UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

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MOBILEFAX CORPORATION,
Complainant,

v.

AMERICAN NATIONAL TRADING CORP.
d/b/a ANCO DISCOUNT FUTURES,
Respondent.

CFTC Docket No. 05-R053

INITIAL DECISION

Introduction

Mobilefax Corporation's complaint arises from a series of Euro FX futures orders that had been placed on ANCO Discount Future's on-line trading system. Mobilefax's principal allegations are: that ANCO's on-line trading platform failed to report the status of the Euro trades in a timely and accurate manner; that ANCO failed to disclose that its on-line trading system was unreliable; that ANCO's trading desk failed to investigate Mobilefax's complaint about inaccurate on-line reports in a timely manner after promising to do so; that ANCO failed to disclose that day trades are offset on a *last-in, first-out* basis; and that ANCO improperly liquidated Mobilefax's under-margined position. Mobilefax seeks $23,293 in damages. In response, Mobilefax asserts that its on-line trading system is reliable, and denies any errors, omissions, misrepresentations, or violations.[1]

[1] This case was originally assigned to the docket of Judge Maillie. This case was reassigned to my docket on June 21, 2006.

As explained below, after reviewing the parties' documentary submissions[2] and oral testimony,[3] I have concluded that Mobilefax has failed to establish the bulk of the alleged violations. However, I have concluded that Mobilefax has established that an agent of ANCO undertook a special duty and convinced Mobilefax to defer meeting the margin call by promising to investigate Mobilefax's complaint about inaccurate on-line reports, and that ANCO's subsequent failure to conduct a prompt review and to provide a timely explanation breached its fiduciary duty in violation of Section 4b of the Commodity Exchange Act. This violation proximately caused $3,962.50 in damages, based on the difference in the market price, from the time that ANCO promised to perform the special duty, to fifteen minutes before the close.

Factual Findings

1. Mobilefax, a Nevada corporation, has its principal place of business in Las Vegas. Brian Silk, a resident of Wooodland Hills, California, is the president and owner of Mobilefax. Pursuant to a corporate resolution, Silk was authorized by Mobilefax to open an account with ANCO, and to trade futures and options. Before opening the

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[2] The parties' principal submissions that were reviewed include: (1) the account-opening documents, especially the account application, the customer agreement, and the online trading agreement (attachment to addendum to complaint); (2) the ANCO online tutorial (attachment to complaint); (3) the May 2003 monthly account statement, and the May 14, 15 and 19, 2003 confirmation statements (attachment to addendum to complaint); (4) the equity runs for May 15 and 16, 2003 (Exhibits 4 and 5 of ANCO's pre-hearing submission); (5) the time and sales report for the June Euro FX future, for May 15 through 19, 2003 (attachments to complaint and addendum to complaint); (6) various order tickets (attachment to complaint and addendum to complaint); (7) ANCO's list of orders (Exhibit 7 of ANCO's pre-hearing submission); (8) the series of numerous screen shots from May 14 to May 19, 2003 (Exhibits 1, 2 and 6 of Mobilefax's pre-hearing submission); (9) Brian Silk's two May 15 faxes (Exhibits 1 and 2 of Mobilefax's pre-hearing submission); (10) Silk's May 23 letter to Roy (Exhibit 4 of Mobilefax's pre-hearing submission); (11) the transcripts of recorded conversations on May 15, 16 and 19 (Exhibits to ANCO's and Mobilefax's pre-hearing submissions); (12) Mobilefax's and ANCO's post-hearing statements; (13) Mobilefax's complaint and addendum to complaint; and (14) ANCO's answer.

[3] Brian Silk appeared and testified on behalf of Mobilefax. Steve Roy and Don Varden appeared and testified on behalf of ANCO.

ANCO account, Silk had invested in securities for about 25 years, and had briefly traded commodities.

2. American National Trading Corporation, doing business as ANCO Discount Futures, is a registered futures commission merchant, with its principal place of business in Los Angeles, California.

Harry Estrada worked as a clerk at ANCO's trading desk during the relevant time. ANCO principals testified that Estrada's principal duty was to handle the orders, and that on busy trading days, he could not promptly investigate and resolve customer complaints. ANCO did not produce Estrada as a witness.

Estrada spoke to Silk on May 15, 16, and 19, about the disputed Euro FX futures trades. Silk produced recordings of these three conversations.[4]

3. In December 2001, Mobilefax opened a discount, self-directed, account with ANCO. In late December 2002, Mobilefax opened a discount, self-directed, online trading account.

