

USDC SDNY
DOCUMENT
ELECTRONICALLY FILED
DOC #:
DATE FILED: 5/22/12

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

U.S. Commodity Futures Trading
Commission,

Plaintiff,

v.

KENT R.E. WHITNEY,

Defendant.

CASE NO. 10-CV-9238
ECF CASE

**PROPOSED CONSENT ORDER FOR PERMANENT INJUNCTION, CIVIL
MONETARY PENALTY AND OTHER EQUITABLE RELIEF
AGAINST DEFENDANT KENT R.E. WHITNEY**

I. INTRODUCTION

On December 10, 2010, Plaintiff Commodity Futures Trading Commission ("Commission" or "CFTC") filed a Complaint against Defendant Kent R.E. Whitney ("Whitney" or "Defendant") seeking injunctive and other equitable relief, as well as the imposition of civil penalties, for violations of Section 4c(b) of the Commodity Exchange Act ("the Act"), 7 U.S.C. § 6c(b), Section 9(a)(4) of the Act, 7 U.S.C. § 13(a)(4), as amended, and Commission Regulation ("Regulation") 33.10, 17 C.F.R. § 33.10 (2010). The Court entered a Consent Order of Preliminary Injunction and Other Equitable Relief against Whitney on January 4, 2011.

In summary, at various times from May 2008 through April 2010, Defendant engaged in a fraudulent scheme to avoid substantial margin calls when placing orders for commodity options traded on the New York Mercantile Exchange ("NYMEX") and the Chicago Mercantile Exchange ("CME"). Whitney committed this margin call avoidance scheme in connection with

out-of-the-money options by knowingly making false and misleading statements to clearing firms, floor brokers, and other persons.

Additionally, Whitney made false and misleading statements to, and willfully deceived, a staff representative of CME, a registered entity.

II. CONSENTS AND AGREEMENTS

To effect settlement of all charges alleged in the Complaint against Defendant without a trial on the merits or any further judicial proceedings, Defendant:

1. Consents to the entry of this Consent Order for Permanent Injunction, Civil Monetary Penalty and Other Equitable Relief against Defendant Kent R.E. Whitney ("Consent Order");
2. Affirms that he has read and agreed to this Consent Order voluntarily, and that no promise, other than as specifically contained herein, or threat, has been made by the Commission or any member, officer, agent or representative thereof, or by any other person, to induce consent to this Consent Order;
3. Acknowledges proper service upon him of the Summons and Complaint;
4. Admits the jurisdiction of this Court over him and the subject matter of this action pursuant to Section 6c of the Commodity Exchange Act, to be codified at 7 U.S.C. § 13a-1;
5. Admits the jurisdiction of the Commission over the conduct and transactions at issue in this action pursuant to the Act, 7 U.S.C. §§ 1, *et seq.*;
6. Admits that venue properly lies with this Court pursuant to Section 6c(e) of the Act, as amended, 7 U.S.C. § 13a-1(e);
7. Waives:

a) 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 Regulations, 17 C.F.R. §§ 148.1 et seq. (2011), relating to, or arising from, this action;

b) any and all claims that he may possess under the Small Business Regulatory Enforcement Fairness Act of 1996, Pub. L. 104-121, §§ 201- 253, 110 Stat. 847, 857-868 (1996), as amended by Pub. L. No. 110-28, § 8302, 121 Stat. 112, 204-205 (2007), relating to, or arising from, this action;

c) any claim of Double Jeopardy based upon the institution of this action or the entry in this action of any order imposing a civil monetary penalty or any other relief, including this Consent Order; and

d) any and all rights of appeal from this action;

8. Consents to the continued jurisdiction of this Court over him for the purpose of implementing and enforcing the terms and conditions of this Consent Order and for any other purpose relevant to this action, even if Defendant now or in the future resides outside the jurisdiction of this Court;

9. Agrees that he will not oppose enforcement of this Consent Order by alleging that it fails to comply with Rule 65(d) of the Federal Rules of Civil Procedure and waives any objection based thereon;

10. 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 allegation in the Complaint or the Findings of Fact or Conclusions of Law in this Consent Order, or creating or tending to create the impression that the Complaint and/or this Consent Order is

without a factual basis; provided, however, that nothing in this provision shall affect his: (a) testimonial obligations, or (b) right to take legal positions in other proceedings to which the Commission is not a party. Defendant 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;

