UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS,
EASTERN DIVISION

U.S. COMMODITY FUTURES TRADING COMMISSION Plaintiffs, v. IGOR B. OYSTACHER and 3 RED TRADING LLC, Defendants.	Case No. 15-cv-9196 Hon. Amy J. St. Eve

MEMORANDUM OF 3 RED TRADING, LLC AND IGOR OYSTACHER IN OPPOSITION TO PLAINTIFF'S MOTION FOR PRELIMINARY INJUNCTION

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Igor Oystacher is not a computer. He is a manual trader. As such, his strengths and weaknesses differ from those of the high-frequency algorithmic trading firms that dominate the electronic futures markets. And because his strategies are tailored accordingly, his trading patterns do not fit the mold to which the algorithms—or the CFTC—have apparently become accustomed. Mr. Oystacher's orders are big. They are frequent. And, by human standards, he places his orders very quickly. Because of this, the CFTC and the algorithmic trading firms with which it is aligned have decided that Mr. Oystacher's trading is anomalous. They now ask this Court to conclude that it is improper. But placing large orders that comply with exchange limits is not illegal; neither is placing orders "too quickly" or "too often." And Mr. Oystacher has no obligation to trade in a way that enables the algorithms to profit.

The CFTC concedes that "spoofing" is difficult to parse from legitimate conduct. *See* PI Mot. Mem. (ECF No. 20-1) ("PI Motion") at 32 ("[S]poofing is inherently difficult to detect"). This case illustrates that point well. The CFTC spent more than four years determining whether it had a colorable claim. It then waited another month before seeking a preliminary injunction. Relying on result-oriented and arbitrary criteria that it reverse-engineered solely for this case, *see infra* Part II.B, the CFTC now purports to challenge a minute sub-set of Mr. Oystacher's trading between December 2011 and February 2016. To that end, the CFTC contends that Mr. Oystacher must have "spoofed" the market primarily because he placed certain orders and then cancelled them within one second. Never mind that one second is an eternity in modern markets. *See infra* Part III. Never mind that trained professionals are demonstrably able to process and react to relevant information within just a fraction of that time. *See id.* And never mind that algorithms typically do so even faster. *See id.*

The CFTC also contends that Mr. Oystacher used his wash-blocker to further the so-called "spoofing" scheme in violation of Rule 180.1 (Count II) because the wash-blocker cancelled the original orders[1] almost simultaneously with the placement of new orders in the opposite direction -- a practice known as "flipping." But even the CFTC's witnesses concede that flipping occurs "every few seconds" and is not itself improper. *See infra* Part I.C. They also recognize that simultaneous order cancellation and replacement is precisely what wash-blockers are designed--and made available by both the exchanges and the publicly-available trading platform that Mr. Oystacher used—to accomplish.

Notwithstanding its implausibility, the CFTC relies on this "spoofing" theory to conclude that Mr. Oystacher never intended to execute his original orders. On that basis, the CFTC seeks to ban him from trading in the six markets with which he is most familiar, pending the outcome of a trial that has yet to be scheduled. The request is more than extraordinary. It is meritless.

A preliminary injunction is an extreme remedy. It is not simply to be awarded upon request. Instead, the Court must conduct an appropriately searching inquiry. This is particularly important where, as here, the injunction would drastically alter the status quo, *see infra* Part I.A, based upon a novel provision of law that is hotly disputed, *see infra* Parts A & I.B. In far less egregious circumstances, courts have required regulators to make a "more persuasive" and "substantial showing" that they are likely to succeed on the merits and that the conduct is likely to recur. This Court should follow suit.

Regardless of what standard the Court chooses to apply, the CFTC ultimately cannot establish that Mr. Oystacher "spoofed" any market. To be sure, the competent evidence reflects

[1] For purposes of this brief, the term "original order(s)" refers to what Professor Bessembinder calls the "cancel-side order(s)," and the term "new order(s)" refers to what Professor Bessembinder calls the "trade-side order(s)."

that when Mr. Oystacher submitted his bids and offers, he was willing to honor them. *See infra* Part II.A. Just as importantly, the components of Mr. Oystacher's trading are all legitimate and customary industry practices. *Id.*; *see also infra* Part II.B. Certainly, there has never been any requirement as to how long an order must rest, or how limited in size it must be beyond the exchange's position limits, before a trader may cancel it; nor does any industry authority outlaw the placement of new orders in the opposite direction following such a cancellation. *See infra* Part II.A. The flawed analysis of the CFTC's purported expert does not establish otherwise. *See infra* Part II.B.

A similar analysis applies to Mr. Oystacher's use of his wash-blocker. He used the wash-blocker to comply with the law; not violate it. Indeed, the wash-blocker's speed is not the result of any nefarious plan, but rather of software that the exchanges and common third-party systems offer. *See infra* Part II.C. And because there was never any "spoofing" scheme, *see infra* Parts II.A & II.B, Mr. Oystacher cannot have employed the wash-blocker to further one. *See infra* Part II.C.

Finally, Mr. Oystacher is not a threat to the market. *See infra* Part III. If he was, then the exchanges would not currently permit him to trade. The CFTC would also have filed the PI Motion sooner, together with the Complaint (as it typically does when it fears future violations), or sought a more aggressive approach to cease his trading years ago. In any event, 3 Red has voluntarily modified Mr. Oystacher's trading in several ways that, together with internal controls, substantially eliminate the likelihood that future orders may be misinterpreted as "spoofing."

For each of these reasons and the ones set forth below, 3 Red respectfully requests that the Court deny the PI Motion in its entirety.

BACKGROUND

A. The Spoofing Provision[2]

As part of the Dodd-Frank Wall Street Reform and Consumer Protection Act, Congress added on July 21, 2010 a new provision to the Commodity Exchange Act (the "Act") that prohibits futures traders from engaging in "any trading, practice, or conduct that . . . is, is of the character of, or is commonly known to the trade as, 'spoofing' (bidding or offering with the intent to cancel the bid or offer before execution)." Commodity Exchange Act, 7 U.S.C. § 6c(a)(5)(C) (2012) (the "Spoofing Provision"). Since then, the industry has struggled to comprehend what that means. This is not only because the statute hinges on a colloquial term that did not even exist in the futures industry at the time (much less have a common definition, *see, e.g.*, Ex. 1 to Declaration of Kimberly Perrotta Cole in Support of Igor Oystacher and 3 Red Trading LLC's memorandum in opposition to Plaintiff's Motion for Preliminary Injunction (Apr. 1, 2016) ("Cole Decl."), Proposed Interpretive Order: Antidisruptive Practices Authority, 76 Fed. Reg. 14944 (issued Feb. 24, 2011; published Mar. 18, 2011) (the "Proposed Order")), but because the CFTC has failed to develop any meaningful standards for distinguishing between: (i) actual "spoofing;" and (ii) conduct that objectively looks like "spoofing," but is undertaken ***without*** the intent to "cancel . . . before execution." There is even less clarity regarding how the CFTC will identify conduct that is not "spoofing," but is somehow "of the character of" it.

[2] We are mindful of the Court's order of February 1, 2016, *see* Minute Entry (Feb. 1, 2016) (ECF No. 68), which exempts from the PI Hearing the various Constitutional and other challenges that 3 Red has raised as affirmative defenses. 3 Red presents here the history of the Spoofing Provision and relevant administrative interpretations for two primary reasons: (i) to provide the requisite context and foundation for the arguments set forth below in Part I.C, regarding why the circumstances justify the Court's application of a heightened preliminary injunction standard under *Unifund*, 910 F.2d at 1039 and its progeny; and (ii) to demonstrate that Mr. Oystacher was unable to comprehend in advance what trading behavior would be deemed to qualify as "spoofing."

Cancelling a trade has never been illegal, and there has never been any statute, rule, or regulation specifying a minimum period of time for which a trade must rest before a trader may cancel it. *See, e.g.*, Deposition of Hendrik Bessembinder (Mar. 23, 2016) ("Bessembinder Tr.") at 247:19-23 (conceding that cancelling a trade has never been illegal "to [his] knowledge"); Ex. 2 to Cole Decl., Excerpts of Deposition of CFTC Investigator Joy McCormack (Mar. 2, 2016) ("McCormack Tr.") at 282:14-283:5 ("It is my understanding that there is no set industry standard for how long an order has to be resting before it can be canceled."); *see also, e.g.*, Expert Report of Jerry W. Markham (Feb. 26, 2016) (ECF No. 81) ("Markham Rep.") at ¶ 113. The same is true of placing a new order on the other side of the market following such a cancellation ("flipping"). *See, e.g.*, Markham Rep. at ¶ 99; *see also* Deposition of Jerry W. Markham (Mar. 21, 2016) ("Markham Tr.") at 173:17-174:5 (stating that "flipping can be part of a legitimate trading strategy"). In fact, cancellations and flips have long been routine in the futures markets and are necessary to pursue any number of legitimate objectives. *See* Markham Rep. at ¶¶ 76, 99, 113; *see also* Expert Report of Daniel R. Fischel (Feb. 26, 2016) (ECF No. 80) at ¶ 9; McCormack Tr. at 82:10-12 ("flipping occurs every day thousands of times in the marketplace."); May Tr. at 225:19-227:10 (explaining that the market flips "once every few seconds"); Bessembinder Tr. at 248:9-14 (conceding that "cancellations and flips can occur pursuant to legitimate trading strategies"). For this reason, Congress tasked the CFTC with the obligation to "make and promulgate such rules and regulations as, in the judgment of the C[FTC], are reasonably necessary to prohibit the trading practices described in" the Spoofing Provision. Commodity Exchange Act, 7 U.S.C. § 6c(a)(6) (2012).

Recognizing both the need for additional clarity and its obligation to provide it, the CFTC initially sought to promulgate rules that would inform market participants of how the CFTC

would distinguish "spoofing" from customary trading. To that end, on November 2, 2010, the CFTC issued an Advanced Notice of Proposed Rulemaking. *See* Ex. 3 to Cole Decl., Advance Notice of Proposed Rulemaking; Request for Comments: Antidisruptive Practices Authority Contained in the Dodd-Frank Wall Street Reform and Consumer Protection Act, 75 Fed. Reg. 67301-03 (Nov. 2, 2010) (the "ANPR"). The ANPR identified more than nineteen issues for public comment. Appropriately, they included:

- Whether to "provide additional guidance as to the nature of the conduct that is prohibited by" the Spoofing Provision;
- How to distinguish "spoofing" from legitimate trading activity;
- Whether "submitting or cancelling multiple bids or offers to create an appearance of market depth that is false" qualifies as "spoofing"; and
- How "to more clearly distinguish the practice of [']spoofing['] from the submission, modification, and cancelation of orders that may occur in the normal course of business."

Id. at 67302.

Dozens of market participants provided input before the comment period closed on January 3, 2011. *See* Ex. 4 to Cole Decl., Advanced Notice of Proposed Rulemaking; Notice of Termination: Antidisruptive Practice Authority, 76 Fed. Reg. 14826 (Mar. 18, 2011) ("Termination Notice"). Of particular relevance here, they conveyed that there was "no commonly-accepted definition of 'spoofing' throughout the industry." *See* Proposed Order at 14943, 14947; *see also, e.g.*, Ex. 5 to Cole Decl., Comment Letter from John M. Damgard (President of FIA) (Dec. 23, 2010) ("Damgard Comment Letter") at 1, 3, 6 ("[T]he term 'spoofing' is not one that has been commonly used in the futures and derivatives markets and there is no generally understood or accepted meaning of the term in this context"); Ex. 6 to Cole Decl., Comment Letter of Stuart J. Kaswell (General Counsel of Managed Funds Ass'n) at 7

(Dec. 28, 2010) ("'[S]poofing' is not a term that has ever been commonly used in the futures and derivatives markets. . . . [I]ts application in [those] . . . markets is not at all clear"). They therefore stressed the need for "additional Commission guidance [so] that any definition of 'spoofing' . . . would not capture legitimate trading behavior." *See* Proposed Order at 14947; *see also* Ex. 7 to Cole Decl., Comment Letter of Craig S. Donohue (CEO of CME Group) (Jan. 3, 2011) ("Donohue Comment Letter") at 8 ("[T]he statute's definition of 'spoofing' . . . is too broad and does not differentiate legitimate market conduct from manipulative conduct that should be prohibited").

The CFTC also held a roundtable discussion on December 2, 2010. *See* Ex. 8 to Cole Decl., CFTC Staff Roundtable on Disruptive Trading Practices (December 2, 2010) ("Roundtable Tr.").[3] Once again, multiple speakers underscored that there was no industry consensus as to what "spoofing" was. *See* Roundtable Tr. at 64:3-8 ("[I] really don't know what spoofing is . . . and I'm not sure [i]f the definition of spoofing can be agreed upon by the ten people around this table"); *id.* at 81:18-22 ("[T]he recurring theme in terms of spoofing that I hear is . . . I don't know how to define it, but I know it when I see it"); *id.* 96:19-97:1 ("[T]here seems to be a notion that somehow spoofing and the life of orders or the speed with which they're entered and canceled[] are . . . tightly connected and I don't think that that's necessarily the case"); *id.* at 111:16-18 ("[I]f you're putting orders out that are taking risk, can you be defined as spoofing?").[4] In fact, the term "spoofing" had never been used in a futures industry treatise; did not previously surface in any futures industry statute, rule or regulation; and had not

[3] Available at http://www.cftc.gov/idc/groups/public/@swaps/documents/dfsubmission/dfsubmission24_120210-transcri.pdf (last accessed March 30, 2016).

[4] *See also id.* at 171:10-11 ("I'm not quite sure I know what spoofing is"); *id.* at 166:12-17 ("[U]nlike pornography, I'm not even sure I know disruptive trading when I see it, and so there's a great deal more effort that's required for us to be able to get to the point where we can start thinking about what it really means").

been construed by a court of law. *See, e.g., id.* at 171:21-172:5. Nor was there anything else "commonly used in the industry to define the[]. . . terms . . . in the statute." *Id.* The speakers therefore expressed concern that absent workable standards, the CFTC might target well-intended cancellations that, with the benefit of hindsight, appear to resemble "spoofing." *See, e.g., id.* at 41:5-42:5 (noting, in relevant part, that "[i]f rules are not clear, or if rules are backward looking," then there is a risk that orders may be "after the fact deemed to be disruptive" based merely on their apparent effects and not based on the requisite intent).

The CFTC again recognized the industry's need for additional guidance. *See* Proposed Order at 14944 ("The Commission is issuing this proposed interpretive order to provide market participants and the public with guidance on the scope of the statutory prohibitions set forth in section 4c(a)(5)"). Nevertheless, it terminated the ANPR on March 18, 2011, without having promulgated a single rule or regulation. *See generally* Termination Notice. Instead, the CFTC published a proposed interpretive order (the "Proposed Order") that merely re-stated the obvious: "legitimate, good faith attempt[s] to consummate a trade" would not constitute "spoofing." *See* Proposed Order at 14947. The Proposed Order then supplied a "non-exclusive" list of four examples that, in the CFTC's view, ***do*** qualify as "spoofing." *Id.* Each of them turned on the trader's subjective purpose rather than on her conduct. *Id.*

One such example was the "submi[ssion] or cancel[ation of] multiple bids or offers to create an appearance of false market depth." *Id.* Crucially, the Proposed Order did not explain why the CFTC might conclude that a particular trade was not "part of a legitimate, good faith attempt to consummate a trade," but had rather been submitted for the purpose of "creat[ing] an appearance of false market depth." Instead, the Proposed Order described in one sentence a pliable enforcement policy pursuant to which the CFTC would supposedly "distinguish[] . . .

between legitimate trading and 'spoofing' by evaluating all of the facts and circumstances of each particular case, including a person's trading practices and patterns." *Id.* (emphasis added); *see also id.* (indicating that CFTC will ascertain intent by "evaluat[ing] the market context, the person's pattern of trading activity (including fill characteristics), and other relevant facts and circumstances").

