

futures contracts (“IDCH Contracts”) traded on the NASDAQ OMX Futures Exchange and cleared by the International Derivatives Clearinghouse (“IDCH”).¹

2. The CFTC’s theory of liability depends upon a novel and legally untenable claim: namely, that DRW’s submission of certain orders—placed transparently, in an open market, in conformance with the exchange’s rules, and at prices determined by rigorous economic analysis—must have been manipulative simply because: (i) DRW’s orders allegedly affected settlement prices for IDCH Contracts because IDCH considered the same in calculating settlement prices; and (ii) the orders deviated from prevailing yields of comparable uncleared over-the-counter (“OTC”) swaps (which the CFTC mistakenly believes were economically equivalent to the IDCH Contracts) and thus, according to the CFTC, the orders must have produced an “artificial” price.²

3. However, DRW’s economic analysis, which it discussed publicly at an industry conference during the Relevant Period and published in a scholarly White Paper, demonstrated that IDCH Contracts and the comparable uncleared OTC swaps were *not* economically equivalent because of the different cash flows provided for in the contract terms of the two instruments, and that differentiation justified the different price levels (yields). IDCH Contracts had not been designed to account for such differences, and thus presented an opportunity for a trader to profit by arbitraging this discrepancy. Moreover, no statutory provision, rule, regulation or pronouncement exists indicating that the “legitimate demand” for, or the fair market value of, a cleared instrument such as the

¹ Because of the time period within which the relevant trading occurred, the CFTC has acknowledged that it is seeking to penalize DRW under the law as it existed prior to the implementation of the amendments to the CEA and directives to the CFTC resulting from the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”).

² The products at issue here typically trade based on the contract’s expected yield. For simplicity, the terms “price” or “market price,” rather than yield, are used herein.

IDCH Contract must be determined based upon the prevailing price of a comparable OTC swap. In particular, no existing public laws or pronouncements informed a reasonable trader in DRW's position at the time that to avoid being exposed to a claim of unlawfully manipulating the market for a new swaps future product, its orders must closely track (or be identical to) the prevailing price of comparable OTC swaps.

4. Accordingly, the CFTC's enforcement action based on DRW's orders in connection with the IDCH Contract would violate DRW's constitutional due process right to receive fair notice of which activities constitute market manipulation, as well as its right to be free from arbitrary and unreasonable government actions.

5. This matter is ripe for adjudication because the filing and pendency of an enforcement action asserting unlawful manipulation of the IDCH Contract market would subject DRW to hardship and cause it immediate and irreparable harm. Additionally, it is in the public interest for the Court to consider whether the CFTC, by exercising its regulatory authority arbitrarily and unreasonably, undermines the intention of the Dodd-Frank Wall Street Reform Act ("Dodd-Frank") to promote the migration of derivatives trading to clearinghouses and exchanges such as the IDCH. DRW therefore seeks both: (a) a declaration from this Court that such an enforcement action for market manipulation would be unconstitutional either facially, to the extent it reflects a new and previously unstated rule of the CFTC, or "as applied" in DRW's particular case; and (b) in the interim, a preliminary injunction prohibiting the CFTC from commencing and pursuing such an action, which could be filed in a matter of days.

THE PARTIES

6. Plaintiff DRW Investments, LLC is a U.S. company that is a subsidiary of DRW Holdings, LLC and undertakes, among other things, fixed-income derivatives and other futures-based trading. It, along with DRW Holdings, LLC, has headquarters at 540 W. Madison Street, Chicago, Illinois 60606.

7. Plaintiff Donald R. Wilson, Jr. is an individual citizen who resides in Chicago, Illinois. He is the founder, Chief Executive Officer and manager of DRW Holdings, LLC, and the manager of DRW Investments, LLC. He also has an indirect ownership interest in both DRW Holdings, LLC and DRW Investments, LLC.

8. Defendant CFTC is a federal agency charged with regulating futures and options markets. The CFTC maintains its headquarters at Three Lafayette Centre, 1155 21st Street, NW, Washington, DC 20581 as well as a Regional Office at 525 West Monroe Street, Suite 1100, Chicago, Illinois 60661.

