DFA, Two Former Executives To Pay $12 Million To Settle CFTC Charges

CFTC Believes DFA, Hanman, Bos Attempted To Manipulate Class III Futures Prices By Buying Cheese On CME Cash Market

Washington—Dairy Farmers of America (DFA), its former chief executive officer Gary Hanman, and its former chief financial officer Gerald Bos will pay a $12 million civil monetary penalty for attempting to manipulate the Class III milk futures contract and exceeding speculative position limits in that contract, the US Commodity Futures Trading Commission (CFTC) announced Tuesday.

Also, Frank Otis, former president and CEO of a DFA subsidiary, and Glenn Millar, former executive vice president of that subsidiary, will pay $150,000 for aiding and abetting DFA’s speculative position limit violations, the CFTC said.

In addition to imposing civil penalties, the CFTC administrative order bars Hanman and Bos from trading futures for five years.

It also bars DFA from engaging in speculative trading in Class III milk futures contracts for two years, and orders DFA to comply with certain undertakings, including:
- Implement and maintain a compliance and ethics program designed to detect and prevent violations of the Commodity Exchange Act and CFTC regulations by any DFA director, officer, employee or agent.
- Retain a monitor, at DFA’s expense, to review for a period of two years: DFA’s futures trading for compliance with speculative trading prohibitions and DFA’s sales and purchases on the Chicago Mercantile Exchange (CME) cash cheese market to ensure that any such cheese purchases are made for “legitimate business purposes,” and “not in an attempt to manipulate Class III milk futures contracts.”
- The monitor’s authority and duties are to be broadly construed. In order to determine DFA’s compliance with the order, the monitor will inspect such DFA documents as reasonably necessary relating to DFA’s transactions in Class III milk futures and/or the CME cash cheese market; and meet with and interview such employees, officers, and directors of DFA, and any other relevant persons, relating to DFA’s activities in the Class III milk futures and the CME cash cheese markets.
- The monitor will prepare a confidential annual report on the yearly anniversary of the engagement that will describe the execution of his responsibilities required by the order. DFA will be required to cooperate fully with the monitor, and the monitor will have the authority to take such reasonable steps, in his view, as may be necessary to be fully informed about the operations of DFA within the scope of his responsibilities as set forth in the order.

DFA is also required to provide future cooperation to the CFTC.

DFA said the settlement ends the CFTC’s investigation into DFA’s trading activities on the Chicago Mercantile Exchange (CME). Rick Smith, who succeeded Hanman as DFA’s president and CEO, said that agreeing to the settlement, which it did without admitting or denying the CFTC’s findings in the administrative order, was in the best interests of the cooperative and its members.

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tained in the order against DFA, Hanman and Bos, during the period from May 21 through June 23, 2004, DFA, Hanman and Bos “attempted to manipulate the price” of the CME June, July, and August Class III milk futures contract.

DFA, Hanman and Bos attempted to manipulate Class III futures contract prices through purchases of Cheddar blocks on the CME cash market in an effort to minimize potential losses from DFA’s speculative long Class III milk futures positions while liquidating such positions, the order stated.

In addition, on one or more days in 2004, DFA accumulated speculative contracts in Class III milk futures positions while liquidating such positions, the order noted.

Going into more detail, the order explains that, in early 2004, DFA, acting at the direction of Hanman and Bos, purchased speculative June, July and August Class III milk futures contracts.

These long positions were tracked by DFA in an internal sub-account referred to as the “Arbitrage Account” and in internal sub-accounts designated for two subsidiaries, according to the order.

Beginning on April 14, 2004, as sellers offered Cheddar blocks on the CME cash market, DFA purchased block Cheddar cheese, the order continued. From May 21 to June 23, 2004, DFA, at the direction of Hanman and Bos, purchased and took delivery of 323 loads of Cheddar blocks at $1.80 per pound.

During this period, DFA was the sole buyer of Cheddar blocks on the CME, the order pointed out.

As of May 21, 2004, the Class III milk futures position held in all DFA accounts, including those of its subsidiaries, totaled in excess of $12 million civil penalty and a trading ban, and ensures future compliance with federal commodities laws through the imposition of a monitor, said Stephen J. Obie, CFTC acting director of enforcement.

“Given the severity of the past misconduct, we are pleased that DFA has committed to reforming its trading practices,” Obie added.

“Settling this matter will allow us to focus wholly on serving our members and moving the cooperative forward,” said Smith, who took the helm of DFA in 2006. “We are looking beyond past problems and forward to our bright future.”

The CFTC thanked the US Department of Agriculture (USDA) and Tom Sandy and Estelle Nwadike of the CME’s market regulation department for their assistance in this matter.

A separate order concerning Otis and Millar states that, on one or more days in 2004, Otis and Millar “aided and abetted” DFA’s violations of the CME’s speculative position limits in Class III milk futures contracts by directing the speculative trading of Class III milk futures in an internal sub-account designated for one of DFA’s subsidiaries.

Under the order, Otis is liable for, and will pay, a civil monetary penalty in the amount of $60,000, plus post-judgment interest, and Millar is liable for, and will pay, a civil monetary penalty in the amount of $90,000, plus post-judgment interest.

US Sen. Russ Feingold (D-WI), who has been “working to improve protections against the manipulation of cheese prices” since the National Cheese Exchange was still operating in Green Bay, WI, said he was “pleased to see the CFTC’s investigation of a CEO who blatantly bragged about influencing prices yielded these significant penalties.”

While Dairy Farmers of America’s new management “seems committed to changing their culture, there is more that needs to be done to fully understand the problems and make sure they do not happen again,” Feingold continued.

For “some time now,” the US Department of Justice has reportedly had an open investigation regarding possible antitrust violations and improper executive payments from DFA’s previous management team, Feingold noted.

“I will push for the new administration to take a fresh look at these and other cases along with taking steps to ensure that there is sufficient oversight and coordination by the USDA, Justice Department and CFTC so that farmers, processors and consumers can have confidence in dairy prices,” Senator Feingold added.

DFA has committed to reform its trading practices and to liquidate its long speculative futures contract positions, the order noted.

The CFTC’s enforcement action “punishes those responsible for DFA’s manipulative scheme with a