UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

In the Matter of

William K. Kerstein,

Respondent.

CFTC Docket No: 12-29

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

I.

The Commodity Futures Trading Commission ("Commission") has reason to believe that from May 2009 to at least September 2010 (the "Relevant Period"), Respondent William K. Kerstein ("Kerstein" or "Respondent") violated Section 4c(a) of the Commodity Exchange Act (the Act'), to be codified at 7 U.S.C. §6c(a) and Commission Regulation 1.38, 17 C.F.R. § 1.38 (2011). Therefore, the Commission deems it appropriate and in the public interest that public administrative proceedings be, and hereby are, instituted to determine whether Kerstein engaged in the violations set forth herein, and to determine whether an order shall be issued imposing remedial sanctions.

II.

In anticipation of the institution of an administrative proceeding, Respondent has submitted an Offer of Settlement ("Offer"), which the Commission has determined to accept. Without admitting or denying the findings or conclusions herein, Respondent consents to the entry of this Order Instituting Proceedings Pursuant to Sections 6(c) and 6(d) of the Commodity Exchange Act, as Amended, Making Findings and Imposing Remedial Sanctions ("Order") and acknowledge service of this Order.[1]

[1] Respondent consents to the entry of this Order and to the use of these findings in this proceeding and in any other proceeding brought by the Commission or to which the Commission is a party; provided, however, that Respondent does not consent to the use of the Offer, or the findings or conclusions in this Order consented to in the Offer, as the sole basis for any other proceeding brought by the Commission, other than a proceeding in bankruptcy or to enforce the terms of this Order. Nor does Respondent consent to the use of the Offer or this Order, or the findings or conclusions in this Order consented to in the Offer, by any other party in any other proceeding.

III.

The Commission finds the following:

A. SUMMARY

Between May 2009 and September 2010, Kerstein, a floor broker in the trading pit of the Chicago Mercantile Exchange Group's ("CME") Standard & Poor's 500 Stock Price Index futures contract ("S&P 500"), accommodated another broker in trading opposite that broker's customers' orders in violation of Section 4c(a) of the Act. Kerstein engaged in this conduct on seven dates in 2009 and 2010.

On each of these referenced dates, Kerstein took the opposite side of the same broker's customer's order. Immediately afterward, Kerstein traded a second time in the other direction with the same broker on behalf of the broker's personal account. Both the buy and sell trades in each of these "trade sequences" were executed at the same trade price within seconds of one another.

Kerstein thus engaged in accommodation trades in violation of Section 4c(a) of the Act and noncompetitive trades in violation of Commission Regulation 1.38(a).

B. RESPONDENT

William Kerstein is a registered floor broker in the CME's S&P 500 trading pit. He has been registered since 1990.

C. FACTS

On seven occasions between May 2009 and September 2010, Kerstein accommodated another broker in the S&P 500 pit who indirectly traded opposite his customers' orders. The broker then offset these positions in the S&P 500 pit or on the CME's electronic trading platform Globex ("Globex"). Kerstein engaged in noncompetitive round-turn trades, for his personal account, with the broker and thereby accommodated the broker in taking the opposite side of his customer orders into his own account. This conduct by the broker is also known as "indirect bucketing."[2]

The indirect buckets exhibited the following trading pattern or configuration: Kerstein noncompetitively purchased and sold the same month of the S&P 500 contract, at the same price at or about the same time, opposite the broker. One side of the broker's trades was for a customer and the other side was for the broker's own account. As the accommodating trader, both the purchase and sales in each trade sequence were for Kerstein's own account. By

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[2] "Bucketing" is defined by the Commission as "directly or indirectly taking the opposite side of a customer's order into a broker's own account or into an account in which a broker has an interest, without open and competitive execution of the order on an exchange." The CFTC Glossary (http://www.cftc.gov/ConsumerProtection/EducationCenter/CFTCGlossary/ glossary_b 2012).

engaging in this conduct, Kerstein accommodated the broker in establishing a position for his own account, opposite his customer, without competitive execution.