11. By consenting to the entry of this Consent Order, Defendant neither admits nor denies the allegations of the Complaint or the Findings of Fact and Conclusions of Law in this Consent Order, except as to jurisdiction and venue, which he admits. Further, Defendant agrees and intends that the allegations contained in the Complaint and all of the Findings of Fact and Conclusions of Law contained in this Consent Order shall be taken as true and correct and be given preclusive effect, without further proof, in the course of: (a) any current or subsequent bankruptcy proceeding filed by, on behalf of, or against Whitney; (b) any proceeding pursuant to Section 8a of the Act, as amended, 7 U.S.C. § 12a, and/or Part 3 of the Regulations, 17 C.F.R. §§ 3.1 *et seq.* (2011); and/or (c) any proceeding to enforce the terms of this Consent Order;

12. Agrees to provide immediate notice to this Court and the Commission by certified mail, in the manner required by Paragraph 33 of Part VI of this Consent Order, of any bankruptcy proceeding filed by, on behalf of, or against him whether inside or outside the United States; and

13. Agrees that no provision of this Consent Order shall in any way limit or impair the ability of any other person or entity to seek any legal or equitable remedy against Whitney in any other proceeding.

III. FINDINGS AND CONCLUSIONS

The Court, being fully advised in the premises, finds that there is good cause for the entry of this Consent Order and that there is no just reason for delay. The Court therefore directs the entry of the following Findings of Facts, Conclusions of Law, permanent injunction, and equitable relief pursuant to Section 6c of the Act, as amended, 7 U.S.C. § 13a-1, as set forth herein.

THE PARTIES AGREE AND THE COURT HEREBY FINDS:

A. Findings of Fact

The Parties to This Consent Order

14. Plaintiff Commodity Futures Trading Commission is an independent federal regulatory agency that is charged by Congress with administering and enforcing the Act, as amended, 7 U.S.C. §§ 1 *et seq.*, and the Regulations promulgated thereunder, 17 C.F.R. §§ 1 *et seq.* (2011).

15. Defendant Kent Ralph Emerson Whitney is a resident of Chicago, Illinois and has been registered with the Commission as a floor broker since August 29, 2003. Whitney is also a principal and Associated Person of Lone Star Trading Group, Inc., a registered Introducing Broker with its place of business located in Deerfield Beach, Florida.

The Facts

16. NYMEX and CME are designated contract markets that are located in New York, New York and Chicago, Illinois, respectively. NYMEX and CME are both part of CME Group Inc. ("CME Group").

17. On several occasions between May 2008 and April 2010, Whitney engaged in a fraudulent scheme to avoid margin calls on NYMEX and CME options positions. As part of the

scheme, Whitney placed orders to sell a large volume of front month out-of-the-money options to the NYMEX and CME floors one or two business days before the expiration of the front month options.¹ At the time he placed these options orders, Whitney knowingly provided clearing firms invalid account numbers for the trade allocation. In doing so, Whitney implicitly represented that the accounts were open and held sufficient margin to cover the trades and/or deceptively failed to disclose that the accounts were, in fact, closed and thus held no funds for margin.

18. Because the account numbers Whitney provided were invalid or closed, the clearing firms that received the initial allocations rejected the trades and returned the trades to the clearing firms of the executing floor brokers.

19. The next business day, Whitney would provide valid account numbers to clear the trades.

20. By this process, Whitney shifted the overnight margin risk to the clearing firms of the executing brokers, thus avoiding the posting of margin.

21. As the next business day was usually the expiration of the front month options contract, when the clearing firm Whitney used did not require margin calls, neither Whitney, nor the accounts he used, received any margin calls. The accounts that Whitney traded then collected the premiums on these out-of-the-money options that usually expired worthless.²

22. Whitney repeated this margin avoidance scheme on eight different occasions, as described more fully in the Complaint filed on December 10, 2010 and listed in the chart below:

¹The front month is the spot or nearby delivery month, the nearest traded contract month. An out-of-the-money option is an option with no intrinsic value.

²A premium is the payment the option buyer makes to the option writer or seller for granting an option contract.

