by consent. Case dismissed.

Registration of a firm as futures commission merchant and trading privileges suspended for six months; floor broker registration of another respondent revoked and trading privileges suspended for 1 year; trading privileges of a third respondent suspended for 11 months.

By consent, a respondent agreed that, if it should violate the Commodity Exchange Act within 1 year, its registration as a futures commission merchant would be suspended for a period of 30 days. Also, 2 individual respondents' trading privileges were suspended for 8 months.
<table>
<thead>
<tr>
<th>Case Name</th>
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<tbody>
<tr>
<td>Case Details</td>
<td>Date of Event</td>
<td>Length of Suspension</td>
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<td>Nov. 4, 1965 by consent.</td>
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<td></td>
<td>Registration of 2 respondents as floor brokers suspended for 30 days and trading privileges suspended for 30 days except that 10 days of these sanctions were waived provided that the respondent did not violate the Commodity Exchange Act within 1 year; Registration of 2 respondents as floor brokers and trading privileges suspended for 30 days; registration of a futures commission merchant suspended for a period of 30 days and trading of its own account prohibited for 30 days except that the suspension of registration of the futures commission merchant was waived if the respondent did not violate the Act within 1 year from the date of the order, all by consent.</td>
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<tr>
<td></td>
<td>Cease and desist order; prohibition from trading for 30 days and registration as floor broker suspended for 30 days.</td>
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<tr>
<td></td>
<td>Cease and desist order issued against respondents; one individual respondent’s trading privileges suspended for one year; two other respondents’ trading privileges suspended for sixty days; two other respondents’ trading privileges suspended for 180 days; respondent company subjected to civil penalty of $100,000 prohibited from trading futures contracts for a period of 1 year except for bona fide hedging transactions in certain commodities, all by consent.</td>
<td></td>
</tr>
<tr>
<td>Case Name</td>
<td>Commodity At Issue</td>
<td>Date and Type of Alleged Manipulation</td>
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Manipulation of Commodity Futures Prices

<table>
<thead>
<tr>
<th>Case Reference</th>
<th>Alleged Manipulation</th>
<th>Commodity</th>
<th>Exchange</th>
<th>Action Taken</th>
</tr>
</thead>
<tbody>
<tr>
<td>In re Indiana Farm Bureau Cooperative Association (1980-1984)</td>
<td>Approximately 8 years</td>
<td>Cotton</td>
<td>Commodity Exchange</td>
<td>Speculating, rigging, and manipulation</td>
</tr>
<tr>
<td>In re Indiana Farm Bureau Cooperative Association (1980-1984)</td>
<td>Approximately 4 months</td>
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<td>Commodity Exchange</td>
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Note: The cases listed above involve alleged manipulation of commodity futures prices. The actions taken include penalties, bans from trading, and other regulatory measures. The specific details of the actions and the commodities involved are outlined in the table.
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<p>| In re Hunt [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,296 and ¶ 23,244 (C.F.T.C. 1987). | Sep. 1979 and March 1980 silver futures contracts on the Chicago Board of Trade and COMEX. | Approximately mid-1979 through March 1980. Market Power. | Case still incomplete. | Over 9 years. | By consent a futures commission merchant was ordered to cease and desist and a civil penalty of $1.5 million was ordered with respect to these and other allegations against it; an individual defendant (Nahas) was ordered to cease and desist, to supply documents to the Commission, to pay a civil penalty of $250,000 and prohibition from trading for 5 years; two respondents (W.H. and N.B. Hunt) barred from trading and assessed $10 million civil penalty but recovery was limited in bankruptcy. Another respondent assessed $100,000 civil penalty and ordered to cease and desist by consent. |</p>
<table>
<thead>
<tr>
<th>Case</th>
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<th>Date</th>
<th>Duration/Outcome</th>
</tr>
</thead>
</table>

Approximately 3 years for a consent decision.