On seven occasions, Kerstein knowingly engaged in trades opposite the broker which fit the indirect bucketing pattern. Specifically, on May 29 and July 2, 2009 as well as February 23, March 24, March 26, September 28, and September 30, 2010, Kerstein's conduct accommodated the broker in indirectly trading opposite his customers' orders. On each occasion, the broker filled a customer order with Kerstein and took a portion of the order back for the broker's personal account.

The May 29, 2009 trades are illustrative of how Kerstein's trading accommodated the broker in indirectly taking the opposite side of his customer's orders. At or about 2:56:06 that day, the broker received a customer order to buy S&P 500 contracts. At 3:00:44 PM, the broker executed a part of the customer order by buying fifty S&P 500 contracts from Kerstein at a price of 924.00. About a second later, at 3:00:45, the broker sold ten contracts back to Kerstein for the broker's personal account at the same price of 924.00. The broker ultimately earned a profit of $6,400, because the broker had earlier, bought the equivalent number of contracts on Globex at prices ranging from 921.25 to 921.50.

The dates, type of trade, number of contracts, time brackets, and prices for these seven occasions on which Kerstein accommodated the broker in indirectly taking the opposite side of his customers' orders, are detailed in the following chart, listing the trades from the broker's perspective:

Date	Trade Type	Amount (Contracts)	Time Bracket	Price
05/29/09	Buy (customer)	50	3:00:00/3:15:00	924.00
05/29/09	Sell (personal)	10	3:00:00/3:15:00	924.00
07/02/09	Sell (customer)	39	3:00:00/3:15:00	893.20
07/02/09	Buy (personal)	10	3:00:00/3:15:00	893.20
02/23/10	Buy (customer)	100	3:00:00/3:15:00	1094.30
02/23/10	Sell (personal)	20	3:00:00/3:15:00	1094.30
03/24/10	Sell (customer)	60	3:00:00/3:15:00	1163.50
03/24/10	Buy (personal)	10	3:00:00/3:15:00	1163.50
03/26/10	Sell (customer)	24	9:00:00/9:15:00	1165.30
03/26/10	Buy (personal)	4	9:00:00/9:15:00	1165.30
09/28/10	Sell (customer)	40	3:00:00/3:15:00	1141.80
09/28/10	Buy (personal)	10	3:00:00/3:15:00	1141.80
09/30/10	Buy (customer)	30	8:30:00/8:45:00	1147.00
09/30/10	Sell (personal)	10	8:30:00/8:45:00	1147.00

IV.

LEGAL DISCUSSION

Section 4b(a) of the Act prohibits bucketing of customer orders. A floor broker "buckets" a customer's order, when that broker trades "opposite the order for the broker's own account or for an account in which the broker has an interest." *Reddy v. CFTC*, 191 F.3d 109, 115 (2nd Cir. 1999). "'Indirect bucketing' occurs when a broker, aided by an accommodating trader, trades opposite his own customer while appearing to trade opposite the accommodator." *Id. Accord In re Gorski*, [2003-2004 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 29,726 at 56,068 n.15 (CFTC March 24, 2004) ("In an indirect bucket, a floor broker trades against his customer in a non-competitive transaction. The opposite trader, often called the accommodator, assists the floor broker by making it appear that the customer traded with him, rather than with the floor broker."). The practice is illegal because the customer's order is not executed competitively and the futures market's purpose of aiding price discovery is frustrated. In addition, "because the transaction is arranged in a manner that permits the opposite trader to buy and sell the same month of the same futures contract at the same or similar price, the accommodating trader is able to negate market risk while breaking even or earning a profit." *In re Gorski*, [2003-2004 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 29,726 at 56,068 n.15.

