CRS Reports & Analysis

Legal Sidebar

First Spoofing Conviction Gives Teeth to Dodd-Frank in Prosecuting Commodities Violations

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"Spoofing," for the purpose of this sidebar, is the practice of manipulating commodities prices by placing orders without intending to trade on them, often by canceling the orders soon after the orders are placed. This can briefly create the appearance of movement in the commodities markets and result in profit to the spoofer. On November 3, 2015, an Illinois jury found Michael Coscia guilty of violating an anti-spoofing provision of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) (*United States v. Coscia*. No. 14-cr-00551 (*jury verdict* N.D. Ill. Nov. 3, 2015)). This is the first conviction under the anti-spoofing law since Dodd-Frank was enacted in 2010.

Section 747 of Dodd-Frank amended section 4(c)(a) of the Commodity Exchange Act (CEA) to prohibit any person from engaging in trading, practice, or conduct on a registered entity, such as a commodities exchange, that violates bids or offers, shows intentional or reckless disregard for the orderly execution of commodities transactions during the closing period, or spoofing. Dodd-Frank gave the Commodity Futures Trading Commission (CFTC) the authority to issue rules that are reasonably necessary to prohibit the trading practices set out in section 747. The CFTC issued interpretive guidance to provide participants in the commodities markets with the scope and application of the statutory prohibitions.

The United States alleged that Coscia created two computer algorithms, Flash Trader and Quote Trader, that posted orders to two commodities exchanges and that Coscia intended to cancel the orders and did in fact cancel the orders before they were completed. He allegedly took advantage of the brief resulting price fluctuations to profit $1.3 million over three months. The jury took only a short time to agree with the government's arguments and found Coscia guilty of violating the anti-spoofing statute and other commodities law violations. Before the anti-spoofing provision of Dodd-Frank, prosecutors might have used other commodities statutes, such as the anti-fraud provision of section 6b of the CEA, to prosecute such activity. However, the anti-spoofing statute provides a specific remedy and sets out a specific standard of proof—intent or reckless disregard for execution during the closing period of the commodities transaction.

Some commenters had expressed concern that the complexity of the case and the strong defense team might have caused confusion among members of a jury. However, the complexity of the case may not have been a problem for the jury, as it debated about an hour before returning the guilty verdict. This victory for the government may encourage it to use the anti-spoofing statute to prosecute other alleged high-profile spoofers, such as U.K. trader Navinder Sarao, who is accused of contributing to the 2010 flash crash and thereby profiting $40 million over five years. (The U.S. Department of Justice filed a criminal complaint against Sarao in February 2015. He has been indicted by a U.S. federal grand jury for various market manipulation practices and is facing extradition to the U.S.) (For additional information on high frequency trading and flash crashes, see a previously published sidebar.)

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