The ANCO On-line Trading Agreement provided, in pertinent part, that: "ANCO's online services include order entry and account status systems, market trading, and general information including quotes, charts, news, system information and other services that may be added from time to time." The online agreement also provided that: "[The customer acknowledges] that the accuracy, completeness, timeliness, and correct sequencing of the information concerning your trading and account activity, the quotes, market and trading news, charts, trading analysis . . . is not guaranteed."

4. Each business day, Silk normally first checked his account around 5:00 a.m. Pacific Time (by which time ANCO had completed its overnight reconciliation), and Silk

[4] Both sides produced virtually identical transcripts of these recorded conversations.

normally last checked the account around 11:00 p.m. Pacific Time. Silk placed almost all orders via the on-line system. Silk typically made long-term trades, and did not trade the same contract in-and-out on the same day.

Each time that ANCO had generated a margin call, Estrada typically consulted with Silk who then decided whether to add funds or to liquidate the under-margined position.

5. This dispute arises from a series of June Euro FX futures orders placed by Silk via the on-line system on Thursday, May 15, 2003. Mobilefax does not dispute ANCO's assertion that on May 15 trading in the June Euro was hectic.

On Wednesday, May 14, Silk had placed order *#541*, to sell two June Euro FX futures at 11494.[5] On May 15, at 5:25 a.m. PDT, 7:25 a.m. CDT, the June Euro opened at 11444. Thus, at the open of pit trading, the two Euros had a positive liquidation value of $1,250.[6]

During the morning of May 15, Silk deviated from his normal pattern of trading, and day-traded the June Euro by making the following sequence of orders:

- At 5:25 a.m. PDT, 7:25 a.m. CDT: Silk placed order *#893*, to buy two June Euro FX futures at 11440. The fill on order *#893* was reported at 5:43 a.m. PDT, 7:43 a.m. CDT. (Silk mistakenly assumed that order *#893* would offset order *#541*.)

- At 5:45 PDT, 7:45 a.m. CDT: Silk placed order *#907*, to sell three June Euro FX futures at 11460. The fill on order *#907* was reported at 9:01 a.m. PDT, 11:01 a.m. CDT.

- At 9:53 a.m. PDT, 11:53 a.m. CDT: Silk placed order *#1227*, to buy three June Euro FX futures at 11413. Order *#1227* was filled at 9:54 a.m. PDT, 11:54 a.m. CDT. However, due to hectic trading conditions in the pit, the fill report would be delayed until 10:28:08 a.m. PDT, 12:28:08 p.m. CDT. (Silk mistakenly assumed that order *#1227* would offset order *#907*.)

[5] Silk placed all orders via ANCO's on-line trading platform, unless otherwise noted.
[6] The Euro future trades at $12.50 per tick.

- At 9:56 a.m. PDT, 11:56 a.m. CDT: Silk placed order *#1230*, to cancel-replace order *#1227* with a market order. Order *#1230* was rejected by the floor broker because order *#1227* was too-late-to-cancel. However, as late as 10:28 a.m. PDT, 12:28 p.m. CDT, the online system reported order *#1230* as a working order.

- At 10:27 a.m. PDT, 12:27 p.m. CDT: Silk placed order *#1269*, to sell five June Euro FX futures at the market. Order *#1269* was filled at 11378. The fill on order *#1269* was reported at 10:28:37 a.m. PDT, 12:28:37 p.m. CDT. (Silk mistakenly assumed that order *#1269* would be the open order after the close. In actuality, order *#1269* would offset orders *#893* and #1227, leaving orders *#541* and *#907* as the open orders at the close of pit trading.)

6. By 10:27 a.m. PDT, 12:27 p.m. CDT, the ANTC on-line system had reported the fills on orders *#893*, *#907*, *#1227,* and *#1229.* Throughout the day, the ANTC online system would report order *#541* as an open order.

7. Thirty-five minutes before the close of pit trading on May 15 -- at 11:25 a.m. PDT, 1:25 p.m. CDT -- Silk spoke to Estrada for about a minute. Silk told Estrada that he "had a couple of problems:" *i.e.*, that he believed that he had placed order *#1230* in time to cancel order *#1227*, but that the on-line system reported *#1227* as filled, and reported order *#1230* as still working; and that the fill on *#1227* did not appear to match the prevailing market price.[7] Estrada could not explain what had happened, but guessed that there had been a delay in key-punching the trade, because "they [*i.e.*, the traders in the pit] went a little bit crazy." Estrada advised Silk to wait a bit and to review the fill price to make sure it was "reasonable."

[7] The time and sales report that ANCO would forward to Silk several days later establishes that order *#1230* had properly been rejected, because order *#1227* had been filled at the prevailing price almost immediately, and well before Silk had placed order *#1230*. The delay in the fill report appears to have been a product of the hectic trading conditions.