Section 4c(a) of the Act makes it unlawful for any person to enter into the execution of a transaction "involving the purchase or sale of any commodity for future delivery" that "is, is of the character of, or is commonly known to the trade as ... a[n] accommodation trade." Accommodation trading involves ostensibly independent trades that were actually envisioned as paired at the time of initiation. The paired trades are designed to offset each other with little or no change in the trader's financial position. When traders assist a broker in achieving an unlawful purpose such as bucketing a customer's order, they are understood to be undertaking an accommodation trade with the broker. In these circumstances, market risk is negated because, by pairing the ostensibly independent trades at the time of initiation, the trader can predictably reduce risk to an inconsequential level. *In re Fisher*, [2003-2004 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 29,725 (CFTC Mar. 24, 2004). By engaging in noncompetitive trades with a broker to facilitate the indirect bucketing of customer orders, Kerstein engaged in accommodation trading in violation of Section 4c(a).

Regulation 1.38 requires that "[a]ll purchases and sales of any commodity for future delivery, and of any commodity option, on or subject to the rules of a contract market shall be executed openly and competitively by open outcry or posting of bids and offers or by other equally open and competitive methods, in the trading pit or ring or similar place provided by the contract market, during the regular hours prescribed for trading in such commodity or commodity option." "The purpose of this requirement is to insure that all trades are executed at competitive prices and that all trades are directed into a centralized marketplace to participate in the competitive determination of the price of the futures contracts." S. REP. No. 93-1131, 93d Cong., 2d Sess. 16-17 (1974). Trades can be noncompetitive even though they were executed in the pit. *In re Buckwalter*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,994 at 37,683 (CFTC Jan. 25, 1991). By engaging in trades intended to accommodate the indirect bucketing of customer orders, Kerstein engaged in noncompetitive trading in violation of Regulation 1.38.

"The Division must prove intent to establish a violation of 4b or 4c of the Act." *Reddy*, 191 F.3d at 119. Regulation 1.38(a) also incorporates a scienter requirement. *In re Gilchrist*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,993 at 37,651 (CFTC Jan. 25, 1991). The relevant state of mind for a violation under Section 4c of the Act is knowing participation in transactions structured in a manner to negate price competition or market risk. *Id.* at 37,653 n.23. "[I]nferences arising from circumstantial evidence" are sufficient to prove that the proposed respondents acted with scienter. *See In re Buckwalter*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,995 at 37,686.

V.

FINDINGS OF VIOLATIONS

Based on the foregoing, the Commission finds that, during the Relevant Period, Kerstein violated Section 4c(a) of the Act and Regulation 1.38.

VI.

OFFER OF SETTLEMENT

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

A. Acknowledges receipt of service of this Order;

B. Admits the jurisdiction of the Commission with respect to all the matters set forth in this Order and for any action or proceeding brought or authorized by the Commission based on violation of or enforcement of this Order;

C. Waives:

1. the filing and service of a complaint and notice of hearing;
2. a hearing;
3. all post-hearing procedures;
4. judicial review by any court;
5. any and all objections to the participation by any member of the Commission's staff in the Commission's consideration of the Offer;
6. any and all claims that he may possess under the Equal Access to Justice Act, 5 U.S.C. § 504 (2006) and 28 U.S.C. § 2412 (2006), and/or the rules promulgated by the Commission in conformity therewith, Part 148 of the Commission's Regulations, 17 C.F.R. §§ 148.1 et seq. (2011), relating to, or arising from, this proceeding;

7. any and all claims that he may possess under the Small Business Regulatory Enforcement Fairness Act of 1996, Pub. L. No. 104-121, §§ 201-253, 110 Stat. 847, 857-68 (1996), as amended by Pub. L. No. 110-28, § 8302, 121 Stat. 112, 204-205 (2007), relating to, or arising from, this proceeding; and

8. any claims of Double Jeopardy based upon the institution of this proceeding or the entry in this proceeding of any order imposing a civil monetary penalty or any other relief.

