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UNITED STATES OF AMERICA  
Before the  
COMMODITY FUTURES TRADING COMMISSION

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**In the Matter of** )  
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**San Diego Gas & Electric Company,** )  
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**Respondent.** )  
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**CFTC Docket No:** 10-08

**ORDER INSTITUTING PROCEEDINGS  
PURSUANT TO SECTION 6(c) OF THE  
COMMODITY EXCHANGE ACT,  
MAKING FINDINGS AND IMPOSING  
REMEDIAL SANCTIONS**

**I.**

The Commodity Futures Trading Commission ("**Commission**") has reason to believe that San Diego Gas & Electric Company ("**SDG&E**" or "**Respondent**") has violated Section 4c(a) of the Commodity Exchange Act, as amended (the "**Act**"), 7 U.S.C. § 6c(a) (2006). Therefore, the Commission deems it appropriate and in the public interest that public administrative proceedings be, and thereby are, instituted to determine whether SDG&E engaged in the violations set forth herein and to determine whether any order should be issued imposing remedial sanctions.

**II.**

In anticipation of the institution of this administrative proceeding, SDG&E has submitted an Offer of Settlement ("**Offer**"), which the Commission has determined to accept. Without admitting or denying any of the findings of fact or violations herein, SDG&E acknowledges service of this Order Instituting Proceedings Pursuant to Section 6(c) and 6(d) of the Commodity Exchange Act, Making Findings and Imposing Remedial Sanctions ("**Order**").<sup>1</sup>

<sup>1</sup> SDG&E consents 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 SDG&E does not consent to the use of the Offer or this Order, or the findings consented to in the Offer or this Order, as the sole basis for any other proceeding brought by the Commission, other than in a proceeding in bankruptcy or enforce the terms of this Order. SDG&E does not consent to the use of the Offer or this Order, or the findings consented to in this Offer or this Order, by any other party in any other proceeding.

### III.

The Commission finds the following:

#### A. SUMMARY

On one or more occasions during the period from January 26, 2006, through February 2, 2006 (the "relevant period"), an SDG&E employee contacted an introducing broker to place market orders for the execution of certain offsetting sales and purchases of New York Mercantile Exchange ("NYMEX") natural gas futures contracts at a minimum price difference (the "Futures Orders").

Each of the Futures Orders was then executed by NYMEX floor brokers at or about the same time and at or about the same price with the effect of liquidating and immediately re-establishing NYMEX futures contracts previously held by SDG&E. This resulted in no material net change in the market position of SDG&E. SDG&E asserts that it instructed the execution of the Futures Orders for reasons relating solely for the purpose of managing its internal liquidity and risk management limits.

When SDG&E initiated the Futures Orders, it did not intend to materially change its overall position in the market or hedge an existing market position. Because the Futures Orders were executed in a manner meant to negate market risk, and thereby avoided making a bona fide market transaction, SDG&E violated Section 4c(a) of the Act, 7 U.S.C. § 6c(a) (2006), which, inter alia, prohibits any person from entering into a transaction that is, or is of the character of, or is commonly known to the trade as, a "wash sale."

#### B. RESPONDENT

**San Diego Gas & Electric Company** is a California-based, investor-owned, regulated utility. SDG&E's address is 8315 Century Park Court, San Diego, CA. SDG&E has never been registered with the Commission in any capacity.

#### C. FACTS

Prior to January 2006, SDG&E had established as a price hedge a long position in NYMEX natural gas futures contracts for delivery months August through October 2006 ("**NYMEX Contracts**"). On one or more occasions during the relevant period, an SDG&E employee gave instructions to an introducing broker to place the Futures Orders that would have the effect of liquidating and then re-establishing the same NYMEX Contracts at a minimum price difference. Upon those instructions, the broker placed simultaneous purchase and sale orders with NYMEX floor brokers that resulted in the sales and purchases that constitute each of the Futures Orders being executed for SDG&E at the same or nearly the same price.

In each case, SDG&E gave the instruction to place the order to sell and the order to buy the futures contracts on the same phone call. Further, SDG&E was aware that the introducing broker placed each of the Futures Orders with the NYMEX floor brokers together and requested that the prices in respect of each of the Futures Orders be at or near the same price. As a result,

NYMEX floor brokers executed both the sell order and the buy order at or about the same time and at or about the same price, and the various Futures Orders collectively resulted in SDG&E selling NYMEX contracts and then repurchasing NYMEX Contracts without materially changing its futures market position.