Silk then asked for Estrada's fax number. Estrada gave Silk a number for a fax machine in ANCO's front office. Estrada would leave work at his usual time, around 1:30 p.m. Pacific Time.

8. Pit trading in the Euro closed at 12:00 noon PDT, 2:00 p.m. CDT, on May 15. That day, the June Euro FX future settled at 11388.

Overnight, ANTC conducted its routine end-of-day reconciliation. ANTC followed standard *last-in, first-out* protocols,[8] by treating orders *#893, #1227,* and *#1269,* as day orders, and offsetting orders *#893* (buy two June Euro FX futures, at 11440) and *#1227* (buy three June Euros, at 11413) with order *#1269* (sell five June Euros, at 11378). The purchase and sale of five Euros realized a loss of $2,862.50, which reduced the account cash balance to $3,045.59.

After the purchase and sale, the open five-contract short position consisted of orders *#541* (sell two June Euros, at 11494) and *#907* (sell three June Euros, at 11460). At the close, these five short June Euros had a positive liquidation value of $5,350.

Since, the account value was $8,395.59, and the margin for the five Euros was set at $11,475, the account had a margin deficit of $3,079.41.

9. A series of misconceptions flowed from Silk's mistaken assumption that day trades were offset on a *first-in, first-out* basis. First, Silk erroneously deduced that order *#893* had offset order *#541,* and that order *#1227* had offset order *#907,* for $3,113.50 in profits, rather than $2,862.50 in losses. Second, Silk erroneously deduced that order *#1269* was open, with a positive liquidation value of around $750. As a result, when he noticed that ANCO's on-line status reports did not comport with his own version of

[8] *See* CFTC rule 1.46(c).

trading results, Silk concluded that it had to be the on-line reports that were erroneous and unreliable.

10. Around 11:00 p.m. Pacific Time on May 15, Silk faxed to Estrada a memo titled "Error in Execution of Market Order." In his fax, Silk complained that order *#1227* should have been cancelled, and that order *#1230* should have been filled at 11420. Silk calculated that the difference between the reported fill and the fill that he should have received was $1,125. Silk revealed that he assumed that order *#541* had been offset by order *#893*. Silk also indicated that he knew that he was short five June Euros, then currently trading at 11399 on the Globex.[9]

A short while later, Silk sent a second fax to Estrada titled "An Explanation Please," in which he complained about what he perceived to be various inaccurate on-line reports, including the fact that the on-line system showed order *#541* as still open.

Silk's two faxes were received in ANCO's front office, which would be empty until 6:30 a.m. PDT the next morning – an hour after the open of pit trading in Chicago. ANCO's front office employees would not deliver the faxes to Estrada until later that morning, by which time he was pre-occupied with handling orders in the midst of another hectic day.

11. On Friday, May 16, about half an hour before the open, around 5:00 a.m. PDT, 7:00 a.m. CDT, Silk checked his account. The ANCO online system reported that orders *#541* and *#907* were open, and that the June Euro was trading at 11472. At this price, the five Euro's were barely above break-even.

[9] At this price, even under Silk's best-case scenario (*i.e.*, *#541* offset by *#893*, *#907* offset by *#1230*, and *#1269* open at the close), the account would have been under-margined, albeit to a lesser degree.

Although Silk had been "anxious" to hear from Estrada, he decided to allow Estrada until 10:00 a.m. Pacific Time to call. Estrada did call Silk, but not until 9:50 a.m. PDT, 11:50 a.m. CDT, by which time, the Euro had jumped to 11525. Estrada and Silk spoke for a little under a minute:

Silk:	Did you get my faxes? I expected to hear from you. What's going on?
Estrada:	I haven't really had a chance this morning to go over them.
Silk:	The market's crazy, and my account's crazy, and I'm not doing anything. I appreciate you going over what you can.
Estrada:	I will.
Silk:	As I am looking at the trades, the initial maintenance margin requirements are five dollars, and I know this is wrong.
Estrada:	Hold on a sec. Your initial requirement is $9,459. But you know, because it's Globex versus IMM . . .
Silk:	Oh, is that what it is?
Estrada:	Yeah. It's just some computer thing they have to do.
Silk:	Well. Everything is screwed up. I'm not doing anything today, until I hear from you. I just don't know what is going on anymore.
Estrada:	Alright. But there is a margin call on your account. You know.
Silk:	No. I don't know.
Estrada:	There is. There is. I'll look at your fax. And we'll try to go from there. Okay?
Silk:	I'll wait for your call.
Estrada:	All right.
Silk:	Thank you.

