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UPDATE

"Spoofing" Continues to Draw Heavy Enforcement Attention

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Spoofing, a form of manipulative trading conduct in which a trader enters buy or sell orders into the market that they have no genuine intention of fulfilling, remains an area of keen interest for regulators as well as exchange-level enforcement officers. At the end of September alone, the CFTC, the Intercontinental Exchange ("ICE") and the CME Group announced settlement of a number of spoofing cases.

- Most prominently, on Sept. 29, 2020,[1] the CFTC issued an order filing and settling charges against JPMorgan Chase & Company and several subsidiaries (collectively "JPM") for extensive manipulative conduct over at least an eight-year period involving hundreds of thousands of spoofed precious metals and U.S. Treasury futures orders on the COMEX, NYMEX and CBOT exchanges. The order, which includes restitution, disgorgement and civil monetary penalties totaling over $920 million, is the largest monetary relief ever imposed by the CFTC. Parallel criminal, civil and individual enforcement actions for key involved traders were also implicated. According to the order, JPM's conduct involved numerous traders sending false market signals to induce counterparties to execute against certain orders by placing misleading buy or sell orders with an intent to cancel prior to execution, thus artificially affecting prices. Contrary to its compliance obligations, JPM failed to identify, investigate and terminate such practices. Its supervision failures persisted in spite of a variety of red flags and internal alerts, as well as regulators' inquiries. While noting that JPM became cooperative in later phases of its investigation, the CFTC remarked that JPM's responses to certain earlier communications had been misleading.
- On Sept. 30, the CFTC issued an order[2] filing and settling charges against Sunoco LP for spoofing-related violations. For approximately a year, ending January 2015, the CFTC found that on multiple occasions a former Sunoco LP trader engaged in a pattern of placing small and large orders on opposite sides of the market in NYMEX crude oil, gasoline and heating futures, frequently canceling the larger buy or sell order shortly their smaller (actually intended) order was filled. Sunoco was fined $450,000 for this disruptive conduct. The CFTC did, however,

[1] *See* CFTC Release No. 8260-20 (Sept. 29, 2020), available here.

[2] *See* CFTC Release No. 8267-20 (Sept. 30, 2020), available here.

acknowledge that upon discovering the trader's spoofing, the firm took substantial remedial actions, including conducting a full investigation, suspending the implicated trader, and improving its trade monitoring, compliance processes and training to make its compliance program more robust against spoofing. These measures appear to have resulted in a reduced financial penalty.

- Also on Sept. 30, ICE announced a settlement with ARB Trading Group North LLC involving approximately $78,500 in penalties including fines and disgorgement for ARB, along with separate financial penalties (spanning approximately 40 to 56 thousand dollars each) and trading suspensions for three affiliated traders.[3] In each case, ICE had identified conduct involving a pattern of futures trading in which the sanctioned persons "instead of entering orders with the intent to trade, … appeared to have entered multiple orders on one side of the orderbook to create false depth, put pressure on the market, and mislead market participants into trading against, or moving the market closer to, [their] opposing small-quantity orders." In addition to possible trading practices violations, ICE also observed that ARB may have failed to adequately supervise its employees. Under the terms of the settlements, ARB and its traders neither admitted nor denied rule violations.
- On the same day, CME Group announced two spoofing-related settlements totaling $75,000[4] against 303 Proprietary Trading LP (for activity on both CME and COMEX), as well as two settlements (including trading suspensions) of $35,000[5] and $50,000[6] against individual traders for activity on CME and COMEX, respectively. In each case, the sanctioned party neither admitted nor denied violating any rules. CME Group sanctioned Proprietary Trading LP for failing to adequately train and supervise its employees (rather than for disruptive trading, per se), citing conduct in which an employee entered layered orders without the intent to trade ("after receiving fills on smaller orders he entered that were resting on the opposite side of the order book, the employee canceled the layered orders"). In each of the latter cases, the involved individual was sanctioned for disruptive trading involving a similar pattern of conduct.

Managers should note that these cases illustrate the same basic pattern of conduct: In an attempt to improve the favorability of an authentic, smaller, buy or sell order, a trader places a much larger order opposite to this position, only to cancel it as soon as their desired position is filled. Such behavior can potentially disrupt efficient price discovery in the market, which makes spoofing a persistent and serious concern for regulators and exchange-level enforcement officers.

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[3] *See* ICE Disciplinary Notice (Sept. 30, 2020), available here; ICE Disciplinary Notice (Sept. 30, 2020), available here; ICE Disciplinary Notice (Sept. 30, 2020), available here; and ICE Disciplinary Notice (Sept. 30, 2020), available here.

[4] *See* CME Notice of Disciplinary Action (Sept. 30, 2020), available here; COMEX Notice of Disciplinary Action (Sept 30, 2020), available here.

[5] *See* CME Notice of Disciplinary Action (Sept. 30, 2020), available here.

[6] *See* COMEX Notice of Disciplinary Action (Sept. 30, 2020), available here.

As always, market participants must remain vigilant about enforcing compliance with all applicable rules (including exchange-level rules) against non-bona fide, disruptive and manipulative trading, such as spoofing. Merely adopting written policies against such trading, without further surveillance and similar actions, likely will not be deemed to be sufficient.

Compliance officers should also take note that enforcement actions in these areas can be based on failure to supervise as well as trading conduct violations. Accordingly, employees must be fully trained so as to understand what constitutes impermissible trading under a firm's policies, and firms must actively monitor for employee compliance.

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