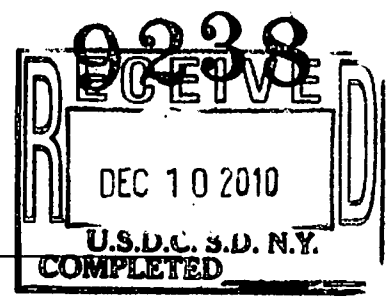


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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

U.S. COMMODITY FUTURES TRADING
COMMISSION,

Plaintiff,

v.

KENT R.E. WHITNEY,

Defendant.

Case No. _____

ECF Case

COMPLAINT FOR INJUNCTIVE AND
OTHER EQUITABLE RELIEF AND
FOR CIVIL MONETARY PENALTIES
PURSUANT TO THE COMMODITY
EXCHANGE ACT

By and for its complaint, the U.S. Commodity Futures Trading Commission (the
“Commission” or the “CFTC”), alleges as follows:

I.

**SUMMARY OF DEFENDANT’S VIOLATIONS
OF THE COMMODITY EXCHANGE ACT**

1. At various times from May 2008 through April 2010, Defendant Kent R.E. Whitney (“Whitney” or “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”).

2. Whitney committed this margin call avoidance scheme in connection with out-of-the-money options by knowingly or recklessly making false and misleading statements to clearing firms, floor brokers, and other persons, and thereby violated Section 4c(b) of the Commodity Exchange Act (the “Act”), as amended, 7 U.S.C. § 6c(b), and Commission Regulation 33.10, 17 C.F.R. § 33.10 (2010).

3. Furthermore, on January 15, 2010, Whitney made false and misleading statements to, or willfully deceived staff of, CME Group Inc., a registered entity, in violation of Section 9(a)(4) of the Act, as amended, 7 U.S.C. § 13(a)(4).

II.

JURISDICTION AND VENUE

4. The Court has jurisdiction over this action pursuant to Section 6c(a) of the Act, as amended, 7 U.S.C. § 13a-1, which authorizes the Commission to seek injunctive relief against any person whenever it shall appear to the Commission that such person has engaged, is engaging, or is about to engage in any act or practice constituting a violation of the Act or any rule, regulation, or order thereunder.

5. Venue properly lies with the Court pursuant to Section 6c(e) of the Act, as amended, 7 U.S.C. § 13a-1(e), in that Defendant transacted business in this District, and acts and practices in violation of the Act have occurred, are occurring, or are about to occur within this District.

III.

PARTIES

6. **Plaintiff U.S. Commodity Futures Trading Commission** is an independent federal regulatory agency that is charged by Congress with the responsibility for administering and enforcing the provisions of the Act and Commission Regulations.

7. **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 (“AP”) of Lone Star Trading Group, Inc., a registered Introducing Broker with its business address in Deerfield Beach, Florida.

IV.
FACTS

8. NYMEX and CME are designated contract markets and are located in Manhattan, New York and Chicago, Illinois respectively. NYMEX and CME are both a part of CME Group Inc. (“CME Group”).

9. 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. In summary, this scheme involved Whitney placing 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 front month options expiration.¹ At the time he placed these options orders, Whitney knowingly provided clearing firms invalid (closed) account numbers for 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.

10. 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.

11. The next business day, Whitney provided valid (open) account numbers to clear the trades.

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

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

13. 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

A. May 14-15, 2008

14. On May 14, 2008 (one day before the Crude Oil Option June 08 expiration), Whitney placed orders to sell 2,820 out-of-the-money NYMEX crude oil options with ESCO Commodities (“ESCO”), a NYMEX floor operation. ESCO floor broker(s) executed these options orders. These orders were placed for accounts controlled by Ivan Gellerman (“Gellerman”).

15. At Whitney’s direction, all trades that were executed were initially allocated to account #20430 at clearing firm Royal Bank of Canada (“RBC”). However, RBC account #20430 was an invalid (non-existent) account, as Whitney knew, and therefore RBC rejected the trades and sent them back to the executing broker’s clearing firm. Thus, Whitney was able to shift the overnight margin risk on these options trades to the executing broker’s account.

16. On May 15, 2008, Whitney directed ESCO to allocate all trades to DT Clearing LLC (“DT Clearing”) account #20882, cleared by Fortis Clearing Americas LLC (“Fortis”), which was a valid account and where the trades ultimately cleared. Account #20882 was controlled by Gellerman.

