How ex-JP Morgan silver trader's guilty plea could boost manipulation claim against bank

PUBLISHED TUE, NOV 13 2018 7:00 AM EST UPDATED TUE, NOV 13 2018 11:36 AM EST

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KEY POINTS

- John Edmonds, a 36-year-old Brooklyn resident, pleaded guilty in October to fraudulently manipulating the precious metals markets from 2009 to 2015.
- Nearly four years ago, a New York lawyer sued J. P. Morgan on behalf of three traders, accusing the bank of manipulating the silver futures market from 2010 through 2011, costing his clients $30 million in losses.
- Regulators have been cracking down on market manipulation in the decade since the 2008 financial crisis. Financial watchdogs have focused their attention on areas of Wall Street that few laymen pay any attention to.
- David Kovel, an attorney, told CNBC he was struck by how much in common his civil case pending in New York federal court has with the conduct admitted to by Edmonds in the ongoing criminal case in Connecticut.

The J.P. Morgan Chase & Co. headquarters in New York.

Amr Alfiky | Reuters

A previously secret guilty plea by a former commodity trader at J. P. Morgan Chase, who admitted that he rigged precious metals markets, has drawn the attention of a lawyer who has already accused traders at the nation's largest bank of similar conduct.

The lawyer, David Kovel, told CNBC he was struck by how much in common his civil case pending in New York federal court against J. P. Morgan Chase has with the conduct outlined in the ongoing criminal case in Connecticut against John Edmonds.

Edmonds, a 36-year-old Brooklyn resident, pleaded guilty in October to fraudulently manipulating the precious metals markets from 2009 to 2015.

He admitted working with "unnamed co-conspirators" at his former employer, J. P. Morgan, the Justice Department made public Nov. 6, when it unsealed the case in U.S. District Court in Connecticut.

Edmonds' criminal plea related to "spoofing," a certain type of improper trading that has been the subject of a broader regulatory crackdown on market manipulation in the decade since the 2008 financial crisis.

So far this year, the Commodity Futures Trading Commission has announced 26 enforcement actions that involved market manipulation, attempted manipulation, false reporting, spoofing or deceptive conduct. That is more than double the number in 2017 — and six times that in 2016.

Prosecutors said Edmonds learned the deceptive strategy "from more senior traders" at the bank, and that he "personally deployed this strategy hundreds of times with the knowledge and consent of his immediate supervisors." His guilty plea related specifically to trading in silver futures contracts, as well as in gold, platinum and palladium futures.

Nearly four years ago, Kovel sued J. P. Morgan on behalf of a colorful hedge fund operator and big-stakes poker player, Daniel Shak, and two metals traders, Mark Grumet and Thomas Wacker. The civil lawsuit accused J. P. Morgan of manipulating the silver futures market from 2010 through 2011, costing Kovel's clients $30 million in losses.

Edmonds isn't named in the Kovel case, or mentioned in its allegations. But he was questioned under oath by lawyers for the traders. And Edmonds worked at J. P. Morgan in the same group of traders who are identified as participants in the scheme alleged in the civil case.

“The conduct that Mr. Edmonds admits to is highly consistent with the conduct that my clients allege harmed them and it’s not surprising because he was working with the same people at J. P. Morgan trading in the silver markets at that time,” Kovel told CNBC.

“We are currently exploring how this could impact the evidence we will put forward in the case,” Kovel said.

Separately, last Wednesday, another group of lawyers filed suit in Manhattan federal court against Edmonds, J. P. Morgan and unnamed precious metals traders. The suit, which is seeking class action status, claims the parties engaged in manipulative precious metals futures trading.

Ordering but not executing

In spoofing, a trader uses a high-speed computer to send out a flurry of buy or sell orders to make it look like there is supply and demand in the market, without intending to complete the trades. The practice can distort prices for a commodity.

Edmonds’ scheme was designed to, and did, artificially move the price of precious metals futures contracts in a way that was favorable to him and his co-conspirators at J. P. Morgan to the detriment of other market participants, prosecutors said.

