High-Frequency Trader Indicted for Manipulating Commodities Futures Markets in First Federal Prosecution for Spoofing

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CHICAGO—In the first federal prosecution of its kind, a high-frequency trader was indicted for allegedly manipulating commodities futures prices and illegally profiting nearly $1.6 million as a result of trading orders he placed through CME Group and European futures markets in 2011. The defendant, Michael Coscia, was the manager and sole owner of the former Panther Energy Trading LLC, of Red Bank, N.J., which he formed in 2007.

Coscia, 52, of Rumson, N.J., a registered commodities trader since 1988, was charged with six counts of commodities fraud and six counts of "spoofing" in a 12-count indictment returned yesterday by a federal grand jury, Zachary T. Fardon, United States Attorney for the Northern District of Illinois, and Robert J. Holley, Special Agent-in-Charge of the Chicago Office of the Federal Bureau of Investigation, announced today.

The indictment marks the first federal prosecution nationwide under the anti-spoofing provision that was added to the Commodity Exchange Act by the 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act.

Coscia will be arraigned on a date to be determined in U.S. District Court in Chicago.

"Traders and investors deserve a level playing field, and when the field is tilted by market manipulators, regardless of their speed or sophistication, we will prosecute criminal violations to help ensure fairness and restore market integrity," Mr. Fardon said. "This case reflects the reasons why, earlier this year, we established a Securities and Commodities Fraud Section, which is dedicated to protecting markets and preserving investors' confidence," he added.

According to the indictment, high-frequency trading is a form of automated trading that uses computer algorithms for decision-making and placing a high volume of trading orders, quotes, or cancelation of orders in milliseconds. Coscia designed two computer programs he allegedly used in 17 different CME Group markets and three different markets on the London-based ICE Futures Europe exchange, including gold, soybean meal, soybean oil, high-grade copper, Euro FX and Pounds FX currency futures, to implement his fraudulent strategy. It was illegal for traders to place orders in the form of "bids" to buy or "offers" to sell a futures contract with the intent to cancel the bid or offer before execution.

Between August and October 2011, Coscia allegedly defrauded participants in the CME Group and ICE Futures Europe markets. In August 2011, Coscia began a high-frequency trading strategy in which he entered large-volume orders that he intended to immediately cancel before they could filled by other traders, the indictment alleges.

Coscia devised this strategy to create a false impression regarding the number of contracts available in the market, and to fraudulently induce other market participants to react to the deceptive market information he created, the indictment states. His strategy moved the markets in a direction favorable to him, enabling him to purchase contracts at prices lower than, or sell contracts at prices higher than, the prices available in the market before he entered and canceled his large-volume orders, it adds. Coscia then allegedly repeated this strategy in the opposite direction to immediately obtain a profit by buying futures contracts at a lower price than he paid for them, or by selling contracts at a higher price than he paid for them. Each such trade allegedly occurred in a matter of milliseconds. As a result of the aggregate of those fraudulent high-frequency trades, Coscia illegally profited approximately $1,592,867 over approximately three months, the indictment alleges.

As part of the scheme, Coscia's trading programs looked for market conditions such as price stability, low volume at the best prices, and a narrow difference between the prices at which prospective purchasers were willing to buy and prospective sellers were willing to sell because his allegedly fraudulent trading strategy worked best under these conditions. His trading programs sometimes placed a "ping order" of one contract to test the market and ensure that conditions would allow his strategy to work well.

Coscia allegedly designed his trading programs to place a "trade order" on one side of the market, intending that the trade order be filled. He profited from his fraudulent strategy by filling the "trade order," the charges allege.

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He also designed his programs to place several layers of “quote orders” on the other side of the market from his trade orders – either to buy contracts at a price higher than the prevailing offer, or to sell contracts at a price lower than the prevailing bid – to create the illusion of market interest. The quote orders would typically be the largest orders in the market within three ticks (the minimum price increment at which a futures contract could trade) of the best bid or offer price, usually doubling or tripling the total quantity of contracts within the best bid or offer price.

The indictment alleges that Coscia designed his programs to cancel the quote orders within a fraction of a second automatically, without regard to market conditions, even if the market moved in a direction favorable to the quote orders. He programmed the quote orders to cancel because he did not intend for them to be filled, but instead intended to trick other traders into reacting to the false price and volume information, it adds. Further, Coscia designed his programs to cancel all fraudulent and misleading quote orders immediately if any of them were even partially filled, because he intended them only to trick other traders into reacting to what appeared to be a substantial change in the market.

After Coscia filled his trade order through the use of fraudulent and misleading quote orders, he immediately entered a second trade order on the other side of the market and repeated his steps with misleading quote orders, causing the second trade order to be filled. As a result, Coscia allegedly profited on the difference in price between the first and second trade orders.

The indictment details an example through trades that Coscia placed milliseconds apart in the Euro FX market during the early morning on Sept. 1, 2011. By entering large orders that he intended to cancel at the time he placed them, and caused to be canceled before other traders could fill them, Coscia made a profit by buying 14 contracts at 14288 ticks and selling them at 14289 ticks less than one second later.

The government is being represented by Assistant U.S. Attorney Renato Mariotti.

Each count of commodities fraud carries a maximum sentence of 25 years in prison and a $250,000 fine, and each count of spoofing carries a maximum penalty of 10 years in prison and a $1 million fine. If convicted, the Court must impose a reasonable sentence under federal sentencing statutes and the advisory United States Sentencing Guidelines.

The public is reminded that an indictment contains only charges and is not evidence of guilt. The defendant is presumed innocent and is entitled to a fair trial at which the government has the burden of proving guilt beyond a reasonable doubt.

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