17. Fortis is registered with the Commission as a Futures Commission Merchant (“FCM”).³

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

³ A FCM is an individual, association, partnership, corporation, or trust that solicits or accepts orders for the purchase or sale of any commodity for future delivery on or subject to the rules of any exchange and that accepts payment from or extends credit to those whose orders are accepted.

18. DT Clearing is registered with the Commission as an Introducing Broker (“IB”).⁴
19. Whitney avoided a margin call of approximately \$10.3 million for these options trades.
20. These options expired worthless, i.e., with no value, and Whitney collected the premium on these options executed on May 14, 2008.

B. June 13, 2008

21. On June 13, 2008 (two business days before the Crude Oil Option July 08 expiration), Whitney placed orders with ESCO to sell 3,205 out-of-the-money NYMEX crude oil options. The orders were placed in accounts controlled by Gellerman.

22. At Whitney’s direction, these options were initially allocated to FC Stone account #30750, which was undermargined, i.e., did not have enough funds to cover any margin calls. Whitney knew this account was undermargined when he placed the order. FC Stone, therefore, rejected the trades and returned them to the clearing firm of the executing broker.

23. As a result of Whitney’s actions, the overnight margin risk for these NYMEX crude oil options was shifted to the executing broker’s clearing firm.

24. The next business day, June 16, 2008, Whitney directed the ESCO phone clerks to allocate the trades to accounts #20850, 20852, and 20882, all cleared by Fortis and all controlled by Gellerman. Whitney told the ESCO phone clerk to place/make these allocations as late as possible. These trades ultimately cleared in those new account numbers that Whitney provided on June 16, 2008.

⁴ An IB is a person or entity (other than an FCM) who is engaged in soliciting or accepting orders for the purchase or sale of any commodity for future delivery on an exchange who does not accept any money, securities, or property to margin, guarantee, or secure any trades or contracts that result therefrom.

25. By these actions, Whitney avoided a margin call of approximately \$2.6 million. Gellerman's accounts, which Whitney used, collected the premium on these options, which had expired worthless.

C. June 16-17, 2008

26. On June 16, 2008 (one day before the Crude Oil Option July 08 expiration), Whitney placed orders to sell 4,500 out-of-the-money NYMEX crude oil options through ESCO. ESCO floor brokers executed this order.

27. Whitney initially directed ESCO to allocate the options trades to RBC account #40230, which Whitney knew was a closed account that had been under Gellerman's control.

28. Because the account was closed, RBC rejected the allocations and sent the trades back to the clearing firm of the execution brokers. Thus, Whitney was able to shift the overnight risk of posting margin to the clearing firm of the executing broker.

29. The next business day, June 17, 2008, Whitney directed ESCO to allocate these options to two different accounts, #20858 cleared by Fortis, and account #GWG214 cleared by Citigroup Global Markets, Inc. ("Citigroup"). Both of these accounts were controlled by Gellerman.

30. Because these trades ultimately cleared into valid accounts on expiration day, Whitney avoided a margin call of approximately \$5 million by transferring the overnight margin risk to the executing broker's clearing firms. Gellerman's accounts, which Whitney used, collected the premium on these options as they expired worthless.

D. July 16-17, 2008

31. On July 16, 2008 (one day before the August 08 Crude Oil Option expiration), Whitney placed orders to sell 3,200 out-of-the-money NYMEX crude oil options through ESCO.

32. Whitney initially allocated these crude oil options to FIMAT account #2906094, which Whitney knew had been closed in November 2007 and had been controlled by Gellerman.

33. Because the account was closed, FIMAT rejected the allocations and sent the trades back to the clearing firm of the execution brokers. Thus, Whitney was able to shift the overnight risk of posting margin to the clearing firm of the executing broker.

34. On July 17, 2008 (expiration day), Whitney directed ESCO to allocate these option trades to account #20854, cleared by Fortis and controlled by Gellerman, where the trades then cleared.

35. Because these trades ultimately cleared into valid accounts on expiration day, when the clearing firm used by Whitney did not require a margin call, Whitney avoided a margin call of approximately \$13.7 million by transferring the overnight margin risk to the executing broker's clearing firms. As these options ultimately expired worthless, Gellerman's account, which Whitney used, collected the premium on them.