D. Stipulates that the record basis on which this Order is entered shall consist solely of the findings contained in this Order to which Respondent has consented in the Offer; and

E. Consents, solely on the basis of the Offer, to the Commission's entry of this Order, that:

1. makes findings by the Commission that Kerstein violated Section 4c(a) of the Act and Regulation 1.38;

2. orders Kerstein to cease and desist from violating Section 4c(a) of the Act and Regulation 1.38;

3. orders Kerstein to pay a civil monetary penalty in the amount of fifty thousand dollars ($50,000), plus post-judgment interest, within ten (10) days of the date of the entry of this Order;

4. orders that Kerstein's registration with the Commission as a floor broker shall be suspended for a period of one (1) month, commencing from the date this Order is entered, during which time all registered entities (as that term is defined in Section 1a of the Act, as amended, 7 U.S.C. § 1a), shall refuse Kerstein floor trading privileges; and

5. orders Kerstein to comply with the conditions and undertakings consented to in the Offer and as set forth in Paragraph D of Part VII of this Order.

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

VII.

ORDER

Accordingly, IT IS HEREBY ORDERED THAT:

A. Kerstein shall cease and desist from violating Section 4c(a) of the Act, to be codified at 7 U.S.C. § 6c(a) and Regulation 1.38, 17 C.F.R. § 1.38 (2011).

B. Kerstein shall pay a civil monetary penalty in the amount of fifty thousand dollars ($50,000), plus post-judgment interest, within ten (10) days of the date of the entry of this Order (the "CMP Obligation"). If the CMP Obligation is not paid in full within ten (10) days of the date of entry of this Order, then post-judgment interest shall accrue beginning on the date of entry of this Order and shall be determined by using the Treasury Bill rate prevailing on the date of entry of the Order pursuant to 28 U.S.C. § 1961 (2006). Kerstein shall pay his civil monetary penalty by electronic funds transfer, U.S. postal money order, certified check, bank cashier's check, or bank money order. If payment is to be made other than by electronic funds transfer, then the payment shall be made payable to the Commodity Futures Trading Commission and sent to the address below:

Commodity Futures Trading Commission
Division of Enforcement
ATTN: Accounts Receivables – AMZ 340
E-mail Box: 9-AMC-AMZ-AR-CFTC
DOT/FAA/MMAC
6500 S. MacArthur Blvd.
Oklahoma City, OK 73169
Telephone: (405) 954-5644

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

C. Kerstein's registration with the Commission as a floor broker is suspended for a period of one (1) month, commencing from the date this Order is entered, during which time all registered entities (as that term is defined in Section 1a of the Act, as amended, 7 U.S.C. § 1a), shall refuse Kerstein floor trading privileges.

D. Kerstein and his successors and assigns shall comply with the following undertakings set forth in his Offer:

1. During the one-month period that Kerstein's registration is suspended, Kerstein shall not apply for registration or claim exemption from registration with the Commission in any capacity, nor engage in any activity requiring such registration or exemption with the Commission except as provided for in Regulation 4.14(a)(9), 17 C.F.R. § 4.14(a)(9) (2011);

2. Public Statements: Kerstein agrees that neither he nor any of his agents or employees under his authority or control shall take any action or make any public statement denying, directly or indirectly, any findings or conclusions in this Order or creating, or tending to create, the impression that this Order is without a factual basis; provided, however, that nothing in this provision shall affect Kerstein's:

(i) testimonial obligations; or (ii) right to take legal positions in other proceedings to which the Commission is not a party. Kerstein shall undertake all steps necessary to ensure that all of his agents and/or employees under his authority or control understand and comply with this agreement.

E. Partial Satisfaction: Kerstein understands and agrees that any acceptance by the Commission of partial payment of his CMP Obligation shall not be deemed a waiver of his obligation to make further payments pursuant to this Order, or a waiver of the Commission's right to seek to compel payment of any remaining balance.

F. Change of Address/Phone: Until such time as Kerstein satisfies in full his CMP Obligation as set forth in this Order, he shall provide written notice to the Commission by certified mail of any change to his telephone number and mailing address within ten (10) calendar days of the change.

Kerstein acknowledges that failure to comply with the Order shall constitute a violation of the Order and may subject him to administrative or injunctive proceedings, pursuant to the Act.

The provisions of this Order shall be effective on this date.

Dated: July 26, 2012

By the Commission.

David A. Stawick
Secretary of the Commission
Commodity Futures Trading Commission