The Proposed Order did not clarify the statute. As Commissioner Jill Sommers conveyed at the CFTC's open meeting on February 24, 2011, it "raised more questions than it answer[ed]." *See* Ex. 9 to Cole Decl., Comments of Commissioner Jill Sommers, CFTC Open Meeting on the Twelfth Series of Proposed Rulemakings Under the Dodd-Frank Act at ¶ 7 (Feb. 24, 2011) ("Comments of Commissioner Sommers"). In this regard, Commissioner Sommers specifically noted that she and her colleagues at the CFTC "belie[ved] . . . that the language [of the statute] was too vague" and that "clarifying rules would be [both] necessary and appropriate." *Id.* at ¶ 5. She underscored that this was also "the message" that the CFTC had "received from the public in response to the ANPR and the roundtable." *Id.* Because "this [Proposed Order] does not cure that vagueness," Commissioner Sommers voted against it. *Id.* at ¶ 7.

In the wake of the Proposed Order, market participants echoed Commissioner Sommers' sentiments. They continued to call for "additional guidance and suggested that additional clarity was needed regarding how the Commission would interpret and apply" the Spoofing Provision. *See* Ex. 10 to Cole Decl., Antidisruptive Practices Authority, Interpretive Guidance & Policy Statement, 78 Fed. Reg. 31890-01 at *31891 (May 28, 2013). Yet again, commentators stressed that if the CFTC did not develop clear boundaries, then the Spoofing Provision would "capture legitimate trading practices that may be indistinguishable from the proposed prohibited conduct." *Id.*

The CFTC never issued any rule, final order or other meaningful guidance. Instead, it published on May 28, 2013, an "interpretive guidance and policy statement" (the "Policy Statement") that parrots the Proposed Order. *See* Policy Statement at 31892.

B. This Case

i. Mr. Oystacher and 3 Red

3 Red is a proprietary trading firm with offices in Chicago and New York. *See* Declaration of Igor Oystacher (Apr. 1, 2016) ("Oystacher Declaration") at ¶ 6. Igor Oystacher is 3 Red's owner and principal trader. *See* Oystacher Decl. at ¶ 6; *see also* Ex. 11 to Cole Decl., Excerpts of Deposition of Igor Oystacher (March 10-11, 2016) ("Oystacher Tr.") at 23:16-18. He trades futures contracts manually, using a mouse, a screen, and a point-and-click protocol. *See* Oystacher Tr. at 44:2-8; *see also* Oystacher Decl. at ¶¶ 7, 9. He does not use algorithms. *See* Oystacher Tr. at 315:17-19. All of Mr. Oystacher's trading decisions are therefore the result of his own judgment and intuition, as well as the time that it takes to process relevant information ("signals") and then react. *See, e.g., id.* at 179:24-180:9; *see also* Oystacher Decl. at ¶ 11; Markham Tr. at 112:15-113:4 (explaining various factors that traders generally take into consideration when making decisions).

Mr. Oystacher immigrated to the United States from Russia in 1998. *See* Oystacher Decl. at ¶ 2. At the age of sixteen, he enrolled at Northwestern University, where he focused on math and economics. *Id.* at ¶ 3. In the summer following his sophomore year, Mr. Oystacher began trading financial instruments. *Id.*. He subsequently decided to pause his college studies so that he could pursue a trading career. *Id.* Mr. Oystacher began trading full-time in 2001 and has been developing and executing trading strategies ever since. *Id.*.

Mr. Oystacher was a competitive "speed chess" player in Russia. *Id.* at ¶ 22. He still plays today. *Id.* Speed chess is structured as a "single, sudden-death time control[]," is typically set at three or five minutes, and does not use a time delay. *See* US Chess Fed'n, Ch. 11: Blitz Chess, at 1, *available at* http://www.uschess.org/docs/gov/reports/BlitzRulesChanges.pdf; Oystacher Decl. ¶ 22. To excel, a speed chess player must therefore be able to process relevant information, forecast his opponents' actions, and react appropriately, all on an expedited timeline. Mr. Oystacher's success at speed chess is likely due to two talents: *first,* his "very superior abilities (above the 99th percentile)" with respect to "nonverbal reasoning," "complex pattern recognition," "performing mental calculations," and "applying mathematical concepts to practical problems of varying complexity;" and *second,* his above average ("91st percentile") reaction speeds for "highly familiar tasks." *See* Expert Report of Dr. Brian Leahy ("Leahy Rep.") at 4. In particular, reaction-time testing shows that Mr. Oystacher is capable of reacting to information within approximately 300 milliseconds—an interval that is very fast by human standards, but comparatively slow in relation to algorithmic traders. *See* Leahy Rep. at 4.

ii. Mr. Oystacher's Trading

Mr. Oystacher is a speculator. *See, e.g.*, Markham Rep. at ¶¶ 29-30, 63, 69-71; *see also* Markham Tr. at 130:9-19. Accordingly, he trades for 3 Red's own account, for the purpose of making a profit. *See* Markham Tr. at 121:14-122:3 (explaining that speculators are "seeking to profit by changes in the marketplace"). Sometimes he bets on the market; sometimes he bets against it. But every time Mr. Oystacher submits a bid or offer, he is willing to transact. *See* Oystacher Tr. at 453:18-22.

Mr. Oystacher's trading strategy is highly individual. It is also proprietary. *See* Ex. 12 to Cole Decl., Excerpts of Deposition of Gregory O'Connor (Mar. 7, 2016) ("O'Connor Tr.") at

27:10-28:2; *see also* Oystacher Decl. at ¶¶ 11, 17-19. He developed and refined this strategy through the investment of substantial resources, over the course of fifteen years. *See* Oystacher Decl. at ¶ 4. And because the success of 3 Red is dependent upon the success of Mr. Oystacher's trading, both 3 Red and Mr. Oystacher strive to keep competitors from unwinding his strategy. *See, e.g.*, Oystacher Tr. at 487:14-489:15; Oystacher Decl. at ¶ 10. If a competitor were to reverse-engineer it, then that competitor could, among other things, predict 3 Red's trades and profit at 3 Red's expense. *See* Markham Rep. at ¶ 105 (citing Interactive Brokers, *Iceberg/Reserve Orders*, available at https://www.interactivebrokers.comienl?f=%2Fen%2Ftrading%2Forders%2Ficeberg.php (accessed on Jan. 19, 2016)).

Order size is an important component of Mr. Oystacher's trading strategy. As a manual trader, he cannot actively manage numerous small orders at one time (as the algorithmic trading firms can do. *See infra* Part B.iv). Mr. Oystacher therefore chooses to transact in larger quantities. *See* Oystacher Decl. at ¶ 8. He thus balances the greater risks of larger order placement with the corresponding potential for reward. *Id.*

In general, Mr. Oystacher develops forecasts for the market and then trades accordingly. His forecasts are based on certain signals that, in his view, inform of potential price movements of particular futures contracts. *See* Markham Rep. at ¶¶ 51-52, 63, 70; Oystacher Decl. at ¶ 11. Two of the signals that Mr. Oystacher considers to be more useful are: (i) elasticity (i.e., the number of contracts transacted over a given period of time, compared to the price movement during that same period of time); and (ii) the characteristics of executed trades (e.g., how many consecutive contracts have traded at a given price and how quickly). *See id.*

One signal on which Mr. Oystacher does not rely as much is the level of market interest that is displayed in the order book ("book pressure"). *Id.* at ¶ 12. This is particularly true for markets that allow "Iceberg" orders.[5] *Id.* at ¶ 12. An Iceberg order is only partially displayed in the order book. *See* Markham Rep. at ¶ 135 (citing Financial Times, Definition of Iceberg Order, available at http://lexicon.ft.com/Term?term~icebergorder (accessed on Jan. 19, 2016)). The remainder is hidden. *Id.* Because the order book therefore reflects only a portion of actual interest, Mr. Oystacher does not consider book pressure to be a reliable proxy for true market depth. *See* Oystacher Decl. at ¶ 12.

To facilitate his trading, Mr. Oystacher combines aspects of several time-tested—and perfectly legitimate—industry practices:

1. *Charting*. As a chartist, Mr. Oystacher makes decisions based on his view of market data and the signals that he considers important. *See* Markham Rep. at ¶ 70; Oystacher Decl. at ¶ 17. This not only includes elasticity, but also information relating to correlated products. *See* Markham Rep. at ¶ 70; Oystacher Decl. at ¶¶ 11, 16. To optimize his charting, Mr. Oystacher uses a proprietary software program called Charter. *See* Oystacher Tr. at 130:7-23; *see also* Oystacher Decl. at ¶ 16. Charter receives market data from a third-party provider and then visually displays elasticity measurements and correlated market data in the form of charts. *See, e.g.*, Markham Rep. at ¶ 83; Oystacher Decl. at ¶ 16. The information appears on a screen (or set of screens) next to the ones that Mr. Oystacher uses for trading. *See* Oystacher Tr. at 138:17-139:23.

Mr. Oystacher also relies on information that is reflected on the "pricing ladder" display through which he enters his orders. *See, e.g.*, Oystacher Tr. at 233:1-18; *see also* Oystacher

[5] With the exception of VIX, each of the Relevant Markets permitted Iceberg orders during the relevant period. *See* CFTC Complaint (October 19, 2015) (ECF No. 1) ("Complaint") at ¶ 27.

Decl. at ¶ 15. Among other things, the pricing ladder reflects the price at which a particular product is trading, as well as Mr. Oystacher's current position (long or short) and the number of contracts that other market participants have bid and offered at the best prices (commonly five or ten prices on both sides of the market). *See* Oystacher Decl. at ¶ 15. It also shows Mr. Oystacher's pending orders at various prices and the number of contracts that he has already transacted at those prices. *Id.* By monitoring the pricing ladder information together with the Charter displays, Mr. Oystacher can track the elasticity of specific products, as well as the elasticity of those products in relation to others with which they are correlated. *See* Oystacher Tr. at 149:3-152:16; *see also* Markham Rep. at ¶ 70; Oystacher Decl. at ¶ 11.

2. *Scalping*. As a scalper, Mr. Oystacher seeks to profit from rapid price changes by moving quickly in and out of various positions. *See* Markham Rep. at ¶ 69. He attempts to benefit from even small changes in pricing. *See* Oystacher Decl. at ¶ 18; Markham Rep. at ¶¶ 69, 99. The result is increased market efficiency and more accurate pricing for market participants. *See* Markham Rep. at ¶ 69. Mr. Oystacher's superior reaction time abilities are particularly relevant to this aspect of his trading, as he makes rapid trading decisions based on information gathered after discerning patterns in rapidly shifting price ladders. *See* Oystacher Decl. at ¶ 15; *see also* Deposition of Dr. Brian Leahy (Mar. 24, 2016) ("Leahy Tr.") at 346:7-9, 360:11-361:24.

3. *Active Market Making*. As a market maker, Mr. Oystacher is not committed to either side of the market, but instead aims to profit by selling and buying. *See* Markham Rep. at ¶ 84; *see also* Oystacher Decl. at ¶ 17. By definition, Mr. Oystacher is therefore frequently active on both sides of the market (but not necessarily at the same time). *See, e.g.*, Markham Rep. at ¶ 84; Markham Tr. at 117:1-17; *id.* at 130:9-18.

4. *Market Taking.* Mr. Oystacher also sometimes acts as a market taker, meaning that he takes available liquidity in the market when it is advantageous to do so. *See* Oystacher Decl. at ¶ 17.

Mr. Oystacher's trading is fluid. *See* Oystacher Decl. at ¶¶ 18, 19. He recursively develops and revisits his predictions about relevant price movements and trends. *See id*. He then reacts intuitively by placing new orders that he considers advisable, or by withdrawing existing orders that he was originally willing to execute, but no longer desires. *See, e.g.*, Oystacher Tr. at 179:24-183:17. Mr. Oystacher may cancel an original order if, among other things:

- Prices or other conditions change in the specific market;
- Prices or other conditions change in a related market;
- Mr. Oystacher's forecasts change with respect to the particular product;
- Mr. Oystacher's forecasts change with respect to a correlated product;
- The orders are no longer needed because Mr. Oystacher has been filled to the desired level elsewhere;
- The existing order is not filled;
- The existing order is not filled as anticipated (i.e., within the desired time interval, or to the desired percentage);
- Mr. Oystacher perceives a need to obscure his trading from competitors; or
- There is momentum in a given or related market.

See Oystacher Decl. at ¶ 18; Markham Rep. at ¶ 75. In other circumstances, Mr. Oystacher may decide that the best course of action is to change his bias and flip—i.e., to both withdraw an original order and to submit a new order that he is willing to execute in the opposite direction. There are many reasons why Mr. Oystacher may decide to do this. They include, among others:

- To get ahead of a new price forecast;

- To conform to a revised view of the market;
- To position himself as a counterparty to a desired trade (rather than losing that trade to someone else);
- To withdraw an order that is not filled;
- To terminate a trade that has not been filled as desired (i.e., a trade that has only partially been filled);
- To chase a market that has begun to move away from him;
- To hedge or exit long or short positions; and
- Momentum in a given or related market.

See Oystacher Decl. at ¶ 19; Markham Tr. at 173:17-174:5; *see also, e.g.*, Bessembinder Tr. at 248:16-250:6 (acknowledging that there are numerous legitimate reasons for flipping, including the desire to withdraw an order that has not been filled and the desire to reduce a short position).[6]

iii. Mr. Oystacher's Trading Platforms and Functionalities

To optimize trading and compliance, Mr. Oystacher used certain order-entry platforms and computer functionalities during the Relevant Period.

Manual traders need basic access to the electronic exchanges and to order book displays. For this purpose, they use front-end order-entry platforms. *See* Oystacher Decl. at ¶ 13. Until early October of 2014, Mr. Oystacher used a third-party, off-the-shelf software product called X_Trader in combination with a proprietary add-on that 3 Red developed, called MoneyMaker. *See id.* The purpose of MoneyMaker was to overcome problems with, and to simplify the appearance of multiple sets of market data received through, X_Trader. *See id.* It also enabled universal order-entry applications across trading venues. *See id.* Mr. Oystacher switched from X_Trader and MoneyMaker to a different proprietary platform called PiCNIC in early October

[6] When a trader places an order and that order is not filled, that is, in and of itself, market information.

of 2014. *See, e.g.*, Oystacher Tr. at 128:5-7; *see also* O'Connor Tr. at 155:11-13. He still uses PiCNIC today. *See* Oystacher Tr. at 43:6-18. Through PiCNIC, Mr. Oystacher can implement enhanced safeguards that are customized to his trading and based upon the feedback that he receives from the exchanges. *See* Oystacher Decl. at ¶ 14.

Moreover, speed is of the essence in modern electronic futures markets, where sub-second algorithmic trading is the norm. *See* Markham Rep. at ¶ 113 (discussing trading that occurs within milliseconds or microseconds); *see also* Bessembinder Tr. at 406:7-24 (conceding that an algorithm can be programmed to enter a resting order and then cancel or flip to the other side of the market if that order is not hit within one millisecond). As the CFTC's own research shows, orders are commonly subject to execution even when they are exposed to the market for less than one second. *See* Ex. 13 to Cole Decl., Richard Haynes & John S. Roberts, *Automated Trading in Futures Markets,* at 9 (March 13, 2015) ("Haynes & Roberts Report"), available at: http://www.cftc.gov/idc/groups/

public/@economicanalysis/documents/file/oce_automatedtrading.pdf (last accessed March 23, 2016) ("Across the selected commodities, a significant fraction of passive execution activity happens within one second of order entry or modification). The time that it takes for an order to travel from Mr. Oystacher to the exchange, or for information about relevant signals to travel from the exchange to Mr. Oystacher, therefore introduces risk ("latency"). *See* Markham Rep. at ¶¶ 46-47. So does the amount of time that it takes Mr. Oystacher to click the button of his mouse or press a key on his keyboard. *Id.* The price of a contract may change in that time ("slippage"), as may the quantity bid or offered, and some of the other signals that are relevant to Mr. Oystacher's forecasts. *Id.* at ¶ 46. This is largely due to algorithmic trading activity, which

typically transpires within microseconds (one millionth of a second or 0.000001 seconds). *Id.* at ¶ 116 (citing authority).