E. November 20, 2009

36. In or around August 2008, Gellerman ended his relationship with Whitney.

37. Whitney continued his margin call avoidance scheme by using accounts in the name of Whitney's friend, David Parrish ("Parrish").

38. On November 20, 2009 (expiration day for the November 09 S&P 500 Option), Whitney placed an order to sell 450 November 09 S&P 500 options to the floor of the CME on behalf of Parrish.

39. Shortly after the 450 lot order was executed and before the options market had closed on November 20, 2009, Whitney obtained the order tickets from the executing brokers and presented them to William Strubing ("Strubing") of NKO Group Inc. ("NKO"), a floor

broker operation at CME in Chicago, IL. Whitney asked Strubing to allocate this 450 lot order among four accounts that Whitney claimed belonged to Parrish. Whitney represented to Strubing that these trades were good and the accounts for allocation were also valid.

40. Strubing first called each of the four FCMs where these accounts were purportedly located but each of them refused to accept these orders. Strubing then spoke again to Whitney and informed him that none of the FCMs Whitney had identified would accept this 450 lot options order.

41. Whitney insisted these trades were good but took back the order tickets for this 450 lot options order.

42. These 450 lot options trades were never cleared in any of Whitney's accounts.

F. January 14-15, 2010

43. On January 14, 2010 (one day before expiration of the February 2010 Crude Oil Option), Whitney placed an order, on behalf of Parrish, to the NYMEX floor to sell over 1,800 out-of-the-money crude oil options.

44. After this crude oil options sell order was executed, Whitney initially directed NYMEX phone clerks to allocate these options to account #C4756 in the name of Parrish at Cunningham Commodities LLC ("Cunningham"). These trades were rejected as the account was closed. Whitney knew these initial allocations would be rejected because he knew Parrish's account at Cunningham was closed.

45. Before the close of trading on January 14, 2010, Whitney then directed NYMEX phone clerks to allocate these trades to four different accounts at Cunningham and instructed them to wait until just before the phone clerk left for the day before allocating them. These four allocations were also rejected and sent back to the executing brokers.

46. As a result of Whitney's actions, the overnight margin risk was shifted to the clearing firms of the executing brokers, which received an \$18 million margin call on January 15, 2010. Whitney's fraudulent actions allowed him and Parrish to avoid a substantial margin call.

47. In the afternoon of January 15, 2010, Mark Solazzo ("Solazzo"), one of the executing brokers, informed Whitney that all of Whitney's trade allocations had been rejected and that there was an \$18 million margin call.

48. Whitney never provided a valid account number for clearing of these approximately 1,800 NYMEX crude oil options, and the options expired worthless in the accounts of the executing brokers.

G. Summary Access Denial by CME Group

49. 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. 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.

H. March 26, 2010

50. Despite knowing that he was banned from trading for himself or others on NYMEX and CME, on March 26, 2010, Whitney either directly or indirectly attempted to place a telephone order, on behalf of Parrish, to sell out-of-the-money NYMEX April 2010 natural gas options.

51. Whitney falsely identified himself on the telephone to Robert Elder (“Elder”), a NYMEX phone clerk, as David Parrish when Whitney placed this order to the NYMEX floor.

52. However, Elder recognized Whitney’s voice on the phone and refused to accept the order because Whitney had been banned from trading by CME Group.

I. April 16, 2010

53. On April 16, 2010 (expiration day for the May 2010 S&P 500 Option), Whitney placed orders to sell 2,500 out-of-the-money CME S&P 500 options in Parrish’s account through FCM Penson GHCO (“Penson”).

54. Penson determined that the margin call on these orders was approximately \$47 million, but Parrish’s account had less than \$100,000 at the time.

55. Carl Gilmore (“Gilmore”), a Penson employee, called the telephone number listed on Parrish’s account opening forms and the call was answered by Whitney, as it was Whitney’s telephone number.

56. Gilmore asked Whitney if he had placed these orders and, why Whitney was placing orders when he knew he had been denied trading access by CME Group. Whitney falsely denied placing this order and claimed the order was made by Parrish.

57. Gilmore then contacted Parrish and told Parrish that Parrish needed to provide \$47 million to cover the margin on these positions. Parrish did not have sufficient funds to meet this margin call, so Penson liquidated the trades at a net loss of approximately \$20,000 to Parrish’s account.