Silk then waited all day on Friday May 16, and then all evening and all weekend, for Estrada to call.

Meanwhile, the June Euro continued to climb: at 11:00 a.m. PDT, trading at 11543; at 11:30 a.m. PDT, trading at 11545; and at 11:45 a.m. PDT, trading at 11558. At 12 noon PDT, pit trading closed, with the June Euro settling at 11565. At this point, the June Euros had a negative liquidation value of $5,712.50, resulting in a margin deficit of $14,142.

12. Over the weekend, the margin deficit worsened as the June Euro continued to climb in trading on Globex. About half an hour after the open on Monday, May 19, ANCO liquidated the five June Euros, at 11650, for a loss of $11,025.[10]

At 9:08 a.m. PDT, Estrada advised Silk about the liquidation. Estrada told Silk that he had finally reviewed the faxes. Estrada explained why order #1227 had been too-late-to-cancel, and also explained the *last-in, first-out* rule for day trades.

Conclusions

As a discount broker, ANCO's principal fiduciary duty to Mobilefax was to exercise diligence and due care in the handling and reporting of Mobilefax's orders. Consistent with this level of duty, ANCO was not obligated to disclose that day trades are offset on a last-in, first out basis, especially where Mobilefax had abruptly shifted to a day-trading strategy without seeking advance advice. Since ANCO diligently executed Mobilefax's orders and accurately reported the status of orders, ANCO cannot be held responsible for the misconceptions and losses that flowed from Brian Silk's ignorance of

[10] The June Euro continued to climb after the liquidation. Thus, if liquidation had been further delayed, Mobilefax's losses would have been greater.

the last-in, first out convention. However, ANCO is responsible for any losses that flowed from Henry Estrada's promise to investigate Silk's assertion that ANCO had mishandled orders and misreported the status of the account.

Previously, when Estrada had notified Silk of a margin call, he had given Silk an opportunity to deposit additional funds or to liquidate the under-margined position. However, in this instance, Estrada induced Silk to defer that decision by promising that he first would review Silk's faxes in which Silk explained his concerns that ANCO had not properly handled and reported his orders. By making this promise, Estrada assumed on behalf of ANCO a special duty to Mobilefax. *Avis v. Shearson Hayden Stone, Incorporated, et al.*, Comm. Fut. L. Rep. (CCH) ¶21,739, at page 25,831, n. 8 (CFTC 1982):

> "[W]hen a customer makes it known that he intends to rely on the commodity professional to perform special instructions given by the customer, the commodity professional, as part of his fiduciary obligation, must, in order to disavow that duty, either disclose to the customer in unequivocal language that he cannot or will not perform the additional duty requested of him or that he will only do so conditionally or without warranty as to result. Where . . . the commodity professional remains mute in the face of those instructions, he must be understood to have agreed to carry out the customer's request with a professional standard of care. Traditional principles of the law of agency would require no less."

Here, where Mobilefax's position was quickly deteriorating, Estrada was obligated to promptly research Silk's complaint and promptly confirm that ANCO's on-line system was accurately reporting the status of the Euro trades and that the account was in fact seriously under-margined. The time that passed, without explanation, from when Estrada promised to confirm the accuracy of the margin call – mid-day on Friday, May 16 – to when he reported back to Silk – mid-morning on Monday, May 19 – could not reasonably be called consistent with a prompt or diligent effort. Thus, Estrada's unexplained failure to perform a prompt review of the handling and reporting of the Euro trades constituted a reckless violation of his fiduciary duty, and ANCO is liable for the losses that began to accrue from the time that Estrada agreed to undertake the special task. Concomitantly, Silk was not free to delay action while his losses steadily mounted, particularly when he had reason to believe that his account would be under-margined under his own best-case scenario. In these circumstances, the latest that Silk could reasonably wait before taking necessary action to limit his losses was fifteen minutes before the close of pit trading. Thus, the proper measure of damages is $3,962.50, based on the difference in the market price, from the time that Estrada promised to perform the special duty, to fifteen minutes before the close.

ORDER

Mobilfax Corporation has established that an agent of ANCO Discount Futures violated Section 4b of the Commodity Exchange Act, that this violation proximately caused $3,962.50 in damages, and that ANCO Discount Futures is liable for the violations of its agent pursuant to Section 2(a)(1)(B) of the Act. Accordingly, ANCO Discount Futures is ordered to pay to Mobilefax Corporation reparations of $3,962.50, plus interest on that amount at 4.96 % compounded annually from May 16, 2003, to the date of payment, plus $125 in costs for the filing fee.

Dated December 29, 2006.

Philip V. McGuire,
Judgment Officer