JURISDICTION AND VENUE

9. This is an action for declaratory judgment pursuant to 28 U.S.C. §§ 2201, *et seq.*, for the purpose of determining a question of actual controversy between the parties.

10. The Court has jurisdiction over this cause of action pursuant to 28 U.S.C. §§ 1331 and 1337.

11. Venue is proper in this judicial district under 28 U.S.C. § 1391(e).

THE FACTS

12. Based on DRW's knowledge, information and belief, the following facts are undisputed.

A. Definitions

13. DRW is a trading firm and its purpose is to make profit from executing complex trading strategies based on its own rigorous economic analysis, and also provide liquidity in financial markets.

14. An OTC swap is a bilateral derivative contract between two parties that typically involves a private over-the-counter exchange of one or more payments based on the underlying value of a notional amount of one or more commodities, or other financial or economic interest. Payments are then made directly by each party to the other party.

15. An interest rate swap is a commonly used financial derivative instrument in which two parties agree to exchange regular interest payments. The interest payment paid by each party is calculated based on the same specific notional amount (e.g., US \$1,000,000) but a different interest rate. Typically one party agrees to pay the other a fixed rate of interest (the “pay-fixed” side of the swap) while the other pays a floating rate of interest (the “pay-floating” side of the swap). Interest rate swaps are used for both hedging and speculating. U.S. dollar interest rate swaps typically reference the 3-month LIBOR index for the floating rate payment.

16. Interest rate swaps can be transacted on a cleared or uncleared basis. Cleared swaps are generally negotiated bilaterally, but are then submitted to a clearinghouse for clearing, and the clearinghouse becomes the central counterparty to swaps with each bilateral party. Cleared swap futures—including the IDCH Contract at issue here—are both centrally cleared and traded on an exchange.

17. In contrast with cleared swaps, uncleared swaps are swaps that are not booked with a clearinghouse, but instead are transacted bilaterally (over-the-counter)

without being cleared. The parties to an uncleared swap transaction therefore are directly responsible to each other for performance (including collateral payments), whereas in the case of cleared financial instruments, such as the IDCH Contract, each party's payment obligations are to the clearinghouse.

18. Swaps and swap futures are typically valued, or "marked to market," on a regular basis. For cleared swaps and swap futures, the clearinghouse generally determines the settlement (*i.e.*, closing) price at which a swap is valued. The party that has a marked-to-market loss on the transaction is typically required to provide variation margin to the clearinghouse, which is then passed on to the other party. For uncleared swaps, one or both of the parties determine the value of the swap. The party that has a marked-to-market loss on the transaction is typically required to post collateral with the other party. DRW (and others) believed and stated publicly during the Relevant Period that different cash flows caused by the difference between the contractual terms governing variation margin and collateral meant that IDCH Contracts and OTC swaps should have traded at different prices.

B. DRW's Participation In The Interest Rate Swap Futures Markets

19. Beginning in or about the first few months of 2010, IDCH began offering an interest rate swap futures contract.

20. During the Relevant Period, there was no statutory provision or CFTC rule, regulation or pronouncement governing the pricing of interest rate swap futures. In particular, the CFTC had never specifically addressed the issue under what circumstances it would consider an order in such a market to not reflect legitimate demand (especially in the case of illiquid markets such as those for IDCH Contracts). The CFTC also had never

provided published guidelines indicating when it believed that an interest rate swap futures contract and a comparable uncleared OTC swap were economically equivalent, or how they would be treated as such for purposes of its anti-manipulation rule.

21. DRW entered the IDCH Contract market in approximately August of 2010.

22. During the Relevant Period, there were only a few other market participants in addition to DRW.

23. Throughout the Relevant Period, DRW placed legitimate orders in IDCH Contracts through a voice-broker at Newedge.

24. From January 24, 2011 through sometime in August 2011, DRW additionally submitted legitimate orders electronically to the IDCH trading platform. Most of the electronic and voice-broker orders transmitted through Newedge were at different prices than those prevailing in the market for comparable OTC uncleared swaps. This was because DRW believed, based on its analysis of the economic difference between the two derivatives, that the IDCH Contracts should be trading at a different price than those of comparable uncleared OTC swaps. DRW used the same model to price its orders irrespective of whether the orders were submitted through the voice-broker or electronically.