J. Whitney's false and misleading statements to CME

58. On the afternoon of January 15, 2010, CME Group staffer, Greg Benbrook ("Benbrook"), questioned Whitney about the options trades Whitney had attempted to place in Parrish's account on January 14, 2010.

59. Benbrook asked Whitney about the initial trade allocations that had been rejected by the clearing firms. Whitney falsely told Benbrook that Whitney was unaware of any rejected trade allocations that Whitney had made on January 14, 2010.

60. Whitney's statement to Benbrook was false and misleading because earlier in the day on January 15, 2010, Solazzo specifically told Whitney those January 14, 2010 options trades were rejected and had not cleared.

K. Whitney's Knowing or Reckless Conduct

61. In conducting his margin call avoidance scheme, Whitney knew the initial allocations he provided clearing firms were for closed or invalid accounts. 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.

62. In conducting his margin call avoidance scheme, Whitney knew the clearing firms would certainly reject allocations to closed or invalid accounts, thereby transferring the overnight margin risk to the clearing firms of the executing brokers.

63. Although Whitney did not receive actual margin calls in carrying out his scheme, he or the accounts he traded would have received substantial margin calls if the market had moved against Whitney and the out-of-the-money options he traded suddenly became in-the-money. Whitney, or the accounts he traded, would have to pay substantial amounts, and if he, or the

accounts Whitney traded, could not cover the margin calls, then the clearing firms or even the exchange would have to.

64. After January 28, 2010, Whitney knew he had been prohibited from trading on all CME Group markets, either for himself or others, when Whitney placed or attempted to place commodity options orders on behalf of Parrish.

65. On March 26, 2010, Whitney directly or indirectly attempted to place an options order for Parrish by falsely claiming Whitney was Parrish when Whitney himself (not Parrish) placed the order.

66. On April 16, 2010, Whitney falsely told a Penson employee that Whitney had not placed a commodity options order for Parrish, when in fact, Whitney had placed that order himself.

V.

VIOLATIONS OF THE COMMODITY EXCHANGE ACT AND COMMISSION REGULATIONS

COUNT I

Violations of Section 4c(b) of the Act and Regulation 33.10 (Options Fraud)

67. The allegations set forth in paragraphs 1 through 66 above are re-alleged and incorporated herein by reference.

68. Section 4c(b) of the Act, as amended, 7 U.S.C. § 6c(b), makes it unlawful to offer to enter into, enter into or confirm the execution of commodity option transactions contrary to any rule or regulation of the Commission prohibiting such transaction or allowing any such transaction under such terms and conditions as the Commission shall prescribe.

69. Regulation 33.10, 17 C.F.R. § 33.10, makes it unlawful for any person, in or in connection with an offer to enter into, the entry into, the confirmation of the execution of, or the

maintenance of, any commodity option transaction, directly or indirectly to: (a) cheat or defraud or attempt to cheat or defraud; (b) make or cause 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) to deceive or attempt to deceive any other person by any means whatsoever.

70. Whitney knowingly or recklessly, in connection with commodity options transactions, cheated or defrauded or attempted to cheat or defraud other persons including clearing firms.

71. Whitney knowingly or recklessly, in connection with commodity options transactions, made or caused to be made false reports or statements to other persons, including clearing firms, or caused to be entered for other persons false records thereof.

72. Whitney knowingly or recklessly, in connection with commodity options transactions, deceived or attempted to deceive other persons by making false and misleading statements to such persons, including clearing firms.

73. Each material false or misleading statement, cheat or attempted cheat, fraud or attempted fraud, by Whitney, including but not limited to those specifically alleged herein, is a separate and distinct violation of Section 4c(b) of the Act, as amended, 7 U.S.C. § 6c(b), and Regulation 33.10, 17 C.F.R. § 33.10.

COUNT II

Violations of Section 9(a)(4) of the Act; False Statements to the CME Group

74. The allegations set forth in paragraphs 1 through 66 above are re-alleged and incorporated herein by reference.

75. Section 9(a)(4) of the Act, as amended, 7 U.S.C. § 13(a)(4), makes it unlawful for any person willfully to falsify, conceal, or cover up by any trick, scheme, or artifice a material

fact, make any false, fictitious, or fraudulent statements or representations, or make or use any false writing or document knowing the same to contain any false, fictitious, or fraudulent statement or entry to a registered entity, board of trade, or futures association designated or registered under the Act acting in furtherance of its official duties under the Act.