Edmonds’ attorney did not respond to requests for comment from CNBC. J. P. Morgan declined to comment.

In addition to Kovel, Mark Williams, a former Federal Reserve examiner and commodities risk manager, also sees similarities between the claims made in the criminal case and the lawsuit filed by Kovel.

“The M.O. seems to be the same, which is to potentially manipulate the market by providing false information for their own benefit,” Williams said. “That’s fraudulent behavior.”

The criminal case against Edmonds focuses specifically on a trade on Oct. 12, 2012, when he entered an order to sell 402 silver futures contracts at just after 1:08 p.m. CT.

Prosecutors said that when Edmonds made his offer, he did so “with the intent, at the time the offer was entered” to cancel the bid before it could be executed.”

Edmonds did that “so that [he] could purchase approximately six silver futures contracts at a below-market price.” The spoof order caused other traders to sell their positions or react in a way they would not otherwise have acted.

Kovel’s suit says that J. P. Morgan’s traders made “large manipulative trades” that caused “artificial fluctuations” in the prices of silver futures. Specifically, the bank’s traders allegedly made offers to buy or sell futures in a way that would affect the difference in prices between what sellers of silver futures contracts were asking and what buyers were offering. Some of this activity, he alleges, took place on the floor of the metals exchange.

A former J. P. Morgan executive, Robert Gottlieb, who now works for Koch Industries according to his LinkedIn profile, is described in the civil lawsuit as controlling “the decision making for J. P. Morgan’s silver positions and took the primary role in trading JP Morgan’s silver spreads.”

Gottlieb did not respond to requests for comment.

Lawyers for plaintiffs in the civil lawsuit have questioned Gottlieb under oath, and also J. P. Morgan’s former global commodities chief Blythe Masters and more than a half-dozen other current and former employees at the bank, court filings indicate. Masters declined to comment.

Federal prosecutors say they continue to investigate in connection with the criminal case lodged against Edmonds.

“By conspiring with his trading partners to place spoof orders, [Edmonds] blatantly attempted to profit off of an unfair market that he helped create,” said William Sweeney, assistant director in charge of the FBI’s field office in New York.

“The FBI will continue to work with our partners to insure financial markets remain a level playing field for all investors.”

Trading crackdown

In a broader sweep against market manipulation, financial watchdogs have focused their attention on areas of Wall Street that few laymen pay any attention to.

For example, regulators have gone after traders and the world’s biggest banks for price-rigging a key international interest rate — the London Interbank

Offered Rate, or Libor. They also have brought cases related to the rigging in foreign exchange trading. J. P. Morgan has been one of several banks collectively fined billions of dollars in the scandals.

Earlier this year, the CFTC's Neel Chopra, special counsel to the agency's director of enforcement, began leading a 20-member Spoofing Task Force.

CFTC Enforcement Actions Manipulation, Attempted Manipulation, False Reporting, Spoofing, and/or Manipulative or Deceptive Device	
Fiscal Year	Total # Cases
FY 2018	26
FY 2017	12
FY 2016	4
FY 2015	11
FY 2014	6
Total	**59**

Source: CFTC

In January, the CFTC and the Justice Department filed what they called "the largest futures market criminal enforcement action in [Justice] Department history." CFTC charged six individuals and three banks, while the DOJ brought charges against eight individuals. In the same month, Deutsche Bank settled with the CFTC for $30 million, the highest civil monetary penalty imposed by the agency for spoofing-related misconduct.

Former Fed examiner Williams, who also lectures at Boston University, said a common thread connecting many of these scandals is a compensation structure for traders and executives that pays higher bonuses for bigger trading profits.

"History proves that traders who are unchecked tend to skate to the edges, or cross into doing fraudulent things to increase their bonuses," Williams said.

"You're going to have these problems at companies that don't do enough to monitor their traders. Whether it's the Libor scandal or spoofing in metals, these are all behaviors that get reinforced with bad incentive systems," he said.

— CNBC's Hugh Son contributed reporting