To help mitigate the risks of latency and slippage and speed his trading, Mr. Oystacher configured his mouse to incorporate certain shortcuts. *See* Oystacher Decl. at ¶ 9. Specifically, the left button placed a large order for a pre-set number of contracts with just one click, and the right button placed a smaller order for fewer contracts. *See, e.g.,* Oystacher Tr. at 72:6-14; *see also* Oystacher Decl. at ¶ 9; Markham Rep. at ¶ 92. Because there are only two buttons on the mouse, and each corresponds to a set order size, it may take several clicks for Mr. Oystacher to achieve his desired total order size (thereby resulting in the placement of several orders at the same price). *See e.g.* Oystacher Tr. at 67:16-69:16; 72:7-14. Mr. Oystacher also configured a shortcut button on his keyboard for placing orders in Iceberg format. *See , e.g., id*. at 96:1-10; Oystacher Decl. at ¶ 9.

In addition, proprietary traders like Mr. Oystacher typically seek to avoid having competitors identify patterns in their trading. *See* Bessembinder Tr. at 315:5-24 (conceding that "it would be wise for a given trader to take into account that others might be trying to anticipate their . . . orders and strategies" and that "one might potentially randomize" certain aspects of trading for this reason); *see also* Markham Rep. at ¶ 105 ("Active traders. . .seek to avoid trading in predictable sizes, amounts or frequencies that can be detected by [high-frequency algorithmic trading systems]"). For this purpose, Mr. Oystacher used a randomizer. *Id.* at ¶¶ 92-93; *see also* Oystacher Tr. at 489:6-15. When enabled, the randomizer would cause either the left or right button of Mr. Oystacher's mouse to enter that slightly deviates from the default setting (up to, e.g., 10% more, or 10% fewer, contracts). *See* Oystacher Decl. at ¶ 10. He could also split a

single large order into a few smaller orders in order to avoid telegraphing his total desired quantity to other traders. *Id.*

Finally, intentional self-trades are generally illegal. *See* Commodity Exchange Act, 7 U.S.C. § 6c(a)(2) (2012). Among other things, such "wash sales" may be considered deceptive. *Id.; see also* Markham Rep. at ¶ 123. For this reason, both PiCNIC and X_Trader incorporated a standard "wash-blocker" function that immediately withdrew Mr. Oystacher's original order if that order could otherwise have been matched with a new order in the opposite direction. *See* O'Connor Tr. at 151:17-152:21; *see also* Oystacher Tr. at 193:10-196:8. Many exchanges offer this same functionality (including CME). *See, e.g.*, Ex. 14 to Cole Decl., Excerpts of Deposition of Richard Ting May (March 15, 2016) (the "May Tr.") [redacted]; McCormack Tr. 206:2-7 (acknowledging that some exchanges have made wash-blockers part of their own platforms); Ex. 15 to Cole Decl., Exchange Notice from ICE Futures U.S. (October 9, 2013) at 1 (mandating that some traders use exchange-provided wash-blocker).

iv. Modern Futures Markets

Manual traders like Mr. Oystacher are increasingly rare. Modern futures markets are largely dominated by sophisticated algorithmic trading firms. *See* Expert Report of Hendrik Bessembinder (November 2, 2015) (ECF No. 20-4) ("Bessembinder Rep.") at ¶ 11; *see also* Markham Rep. at ¶ 62 (citing Statement of CFTC Commissioner J. Christopher Giancarlo, *Regulation of Automated Trading*, 80 Fed. Reg. 78824, 78945 (Dec. 17, 2015) (noting that "algorithmic or automated trading . . . now constitutes up to seventy percent of regulated futures markets.")). This is particularly true of large equity futures markets, like the E-Mini Standard & Poor's 500 Stock Price Index futures contract that is traded on CME ("ES"). *See, e.g.*, Affidavit

of Richard May (October 8, 2015) (ECF No. 20-5) ("May Decl.") at ¶ 5 ("Citadel is consistently among the top five traders by volume of executed transactions in the E-Mini S&P 500 Contract"); *see also, e.g.*, Markham Rep. at ¶ 62 (citing Statement of CFTC Commissioner J. Christopher Giancarlo, *Regulation of Automated Trading*, 80 Fed. Reg. 78824, 78945 (Dec. 17, 2015)).

Unlike Mr. Oystacher, algorithmic trading firms do not transact based on intuition; nor are they cabined by human reflex. *See* Markham Rep. at ¶ 60; *see also* May Tr. at 246:17-247:2 (acknowledging that in general "[a] human cannot send orders as fast as a computer if they can only send one order per click of the mouse"). Instead, they rely on algorithms – i.e., automated systems that are structured to make trading decisions without the hindrances (or customization) of human intervention. *See* Ex. 16 to Cole Decl., Excerpts of Deposition of Matthew Wasko (March 11, 2016) ("Wasko Tr.") at 90:17-91:11; *see also* Markham Rep. at ¶ 56. These pre-set computer programs consider various factors and circumstances ("inputs") according to formulas that account for assorted sensitivities, forecasts, and other triggers. *See* May Tr. at 117:14-118:2; *see also* Wasko Tr. at 81:8-82:3; Markham Rep. at ¶ 56. Based on their automated analyses, the algorithms then decide whether to place, modify, cancel, or forego certain orders in particular markets. *See* Wasko Tr. at 63:3-7. They also determine how many orders to place, when to do so, with what bias, and at what price levels. *See* Markham Rep. at ¶ 56 (explaining that algorithms can "generate and execute orders without human intervention"). This is done within millionths of a second. *See* [redacted]; *see also* Wasko Tr. at 161:19-24; Markham Rep. at ¶¶ 115-116.

Algorithmic trading is controversial. This is due in no small part to the strength of the algorithmic trading lobby, which has obtained several forms of special treatment for algorithmic

traders. For example, the exchanges have long permitted algorithmic firms to rent space for their computer servers in the same room as the exchanges' own computers. *See* Bessembinder Tr. at 241:17-242:10; *see also* Markham Rep. at ¶ 57. By "co-locating" their servers, the algorithmic trading firms received and processed market signals directly from the exchanges, rather than having to wait for that information to reach an off-site server. *See* Bessembinder Tr. at 242:4-10 (explaining that co-location "reduces latency"); *see also* Markham Rep. at ¶ 57-58, 60. The exchanges also exempted algorithmic traders from having to route their orders through a futures commission merchant ("FCM") or clearing firm before then being sent onto the exchanges (as many manual traders must do – including Mr. Oystacher prior to October 2014). *See* Declaration of Gregory O'Connor ("O'Connor Decl.") (April 1, 2016) at ¶ 3.

The exchanges also facilitate the dominance of algorithmic traders through their exchange rebate programs. Those programs reduce fees for market participants that have a large number of executions. *See* Ex. 17 to Cole Decl., Excerpts of Deposition of Karen Christiansen (Feb. 24-25, 2016) ("Christiansen Tr.") at 141:9-142:14. Algorithmic trading firms are uniquely positioned to benefit because they are able to place, cancel, and otherwise manage large quantities of smaller orders extremely quickly. *See* Markham Rep. at ¶ 5. Manual traders like Mr. Oystacher do not have that same luxury. *Id.* at ¶ 62; [redacted]

There is much debate regarding how algorithmic trading affects the market. The algorithmic trading firms purport to supply liquidity and, on that basis, claim to benefit the market. But many industry participants take a different view. In fact, some scholars estimate that the algorithms are programmed to cancel 90-95% of the orders that they place. *See, e.g.*, Bessembinder Tr. at 169:3-23 (conceding that it is "ballpark correct" to say that over 90 percent of orders are cancelled in commodities markets); *see also* Haynes & Roberts Rep. at 9; Ex. 18 to

Cole Decl., SEC, *Trade-To-Order Volume Ratios*, (Oct. 9, 2013), available at http://www.sec.gov/marketstructure/research/highlight-2013-01.html#.Vppa TIZlvUI (accessed on Jan. 16, 2016); Markham Rep. at ¶ 76. The CFTC itself has reported that over 50% of market orders are canceled within half of a second in certain markets. *See* Haynes & Roberts Rep. at 9. The algorithmic trading firms have thus been faulted for supplying only "phantom liquidity" and for manipulating the markets. *See* Markham Rep. at ¶ 88; *cf. also* Ex. 19 to Cole Decl., Excerpts of Congressional Research Service Report, High Frequency Trading: Background, Concerns, and Regulatory Developments (June 19, 2014) at 18-19 (noting, in the analogous context of securities markets, that there is a "worry that the liquidity that is provided by high-frequency trades is often not quantitatively comparable to the liquidity provided by traditional market makers" and such liquidity "has been alternatively dubbed 'phantom liquidity' or 'flickering quotes'").[7]

Finally, many algorithms are programmed to reduce competition by poaching the strategies of other traders. To that end, the algorithms affirmatively seek to identify trading patterns and then to reverse-engineer them. *See* Markham Rep. at ¶ 105; *see also* Bessembinder Tr. at 252:15-253:5 (admitting that Bessembinder "wouldn't be surprised" to learn that algorithms unwind competitors' strategies). This undermines the value of their competitors' proprietary strategies.

v. 3 Red's Commitment to Compliance

Since the Spoofing Provision became effective, 3 Red and Mr. Oystacher have, like the rest of the industry, struggled to understand how regulators will separate true "spoofing" from

[7] Available at https://archive.org/stream/R43608High-FrequencyTradingBackgroundConcernsandRegulatoryDevelopments-crs/R43608%20High-Frequency%20Trading_%20Background%2C%20Concerns%2C%20and%20Regulatory%20Developments#page/n0/mode/1up (last accessed April 1, 2016).

legitimate trading that simply looks like it. *See, e.g.*, O'Connor Tr. at 203:19-204:17. Because the exchanges are self-regulated entities, each with its own unique interpretation of the relevant regulations in conjunction with its own rules, 3 Red has actively sought clarity and guidance directly from multiple exchanges. *See* O'Connor Decl. at ¶ 4. Despite these efforts, 3 Red has yet to receive any meaningful guidance. *See, e.g.*, O'Connor Tr. at 71:4-19 (noting that 3 Red has "tried to hold regular conversations," but that all exchanges other than CME "have either denied our request or . . . not responded at all"); *id.* at 201:24-202:10 (noting that 3 Red approached CME, but the exchange was "not as responsive to our requests for information or guidance"); *cf.* [redacted]

From time to time, 3 Red has learned that certain competitors have lodged complaints about 3 Red's trading. *See, e.g.*, O'Connor Tr. at 252:15-253:4. In general, the complaints appear to have been filed by algorithmic trading firms that purport to have identified orders that, in their view, look like "spoofing." *See* PI Mot. at 16; *see also* [redacted] Notwithstanding the lack of certainty regarding what "spoofing" even is, *see supra* Part A, 3 Red's current Chief Compliance Officer, Greg O'Connor, has consistently sought throughout his tenure, together with Mr. Oystacher, to resolve these complaints as promptly as possible. *See* O'Connor Decl. at ¶ 8.[8] To that end, 3Red has met with representatives from CME and Eurex to

[8] Mr. O'Connor began his tenure in July 2013 by seeking to reopen constructive and cooperative lines of communication between 3 Red and the exchanges. *See* O'Connor Decl. at ¶ 6; [redacted]. He made this a priority because communications with the exchanges had been mismanaged by his predecessor (3 Red's former Chief Compliance Officer, Edwin Johnson). O'Connor Decl. at ¶¶ 4, 17. For example, in connection with an inquiry that Eurex made about 3 Red's trading, Mr. Johnson's responses were overly generic, not particularly helpful, and therefore vulnerable to being misinterpreted as evasive. *See* O'Connor Decl. at ¶ 4; *see also* [redacted] Mr. Johnson had also apparently

explore in detail the relevant trade data pertaining to competitor complaints. *See* O'Connor Decl. at ¶ 4. At each such meeting, 3 Red has specifically sought insight as to why the orders may be misperceived as "spoofing" or disruptive trading and how Mr. Oystacher can best modify his trading so that such misunderstandings do not recur. *See* O'Connor Decl. at ¶ 9.

No regulator has provided 3 Red with a helpful response. *See, e.g.*, O'Connor Tr. at 71:4-19; *id.* at 201:24-202:10. In fact, the majority of them (including CFE, ICE US, ICE Europe, and the Trading Surveillance Office of the Frankfurt Stock Exchang) have simply refused to engage in a substantive dialogue with 3 Red. *See, e.g.*, *id.* at 71:4-19; *see also* O'Connor Decl. at ¶ 10. As a result, 3 Red has had to proceed based on its own judgment. In this regard, it has devoted significant resources to modifying Mr. Oystacher's trading in a good-faith effort to reduce the ways in which Mr. Oystacher's legitimate trading activity, in hindsight, may appear to resemble "spoofing." *See* O'Connor Decl. at ¶ 11. 3 Red began these efforts more than ten months prior to this Action. *See* O'Connor Decl. at ¶¶ 12-13. The modifications have largely focused on two areas about which the exchanges and the CFTC have expressed concern: (i) the large size of visible orders; and (ii) the speed with which the wash-blocker function operates (even though such speed is set by third-party software or the exchanges that offer the wash-blocker functionality). *See* O'Connor Decl. at ¶ 12*; see also* Bessembinder Tr. at 243:14-16 ("If my understanding of the wash blocker [software typically used by market participants] is correct . . . the cancel occurs and then the trade-side order enters simultaneously"); *see also id.* at 237-245 (providing "general understanding of what wash blockers do" and acknowledging that they generally cancel and replace within a microsecond).

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addressed Karen Christiansen (who was the Regulatory Officer of CFE at the time) in a hostile and dismissive fashion. O'Connor Decl. at ¶ 4. Although 3 Red and Mr. O'Connor have attempted to build new paths forward with the exchanges, the exchanges have largely been unreceptive. O'Connor Decl. at ¶ 10.

For example, to address any concern about the placement of large, visible orders, 3 Red limits the maximum size of Mr. Oystacher's displayed orders. To that end:

> 3 Red instituted in January 2015 a threshold-iceberg functionality called "Max Order Size." *See* O'Connor Tr. at 186:2-189:1; O'Connor Decl. at ¶ 13. This functionality automatically converts displayed orders that exceed a certain cap size into Iceberg orders. *See id.*[9]

- On May 27, 2015, 3 Red introduced a splitter feature called "Large Order Splitter Tool" for use in certain markets, including the CME markets. *See* O'Connor Decl. at ¶ 13. The tool automatically divides any order greater than the Max Order Size limit into three separate orders with an aggregate displayed size that is equal to the Max Order Size limit. *See id*.; *see also* Ex. 20 to Cole Decl., Excerpts of Deposition of Stephen Strohmer (March 4, 2016) ("Strohmer Tr.") at 103:16-19. The remainder is automatically transformed into Iceberg orders. *See* O'Connor Decl. at ¶ 13.

- On November 10, 2015, 3 Red implemented a limit-show feature called the Max Quantity at Price Tool. *See* O'Connor Decl. at ¶ 13. This functionality prevents the aggregate displayed quantity at a single price from exceeding the number of contracts that is set as the maximum. *See* O'Connor Tr. at 188:23-190:1; O'Connor Decl. at ¶ 13.