#### **D. LEGAL DISCUSSION**

##### **SDG&E Engaged in Wash Sales in Violation of Section 4c(a) of the Act.**

Section 4c(a) of the Act makes it "unlawful for any person to offer to enter into, enter into, or confirm the execution of a transaction" that "is of the character of, or is commonly known to the trade as, a 'wash sale'..." 7 U.S.C. § 6c(a) (2006). A wash sale is a form of fictitious transaction. *In re Gimbel*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,213 at 35,003 (CFTC Apr. 14, 1988), *aff'd as to liability*, 872 F.2d 196 (7<sup>th</sup> Cir. 1989); *In re Goldwurm*, 7 A.D. 265, 274 (CEA 1948).

A wash sale is a transaction made without an intent to take a genuine, bona fide position in the market, such as a simultaneous purchase and sale designed to negate each other so that there is no change in financial position. *Reddy v. CFTC*, 191 F.3d 109, 115 (2<sup>nd</sup> Cir. 1999). *See also Goldwurm*, 7 A.D. at 274. Wash sales are "grave" violations, even in the absence of customer harm or appreciable market effect, because "they undermine confidence in the market mechanism that underlies price discovery." *In re Piasio*, [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 28,276 at 50,691 (CFTC Sep. 29, 2000), *aff'd sub nom. Wilson v. CFTC*, 322 F.3d 555, 559 (8<sup>th</sup> Cir. 2003) (wash sales are designed to give the appearance of submitting trades to the open market, while negating the risk or price competition incident to the market and produce a virtual financial nullity because the resulting net financial position is near or equal to zero). *See also CFTC v. Savage*, 611 F.2d 270, 284 (9<sup>th</sup> Cir. 1979) (wash sales may mislead market participants because they do not reflect the forces of supply and demand).

The central characteristic of a wash sale is the intent to avoid making a *bona fide* transaction or taking a *bona fide* market position. *In re Citadel Trading Co. of Chicago, Ltd.*, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,082 at 32,190 (CFTC May 12, 1986). "The factors that show a wash result are (1) the purchase and sale (2) of the same delivery month of the same futures contract (3) at the same (or a similar) price." *Piasio*, ¶ 28,276 at 50,685 (*citing In re Gilchrist*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,993 at 37,653 (CFTC Jan. 25, 1991)).

In addition to the factors enumerated above, intent must be proved to establish a violation of Section 4c of the Act. *Reddy v. CFTC*, 191 F.3d 109, 119 (2<sup>nd</sup> Cir. 1999). In the context of a customer's liability for a wash sale transaction, the scienter requirement relates to the customer's intent at the time the challenged transactions are initiated; specifically whether the customer intended to negate market risk or price competition. *Piasio*, ¶ 28,276 at 50,685. Negated risk is not "the equivalent of no risk or the complete elimination of risk;" rather the Commission has "clearly held that risk is negated whenever it is 'it is reduced to a level that has no practical impact on the transactions at issue.'" *Id.*, ¶ 28,276 at 50,688 (*quoting Gimbel*, ¶ 24,213 at 35,003 n.7). "[S]cienter may be inferred from the circumstantial evidence" and while motive is not an

element of a trade practice case, “evidence of motive strengthens an inference of intent.” *Reddy*, 191 F.3d at 119 (citations omitted).

SDG&E's purpose in executing the Futures Orders through its broker was to liquidate and then re-establish various positions.<sup>2</sup> SDG&E intentionally placed the Futures Orders at the same time with its introducing broker and sought these transactions be executed at or near the same price. Accordingly, SDG&E knowingly engaged in conduct which constituted wash sales and therefore violated Section 4c(a) of the Act.

The Commission recognizes SDG&E's cooperation in this matter.