DATE	OPTION CONTRACT	CONTRACTS SOLD	MARGIN AVOIDED	PREMIUM EARNED	ADDITIONAL INFORMATION	VIOLATION OF THE ACT
5/14/08-5/15/08	NYMEX Crude Oil; June '08	2,820	\$10.3 million	\$37,900	Options expired worthless, <i>i.e.</i> , with no value; Whitney-controlled accounts collected the premium	4c(b); Whitney knowingly provided clearing firms invalid account numbers for the trade allocation.
6/13/08	NYMEX Crude Oil; July '08	3,205	\$2.6 million	\$59,000	Options expired worthless, <i>i.e.</i> , with no value; Whitney-controlled accounts collected the premium	4c(b); Whitney knowingly provided clearing firms invalid account numbers for the trade allocation.
6/16/08-6/17/08	NYMEX Crude Oil; July '08	4,500	\$5 million	\$26,000	Options expired worthless, <i>i.e.</i> , with no value; Whitney-controlled accounts collected the premium	4c(b); Whitney knowingly provided clearing firms invalid account numbers for the trade allocation.
7/16/08-7/17/08	NYMEX Crude Oil; August '08	3,200	\$13.7 million	\$32,000	Options expired worthless, <i>i.e.</i> , with no value; Whitney-controlled accounts collected the premium	4c(b); Whitney knowingly provided clearing firms invalid account numbers for the trade allocation.

DATE	OPTION CONTRACT	CONTRACTS SOLD	MARGIN AVOIDED	PREMIUM EARNED	ADDITIONAL INFORMATION	VIOLATION OF THE ACT
11/20/09	CME S&P 500; November '09	450	N/A	N/A	Order rejected prior to execution because Whitney used invalid FCM account numbers in attempting to place trades	4c(b); Whitney knowingly provided clearing firms invalid account numbers for the trade allocation.
1/14/10-1/15/10	NYMEX Crude Oil; February '10	1,873	\$18 million	N/A	Trades defaulted to executing broker's account, and therefore Whitney never collected premium ³	9a(4); Whitney made false and misleading statements to, and willfully deceived, staff of CME, a registered entity.
3/26/10	NYMEX Natural Gas; April '10	N/A	N/A	N/A	Trades never executed after phone clerk identified Whitney's voice, claiming to be Whitney's friend, placing orders	4c(b); Whitney knowingly provided clearing firms invalid account numbers for the trade allocation.
4/16/10	CME S&P 500; April '10	2,500	\$47 million	N/A	Trades liquidated by FCM after learning that Whitney impersonated Whitney's friend to place orders	4c(b); Whitney knowingly provided clearing firms invalid account numbers for the trade allocation.

³ On January 28, 2010, the Chief Regulatory Officer of the CME Group filed a Summary Access Denial action against Whitney prohibiting him from trading, either for himself or for others, on any CME Group markets, including CME, NYMEX, CBOT, and COMEX for 60 days. This trading prohibition was later extended to May 29, 2010. Later, on May 24, 2010, the Business Conduct Committee of the CME Group issued an Emergency Action against Whitney prohibiting him from trading, either for himself or for others, on any CME Group markets, including CME, NYMEX, CBOT, and COMEX, for six months ending November 24, 2010. Thus, the Whitney trades for March 26, 2010 and April 16, 2010 were strictly prohibited by virtue of the CME Group's trading ban. See chart above.

23. Additionally, a CME staff representative ("CME Staffer") questioned Whitney about certain options trades Whitney had attempted to place in Whitney's friend's account on January 14, 2010. The CME Staffer specifically asked Whitney about the initial trade allocations that had been rejected by the clearing firms. Whitney lied and falsely represented to the CME Staffer that Whitney was unaware of any rejected trade allocations that Whitney had made on January 14, 2010.

B. Conclusions of Law

Jurisdiction and Venue

24. This Court has jurisdiction over this action pursuant to Section 6c of the Act, as amended, 7 U.S.C. § 13a-1, which provides that whenever it shall appear to the Commission that any person has engaged, is engaging, or is about to engage in any act or practice constituting a violation of any provision of the Act or any rule, regulation, or order promulgated thereunder, the Commission may bring an action in the proper district court of the United States against such person to enjoin such act or practice, or to enforce compliance with the Act, or any rule, regulation or order thereunder.

25. Venue properly lies with this Court pursuant to Section 6c(e) of the Act, as amended, 7 U.S.C. § 13a-1(e), because the acts and practices in violation of the Act occurred within this District.

Fraudulent Misrepresentations

26. By the conduct described above in paragraphs 16-23, Defendant engaged in a fraudulent scheme to avoid substantial margin calls when placing orders for commodity options traded on NYMEX and CME. Whitney committed this margin call avoidance scheme in connection with out-of-the-money options by knowingly making false and misleading statements

to clearing firms, floor brokers, and other persons in violation of Section 4c(b) of the Act, 7 U.S.C. § 6c(b) and Regulation 33.10, 17 C.F.R. § 33.10 (2010). Whitney additionally made false and misleading statements to and willfully deceived a staff representative of the CME, a registered entity as defined by Section 1a(29) of the Act, as amended, 7 U.S.C. § 1a(29), in violation of Section 9(a)(4) of the Act, 7 U.S.C. § 13(a)(4).