- In January 2016, 3 Red began programming an enhanced limit-show feature called the Dynamic Max Quantity at Price Tool. *See id*. This is an enhanced, fully automated tool that caps the maximum quantity of Mr. Oystacher's displayed orders at a single price. *See id.* 3 Red introduced this tool and implemented its mandatory operation across all Relevant Markets on February 16, 2016. *See* O'Connor Decl. at ¶ 13. It has since replaced the Max Order Size Tool, the Max Quantity at Price Tool, and the Large Order Splitter Tool. *See* O'Connor Decl. at ¶ 13.. [redacted], the Dynamic Max Quantity at Price Tool calculates the Maximum Quantity at Price value for each product that is traded as [redacted] (*i.e.*, excluding the [redacted]), as well as orders by the trader at those prices). *See* O'Connor Decl. at ¶ 13.[10]

In a similar vein, to address any concern about the speed with which the wash-blocker function operates, 3 Red has modified the wash-blocker to ensure that algorithmic traders have even ***more***

[9] 3 Red expanded the Max Order Size Tool to the Eurex market in July 2015. *See* O'Connor Decl. at ¶ 13. Eurex does not independently offer the option of entering orders in Iceberg format. Accordingly, 3 Red developed a synthetic Iceberg option to facilitate the implementation of the Max Order Size Tool.

[10] Initially, the time interval was set at [redacted]. *See* O'Connor Decl. at ¶ 13. 3 Red solicited feedback from CME regarding the Dynamic Max Quantity at Price Tool on February 12, 2016. *Id.* This time, CME provided guidance, which 3 Red incorporated by reducing [redacted] the contemplated time interval for the automatic calculation. *Id.*

time to notice and react to changes in available liquidity that was placed by Mr. Oystacher. To that end:

- On May 28, 2015, 3 Red introduced a cross-protection feature called the Reduce Prior to Cancel/Replace Tool for use in certain markets (including the CME markets). *See* O'Connor Decl. at ¶ 14. When the wash-blocker is triggered, this tool cancels a sufficient number of existing orders to reduce Mr. Oystacher's total displayed quantity to below [redacted] of the total displayed size at that price. *See id*. After the reduction is confirmed, the tool cancels the remainder of Mr. Oystacher's existing orders at that price, and then submits the new order on the opposite side of the market. *See* O'Connor Decl. at ¶ 14.

- In January 2016, 3 Red began programming an enhanced cross-protection feature called the Delayed Replace for Cancel/Replace Tool for use in certain markets (including the CME markets). *See* O'Connor Decl. at ¶ 14; *see also* Strohmer Tr. at 101:13-103:15. The tool went live on February 16, 2016, and has since replaced the Reduce Prior to Cancel/Replace Tool. *See* O'Connor Decl. at ¶ 14. In the event that the wash-blocker is triggered, the Delayed Replace for Cancel/Replace Tool currently imposes a f[redacted] delay between the cancellation of any existing order and the placement of a new order in the opposite direction. *See id*.[11]

3 Red has further introduced various internal controls that monitor the firm's trading and alert Mr. O'Connor to orders that fit whatever criteria the exchanges and / or CFTC appear to consider potentially disruptive. *Id.* at ¶ 5. In this regard:

- On September 6, 2013, 3 Red began generating an Execution vs. Inside Market (90%) Report. The report is generated automatically each time a trader places an order that equals at least 90% of the displayed quantity of orders at the BBO on the opposite side of a particular market. *Id.* at ¶ 5.

- 3 Red began generating on September 6, 2013, an Execution vs. Inside Market (50%) Report. This report is also generated automatically and alerts the compliance department whenever a trader places an order that is equal to at least 50% of the aggregate size of displayed quantity of orders at the top three prices on the opposite side of the market. *Id.* at ¶ 5.

- 3 Red began generating Order Bias Reports on approximately January 27, 2015. *See* O'Connor Decl. at ¶ 5.The Order Bias Report identifies when a particular trader changes

[11] The Delayed Replace for Cancel/Replace Tool initially imposed a delay of [redacted]; 3 Red has since gradually increased the minimum delay [redacted]. *See* O'Connor Decl. at ¶ 14.

his bias by placing orders into a market in which that trader previously had resting orders on the opposite side. *See* O'Connor Tr. at 82:7-20.

In addition, 3 Red strives to maintain regular contact with all of the exchanges on which Mr. Oystacher trades, for the purpose of ensuring compliance with exchange rules and federal law. *See* O'Connor Tr. 71:11-19 (explaining that 3 Red tries "to hold regular conversations" with the exchanges); O'Connor Decl. at ¶ 6.

vi. This Action and the PI Motion

The CFTC filed this Action on October 19, 2015, following a four-year investigation that was largely instituted at the behest of certain algorithmic trading firms, including Citadel LLC ("Citadel") and CGTA, LLC ("CGTA"). As previewed above, the two-count Complaint purports to allege that during portions of fifty-one trading days between December 2011 and January 2014, Mr. Oystacher and 3 Red violated the Spoofing Provision (Count I) and that they violated Rule 180.1 (Count II).

The CFTC filed the PI Motion three weeks later, on November 9, 2015. *See generally* PI Mot. It purports to stem from certain order placement and cancellation activity in the high grade copper futures contract ("Copper") traded on CME's Commodity Exchange Inc. ("COMEX"); the light sweet crude oil futures contract ("Crude Oil") traded on CME's New York Mercantile Exchange ("NYMEX"); the Henry Hub natural gas futures contract ("Natural Gas") traded on CME's NYMEX; the Volatility Index Futures Contract ("VIX") traded on CFE; and the S&P 500 E-Mini futures contract ("ES") traded on CME (collectively, the "Relevant Markets"). *Id*. at 4, 5. The vast majority of that trading activity occurred several years ago, with the exception of certain limited ES orders that post-date the ones in the Complaint. *See* PI Mot. at 11-12. The most recent such ES trade is nearly one year old, from May 2015. *See, e.g.*, Bessembinder Rep. at ¶ 7. The CFTC has since notified 3 Red that it intends to incorporate into the PI Hearing

certain orders from the CBOT ten-year treasury note futures market ("ZN" or, together with Copper, Crude Oil, Natural Gas, ES and VIX, the "Relevant Markets") from February 2016. *See generally* CFTC Mot. To Expand Proof (ECF 72) ("Mot. to Expand Proof"). The CFTC has mustered just two instances of trading in ZN that satisfy the self-serving criteria that the CFTC invented for this case. *See infra* Part II.B.

Through the PI Motion, the CFTC seeks an injunction against future violations by 3 Red and Mr. Oystacher, as well as a complete prohibition on Mr. Oystacher's trading in the Relevant Markets. If awarded, the injunction would persist through a verdict in the trial on the merits. In support of its request, the CFTC primarily relies on the analyses of its purported expert, Professor Hendrik Bessembinder, and its investigator, Joy McCormack, as well as affidavits submitted by Karen Christiansen of the Chicago Board Options Exchange, Inc. (formerly of CFE) and representatives of two algorithmic trading firms that compete with 3 Red in the ES market: (i) Richard May of Citadel; and (ii) Matthew Wasko, formerly of CGTA. The Court has scheduled the PI Hearing to begin on April 25, 2016.

ARGUMENT

I. The CFTC Must Make a Persuasive and Substantial Showing that it is Likely to Succeed on the Merits and That There is a Risk of Recurrence

A. The Standard for Obtaining a Preliminary Injunction Turns on the Nature and Scope of Requested Relief

The CFTC is not entitled to an injunction merely because it has asked for one. *See, e.g.*, *Mazurek v. Armstrong*, 520 U.S. 968, 972 (1997) (describing preliminary injunctions as "extraordinary and drastic remedies" that "should not be granted unless the movant, by a clear showing, carries the burden of persuasion"). To the contrary, this Court has wide latitude to deny injunctive relief and may only issue it "upon a proper showing" that a violation has occurred and that repetition is likely. *E.g.*, *CFTC v. Hunt*, 591 F.2d 1211, 1219 (7th Cir. 1979)

(holding that injunctive relief is "never automatic upon the showing of a violation of the Act or regulations"); *see also* 7 U.S.C. 13a-1 (authorizing CFTC to pursue injunctive relief only if it demonstrates that a person "has engaged, is engaging, or is about to engage in any act or practice constituting a violation of . . . this Act or any rule, regulation or order thereunder"); *Hecht Co. v. Bowles*, 321 U.S. 321, 327-28, 331 (1944) (holding that the Emergency Price Control Act, which contains parallel language to 7 U.S.C. 13a-1, "falls short of making mandatory the issuance of an injunction merely because the Administrator asks [for] it"); *CFTC v. Nat'l Inv. Consultants Inc.*, No. C 05-02641 JSW, 2005 WL 2072105, at *4 (N.D. Cal. Aug. 26, 2005) (holding that CFTC's burden is higher than merely offering a "colorable evidentiary showing that it will prevail on the merits" (internal quotation omitted)). What constitutes a "proper showing" is determined by the nature and scope of the requested injunction. *See, e.g.*, *SEC v. Unifund SAL*, 910 F.2d 1028 at 1039 (2d. Cir. 1990).

On this point, *Unifund*, 910 F.2d at 1039, is instructive. There, the Second Circuit considered the district court's award of a preliminary injunction that included a statutory asset freeze as well as a prohibition on future violations of the securities laws. *Id.* at 1029. Ultimately, the Second Circuit concluded that these are distinct forms of equitable relief for which regulators must meet distinct evidentiary burdens. *Id.* at 1040-43. In particular, the asset freeze merely sought to preserve the status quo by ensuring that assets would be available for subsequent disgorgement. *Id.* at 1040-41. It carried no risk of contempt and was ancillary in nature. *Id.* at 1042. The same was not true of the prohibition on future violations. That form of relief had "grave consequences" for the defendant, would cause "serious collateral effects," and "subject[ed] the defendant to contempt sanctions if . . . subsequent trading is deemed unlawful." *Id.* at 1040. It therefore "accomplishe[d] significantly more than [just the] preservation of the

status quo." *Id.* at 1040. On that basis, the Second Circuit held that although the SEC may obtain an asset freeze based on a minimal showing (i.e., a showing that is merely sufficient to send the case to the trier of fact), *id.* at 1041, it may not obtain a prohibition on future violations absent a "more persuasive" and "more substantial showing . . . both as to [the purported] violation and [its] risk of recurrence." *Id.* at 1039. In essence, regulators must establish that success on the merits and a risk of recurrence are not just possible, but probable. *Id.* The Second Circuit therefore vacated and modified in relevant part before remanding. *Id.* at 1043.

There is no meaningful analysis of *Unifund* in the Seventh Circuit. *See, e.g., SEC v. Cherif*, 933 F.2d 403, 408 n.1 (7th Cir. 1991) (noting that parties did not ask court to consider *Unifund* and leaving that "question for another day"); *CFTC v. Garofalo*, No. 10 C 2417, 2010 WL 11245430, at *6 (N.D. Ill. Dec. 21, 2010) (noting that *Unifund* has not yet been adopted in Seventh Circuit). But courts in sister circuits have faithfully applied it. *See, e.g., Garofalo*, 2010 WL 11245430, at *6 ("[A] number of courts have adopted *Unifund's* heightened standard"). Suitably, those courts require the CFTC "[l]ike any litigant . . . to make a more persuasive showing of its entitlement to a preliminary injunction" if the injunction would impose "more onerous . . . burdens" on the defendant. *SEC v. Bravata*, 763 F. Supp. 2d 891, 919 (E.D. Mich. 2011) (quoting *Unifund*, 910 F.2d at 1039); *see also, e.g., SEC v. Life Partners, Inc.*, 898 F. Supp. 14, 23 (D.D.C. 1995) *rev'd on other grounds,* 87 F.3d 536 (D.C. Cir. 1996); *CFTC v. Sterling Trading Grp, Inc.*, 605 F. Supp. 2d 1245, 1291 (S.D. Fla. 2009); *SEC v. Trabulse*, 526 F. Supp. 2d 1008, 1012-13 (N.D. Cal. 2007); *SEC v. Cavanagh*, 1 F. Supp. 2d 337, 359-60 (S.D.N.Y. 1998); *CFTC v. Garcia*, No. 2:15-cv-237, 2015 WL 3453472, at *3 (M.D. Fla. May 29, 2015); *SEC v. Thorn*, No. C:01-CV-290, 2001 WL 1678787, at *1 (S.D. Ohio Nov. 16,

2001); *SEC v. Stratton Oakmont, Inc.*, Civ. A. No. 94–2681 (JHG), 1994 WL 721502, at *3 (D.D.C. Dec. 19, 1994). This Court should do the same.

B. If Awarded, the Injunction Would Subject Mr. Oystacher and 3 Red to Grave Consequences for an Indeterminate Period of Time, on Pain of Contempt

If ever there were a form of preliminary relief that demands a more persuasive and substantial showing, it is the injunction that the CFTC seeks here. Everything about that injunction would replace the existing status quo with a new one. If awarded, it would bar Mr. Oystacher from trading in each of the six Relevant Markets. This trading ban would carry severe and long-lasting reputational consequences for both Mr. Oystacher and 3 Red. It would likely also infringe upon Mr. Oystacher's ability to earn a living, 3 Red's potential profits, and Mr. Oystacher's ability to generate resources that he and 3 Red could otherwise use to defend against this Action. Those conditions would persist under threat of contempt, through the conclusion of a trial that has yet to be scheduled. The trading ban therefore merits heightened scrutiny of the quality and completeness of the CFTC's evidence. *See, e.g.*, *Unifund,* 910 F.2d at 1039; *Cavanagh*, 1 F. Supp. 2d at 359-60; *accord Sterling Trading Group*, 605 F. Supp. 2d at 1291; *Trabulse*, 526 F. Supp. 2d at 1012-13.

The same is true with respect to the requested prohibition on future violations. Much like the trading ban, this prohibition would persist under pain of contempt and for an indeterminate period of time. As the *Unifund* court held, it is thus a drastic remedy that demands a more "substantial showing of likelihood of success as to both a current violation and the risk of repetition." *Thorn*, 2001 WL 1678787, at *2 (quoting *Unifund*, 910 F.2d at 1040); *see also SEC*

v. Compania Internacional Financiera S.A., No. 11 Civ. 4904(DLC), 2011 WL 3251813, at *11 (S.D.N.Y. July 29, 2011) (declining to enjoin future securities law violations).[12]

C. "Spoofing" is a "Grey Area of . . . [the] Law"

Courts have declined to award burdensome injunctions based on purported violations that lie "in a grey area of . . . law." *See Life Partners*, 898 F. Supp. at 23 (D.D.C. 1995) (concluding that SEC was entitled to "more limited preliminary relief than it seeks" because violation implicated "grey area of securities law"), *rev'd on other grounds,* 87 F.3d 536 (D.C. Cir. 1996); *see also CFTC v. J.S. Love & Assocs. Options, Ltd.*, 422 F. Supp. 652, 661 (S.D.N.Y. 1976) (denying preliminary injunction based on recency of relevant CFTC rule and lack of specific guidelines putting defendant on notice that rule encompassed his conduct). This case squarely fits that description.

i. The Spoofing Provision is Facially Vague

The text of the Spoofing Provision purports to prohibit three categories of behavior: (i) "any trading, practice, or conduct [that] is . . . 'spoofing' (bidding or offering with the intent to cancel the bid or offer before execution);" (ii) "any trading, practice, or conduct [that] is . . . commonly known to the trade as 'spoofing' (bidding or offering with the intent to cancel the bid or offer before execution);" and (iii) "any trading, practice, or conduct [that] is of the character

[12] The prohibition on future violations is even more problematic here than it was in *Unifund* because it is tantamount to a complete trading ban in ***all*** markets. This is because the six markets at issue are the six markets with which Mr. Oystacher is most familiar. It is also because there are no reasonably ascertainable standards for assessing when lawful trading might be misinterpreted as "spoofing." *See infra* Part I.C; *see also supra* Part A. As a consequence, the only way for Mr. Oystacher and 3 Red to be substantially certain that the CFTC will not misconstrue their future trading is if they refrain from trading altogether. We respectfully submit that it would be inequitable to impose such sweeping restrictions on Mr. Oystacher and 3 Red based on anything less than what *Unifund* demands. This is particularly so given that the CFTC itself has chosen to obscure, rather than clarify, what future conduct would violate the injunction. *See supra* Part A; *see also infra* Part I.C.

of . . . 'spoofing'(bidding or offering with the intent to cancel the bid or offer before execution)." Spoofing Provision. This language makes no sense.

