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MARKETS

Big Trader Strikes Back Against CFTC

DRW Investments founder Don Wilson Jr. is fighting allegations that his firm placed manipulative bets in an obscure corner of the futures market



Don Wilson Jr. says the CFTC's actions represent 'disruptive regulation at its worst.' PHOTO: KRISTAN LIEB FOR THE WALL STREET JOURNAL

By **BRADLEY HOPE**

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One of the country's biggest traders is going to war with its regulator.

Don Wilson Jr., the founder of DRW Investments LLC, is fighting allegations by the Commodity Futures Trading Commission that his firm placed manipulative bets in an obscure corner of the futures market four years ago.

Rather than settling and possibly paying a fine in a case that doesn't require him to admit guilt, Mr. Wilson is digging in for a fight, turning a dispute over \$20 million in trading profits into a referendum of futures-market oversight that many traders consider heavy-handed. The CFTC hasn't had a market-manipulation case go to trial since 2008, according to a CFTC spokesman. A verdict of guilty against the trader in that

case was overturned by a federal appeals court in 2010.

Mr. Wilson said in a statement that the CFTC's actions represent "disruptive regulation at its worst and we therefore feel compelled to fight these outrageous charges."

In the latest twist in the standoff, one of Mr. Wilson's lawyers—former White House Special Counsel Lanny Davis—has alleged that the CFTC withheld evidence that undermined the government's claims of manipulation until about a year into the case.

The allegation centers on a report produced by another futures industry regulator that Mr. Davis said contradicted the CFTC's allegation that DRW's orders were manipulative. The CFTC had the report when it decided to bring charges against DRW but didn't share it at the time, according to Mr. Davis.

In a letter sent to several congressional staffers, Mr. Davis said the CFTC's behavior "raises a question of intentional abuse of process and violation of civil rights." He also sent letters to CFTC commissioners and is planning to take the issue to members of the Senate and White House, he said in an interview.

The CFTC declined to comment on DRW's lawsuit.

Mr. Wilson and his Chicago-based firm are taking a risk in challenging the allegations, as settling the case could lead to a lower penalty. The trader's aggressive approach might make the regulator less willing to settle, according to former regulators.

The battle with closely held DRW, which has 700 employees and trades on more than three dozen exchanges around the world, reflects broader tensions between the CFTC and traders who believe the regulator has skewed views of what constitutes market manipulation.

The CFTC's case, filed in a Manhattan federal court in 2013, involves trading in futures contracts on interest-rate swaps traded on Nasdaq Inc.'s exchange. Interest-rate swaps are contracts that allow firms to protect or bet against future swings in rates.

The CFTC said DRW earned \$20 million by entering orders it didn't intend to complete during the 15-minute settlement period at the end of a trading session over the span of 118 days, a practice called "banging the close," an illegal tactic. Such orders can influence prices because some exchanges set the closing price of certain derivatives based on the quotes received during that period.

The CFTC alleges in its complaint that DRW sought to manipulate the price to support a

\$350 million bet on interest rates the company had made at the end of 2010. When the market didn't behave in a way their models had predicted it would, according to the CFTC's complaint, DRW entered orders to move the price in a way that earned them the allegedly illegal profits.

Those artificial prices affected the value of 1,000 futures contracts, according to the CFTC's complaint.

"Traders cannot engage in manipulative acts to affect the price of futures contracts to achieve their desired profits, regardless of the so-called motive," the CFTC's acting head of enforcement, Gretchen Lowe, said in a statement at the time.

DRW denied in court documents it manipulated the market, saying it often entered orders throughout the day that were available for others to trade against.

A key piece of evidence the firm said can prove its trading was appropriate is a September 2011 review by the National Futures Association of the timing of DRW's orders over a period that included the same days the CFTC alleged DRW manipulated the market. The review concluded that the manner in which DRW traded reduced the likelihood that the firm manipulated prices. The National Futures Association is a self-regulatory agency that polices the futures industry. The association declined to comment.

DRW's lawyers received the document from the CFTC as part of a discovery process late last year in anticipation of the trial.

The case is a rare public run-in for DRW with regulators since it was founded in 1992 and is an uncustomary turn for Mr. Wilson, who has kept a relatively low profile despite his firm's high volume of trading. Starting out as a floor trader at the Chicago Mercantile Exchange, Mr. Wilson built up DRW from scratch in the 1990s.

In interviews at industry events over the years, he has credited the firm's success to an early understanding that quantitative skills, computers and trading know-how could be combined to reap superior profits.

About a quarter of the company's business involves high-frequency trading that relies on computers that trade automatically using algorithms and high-speed telecommunications connections. In recent years, Mr. Wilson, 47 years old, has expanded into real estate. He also is an avid sailor and supporter of a charter school in Chicago that bears the firm's name.

Even before the CFTC formally charged him and his firm, Mr. Wilson tried some uncommon tactics to get it stopped in its tracks.

He filed a lawsuit against the CFTC after it informed him it was planning to bring charges, but the regulator filed them anyway.

He then filed a motion for the judge to throw out the charges, arguing that despite providing a “dense thicket of technical jargon, trading charts and graphs” the CFTC didn’t prove he intended to create a fake price.

A federal judge disagreed, and the case is headed for a trial in the second half of 2016, lawyers said.

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