27. Unless restrained and enjoined by this Court, there is a reasonable likelihood that Defendant will continue to engage in the acts and practices alleged in the Complaint and in similar acts and practices in violation of the Act and Regulations.

IV. PERMANENT INJUNCTION

IT HEREBY IS ORDERED THAT:

28. Based upon and in connection with the foregoing conduct, pursuant to Section 6c of the Act, as amended, 7 U.S.C. § 13a-1, Whitney is permanently restrained, enjoined, and prohibited from directly or indirectly:

- a) Offering to enter into, entering into or confirming the execution of commodity option transactions contrary to any rule or regulation of the Commission... in violation of Section 4c(b) of the Act, 7 U.S.C. § 6c(b);
- b) Willfully falsifying, concealing, or covering up by any trick, scheme, or artifice a material fact, making any false, fictitious, or fraudulent statements or representations, or making or using any false writing or document knowing the same to contain any false, fictitious or fraudulent statement or entry to a registered entity in violation of Section 9(a)(4) of the Act, 7 U.S.C. § 13(a)(4); and

- c) In or in connection with an offer to enter into, the entry into, the confirmation in the execution of, or the maintenance of, any commodity option transaction, directly or indirectly: (a) cheating or defrauding or attempting to cheat or defraud; (b) making or causing to be made to any other person any false report or statement thereof or cause to be entered for any person any false record thereof; or (c) deceiving or attempting to deceive any other person by any means whatsoever in violation of Regulation 33.10, 17 C.F.R. § 33.10.

29. Defendant is permanently restrained, enjoined, and prohibited from directly or indirectly:

- a) Trading on or subject to the rules of any registered entity [as that term is defined in Section 1a(29) of the Act, 7 U.S.C. § 1a(29)];
- b) Entering into any transactions involving commodity futures, options on commodity futures, commodity options (as that term is defined in Regulation 1.3(hh), 17 C.F.R. § 1.3(hh) (2011) ("commodity options"), security futures products, and/or foreign currency (as described in Sections 2(c)(2)(B) and 2(c)(2)(C)(i) of the Act, as amended, 7 U.S.C. §§ 2(c)(2)(B) and 2(c)(2)(C)(i)) ("forex contracts"), for his own personal accounts or for any account in which he has a direct or indirect interest;
- c) Having any commodity futures, options on commodity futures, commodity options, security futures products, and/or forex contracts traded on his behalf;
- d) Controlling or directing the trading for or on behalf of any other person or entity, whether by power of attorney or otherwise, in any account involving commodity futures, options on commodity futures, commodity options, security futures products, and/or forex contracts;
- e) Soliciting, receiving, or accepting any funds from any person for the purpose of purchasing or selling any commodity futures, options on commodity futures, commodity options, security futures products, and/or forex contracts;
- f) Applying for registration or claiming exemption from registration with the Commission in any capacity, and engaging in any activity requiring such

registration or exemption from registration with the Commission, except as provided for in Regulation 4.14(a)(9), 17 C.F.R. § 4.14(a)(9) (2011); and/or

- g) Acting as a principal (as that term is defined in Regulation 3.1(a), 17 C.F.R. § 3.1(a) (2011)), agent, or any other officer or employee of any person (as that term is defined in Section 1a of the Act, as amended, 7 U.S.C. § 1a) registered, exempted from registration or required to be registered with the Commission except as provided for in Regulation 4.14(a)(9), 17 C.F.R. § 4.14(a)(9) (2011).

V. CIVIL MONETARY PENALTY

30. Defendant shall pay a civil monetary penalty in the amount of six hundred thousand dollars (\$600,000) (the "CMP Obligation"), plus post-judgment interest within ten (10) days of the entry of this consent order. Post-judgment interest shall accrue on the CMP Obligation commencing on the date of entry of this Consent Order and shall be determined by using the Treasury Bill rate prevailing on the date of entry of this Consent Order pursuant to 28 U.S.C. § 1961 (2006).

31. The Defendant shall pay his CMP Obligation 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, 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 by electronic transfer is chosen, Defendant shall contact Linda Zurhorst or her successor at the address above to receive payment instructions and shall fully comply with those instructions. Defendant shall accompany payment of the CMP Obligation with a cover letter that

identifies Defendant and the name and docket number of this proceeding. Defendant shall simultaneously transmit copies of the cover letter and the form of payment to: (1) the Chief Financial Officer, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, D.C. 20581 and (2) the Regional Counsel, Division of Enforcement, Commodity Futures Trading Commission, 140 Broadway, 19th Floor, New York, NY 10005.