To begin with, the meaning of the statute hinges on a term that appears in quotation marks. This is unusual in an Act of Congress, but ordinarily, such quotation marks might indicate an industry term of art. *See Utah v. Evans*, 536 U.S. 452, 464-68 (2002) (construing federal statute authorizing use of statistical method "known as 'sampling'" and noting that use of "the words 'known as' and the quotation marks that surround 'sampling' . . . suggests a term of art with a technical meaning"). Not so here. As the years of public debate following Dodd-Frank make plain, "spoofing" was not a meaningful referent in the futures industry. *See, e.g.*, Roundtable Tr. at 171:17-21 (stating that "after this morning's conversation," the answer to the question of whether there is "a common understanding or meaning to the terms that [are] . . . in the statute" is "no"); Damgard Comment Letter at 1 (referring to the Spoofing Provision as "an overly vague provision that is not clearly defined and prohibits activities that are also not subject to clear definition"); Roundtable Tr. at 154:20-155:1 (referring to the Dodd-Frank provision as "bad law" because "[i]t wasn't done with forethought as to an abusive practice that everybody had admitted was a problem in the marketplace"); *see also supra* Part A. This is why "spoofing" had never been mentioned in any prior industry statute, rule, or administrative guidance. *See, e.g.*, Roundtable Tr. at 171:9-172:7.

The text of the Spoofing Provision simply did not provide Mr. Oystacher any reasonable touchstone for identifying—or avoiding—prohibited conduct. *See, e.g.*, *Grayned v. City of Rockford*, 408 U.S. 104, 108 (1972) (reiterating that to be minimally clear, laws must "give the person of ordinary intelligence a reasonable opportunity to know what is prohibited, so that he may act accordingly"); *United States v. Nat'l Dairy Prods. Corp.*, 372 U.S. 29, 36 (1963)

(suggesting that statutes without a meaningful referent in business practice or usage implicate vagueness concerns). For this reason alone, the challenged conduct falls within a "grey area. . .of law." *See Life Partners, Inc.*, 898 F. Supp. at 23; *see also Grayned*, 408 U.S. at 108-09 (describing statutes that lack reasonably ascertainable standards for distinguishing between permissible and impermissible conduct as "trap[s for] the innocent" that do not "provid[e] fair warning").

The parenthetical description in the statute (i.e., "bidding or offering with the intent to cancel before execution") does not cure the vagueness of the text. It is hardly clear that this description ***defines*** "spoofing." *Contra* Pls.' Mem. Supp. Mot. Strike Aff. Defs. (Jan. 15, 2016) (ECF No. 65-1) at 11-12. In fact, the description more likely offers an example of what may ***sometimes*** constitute "spoofing." Certainly, when Dodd-Frank was passed, the futures industry was flooded with bids and offers that algorithmic traders obviously intended to cancel before execution. *See* Markham Rep. at ¶¶ 76, 112. This included, among others, stop-loss orders (which are set to buy or sell once a stock reaches a certain price), partial fill orders (of which only a portion of the order is executed and the remainder is cancelled), fill-or-kill orders (which are set to cancel if they are not executed immediately), orders placed for price discovery, and orders placed to test system parameters. *See* Bessembinder Tr. at 256:18-258:2; *see also* [redacted] Roundtable Tr. at 60:6-61:3, 78:19-79:1. All of these orders fit what the CFTC characterizes as the definition of "spoofing," but were considered lawful in the futures industry. *See, e.g.*, Markham Rep. at ¶ 113; *see also* [redacted]. They still are today. *See* Markham Rep. at ¶ 113; *see also* [redacted]

This demonstrates that the Spoofing Provision must mean something other than what its language appears to convey. As such, it is vague and does not enable industry participants like

Mr. Oystacher to conform their trading to its requirements. *See, e.g.*, *City of Chicago v. Morales*, 527 U.S. 41, 57 (1999) (holding that ordinance was vague regarding "what loitering is covered . . . and what is not" even though definition of "loitering" was plain, because city "cannot conceivably have meant to criminalize each instance [of loitering] with a gang member"); *Smith v. Goguen*, 415 U.S. 566, 573-74 (1974) (holding that language of statute was vague because it "fails to draw reasonably clear lines between the kinds of nonceremonial treatment [of the flag] that are criminal and those that are not"); *see also Ashton v. Kentucky*, 384 U.S. 195, 199 (1966) (finding vague a statute that was "sweeping in a great variety of conduct under a general and indefinite characterization, and leaving to the executive and judicial branches too wide a discretion in its application").[13]

Finally, the Spoofing Provision purports to outlaw conduct that is not spoofing, but is somehow ***like*** spoofing. *See* Spoofing Provision (prohibiting conduct that "is of the character of . . . 'spoofing'"). Yet there is nothing in the statute, the legislative history or the Policy Statement that indicates how closely the non-spoofing must hew to actual spoofing, or in what way. More fundamentally, it is difficult to square this language with the remainder of the statutory text. After all, if spoofing is the submission of a bid with the intent to cancel it prior to execution, then non-spoofing would have to be the opposite. There would thus be no room for hybrid behavior that is not spoofing, but that could reasonably be viewed as "of the [same] character" as spoofing. This renders the statute unclear. *See, e.g.*, *Winters v. New York*, 333

[13] Congress's inclusion of a parenthetical description implicitly acknowledges that "spoofing" was not an industry term of art with a uniform definition. If it were, then there would not have been any need to supply a description. Notably, Section 1a of the CEA sets forth extensive definitions for terms used in the statute. *See* 7 U.S.C. § 1a. "Spoofing" appears nowhere in Section 1a, even after the extensive revisions that Congress made to that section as part of Dodd-Frank.

U.S. 507, 515 (1948) (reiterating that statute is vague if people "of common intelligence [are] required to guess at the meaning of the enactment"). [14]

In light of the foregoing, the Spoofing Provision is ***at best*** a grey area. It is therefore appropriate and equitable for the Court to require the CFTC to satisfy *Unifund's* heightened standard.[15]

ii. The Policy Statement Further Obscures the Meaning of the Spoofing Provision

The CFTC does not contend that Mr. Oystacher engaged in any conduct that is itself unlawful; nor could it. He did not, for example, trade in excess of position limits, orchestrate a Ponzi scheme, sell off-exchange instruments, or engage in wash sales. *See, e.g.*, *Hunt*, 591 F.2d at 1211; *CFTC v. Noble Metals, Int'l, Inc.,* 67 F.3d 766, 772 (9th Cir. 1995); *CFTC v. Bell*,

[14] In appropriate circumstances, a requirement to prove intent may cure statutory vagueness. *See United States v. Cherry*, 938, F.2d 748, 754 (7th Cir. 1991). This is not such a case. Indeed, the requirement of intent is wholly illusory where, as here, prohibited intent is principally to be proven through circumstantial evidence of lawful and customary trading practices ***and*** there are no sufficiently ascertainable standards for determining when those practices will be assumed to reflect that intent. *See supra* Part I.C.

[15] *United States v. Coscia*, 100 F.Supp.3d 653 (N.D. Ill. 2015), does not compel a different result. That decision involved direct proof of unlawful intent—specifically, an algorithm that was programmed to prematurely cancel its orders. *Coscia*, 100 F.Supp.3d 653 at 660. There is no similar evidence here. *Coscia* was also a criminal case. A grand jury had therefore already vetted the clarity of the statute as applied to the relevant facts. There is no equivalent safeguard in this civil enforcement action. *Coscia* further arose in the context of a motion to dismiss the indictment and, as a result, turned entirely on the government's version of events (which the court was required to accept as true). *See id.* at 655-56. The CFTC is not entitled to any such deference here, where the purpose of the PI Hearing is to ***test*** the CFTC's claims. Moreover, the *Coscia* court appears to have assumed that the parenthetical description in the Spoofing Provision was, in fact, a meaningful limiting principle. *See id.* at 659. For reasons already stated, we respectfully disagree. *See supra* Part I. A.ii. Lastly, *Coscia* passed upon a question that is different from the one that 3 Red raises here: in particular, whether the Spoofing Provision is too vague to be enforced. *Coscia*, 100 F.Supp.3d at 658-59. 3 Red believes that the answer to that question is "yes" and intends to address it in its opposition to the CFTC's Motion to Strike Affirmative Defenses, but is not relying on that affirmative defense at the PI Hearing. *See* Minute Entry of Feb. 1, 2016 (ECF No. 68); *see also* Transcript of Proceedings – Motion before the Honorable Amy J. St. Eve (Jan. 21, 2016) at 3:23-4:11 (confirming that 3 Red will not argue affirmative defenses like void for vagueness in connection with the PI Hearing, but will rely on other arguments regarding vagueness and good faith to negate the element of intent); *id.* at 4:12-24 (confirming that at PI Hearing, 3 Red may raise vagueness and good faith in connection with Mr. Oystacher's lack of intent).

Comm. Fut. L. Rep. (CCH) ¶27, 521, 1998 WL 35989619 (N.D. Okla. 1998). Instead, the CFTC seeks to sanction Mr. Oystacher for having engaged in lawful conduct with a purportedly unlawful ***purpose***. And because there is no direct evidence of that purpose (such as a reliable first-party admission or an algorithmic code that reveals pre-programmed cancellation), the CFTC asks the Court to infer it from otherwise innocuous circumstances. Those circumstances primarily consist of the "too quick" cancellation of original orders that comply with exchange limits, yet purportedly are somehow "too large," followed by the placement of new orders in the opposite direction. *See* Bessembinder Rep. at ¶ 108; PI Mot. at 10-18, 20-24.

If the CFTC had developed some meaningful guidance regarding how quick is "too quick" to cancel, or when it is improper to follow a cancellation with a new trade on the other side of the market, then this enforcement policy ***might*** be less unclear. *Cf., e.g., Satellite Broad. Co. v. FCC*, 824 F.2d 1, 3 (D.C. Cir. 1987) ("Traditional concepts of due process incorporated into administrative law preclude an agency from penalizing a private party for violating a rule without first providing adequate notice of the substance of the rule"). The CFTC could easily have accomplished this by, among other things, promulgating a rule that requires orders to rest for a certain number of milliseconds prior to cancellation, or enacting a regulation that precludes traders from placing a new trade in the opposite direction within a specified time frame from a cancellation (which is precisely the type of guidance 3 Red requested. *See supra* Part A. 3.). Either proposal would have helped to establish a framework pursuant to which Mr. Oystacher could have conformed his trading to the CFTC's interpretation of the Spoofing Provision ***before*** the CFTC assumed that he violated it. It also would have discharged the CFTC's obligation to

"make and promulgate such rules and regulations as . . . are reasonably necessary" regarding the Spoofing Provision. *See* Commodity Exchange Act, § 6c(a)(6). [16]

Rather than fulfill its Congressional mandate, however, the CFTC has chosen to turn away from it in favor of a nebulous Policy Statement that purports to reserve the unfettered discretion to cast the widest of nets and then select which traders will remain inside. The only thing that the Policy Statement makes reasonably clear is that the CFTC will predicate its enforcement decisions on inferences that it may sometimes opt to draw from normal trading practices, should it wish to construe them as badges of prohibited intent on an ad hoc basis. This is worse than a grey area. It is a moving target.[17]

iii. The CFTC's Interpretation of the Spoofing Provision Extends Beyond What this Court Should Reasonably Expect Mr. Oystacher to Have Understood the Spoofing Provision to Mean

[16] Significantly, Citadel -- one of the algorithmic trading firms with which the CFTC is aligned in this case – publicly urged the CFTC to reject a requirement for minimum resting times that might have provided exactly the type of clarity that would have enabled Mr. Oystacher (and others) to conform their conduct to what the CFTC apparently interprets the Spoofing Provision to mean. *See* Ex. 21 to Cole Decl., Citadel LLC Comment Letter to CFTC (Dec. 11, 2013) (urging CFTC to reject requirement of minimum rest times).

[17] Neither the speed of cancellations nor the flipping of positions is mentioned in the Policy Statement, let alone identified as an example of either "spoofing" or "creating an appearance of false market depth." *See generally* Policy Statement at 31890-31897. If the Policy Statement did mention the speed of flips and cancellations, however, then that interpretation would still exceed the scope of what the Court should reasonably expect Mr. Oystacher to have understood the Spoofing Provision to mean because, as set forth below in Part I.C.iii, that interpretation conflicts with what Congress must have intended. To that end, the Court would be well within its discretion to find the CFTC's interpretation of the Spoofing Provision, as stated in its Policy Statement and in this case, to be unjustified. *See, e.g.*, *Christensen v. Harris County*, 529 U.S. 576, 587 (2000) ("[I]interpretations contained in policy statements . . . lack the force of law. . . [and] do not warrant *Chevron*-style deference."); *Skidmore v. Swift & Co.*, 323 U.S. 134, 140 (1944) (making clear that informal agency interpretations are, at most, entitled to "respectful consideration," and only if the court considers them persuasive); *see also Pac. Gas & Elec. Co. v. Fed. Power Comm'n*, 506 F.2d 33, 40 (D.C. Cir. 1974) ("Although the agency's expertise and experience cannot be ignored, the reviewing court has some leeway to assess the underlying wisdom of the policy and need not affirm a general statement of policy that merely satisfies the test of reasonableness").

The CFTC's interpretation of the Spoofing Provision in this case both exceeds the text of the Spoofing Provision and transcends the scope of Congressional intent. It would thus be unreasonable to expect Mr. Oystacher to have divined that interpretation from either the statutory language or the relevant circumstances at the time. Such a "grey area" further merits the application of *Unifund*.

As an initial matter, the CFTC essentially concludes that Mr. Oystacher was "spoofing" because he was flipping. PI Mot. at 10-12. The Spoofing Provision, however, focuses solely on cancellations. 7 U.S.C. § 6c(a)(5)(C) (2012). It does not mention flipping. *Id.* It is thus clear that the text of the Spoofing Provision did not provide Mr. Oystacher with any notice that flipping "too quickly" or "too often" would be deemed a violation.

Furthermore, when Dodd Frank was passed, there was no industry authority that outlawed flipping or restricted the speed at which new orders could be placed in the futures markets following a cancellation. *See* McCormack Tr. at 282:14-283:5, 294:17-23. Quite to the contrary, flips were common occurrences in pursuit of legitimate objectives. *See, e.g.*, McCormack Tr. at 82: 10-14 (agreeing that "flipping occurs every day thousands of times in the marketplace"); [redacted] Regardless of what exactly Congress may have meant by "spoofing," then, it is clear that Congress did not intend for the CFTC to interpret that term as flipping "too quickly" or "too often" (as the CFTC has chosen to do here). There was thus no basis for Mr. Oystacher to think that he could not "flip" or that the CFTC would seek to enjoin him from doing so. *See, e.g.*, *J.S. Love & Assocs. Options, Ltd.*, 422 F. Supp. at 661-62 (denying preliminary injunction in relevant part due to lack of specific guidelines that would provide sufficient notice that rule encompassed defendant's conduct).

Similarly, when Congress passed the Spoofing Provision, there was no authority that outlawed cancellations, regulated their speed or otherwise restricted them in the futures markets (nor is there today). *See* McCormack Tr. at 282:14-283:5, 294:17-23; *see also* Markham Rep. at ¶ 76 ("The overwhelming majority of orders entered on futures and security exchanges are cancelled."). Much like flips, cancellations were extremely common and were widely recognized as legitimately justified. *See, e.g.*, Markham Tr. at 201:3-8; *id*. at 173:17- 174:5; Bessembinder Tr. at 248:9-250:6; *see also, e.g.*, Bessembinder Tr. at 169:3-17 (conceding, in relevant part, that "certainly cancellations are common in these markets"). Accordingly, there is no indication that Congress intended for the CFTC to define "intent to cancel" as "too quick" cancellation. This is particularly so given the absence of any guidelines regarding what qualifies as "too quick." *See, e.g., J.S. Love & Assocs. Options, Ltd.*, 422 F. Supp. at 661-62.