#### IV.

#### **OFFER OF SETTLEMENT**

SDG&E has submitted an Offer in which it, without admitting or denying the findings herein: (1) acknowledges service of the Complaint and this Order; (2) admits the jurisdiction of the Commission with respect to the matters set forth herein; (3) waives a hearing, all post-hearing procedures, judicial review by any court, any objection to the participation by any member of the Commission's staff in the Commission's consideration of the Offer, any and all claims that it may possess under the Equal Access to Justice Act (EAJA), 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 (“**Regulations**”), 17 C.F.R. §§ 148.1-30 (2008), relating to, or arising from, this proceeding, any and all claims that it may possess under the Small Business Regulatory Enforcement Act, Pub. L. 104-121, §§ 231-232, 110 Stat. 862 (1996), as amended by Pub. L. No. 110-28, 121 Stat. 112 (2007), relating to, or arising from, this proceeding, and any claim of Double Jeopardy based upon institution of this proceeding or the entry of any order imposing a civil monetary penalty or any other relief; (4) stipulates that the record basis on which this Order may be entered shall consist solely of the Complaint, this Order and findings in this Order consented to in the Offer; and (5) consents to the Commission's issuance of this Order, which makes findings as set forth below and: (a) orders SDG&E to cease and desist from violating the provision of the Act that it has been found to have violated; (b) imposes a civil monetary penalty upon SDG&E of \$80,000; and (c) orders SDG&E to comply with the undertakings consented to in its Offer and set forth below in Part VI of this Order.

Upon consideration, the Commission has determined to accept the SDG&E's Offer.

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<sup>2</sup> There is no allegation or finding that any SDG&E employee engaged in any fraudulent misconduct with respect to the Futures Orders. However, the fact that SDG&E and its employees may have engaged in the Futures Orders to effect a legitimate economic purpose is not a defense under the Act. *See, e.g., In re Elliott*, [1997-199 Transfer Binder] Comm. Fut. L. Rep. ¶ 27,243 (CFTC Feb. 3, 1998) (“prohibited trading techniques are not made lawful because they are done for a legitimate market purpose”; rejecting argument that defendants' freshening objective, which “when accomplished through open and competitive trading, serves a legitimate market purpose”, was a defense to fictitious sale violation) (citations omitted), *aff'd sub nom. Elliott v. CFTC*, 202 F.3d 926 (7th Cir. 2000).

V.

**FINDINGS OF VIOLATIONS**

Based on the foregoing, the Commission finds that SDG&E engaged in wash sales in violation of Section 4c(a) of the Act, 7 U.S.C. § 6c(a) (2006).

VI.

**ORDER**

**Accordingly, IT IS HEREBY ORDERED THAT:**

1. SDG&E shall cease and desist from violating Section 4c(a) of the Act, 7 U.S.C. § 6c(a) (2006);
2. SDG&E shall pay a civil monetary penalty in the amount of \$80,000 within ten (10) days of the date of entry of this Order. SDG&E shall pay its 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 by other than 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: Marie Bateman - AMZ-300  
DOT/FAA/MMAC  
6500 S. MacArthur Blvd.  
Oklahoma City, OK 73169  
Telephone 405-954-6569

If payment by electronic transfer is chosen, SDG&E shall contact Marie Bateman or her successor at the above address to receive payment instructions and shall fully comply with those instructions. SDG&E shall accompany payment of the penalty with a cover letter that identifies SDG&E and the name and docket number of this proceeding. SDG&E shall simultaneously submit a copy of the cover letter and the form of payment to: (1) the Director, Division of Enforcement, Commodity Futures Trading Commission, at the following address: 1155 21st Street, N.W., Washington, D.C. 20581 and (2) the Chief, Office of Cooperative Enforcement, Division of Enforcement, Commodity Futures Trading Commission at the same address. In accordance with Section 6(e)(2) of the Act, 7 U.S.C. § 9a(2) (2006), if this amount is not paid in full within fifteen (15) days of the due date, SDG&E shall be prohibited automatically from the privileges of all registered entities, and, if registered with the Commission, such registration shall be suspended automatically until it has shown to the satisfaction of the Commission that payment of the full amount of the penalty with interest thereon to the date of the payment has been made; and

3. SDG&E shall comply with the following undertakings:

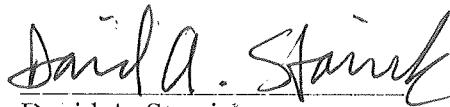
A. SDG&E shall implement immediately, to the extent not already in place, procedures that ensure that transactions made by SDG&E on United States futures markets fully comply with the rules and regulations of those markets and the Act and Regulations;

B. Neither SDG&E, nor any of its agents or employees under its 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 Respondent's: (i) testimonial obligations; or (ii) right to take legal positions in other proceedings to which the Commission is not a party. Respondent shall take all steps necessary to ensure that its agents and employees under its authority or control understand and comply with this undertaking; and

C. SDG&E acknowledges that failure to comply with this Order shall constitute a violation of this Order and may subject it to administrative or injunctive proceedings, pursuant to the Act.

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

By the Commission,



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

Dated: April 22, 2010