25. To determine the daily settlement prices of the newly created IDCH Contract, IDCH rules provided that the clearinghouse could, if it chose to, reference posted bids and offers. IDCH had “sole discretion” under Rule 1002(i) of its Rules—which set forth the process for determining the daily settlement price of the IDCH Contract during the Relevant Period—to establish a price that was “a fair and appropriate reflection of the

market.” The CFTC was aware of IDCH’s rules for determining settlement prices and did not object to them.

26. The orders DRW placed through the voice broker were not referenced in the determination of settlement prices. IDCH chose to reference only orders submitted electronically in determining settlement prices. As stated above, DRW began entering legitimate orders electronically on or about January 24, 2011. Due to the illiquidity of the IDCH Contract market, DRW’s orders, when entered electronically and referenced by IDCH, naturally affected the daily settlement prices. These orders were firm, transparent and based on DRW’s analysis of the value of the IDCH Contracts and its expectation to earn profit from transactions executed thereby.

27. In March 2011, a market participant (“MP”) trading in the IDCH market complained to IDCH that “because IDCH does not apply a price alignment interest (“PAI”) adjustment to the IDCH Contract, these swap future contracts are not the economic equivalent of the original over-the-counter swap agreements that they replaced.” This MP maintained that applying such an adjustment would have made the IDCH Contract more economically similar to a comparable uncleared swap. This MP sought the “retroactive application of PAI to the swap futures contract.” This MP also wrote to the CFTC’s Office of the Inspector General, claiming that the IDCH had misleadingly characterized the IDCH Contract as equivalent to uncleared swaps and requesting an investigation of IDCH’s refusal to amend the IDCH Contract to include a PAI adjustment.

28. In response, IDCH acknowledged that it “d[id] not apply a PAI adjustment to its swap futures contract[s]” and noted that there was “no mention of PAI in the contract

specifications” or its Rule 1002. At the same time, IDCH further acknowledged that the assumption “that swap contracts should have the same price regardless of whether or how they are cleared” was “mistaken.”

29. Although nothing in its rules required it to consider DRW’s or any other market participant’s orders when establishing settlement prices, IDCH further explained that it chose to rely on “posted bids and offers,” which it believed provided a more accurate method of valuing its contracts because those bids and offers are “actionable, receive guaranteed clearing treatment, and necessarily reflect the exact contract specifications and clearing model of the IDCH itself.”

30. The CFTC’s Division of Clearing and Intermediary Oversight (“DCIO”) on June 7, 2011, found that “neither the contract specifications nor IDCH Rule 1002 contemplates any PAI adjustment for the [IDCH Contract],” and further found that “[t]he incorporation of these [posted] bids and offers when available, and the resultant change in settlement prices [for the IDCH Contract], does not establish that IDCH has altered its methodology for calculating the settlement price for these contracts.” In other words, the CFTC (DCIO) during the Relevant Period was informed that IDCH Contracts were *not* the economic equivalent of comparable uncleared OTC swaps and did not make any pronouncements to the contrary.

31. Rather, DCIO left in place the feature of the IDCH Contracts that was the driver of DRW’s trading strategy. This reconfirmed DRW’s belief that its orders relating to the IDCH Contracts were both consistent with exchange rules and based upon a recognized economic feature of the instruments.

32. DRW had to derive its orders in the IDCH Market without any published guidance from the CFTC (or other applicable authority) as to how a regulator would identify an economically equivalent instrument as the basis of “fair market value.”

33. In fact, the CFTC itself has acknowledged that the issue whether certain uncleared swaps are economically equivalent to certain swap futures requires more specific guidance. The CFTC waded into this area in an announcement issued after the Relevant Period regarding a public roundtable to discuss proposed rules designed to implement the amendments to the CEA. In that announcement, the CFTC acknowledged the need to establish rules addressing “the meaning and parameters of ‘economically equivalent swap’” that must be used by clearing organizations to meet reporting and other obligations. The final rule issued by the CFTC (17 CFR § 151.2 (“Position Limits for Futures and Swaps”)), however, only provided position limit requirements (which were subsequently struck down by a federal court as economically unnecessary and not required by the amended CEA) purporting to address the issue of under what circumstances, for purposes of *those* specific rule requirements, a *commodity* swap futures contract would be considered to be economically equivalent to a comparable OTC swap. There still is no rule that is specifically applicable to *financial* swaps contracts and swap futures like the ones at issue here.