For each of these reasons, the interpretation of the Spoofing Provision that the CFTC espouses in this case (as well as in the Policy Statement, *see supra* n.18) extends beyond what this Court should reasonably expect Mr. Oystacher to have understood the Spoofing Provision to mean. The challenged conduct thus falls within a "grey area" of law. On this basis, too, the Court should evaluate the CFTC's evidence pursuant to *Unifund*.

II. Regardless of Which Standard the Court Chooses to Apply, the CFTC Cannot Establish a Violation of Either the Spoofing Provision or Rule 180.1

A. Mr. Oystacher Did Not "Spoof" Any Market

The gravamen of the CFTC's claims is that Mr. Oystacher "tricked" algorithmic traders like Citadel and CGTA into joining him on a particular side of the market by creating book pressure that the algorithms were programmed to rely upon ("false market depth"), after which he then cancelled the original orders and entered new orders in the opposite direction before the algorithms could correct themselves. *See* PI Motion at 17. There are many reasons why this

"spoofing" theory is meritless, both under *Unifund* and under the most basic standards of plausibility. *See, e.g., Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 557, 127 S. Ct. 1955, 1966 (2007) . We discuss some of them here.

First, the best evidence of what Mr. Oystacher subjectively intended when he placed his original orders is his own testimony. In that regard, Mr. Oystacher has testified that he is willing to execute every order that he places, at the moment that he submits it. *See, e.g.*, Oystacher Tr. at 453:18-22. The CFTC has neither elicited nor disclosed any direct evidence to the contrary. Certainly, there are no direct admissions, no written instructions to cancel orders before they execute, and there is no algorithm or other software coding that supposedly reflects premeditated cancellations.[18] For this reason alone, the spoofing theory fails.

Second, the contemporaneous evidence confirms that Mr. Oystacher subjectively believed, in good faith, that his conduct did not constitute "spoofing." In fact, when discussing a Harvard Business Law Review article about the Spoofing Provision, Mr. Oystacher was told on April 11, 2013, by Edwin Johnson –3 Red's Chief Compliance Officer at the time – that 3 Red was "in compliance with the rules." *See, e.g.*, E-mail from Edwin Johnson to Igor Oystacher, dated Apr. 11, 2013 [3RED_CFTC1230655 ("I truly believe we are in compliance with the

[18] The CFTC instead resorts to a text message to which Mr. Oystacher was not even a party. *See* PI Mot. at 8; Ex. 1 to PI Mot. at ¶¶ 50-58. Setting aside for the moment any evidentiary issues (without waiving them), the content of the text message hardly provides direct support for the "spoofing" theory. On its face, the text message merely appears to convey a conversation in which one participant represents that Mr. Oystacher supposedly indicated that he had "found an algo in nat gas" and would stop trading for the year if he reached certain profit levels sooner than anticipated. *See* Ex. 1 to PI Mot. at ¶¶ 50-58. It does not discuss intended cancellations, planned flips, any master plan to trick the "algo," any design to build up book pressure, or any other component of the "spoofing" theory. *Id.* At most, the text message simply suggests that Mr. Oystacher may have identified an opportunity to position himself as a counterparty to certain trades with an algorithm that was willing to transact in Natural Gas. That is legitimate trading; not "spoofing." *See* McCormack Tr. at 312:2-21.

rules.")], attached as Ex. A to Oystacher Decl. On this independent basis, the record belies the "spoofing" theory.

Third, the CFTC's version of events presupposes that Mr. Oystacher knew that algorithmic trading firms like CGTA and Citadel had programmed their algorithms to rely primarily upon book pressure when making trading decisions in particular markets. It further assumes that Mr. Oystacher knew that the algorithms would prioritize that book pressure at certain price levels. But as Mr. Oystacher has testified, he has "no clue" what other traders consider, how much weight they assign to particular factors, or how they otherwise make trading decisions. *See, e.g.*, Oystacher Tr. at 525:13-15. Nor should he. Algorithmic trading firms like Citadel and CGTA view their strategies as "trade secrets" and guard their specifics under lock and key. *See, e.g.*, May Tr. at 211:8-212:8 (refusing to testify regarding the inputs that Citadel's algorithms consider when trading); *see also, e.g.*,Wasko Tr. at 93:1-8 (answering "only. . . generally" about questions regarding CGTA's trading speed in relation to competitors); Bessembinder Tr. at 409:21-410:17 ("[I]t seems a very reasonable conjecture that they would want to keep their algorithms to themselves").

Further, Mr. Oystacher's own decision tree departs from the mold that the CFTC attributes to the algorithms. Far from blindly relying on book pressure, Mr. Oystacher generally assigns it no substantial weight. *See* Oystacher Decl. at ¶ 12. Instead, he trades fluidly and intuitively, based primarily on a combination of other signals that, in his view, more reliably reflect true market depth and inform future prices (like elasticity). *See, e.g.*, Oystacher Tr. at 179:24-180:8. There is thus no factual predicate for any conclusion that Mr. Oystacher subjectively believed that the algorithms would rely upon book pressure to the apparent exclusion of other, more salient factors.

Given the widely recognized presence of hidden Iceberg orders in most of the Relevant Markets, it would actually be imprudent (if not illogical) for a firm to program its algorithms to make decisions based on displayed contract quantity alone. *See* May Tr. at 117:14-119:8, 212:5-8 (acknowledging that Citadel considers "other inputs"); *see also* Wasko Tr. at 105:19-25 ("There is always the potential of an iceberg at a level, yes."). Because the markets are anonymous and each separate order does not necessarily represent an individual trader within the market, it would likewise be illogical for firms to program their algorithms to make trading decisions based solely on the number of displayed orders. *See* Markham Tr. at ¶ 106 (recognizing that "buy-side firms (such as mutual funds and pension funds" may use automated systems and execution algorithms to 'shred' one or more large orders (called 'parent order') into a series of smaller trades ('child orders') to be executed over time"). At bottom, displayed contracts and orders are two signals that are inherently – and objectively – unreliable. There would thus have been no incentive for Mr. Oystacher to "spoof" by creating a "false appearance of market depth" based on book pressure. This undercuts any inference that he intended to do so.

Fourth, 3 Red and Mr. Oystacher have consistently taken steps to trade in a way that regulators view as compliant with whatever it is that those regulators may interpret the Spoofing Provision to mean. *See, e.g.*, O'Connor Tr. at 69:5-16 ("[W]e try to evaluate and interpret the rules that are being applied to Mr. Oystacher and figure out how best we can move forward"); *see also supra* Part B. This is clear from the multiple attempts that 3 Red and Mr. Oystacher have made to discuss Mr. Oystacher's trading with the exchanges and to obtain concrete guidance regarding the meaning and enforcement of the Spoofing Provision (the vast majority of which have been ignored). *See, e.g.*, O'Connor Tr. at 71:4-19; *id.* at 247:6-12. It is also

reflected by 3 Red's investment of its own resources to modify Mr. Oystacher's trading and to adopt additional compliance tools, notwithstanding that many of those measures further disadvantage Mr. Oystacher in relation to algorithmic traders like Citadel and CGTA. *See, e.g.*, O'Connor Tr. at 184:20-185:13 (describing various voluntary measures, including "an automated delay between the cancellation of an order and the placement of an order at the same price"); *see also supra* Part B.

In the face of such good-faith efforts, it is difficult to see how Mr. Oystacher may be deemed to have "intentionally and repeatedly engaged in a manipulative or deceptive spoofing scheme." *Contra* PI Mot. at 1. The more compelling inference is that he simply did not understand the Spoofing Provision or the CFTC's interpretation of it. *See, e.g.*, O'Connor Tr. at 203:19-204:17 (indicating that "there were concerns about activity that could be categorized as spoofing when it is in the view of the trader legitimate trading"); *see also supra* Part A. For this reason, too, the claims are untenable.

Fifth, the CFTC's witnesses concede (as they must) that the components of Mr. Oystacher's trading are lawful and legitimate. Indeed:

- None of the Relevant Markets has any restriction regarding the length of time that a trade must rest prior to cancellation. *See, e.g.*, McCormack Tr. at 282:14-283:5 ("[T]here is no set industry standard for how long an order has to be resting before it can be canceled"); [redacted] Bessembinder Tr. at 247:24-248:7 ("I'm not aware of any. . . minimum time statute"); *see also generally* CFE Rulebook; CME Rulebook; NYMEX Rulebook; COMEX Rulebook.

- None of the Relevant Markets has any restriction regarding the length of time that must pass between the cancellation of an original order and the placement of a new one in the opposite direction. *See, e.g.*, Christiansen Tr. at 180:7-14 (acknowledging that the CFE does not have "any guidance . . . as to how fast [traders] can cancel and replace a trade"); *see also generally* CFE Rulebook; CME Rulebook; NYMEX Rulebook; COMEX Rulebook; McCormack Tr. at 282:14-283:5, 294:17-23.

- Mr. Oystacher's total trading volume was, at all times, within applicable limits for each of the Relevant Markets. *See* Bessembinder Tr. at 207:12-208:22 (indicating that Bessembinder is "not aware of any…evidence" that would suggest that Mr. Oystacher violated exchange limits); *see also generally* CFE Rulebook; CME Rulebook; NYMEX Rulebook; COMEX Rulebook.

- Each of the Relevant Markets on which Mr. Oystacher placed Iceberg orders specifically permitted the Iceberg format during the relevant period, and all instances of Mr. Oystacher's Iceberg usage complied with applicable requirements. *See, e.g.*, Bessembinder Tr. at 258:12-261:11 (conceding lack of "aware[ness] of any violations of the rules" with respect to Mr. Oystacher's use of Iceberg orders and acknowledging that Mr. Oystacher's use of Icebergs "in and of itself" was not improper).

- There are no restrictions against randomizing orders or otherwise obscuring a trading strategy from predatory competitors. *See, e.g.*, Bessembinder Tr. at 250:8-19 ("[I]t's common for traders, presumably including traders like Mr. Oystacher, to want to avoid being completely predictable"); *id.* at 315:5-24 ("[I]t would be wise for a given trader to take into account that others might be trying to anticipate their . . . orders and strategies"); *see also generally* CFE Rulebook; CME Rulebook; NYMEX Rulebook; COMEX Rulebook.

- Similarly, there is no authority that requires traders to enter "balanced" orders. *See* McCormack Tr. at 290:13-18; Markham Rep. at ¶ 133; *see also generally* CFE Rulebook; CME Rulebook; NYMEX Rulebook; COMEX Rulebook.

- Wash-blockers are common compliance tools that serve a beneficial purpose. *See* McCormack Tr. at 206:2-7 (confirming that "[w]ash blockers are commonly used throughout the industry"); Christiansen Tr. at 226:8-11 ("The purpose of a wash blocker is to prevent wash trades from taking place").

- There is nothing wrong with enabling a wash-blocker to cancel existing orders when new ones are placed in the opposite direction. Doing so is consistent with standard wash-blocker use in the industry and is a functionality that many exchanges themselves provide. *See, e.g.*, Bessembinder Tr. at 237:13-238:4.

- The CFTC does not contest that the size of each original order complied with applicable exchange limits and requirements. *See* Bessembinder Tr. at 207:17-209:22 (stating that he "did not assess" and is "not aware of any. . .evidence" that Mr. Oystacher traded in amounts that exceeded permissible limits).

- The same is true with respect to the size of each new order. *See* Bessembinder Tr. at 207:17-209:22.

Both individually and in the aggregate, these are benign components of legitimate trading. They therefore do not support a plausible inference of "spoofing" under *Twombly*, let alone the "more

persuasive" and "substantial" one that *Unifund* requires. *Cf. City of Brockton Ret. Sys. v. Shaw Grp. Inc.*, 540 F. Supp. 2d 464, 475 (S.D.N.Y. 2008) (rejecting argument that "zero plus zero plus zero plus zero plus zero adds up to something").

Sixth, Mr. Oystacher's original orders were subject to genuine market risk. Markham Rep. ¶ 100. Mr. Oystacher placed them at or near the best bid or best offer (the "BBO"). Compl. at ¶ 3. They were therefore competitively priced, which reflects a desire to transact and exposes the orders to a greater risk of execution. Markham Rep. at ¶ 111. In addition, as the CFTC's own research confirms, "a significant fraction of passive execution activity happens within one second of order entry or modification." Haynes & Roberts Rep. at 10. Like all limit orders, the original orders were thus vulnerable to execution prior to cancellation and other traders knew that the orders could be cancelled at any time. *Id.* at ¶ 102. They therefore subjected 3 Red to a risk of loss that is consistent with bona fide trading (and inconsistent with "spoofing"). *Id.*

Seventh, the speculation of Mr. May and Mr. Wasko—two representatives from high-frequency algorithmic trading firms that habitually complain about other traders in an attempt to reduce competition, and further stand to benefit financially from this case because they are whistleblowers[19]—is hardly proof of Mr. Oystacher's subjective intent. *See, e.g., United States v. Coscia*, No. 14 CR 551, 2015 WL 6153602, at *2 (N.D. Ill. Oct. 19, 2015) (excluding evidence of competitor complaints because such evidence "does little, if anything, to prove [the defendant's] intent" with respect to "spoofing"). It is also substantially more prejudicial than it is probative. *Id.* To begin with, the May and Wasko Affidavits focus on purported inducement and harm – two things that the CFTC has insisted it need not prove as elements of its case. *See,*

[19] *See* Wasko Tr. at 171:16-173:1 (admitting that monetary gain "was the reason to make" the whistleblower complaint and that "the idea of the whistleblower claim is you have a potential to make money if there is a successful action"); May Tr. at 32:5-9 (acknowledging that Citadel is seeking whistleblower status for its complaints to the CFTC related to this case).

e.g., PI Mot. at 3-4. Further, the CFTC apparently has not analyzed whether Mr. Oystacher profited from the trading activity at issue; nor has it performed a profit and loss analysis of the trades executed by Citadel or CGTA. *See* McCormack Tr. at 131:12-137:6, 337:2-8; *see also* Bessembinder Tr. at 160:22-161:16 (conceding that Professor Bessembinder "didn't make a causation analysis"). Neither Mr. May nor Mr. Wasko are able to fill that gap. *See* May Tr. at 264:20-265:5; Wasko Tr. at 237:3-238:19. The undisclosed methods that Citadel and CGTA used to "investigate" other traders' orders also appear to have been unreliable, as both firms complained about orders that the CFTC does ***not*** contend are "spoofs." [redacted]; *see also* [redacted] The rank speculation of self-interested competitors simply does not equate to competent evidence of Mr. Oystacher's intent.

Finally, the CFTC's argument that algorithmic traders did not have sufficient time to react to the cancellations, PI Mot. at 9, strains credulity. So, too, does the assertion that Mr. Oystacher could not have placed his original orders, cancelled them, and then flipped them as quickly as he did without premeditation. *Contra* PI Mot. at 16, 23-24. Mr. Oystacher's original orders (excluding ZN) are alleged to have rested for between 614 milliseconds and 752 milliseconds. *See* Compl. at ¶ 64; *see also* Table 4 to Bessembinder Rep. and Table 4 to Rebuttal Report of Hendrik Bessembinder (Mar. 11, 2016) (ECF No. 77) ("Bessembinder Rebuttal Rep.") (substantially similar times for orders at issue in PI Motion); Table 4 to Rebuttal Report of Hendrik Bessembinder (Mar. 11, 2016) (ECF No. 77) ("Bessembinder Rebuttal Rep.") (alleging that Mr. Oystacher's alleged original orders in ZN rested for an average of 690 milliseconds). This time interval is consistent with modern norms and well within the sub-

second capabilities of algorithmic trading firms. *See* Bessembinder Tr. at 26:8-15; *see also* Markham Tr. at 292:16-293:8 (explaining that an order is subject to execution if it rests for more than 350 or 450 ***micro***seconds); Haynes & Roberts Rep. at 9 (CFTC analysis recognizing that "just over 50 percent of market orders are cancelled within half a second" in certain markets); *cf. also, e.g.*, Ex. 21, Citadel LLC Comment Letter to the SEC (Nov. 6, 2013) ("Citadel SEC Comment Letter") at 5 ("[I]n today's markets . . . 350 microseconds [which equals approximately 0.35 milliseconds] is an exceedingly long period of time"). It is also within the demonstrated capabilities of Mr. Oystacher. *See* Leahy Tr. at 346:7-9, 360:11-361:24 (explaining that reaction-time test pursuant to which Mr. Oystacher's average processing time was 309 milliseconds is analogous to what Mr. Oystacher does when processing information from rapidly moving price ladder).[20] In any event, Mr. Oystacher has no obligation to slow his trading so that competitors may react (or profit). [redacted]

On this record and with respect to these claims, the only supportable conclusion is that Mr. Oystacher did not "spoof" any market. The Court should therefore deny the PI Motion.