B. Provisions Related to Monetary Sanctions

32. Partial Satisfaction: Any acceptance by the Commission of partial payment of Defendant's CMP Obligation shall not be deemed a waiver of his obligation to make further payments pursuant to this Consent Order, or a waiver of the Commission's right to seek to compel payment of any remaining balance.

VI. MISCELLANEOUS PROVISIONS

33. Notice: All notices required to be given by any provision in this Consent Order shall be sent by certified mail, return receipt requested, as follows:

Notice to the Commission:

Director, Division of Enforcement
Commodity Futures Trading Commission
1155 21st St., N.W.
Washington, DC 20581

Michael R. Berlowitz
Division of Enforcement
Commodity Futures Trading Commission
140 Broadway, 19th floor
New York, NY 10005
(646) 746-9759 (phone)
(646) 746-9940 (fax)

Notice to Defendant:

**The Law Office of James McGurk
10 South LaSalle Street
Suite 3300
Chicago, IL 60603
(312) 236-8900 (phone)
(312) 277-3497 (fax)**

**Kent R.E. Whitney
233 East Wacker Drive
Apt. 4409
Chicago, IL 60601
(312) 203-2361 (phone)**

All such notices to the Commission shall reference the name and docket number of this action.

34. Change of Address/Phone: Until such time as Whitney satisfies in full his CMP Obligation as set forth in this Consent Order, Whitney 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.

35. Entire Agreement and Amendments: This Consent Order incorporates all of the terms and conditions of the settlement among the parties hereto to date. Nothing shall serve to amend or modify this Consent Order in any respect whatsoever, unless: (a) reduced to writing, (b) signed by all parties hereto, and (c) approved by order of the Court.

36. Invalidation: If any provision of this Consent Order or the application of any provisions or circumstances is held invalid, then the remainder of this Consent Order and the application of the provision to any other person or circumstance shall not be affected by the holding.

37. Waiver: The failure of any party to this Consent Order at any time to require performance of any provision of this Consent Order shall in no manner affect the right of such party at a later time to enforce the same or any other provision of this Consent Order. No waiver

in one or more instances of the breach of any provision contained in this Consent Order shall be deemed to be or construed as a further or continuing waiver of such breach or waiver of the breach of any other provision of this Consent Order.

38. **Continuing Jurisdiction of this Court:** This Court shall retain jurisdiction of this action to ensure compliance with this Consent Order and for all other purposes related to this action, including any motion by Whitney to modify or for relief from the terms of this Consent Order.

39. **Injunctive and Equitable Relief Provisions:** The injunctive and equitable relief provisions of this Consent Order shall be binding upon Whitney, upon any person under his authority or control, and upon any person who receives actual notice of this Consent Order, by personal service, e-mail, facsimile or otherwise insofar as he or she is acting in active concert or participation with Whitney.

40. **Counterparts and Facsimile Execution:** This Consent Order may be executed in two or more counterparts, all of which shall be considered one and the same agreement and shall become effective when one or more counterparts have been signed by each of the parties hereto and delivered (by facsimile, e-mail, or otherwise) to the other party, it being understood that all parties need not sign the same counterpart. Any counterpart or other signature to this Consent Order that is delivered by any means shall be deemed for all purposes as constituting good and valid execution and delivery by such party of this Consent Order.

41. Whitney understands that the terms of the Consent Order are enforceable through contempt proceedings, and that, in any such proceedings he may not challenge the validity of this Consent Order.

There being no just reason for delay, the Clerk of the Court is hereby directed to enter this Consent Order for Permanent Injunction and Other Equitable Relief Against Defendant Kent R. E. Whitney.

IT IS SO ORDERED on this 22^d day of May 2012.

Paul A. Engelmayer
Paul A. Engelmayer
United States District Judge

CONSENTED TO AND APPROVED BY:

By: [Signature]
Kent R.E. Whitney
233 East Wacker Drive, Apt. 4409
Chicago, IL 60601
(312) 203-2361
Date: 3/26/2012

By: [Signature]
Michael R. Berlowitz, Esq.
U.S. Commodity Futures Trading
Commission
Division of Enforcement
140 Broadway
New York, NY 10005
(646) 746-9765
(646) 746-9938 (fax)
mberlowitz@cftc.gov

Date: May 16, 2012

Approved as to form:
[Signature]
James McGurk
Attorney for Defendant
10 South LaSalle Street, Suite 3300
Chicago, IL 60603
(312) 236-8900
(312) 277-3497 (fax)

Date: 3/26/2012