C. The Dispute Leading Up To The Imminent Enforcement Action

34. In approximately August 2011, the CFTC’s Enforcement Division (“Enforcement”) commenced an inquiry into DRW’s trading of the IDCH Contract during the Relevant Period. In the course of the inquiry, the CFTC indicated that the basis for its inquiry was its belief that DRW’s orders were intended to affect the

settlement price and they were entered at something other than a fair and reasonable value because, according to the CFTC, such orders might have deviated to an unacceptable extent from the prevailing market prices for comparable uncleared OTC swaps at that time.

35. At the conclusion of its inquiry, which included testimony from Mr. Wilson, on April 23, 2013 the CFTC issued a Wells Notice indicating the agency's preliminary intent to recommend to the Commission that it commence an enforcement action against DRW for allegedly engaging in market manipulative trading activities in connection with the IDCH Contract.

36. DRW sent its Wells Submission in response on May 24, 2013. In its Wells Submission, DRW stated that (a) there were never many market participants in the IDCH Contract market and, as a consequence, the orders of DRW affected the daily settlement price of the IDCH Contract because IDCH chose to reference those orders in calculating settlement prices; (b) it was apparent to DRW based upon its analysis of the terms of the IDCH Contract that it was not economically equivalent to a comparable uncleared OTC swap because IDCH did not include an adjustment for the differences between variation margin and collateral; (c) DRW submitted orders based upon an analysis it performed on this complex financial derivative indicating that the IDCH Contract should trade at a different price than an uncleared swap; (d) DRW consequently traded and attempted to trade at values that it considered to be fair and reasonable in light of its analysis and that reflected its belief that the IDCH Contract should trade at a different price; (e) all of DRW's orders were firm and transparent, and each of DRW's orders was posted for more than sufficient time for trades to occur; and (f) because subsequent events demonstrate

that DRW was correct in its analysis of the valuation of the IDCH Contract vis-à-vis the valuation of an uncleared OTC swap, and because the CFTC did not dispute that there was any indication that DRW's orders were otherwise not made in good faith or otherwise not based on a fair and reasonable value of the IDCH Contract, there was no basis for contending that those orders were in any way manipulative and intended to lead to an artificial price.

37. On approximately August 2, 2013, the CFTC informed DRW that it had rejected the explanation provided in the Wells Submission and planned to recommend an enforcement action against DRW, and proceed to an enforcement action imminently.

COUNT I

DECLARATORY JUDGMENT

The Theory Of Liability Upon Which The CFTC's Imminent Enforcement Action Is Based Is Unconstitutional On Its Face Or As Applied To DRW In This Case

38. DRW adopts and incorporates each of the foregoing allegations of this Complaint as if hereinafter set forth in full.

39. The CFTC is effectively applying a new and previously unstated standard for determining whether a market participant's order does not reflect the legitimate forces of supply and demand: if the order does not track the prevailing price of a comparable uncleared OTC swap—irrespective of whether there are legitimate differences in the economic characteristics of the two instruments—the market participant can be exposed to liability for market manipulation under the CFTC's construction of the CEA when the market participant's trading activity could affect prices.

40. By threatening and proceeding to an imminent enforcement action against DRW for being involved in allegedly manipulative trading activities of the IDCH

Contract, the CFTC has violated DRW's constitutional right as a matter of substantive due process to be free from arbitrary and unreasonable government action and to receive adequate prior notice of the unlawfulness of conduct.

41. The issue raised solely requires a legal determination by this Court that there was no statutory provision, rule or regulation that provided DRW with the fair warning required as a matter of due process that its conduct during the Relevant Period might expose it to a market manipulation claim as well as liability and penalties.