B. The Speculation of Hendrik Bessembinder Is No Substitute for Competent Evidence of Mr. Oystacher's Intent

[20] Sports enthusiasts are well aware of the vanishingly short period of time in which professional baseball players must: (i) see a pitch; (ii) gauge the type, speed, and location of that pitch; (iii) decide whether to swing, and if so how hard and in what direction; (iv) perform a swing (or stop an existing swing); and (v) actually make contact with a baseball traveling through three dimensions. *See, e.g.*, Ex. 22_to Cole Decl., "The Science of the Swing". Each of these is a difficult and discrete task, the combination of which trained baseball players routinely perform in approximately 400 milliseconds—***less*** than the amount of time in which Mr. Oystacher generally performed the trading activity that the CFTC challenges.

[21] The record is further devoid of any evidence that suggests that Mr. Oystacher knew how quick would be "too quick" for the algorithms. It therefore does not support the inference that he plotted to "trick" them by trading "too fast."

The facts do not support the CFTC's "spoofing" theory. *See supra* Part II.A. As a consequence, the CFTC principally resorts to the suppositions of its retained expert, Professor Hendrik Bessembinder. To that end, Professor Bessembinder has, at the instruction of the CFTC, reverse-engineered an analysis that is designed to conclude that the observable attributes of Mr. Oystacher's trading are "consistent" with the view that Mr. Oystacher wished to induce competitors to enter orders on the same side of the market as his original orders while ensuring that those original orders would not be filled. *See* Bessembinder Rep. at ¶ 108. To satisfy that mandate, Professor Bessembinder focuses on what he describes as a pattern of placing very large original orders at or near the BBO and behind existing orders, most often in non-Iceberg format, followed by "too quick" cancellations and flips. *Id.* at ¶¶ 36-47. He further relies on a "low execution rate" with respect to the original orders, a "relatively high execution rate" of new orders, and a supposed acceleration of the order entry rate just prior to each cancellation and flip. *Id.* at ¶¶ 60, 90. Beyond this, Professor Bessembinder contends that Mr. Oystacher created a large imbalance in buys and sells, and that if he did place the original orders in Iceberg format, then he ceased to do so in the last second before the flip. *Id.* at ¶ 45.

This analysis deserves no weight, for many of the same reasons discussed in Part II.A above. But it also suffers from additional flaws that cast doubt upon the soundness of Professor Bessembinder's conclusions. The expert reports of Daniel Fischel and Professor Jerry Markham address those faults in detail. *See* Fischel Rep. at ¶ 9; Markham Rep. at ¶¶ 84-85, 120. We do not fully reproduce them here. In sum:

1. Selection Bias Pervades Professor Bessembinder's Analysis. Professor Bessembinder focused on a "narrowed set" of data that is comprised solely of a sub-set of bids and offers that Mr. Oystacher placed just before he flipped his position. *See* Bessembinder Rep. at ¶ 48. But a

broader data set reflects that when Mr. Oystacher placed other orders that Professor Bessembinder does ***not*** identify as "spoofing," Mr. Oystacher did so using many of the same trading attributes that Professor Bessembinder interprets as symptomatic of "spoofing" (such as large, imbalanced, and aggressively priced non-Iceberg orders). *See* Fischel Rep. at ¶¶ 22-23. That Mr. Oystacher used those types of orders in connection with orders that are indisputably legitimate underscores that such attributes are not hallmarks of premeditated cancellation. *See* Fischel Tr. at 198:3-10; Markham Tr. at 140:17-141:12; 152:5-12; 155:7-16; 183:11-184:1.

2. Professor Bessembinder's Selection Criteria Are Arbitrary. Relatedly, Professor Bessembinder selected the data to be included in the narrowed set that he analyzed by applying criteria that he contends are characteristic of "spoofing," but that no industry authority identifies as such. *Compare, e.g.,* Bessembinder Rep. at ¶ 49 (indicating that Bessembinder's selection criteria for "narrowed set" required that (i) fully displayed original orders have been entered one second or less before Mr. Oystacher flipped his position, that (ii) one or more orders have already been resting on the limit order book at the order price or at a more aggressive price," and that (iii) Mr. Oystacher's quantity on the side of the original orders in the last second before he flipped his position was equal to or greater than the total quantity of unexecuted orders already resting in the limit order book at the "event price" or better), *with, e.g.,* Markham Tr. at 254:12-255:3 ("There's no exchange rule. There's no commission rule. There's no customer practice that says these criteria are improper or that they indicate something that's wrong"). For example, there is no commission or exchange guidance that identifies one second of elapsed time from order entry to cancellation and flip as an indicator of "spoofing." *Id.* at 291:2-14; *see also* Fischel Tr. at 76:13-77:20 ("I think the correct inference is that cancellations within one second are routine and tell you nothing, like all the other criteria of the narrowing set"); Bessembinder

Tr. at 22:16-20 (conceding that the one-second parameter that he used is not "necessarily an important number for any future analysis of trading behavior").

Nor is "doubling" the size of the order book at a particular price indicative of "spoofing." Bessembinder Tr. at 129:22-130:10 ("There's no objective way to say precisely how big an order . . . is going to be noticed. Let's just say that a very small order would be unlikely to be noticed or less likely to be noticed."). To be sure, an order placed by Mr. Oystacher would double the quantity of orders already resting on the order book at a price—and therefore satisfy Professor Bessembinder's "doubling" criteria—virtually any time the number of preexisting resting orders was small. Such circumstances hardly convey what Mr. Oystacher subjectively intended when he placed the bids and offers.

Remarkably, Professor Bessembinder apparently did not even develop the selection criteria for the narrowed set. Instead, those criteria were hand-picked by the CFTC, at some point ***after*** Professor Bessembinder had begun to review Mr. Oystacher's trade data. *See* Bessembinder Tr. at 13:7-16 ("The final decisions were the decision of the. . . [CFTC] Division of Enforcement[]"); *Id.* at 12:2-15 (explaining that the narrowing criteria were "developed for the purposes of defining the narrowed set of transactions that I analyzed"); *id.* at 58:5-8 (admitting that the narrowing criteria were determined after Professor Bessembinder had received Mr. Oystacher's trade data). Stated otherwise, the CFTC and Professor Bessembinder did not apply accepted criteria to Mr. Oystacher's trading data to determine whether there was a potential violation. Instead, they reversed the scientific process by having Professor Bessembinder use the pre-selected trading data to determine what criteria to incorporate into his analysis in order to conclude that Mr. Oystacher violated the Spoofing Provision. *See* Bessembinder Tr. at 9:15-20 (admitting, in relevant part, that "[t]he narrowing criteria were developed on the basis of certain

patterns in the data."). These self-serving criteria are also far from sufficient in light of what the Policy Statement says the CFTC will consider. *See* Policy Statement at 14947.

3. Professor Bessembinder Abandons His Own Methodology to Shoehorn the ZN Orders Into the PI Hearing. A principled application of Professor Bessembinder's own analysis of challenged orders from the other Relevant Markets does not support his conclusion that the ZN orders are "spoofs." In fact, the ZN orders diverge from several of the purported tests for divining intent to "spoof" on which Professor Bessembinder relies most heavily for his conclusions relating to the non-ZN orders. *See* Bessembinder Tr. at 286:11-23, 295:16-296:6; *see also* Bessembinder Rebuttal Rep. at ¶ 72. The results of the ZN analysis reflect that:

- Only two of the fifty-three ZN flip events include original orders that satisfy Professor Bessembinder's selection criteria. *See* Bessembinder Rebuttal Rep. at ¶¶ 12, 91.

- Mr. Oystacher does not significantly accelerate his order entry on the cancel side within five seconds prior to his flips. *See* Bessembinder Rebuttal Rep. at ¶ 92.

- Nor did "Mr. Oystacher's rate of Iceberg usage on the cancel side decline[] dramatically in the last second before his flips." *See* Bessembinder Rebuttal Rep. at ¶ 76.

- "The magnitude of Mr. Oystacher's cancel side order entry relative to the quantity of displayed orders in the limit order book . . . is not as great on the examined dates in February 2016 as it was during the earlier periods." *See* Bessembinder Rebuttal Rep. at ¶ 92.

- Of the two ZN events that meet his selection criteria, the original ZN orders were "not statistically significant" in improving market quality, meaning that Mr. Oystacher's original ZN orders were not large enough to create the appearance of "false market depth." *See* Bessembinder Rebuttal Rep. at ¶ 89.

- Mr. Oystacher's number of flip events was also relatively low in comparison to his overall trading activity. Specifically, there were twenty-three other traders who had more flip events than Mr. Oystacher did on the examined dates, notwithstanding that Mr. Oystacher ranked fifth in contracts entered and third in contracts traded. *See* Expert Sur-Rebuttal Report of Jerry W. Markham (Mar. 19, 2016) (ECF No. 83) ("Markham Rebuttal Rep.") at ¶ 8; *see also* Supplemental

Report of Daniel R. Fischel (Mar. 21, 2016) (ECF No. 85) ("Fischel Rebuttal Rep.") at ¶ 4.

Moreover, to manufacture an appearance of order entry acceleration with respect to the ZN orders, Professor Bessembinder invented a new purported test that diverges from the one that he previously applied to the non-ZN orders. Pursuant to the new test, Professor Bessembinder analyzed order entry behavior in five second intervals (rather than one second intervals) in the thirty second-period prior to flip events (rather than a ten-second period). *See* Bessembinder Rep. at ¶¶ 39-40; *see also* Bessembinder Rebuttal Rep. at ¶¶ 80-81. This is yet another way in which Professor Bessembinder has retrofitted his methodology to fit his desired conclusion.

In any event, both the old test and the new test are fundamentally flawed because Professor Bessembinder lumps the flip events together and analyzes them ***in the aggregate***. *See* Bessembinder Rebuttal Rep. at ¶¶ 38-39. He then assumes that what is true for the group must be true for the individual trades that comprise the group – a flaw known as "aggregation bias." *Id.* at ¶ 82. It is not. A review by flip event makes plain that, in fact, there is no systematic pattern of acceleration before the ZN flips. *See* Fischel Rebuttal Rep. at ¶ 17; *see also* Fischel Tr. at 270:15-271:5.

Simply stated, the ZN orders have very little in common with what Professor Bessembinder contends are the indicia of "spoofing." By abandoning his own methodology in order to conclude that the ZN orders reflect ongoing "spoofing," Professor Bessembinder implicitly concedes that his processes are arbitrary and his conclusions are unreliable. He also lays bare an unwavering commitment to corroborating whatever story the CFTC pays him to tell.

4. <u>The "Relatively High Execution Rates" of the New Orders are Not a Proxy for Prohibited Intent.</u> *Contra* Bessembinder Rep. at ¶¶ 60-61. The original orders were, by definition, cancelled. At the time they were placed, there were also other orders resting ahead of

them. It is therefore unremarkable that the original orders were not filled at particularly high rates. *See* Fischel Rep. at ¶ 29-30. In contrast, the new orders were entered promptly after Mr. Oystacher observed signals that informed his new view of the market. He therefore entered them as marketable orders. *Id.* at ¶ 9. By definition, such orders are likely to be filled. *Id.* at ¶¶ 9, 30. In addition, Mr. Oystacher generally left the new orders open for longer periods of time while waiting for his revised forecasts to yield the results that he predicted. *Id.* at ¶ 30. The disparity in fill rates is the natural consequence of the foregoing. *Id.* at ¶¶ 9, 30.

5. The Total Number of Contracts Cancelled is Likewise Not a Reliable Indicator of Premeditated Cancellation. Professor Bessembinder's focus on the total number of contracts that Mr. Oystacher cancelled is similarly misplaced. On average, Mr. Oystacher's orders were substantially larger than the orders of other traders. *Id.* at ¶ 9. The fact that Mr. Oystacher cancelled more contracts than other traders is merely the function of that difference. *Id.* In addition, in five of the six Relevant Markets, Mr. Oystacher cancelled "a smaller percentage of his orders than other traders, on average." *Id.* at ¶ 9, 12.

6. The Frequency of Mr. Oystacher's Flipping Does Not Reflect Premeditated Cancellation. Viewed in context, the frequency of Mr. Oystacher's flipping is not anomalous. *Id.* As the market data reflects, traders frequently flip their positions, and other traders did so in the aggregate more often than Mr. Oystacher. *Id.*

8. Iceberg Orders Do Not Signify Premeditated Cancellation. There is nothing nefarious about Iceberg orders. They were specifically allowed in each of the Relevant Markets in which Mr. Oystacher used them, and traders may choose that functionality for any number of legitimate business reasons. *See, e.g.*, Fischel Rep. at ¶ 9, 27. Here, Mr. Oystacher's use of the Iceberg option was consistent with legitimate trading. For example, Mr. Oystacher chose the Iceberg

option when he wanted to insulate his forecasts and / or trading strategy from other market participants – a practice that is not only permissible, but customary. *Id.; see also* Markham Rep. at ¶ 135 ("[Iceberg orders] are a popular form of limit order that allows traders to shield the actual size of their orders from other traders viewing the order book"). Moreover, other market participants, including algorithmic traders, know that "[t]here is always the potential" that Icebergs may be present. *See* Wasko Tr. at 105:19-25. It was likewise appropriate for Mr. Oystacher to forego the Iceberg option when he wanted a passive order to enjoy priority over orders that other traders subsequently entered at the same price. *See* Fischel Rep. at ¶ 9, 26. There is thus no adverse inference to be drawn from Mr. Oystacher's use – or non-use—of the Iceberg functionality. *Id.* at ¶ 9, 23, 26-28.

9. The Extent and Speed of Mr. Oystacher's Cancellations is Consistent with Legitimate Trading. Mr. Oystacher's cancellation rates and speed are not anomalous. *See* Fischel Rep. at ¶ 9, 13; *see also* Fischel Tr. at 48:19-21. In comparison to other traders, he generally cancelled a ***lower*** percentage of his contracts. *See* Fischel Rep. at ¶ 9, 13. The percentage of cancellations that occurred within one second of having entered the original orders is also lower for Mr. Oystacher than it is for other traders. *Id.*

10. Mr. Oystacher's Trading Patterns Concerning Orders that Were Not Followed by a Qualifying Flip Did Not Substantially Diverge from His Trading Patterns Concerning Orders that Were. Professor Bessembinder contends that Mr. Oystacher traded differently when engaged in flipping. He is wrong. For example, Mr. Oystacher's non-flip orders include aggressively-priced non-Iceberg orders (as the original order set does), as well as marketable Iceberg orders (as the new order set does). Fischel Rep. at ¶ 9 ("In fact, the data show that Mr. Oystacher often placed large, imbalanced, aggressively-priced non-Iceberg orders but did ***not*** cancel these orders

in flips within one second"); *see also id.* ¶¶ 23, 27. Furthermore, the original orders were not, on average, materially larger than the non-flip orders. *Id.* at ¶ 9.

11. Mr. Oystacher's Trading is Consistent With Market Making. As noted above, *see supra* Part B, Mr. Oystacher is a market maker. As such, he is not committed to either side of the market, but pursues opportunities relating to both buying and selling and is active on both sides of the market (although not necessarily simultaneously). There has never been any requirement in the futures industry that market makers continuously and simultaneously quote both a bid (buy) and offer (sell) price. *See, e.g.*, Markham Rep. ¶ 41. Accordingly, Professor Bessembinder's conclusion that Mr. Oystacher cannot be a market maker simply because he does not "consistently maintain[]. . . both buy and sell orders on the limit order book," Bessembinder Rep. ¶¶ 98-99, misses the point. Markham Rep. ¶¶ 84-86.