76. CME Group is a registered entity as defined by Section 1a(29) of the Act, as amended, 7 U.S.C. § 1a(29).

77. On or about January 15, 2010, CME Group staff person Benbrook questioned Whitney about Whitney's trading in Parrish's account on January 14, 2010. Whitney falsely told Benbrook that Whitney was unaware the initial allocations he made on January 14, 2010, had been rejected by the clearing firms. In fact, Whitney had been informed on January 14 and the morning of January 15, 2010 by the executing broker that Whitney's initial allocations had been rejected.

78. By his conduct described above, Whitney violated Section 9(a)(4) of the Act, as amended, 7 U.S.C. § 13(a)(4).

79. Each and every instance of a false, fictitious, or fraudulent statement by Whitney is alleged herein as a separate and distinct violation of Section 9(a)(4) of the Act, as amended, 7 U.S.C. § 13(a)(4).

VI.

RELIEF REQUESTED

WHEREFORE, the Commission respectfully requests that the Court, as authorized by Section 6(c) of the Act, as amended, 7 U.S.C. § 13a-1, and pursuant to its own equitable powers, enter:

- a) An order finding that Whitney violated Sections 4c(b) and 9(a)(4) of the Act, as amended, 7 U.S.C. §§ 6c(b) and 13(a)(4), and Regulation 33.10, 17 C.F.R. § 33.10;
- b) An order of preliminary and permanent injunction prohibiting the Defendant and any of his agents, servants, employees, assigns, attorneys, and persons in active concert or participation with the Defendant, including any successor thereof, from engaging, directly or indirectly:
- i. in conduct in violation of Sections 4c(b) and 9(a)(4) of the Act, as amended, 7 U.S.C. §§ 6c(b) and 13(a)(4), and Regulation 33.10, 17 C.F.R. § 33.10;
 - ii. trading on or subject to the rules of any registered entity (as that term is defined in Section 1a(29) of the Act, as amended, 7 U.S.C. § 1a(29));
 - iii. entering into any transactions involving commodity futures, options on commodity futures, commodity options (as that term is defined in Regulation 32.1(b)(1), 17 C.F.R. § 32.1(b)(1) (2010)) (“commodity options”), and/or foreign currency (as described in Sections 2(c)(2)(B) and 2(c)(2)(C)(i) of the Act, as amended, to be codified at 7 U.S.C. §§ 2(c)(2)(B) and 2(c)(2)(C)(i)) (“forex contracts”) for their own personal account or for any account in which they have a direct or indirect interest;
 - iv. having any commodity futures, options on commodity futures, commodity options, and/or forex contracts traded on their behalf;
 - v. 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, and/or forex contracts;

- vi. 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, and/or forex contracts;
 - vii. 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) (2010);
 - viii. acting as a principal (as that term is defined in Regulation 3.1(a), 17 C.F.R. § 3.1(a) (2010)), agent or any other officer or employee of any person 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) (2010);
- c) An order directing Whitney, as well as any other person or entity associated with him, including any successor thereof, to disgorge, pursuant to such procedure as the Court may order, all benefits received from the acts or practices that constitute violations of the Act or Regulations, as described herein, and interest thereon from the date of such violations;
- d) An order directing the Defendant to pay a civil monetary penalty for each violation of the Act and Regulations described herein, plus post-judgment interest, in the amount of the higher of \$140,000 for each violation of the Act and Regulations committed on or after October 23, 2008, \$130,000 for each violation of the Act and Regulations committed

before October 23, 2008, or triple the monetary gain to the Defendant for each violation of the Act and Regulations described herein;

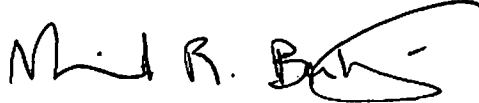
- e) An order requiring Defendant to pay costs and fees as permitted by 28 U.S.C. §§ 1920 and 2412(a)(2) (2006); and
- f) Such other and further remedial ancillary relief as the Court may deem appropriate.

Respectfully submitted,

Attorneys for the U.S. Commodity Futures Trading
Commission

Dated: 12/10/2010

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