42. DRW Investments and its affiliates will be subject to hardship and immediate and irreparable harm in the event the CFTC is able to proceed with filing and litigating an enforcement action against DRW Investments for market manipulation. Specifically, as set forth in detail in the Declaration of Craig Silberberg (Ex. A) :

- a. The CFTC's expected action will lead to the destruction of certain of DRW Investments' businesses. Specifically, DRW Investments is registered as the designated primary market maker in variance swap futures contracts on the CBOE Futures Exchange. This is a fledgling market, which competes with the uncleared OTC market for variance swaps in a manner that is generally consistent with the objectives of the Dodd-Frank Act. Because this is a new and illiquid market, DRW's orders have a definite impact on settlement prices. If DRW is forced to stop providing liquidity in the contract and to withdraw as a market maker, however, the contract will have no chance of being successful. Generally, once a futures contract fails, it is almost impossible to resurrect it.

- b. DRW Investments and its predecessors have been providing liquidity in Eurodollar Options since 1992, and an affiliate of DRW Investments has been providing liquidity in Natural Gas Options since 2002. A formal statement from the CFTC that it believes that DRW Investments' conduct in certain trading in illiquid markets was unlawful would force DRW Investments and its affiliates to exit the liquidity providing businesses as they currently exist in order to protect DRW Investments and its employees. DRW Investments and its affiliates have over many years developed excellent reputations in both the Eurodollar Options market and the Natural Gas Options market as important liquidity providers, and even if DRW Investments were to eventually prevail over the CFTC, the destruction of DRW Investments' liquidity providing businesses once it were forced to exit these markets would have already occurred. Moreover, considerable barriers to entry would make it extremely difficult, if not impossible, for DRW Investments to re-establish itself in these businesses once it had exited.
- c. DRW Investments' reputation will be harmed and its business goodwill—particularly in operating in financial markets and trading with counterparties participating in them—will be impaired by the CFTC's filing of charges, irrespective of whether the CFTC's charges are supported by law.

43. DRW Investments and its affiliates currently engage in the trading of numerous financial instruments on various exchanges in which the market is highly

illiquid and they believe that their orders could be referenced by the exchange in determining daily settlement prices. Because the CFTC lacks a proper guideline for determining what constitutes “legitimate supply and demand” for a financial instrument in an illiquid market, DRW Investments and its affiliates are therefore forced to operate under the constant threat of arbitrary enforcement activity, which impacts day-to-day decisions regarding resource allocation and prevents the Company from conducting its normal business operations. Specifically, as described above, if the imminent enforcement action is allowed to proceed it will shut down those units of DRW’s business that provide liquidity to certain markets.

44. Donald Wilson, as the founder and Chief Executive Officer, will suffer irreparable harm if he and DRW are defendants in the intended enforcement action. As DRW’s founder and Chief Executive Officer, his reputation in the industry is inextricably tied to DRW’s reputation and ability to carry on its business.

45. A declaratory judgment would eliminate uncertainty in the financial derivatives markets regarding whether it is actionable Commodity Exchange Act manipulation for one to place orders for a swap future that can affect settlement prices and are at a price divergent from that of a comparable—but not economically equivalent—OTC swap.

46. Additionally, enjoining CFTC’s unconstitutional action until the resolution of this threshold legal issue by the Court would promote the public interest. In the aftermath of Dodd-Frank and its effort to move trading away from bilateral OTC exchanges to more transparent clearing and trading venues, the CFTC’s enforcement action will inhibit the precise type of detection and correction of inefficiency that DRW accomplished here, and

ultimately discourage trading on cleared exchanges so long as participants' legitimate open-market, transparent orders at prices may render them subject to arbitrary enforcement action.

47. DRW has a direct and vital interest in having this issue resolved.

PRAYER FOR RELIEF

48. WHEREFORE, DRW respectfully requests that this Court issue a Declaratory Judgment that:

A. Declares that the CFTC's imminent enforcement action against DRW asserting market manipulation claims is in violation of the constitutional right of DRW and similarly situated parties to due process of law and freedom from arbitrary and unreasonable government action.

B. Enjoins the CFTC from filing an enforcement action against DRW Investments, LLC or Donald R. Wilson Jr. for violation of the anti-manipulation provisions of the Commodity Exchange Act, 7 U.S.C. §§ 9, 13(b), 13(a)(2) and 13c(a), based on open market orders placed in the IDCH Contract between January 2011 and August 2011, where intent to create an artificial price is based on the facts described in the Complaint.

C. Grants such other and further relief as the Court deems just and equitable.