At their core, Professor Bessembinder's analyses are result-oriented and his conclusions are unsound. The Court should reject them.

C. Mr. Oystacher Did Not Use His Wash-Blocker to Further Any Purported "Spoofing" Scheme

Just as the CFTC cannot establish that Mr. Oystacher violated the Spoofing Provision (either pursuant to *Unifund* or pursuant to the lower standard for which the CFTC advocates, *see Twombly*, 550 U.S. at 547, 127 S. Ct. at 1960), the CFTC cannot demonstrate that he violated Rule 180.1. There was never any "spoofing" scheme. *See supra* Part II.A. As a consequence, Mr. Oystacher cannot have used his wash-blocker to further one. He thus bears no resemblance to a "burglar [who] converts a paperclip from a useful office tool into a manipulative device when she uses it to break into someone's home." *Contra* PI Mot. at 28.

In addition, although the CFTC misrepresents the standard as "knowingly or recklessly." *see* PI Mot. at 2, a violation of Rule 180.1 actually requires proof of intent or, in the alternative,

recklessness that is so egregious that it approximates intent. *See* Rule 180.1(a)(1) ("It shall be unlawful for any person . . . to intentionally or recklessly. . . use or employ, or attempt to use or employ, any manipulative device, scheme or artifice to defraud"); *see also* Final Rule: Prohibition on the Employment, or Attempted Employment, of Manipulative and Deceptive Devices and Prohibition on Price Manipulation, 76 Fed. Reg. 41398-01, at *41404 (July 14, 2011) (confirming that recklessness under Rule 180.1 means "an act or omission that 'departs so far from the standards of ordinary care that it is very difficult to believe the actor was not aware of what he or she was doing'") (quoting *Drexel Burnham Lambert, Inc. v. CFTC*, 850 F.2d 742, 748 (D.C. Cir. 1988)); *Sundstrand Corp. v. Sun Chem. Corp.*, 553 F.2d 1033, 1045 (7th Cir. 1977) (holding that under SEC Rule 10b-5, recklessness is "an extreme departure from the standards of ordinary care, and . . . presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it"). [22] That mental state is missing here.

It is neither manipulative nor reckless to enable a wash-blocker to function as Mr. Oystacher did. *See* Donohue Comment Letter at 8 (recognizing that wash blocking functionality "serves the legitimate purpose of avoiding violation of the prohibition on wash sales" and expressing concern that "the impact on the order book in the market may appear similar to the

[22] Under the circumstances, a violation of Rule 180.1 requires proof of intent. That is because the plain text of Rule 180.1(a) contemplates that the requisite mental state—specific intent or recklessness—will turn on the underlying scheme that is alleged. *See* 17 C.F.R. 180.1(a)(1) (making it unlawful to "intentionally or recklessly" use or employ, or attempt to use or employ, any manipulative device, scheme, or artifice to defraud). Here, the only purported "scheme" is "spoofing," which itself requires proof of premeditated cancellation. *See, e.g.*, PI Mot. at 1 (alleging that Mr. Oystacher "intentionally and repeatedly engaged in a manipulative or deceptive spoofing scheme"); *see also* Compl. at 1 (alleging Mr. Oystacher engaged in a "manipulative and deceptive spoofing scheme"); *id.* at 32-33 (alleging a manipulative or deceptive device, scheme, or artifice to defraud based on purported "spoof orders" and "manipulative and deceptive spoofing strategy"). Because the CFTC cannot demonstrate the requisite intent for a "spoofing" violation, it necessarily cannot establish a violation of Rule 180.1 in connection with such purported "spoofing."

'spoofing example' [. . .] but the original offer was bona fide and there was no *intent* to mislead market participants") (emphasis in original). Wash-blockers are common compliance tools that are sold—and made available by many exchanges--specifically to help traders avoid violating the prohibition on intentional wash-sales. *See, e.g.*, Bessembinder Tr. at 250:20-24; [redacted]; McCormack Tr. 206:2-7. There are generally two ways to accomplish that objective: (i) to cancel existing orders if new ones are placed in the opposite direction with which those existing orders might otherwise be matched; or (ii) to reject an incoming order in the opposite direction. *See* McCormack Decl. at ¶ 28. These are standard functionalities that wash-blockers routinely include; not manipulations of them. It is likewise typical for wash-blockers to cancel an existing order "simultaneously" with entering a new one (as the CFTC alleges that Mr. Oystacher's did). *See* Bessembinder Tr. at 243:14-16 ("If my understanding of the wash blocker [software typically used by market participants] is correct . . . the cancel occurs and then the trade-side order enters simultaneously"); *see also id.* at 237-245 (providing "general understanding of what wash blockers do" and acknowledging that they generally cancel and replace within a microsecond). This is another reason why the Court should deny the PI Motion.

III. Mr. Oystacher is Not a Threat to the Market

Because the CFTC cannot establish either a *prima facie* case or a "more substantial" showing of any purported violation, *see supra* Part II, there is no basis on which to conclude that such violations are even reasonably likely to occur in the future. *See CFTC v. Muller*, 570 F.2d 1296, 1300 (5th Cir. 1978); *see also* PI Mot. at 29-30 (arguing that occurrence of purported violations suggests a likelihood of future violations).

Moreover, as cases like *FTC v. Inbound Call Experts, LLC*, No. 14-71695-CIV, 2014 WL 8105107 (S.D. Fla. Dec. 23, 2014), underscore, the voluntary modification of ongoing conduct

mitigates any purported risk of future violations. *Inbound Call Experts* involved an FTC enforcement action that was filed together with an *ex parte* motion for a temporary restraining order, receivership appointment and statutory asset freeze. *Id.* at *1. The FTC subsequently sought a preliminary injunction to extend the *ex parte* relief. At the hearing, defendants established that they had begun to cease the relevant conduct a few months earlier and that they were willing to implement additional modifications going forward. *Id.* at *5. Based on those good faith efforts, the court ultimately concluded that "the deception of which Plaintiffs complain is unlikely to continue until the date of final resolution of this matter." *Id.* at *5. It therefore substantially dissolved the asset freeze, limited the receiver, and entered a much more modest injunction than what the FTC requested. *Id.* at *6-7.

The changes at issue in *Inbound Call Experts* pale in comparison to the efforts that 3 Red has made. Throughout the relevant period—and more than ten months prior to this Action—3 Red voluntarily modified its trading practices in a good-faith attempt to reduce the likelihood that certain orders may be misperceived, through the use of hindsight analysis, as "spoofing" or resulting from an improper use of the wash-blocker. *See supra* Part B. Those efforts continue today. *See* O'Connor Decl. at ¶ 15. Among other things, 3 Red has adopted the Delayed Replace for Cancel/Replace Tool and increased, currently [redacted], the waiting period between the cancellation of an original order and the placement of a new one in the opposite direction. *See* O'Connor Decl. at ¶ 11b; *see also* O'Connor Tr. at 191:1-192:3. This is an eternity in the Relevant Markets. *See, e.g.*, Citadel SEC Comment Letter at 5 ("[I]n today's markets . . . [just] 350 microseconds is an exceedingly long period of time").

Accordingly, the Delayed Cancel/Replace Tool all but ensures that algorithmic traders have an even bigger temporal advantage with respect to their ability to quickly identify and react

to reduced visible liquidity. It also eliminates the likelihood that Mr. Oystacher may in the future be accused of having "exploited" the wash-blocker to produce "virtually simultaneous[]" flips and cancellations. *See* Bessembinder Tr. at 319:11-320:19 (stating that a one second delay between the cancellation of an order and the placement of a "flip" order "would give somebody much more opportunity to react to the cancellation"); *see also* Bessembinder Rebuttal Rep. at ¶ 19. These and other voluntary modifications, *see supra* Part B, are further buttressed by 3 Red's host of internal controls. See O'Connor Decl. at ¶¶ 5, 13.

Similarly, Mr. Oystacher now limits the displayed size of his orders. *See* O'Connor Tr. at 186:3-190:15. This significantly reduces the possibility that his orders will affect whatever balance is in the observable limit order book, thereby rendering untenable any future suggestion that Mr. Oystacher has placed orders to lure the algorithmic traders into joining him on a particular side of the market. *See* Bessembinder Rebuttal Rep. at ¶¶ 19, 23.[23]

Significantly, 3 Red implemented its preventive measures of its own accord, notwithstanding that they further disadvantage Mr. Oystacher in relation to the already dominant algorithmic traders. *See* O'Connor Decl. at ¶ 11. This was done without any substantial assistance from regulators, despite 3 Red having repeatedly sought—but never received—such guidance. See O'Connor Decl. at ¶ 11. Taken together, the preventive measures therefore not only reduce the ways in which Mr. Oystacher's trading might otherwise appear to resemble "spoofing," but demonstrate a persistent commitment to complying with—rather than violating—whatever it is that regulators have indicated they may interpret the Spoofing

[23] The exchanges' apparent monitoring of 3 Red's trading on a daily basis, coupled with the CFTC's demonstrated ability to do the same, further reduces any likelihood of future violations. *See* McCormack Decl. at ¶ 103; Ex. 2 to PI Mot. (addressing CFTC monitoring of Defendants in November 2015). Moreover, as 3 Red's incorporation of CME's feedback in connection with the Dynamic Max Quantity at Price Tool reflects, 3 Red remains receptive to guidance and willing to consider additional measures. O'Connor Decl. at ¶ 15.

Provision to mean. In this way, the preventive measures betray any assertion that future violations are likely. *Compare, e.g., SEC. v. Big D. Oil & Gas Co.*, 434 F. Supp. 589, 590 (N.D. Tex. 1977) (finding that SEC failed to establish likelihood of recurrence because "defendants voluntarily instituted remedial changes in the structure and direction of its program"); *SEC v. Keller Indus., Inc.*, 342 F. Supp. 654, 660 (S.D.N.Y. 1972) (finding lack of "cognizable danger of recurrent violation" due to defendants' "adopt[ion of] a new method" that they have "followed . . . since" the prior violation); *and CFTC v. Commodities Fluctuations Sys., Inc.*, 583 F. Supp. 1382, 1385-86 (S.D.N.Y. 1984) (finding little likelihood of continuing violations due to defendant's prompt attention to rectifying prior violations after having learned of them); *with* PI Mot. at 30, (arguing that because Mr. Oystacher is a professional trader, future violations are likely).[24]

It is misleading (if not deceptive) for the CFTC to represent that Mr. Oystacher has "persisted in . . . illegal conduct despite multiple regulatory inquiries, sanctions, and warnings." *Contra* PI Mot. at 2. Although the sanctions on which the CFTC relies were finalized in 2014 and 2015, most of them relate to underlying order activity that occurred four to six years ago, primarily between 2010 and 2012. *See* Exs. 6-8 to PI Mot; *see also* O'Connor Decl. at ¶ 17-18. Importantly, 3 Red was not afforded the opportunity to provide a thorough explanation relating to the challenged conduct. *See id*. The majority of them were also the result of settlements to

[24] In the ten months since 3 Red implemented the majority of its voluntary measures, the only orders that the CFTC has identified as "spoofing" are the ZN orders. As detailed above, those orders are wholly inconsistent with the "spoofing" theory. *See supra* Part II.B. They therefore do not support any finding that future violations are likely. Quite to the contrary, they demonstrate that 3 Red's voluntary trading modifications and compliance measures have already substantially reduced the likelihood of future violations. The most recent measures—such as the Delayed Replace for Cancel/Replace Tool and the Dynamic Max Quantity at Price Tool—post-date the ZN orders and will all but eliminate whatever marginal possibility of future violations purportedly remains. Importantly, no regulator has flagged any of 3 Red's order placement and cancellation activity since it instituted those measures. *See* O'Connor Decl. at ¶ 15.

which 3 Red agreed for various reasons—including, among others, that the exchanges are private entities that generally do not consider themselves to be bound by the fundamental fairness of due process—without any admissions of wrongdoing. *See* O'Connor Decl. at ¶ 17.[25] Moreover, none of the exchanges to which the sanctions pertain currently bars Mr. Oystacher from trading in its markets.[26] The Court should reject the CFTC's attempt to manufacture "persiste[nt]. . . illegal conduct" by obscuring the relevant context of the events on which it purports to rely. *See* PI Mot. at 18-19.

Finally, the CFTC's delay in seeking an injunction and the staleness of its purported evidence demonstrate that there is a particularly low likelihood of future violations with respect

[25] The Eurex sanctions are the exception, but they are currently on appeal based, in part, on the following grounds: (i) a lack of due process afforded to 3 Red during the investigation process (e.g., no member of the Trade Surveillance Office of Eurex has agreed to meet or interview Mr. Oystacher) and (ii) misinterpretation and application of German financial market statutes by the Trade Surveillance Office and the Eurex Disciplinary Committee. *See* O'Connor Decl. at ¶ 18. In addition, following the initiation of the most recent trade practice inquiry in the Eurex matter—and prior to the CFTC's commencement of this Action—Eurex acknowledged Mr. Oystacher's trading modifications with approval. *See* E-mail from Michael Peters (Eurex) to Gregory O'Connor, dated Aug. 27, 2015 [3RED_CFTC136533], attached as Ex. A to O'Connor Dec., at ¶ 19 ("Eurex did . . . observe a change in Igor Oystacher's trading behaviour. . . . I do encourage you to continue your efforts to comply with Eurex' rule on market integrity").

[26] The CFTC makes much of the fact that Mr. Oystacher cannot currently trade in the VIX market. *See* PI Mot. at 19, 30. But that is only a fraction of the story. [redacted] *see also* Declaration of Karen Christiansen (October 14, 2015) (ECF No. 20-7) ("Christiansen Decl.") at ¶ 20. CFE accomplished this by threatening that the FCM's failure to block Mr. Oystacher would be viewed by CFE as "extremely aggravating" in the event that his trading conduct were ultimately found to be unlawful. *See* Christiansen Decl. at ¶ 20. At the time, the FCM was already subject to an ongoing investigation by CFE and was therefore particularly vulnerable to this pressure. *See* Ex. 23 to Cole Decl., E-mail from Lizabeth Fagan to Lisa Jones, dated Apr. 24, 2014 (CFE0014735). [redacted]

to five of the Relevant Markets. *Contra* PI Mot. at 31-32. As the record reflects, the CFTC waited four years before filing its Complaint and, when it finally did so, elected to wait another month before seeking a preliminary injunction. That timeline hardly suggests any genuine fear of impending violations. In addition, the CFTC's evidence largely rests on order placement and cancellation activity in the Copper, Crude Oil, Natural Gas and VIX markets that are several years old, and does not even attempt to challenge any conduct in the ES market after May 2015 (which is nearly a year ago). The only logical inference is that with respect to these five Relevant Markets, the challenged conduct has never been of sufficient magnitude or of such frequency as to merit the relief that the CFTC now seeks. *See, e.g.*, *MB Fin. Bank, N.A. v. MB Real Estate Servs., L.L.C.*, No. 02 C 5925, 2003 WL 22765022, at *8 (N.D. Ill. Nov. 21, 2003) (identifying delay of ten months between discovery of defendant's conduct and request for preliminary injunction as "inconsistent" with assertions of urgency). Accordingly, the Court should deny the PI Motion.

CONCLUSION

For the foregoing reasons, and based upon the record to be established at the PI Hearing, 3 Red and Mr. Oystacher respectfully request that the Court deny the PI Motion in its entirety.

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Respectfully submitted,

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CERTIFICATE OF SERVICE

The undersigned, an attorney, hereby certifies that, on April 1, 2016, she caused a true and correct copy of the foregoing ***Opposition to Plaintiff's Motion for Preliminary Injunction*** to be served upon all parties by First-Class Mail.

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