



Still More on “Who’s Spoofing Whom?”

Paul Peterson

Department of Agricultural and Consumer Economics
University of Illinois

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Two recent *farmdoc daily* articles ([December 23, 2015](#) and [December 30, 2015](#)) plus two earlier *farmdoc daily* articles ([May 6, 2015](#) and [May 13, 2015](#)) reviewed three cases of spoofing. Spoofing is a disruptive futures market trading practice defined as “bidding or offering with the intent to cancel the bid or offer before execution.” The cases against Navinder Singh Sarao and Michael Coscia are similar in the sense that both relied on computer programs to submit and then quickly cancel orders to buy and sell, apparently in an effort to “trap” other traders. Coscia was found guilty by a jury in Chicago after just one hour of deliberation; London-based Sarao is fighting extradition to the U.S. and has not yet been tried.

The case against Igor Oystacher and his company, 3Red Trading, differs from the others in several respects. Oystacher made his own trading decisions and used point-and-click to execute his trades, but he used a commercially available trading platform that would cancel his existing orders on one side of the market before placing new orders on the other side of the market. This allowed him to quickly “flip” his orders from one side of the market to the other. Furthermore, Oystacher typically had orders on only one side of the market, and those orders typically were at the best bid (i.e., highest buying price) or best offer (i.e., lowest selling price).

Moving the Market vs. Creating False Impressions

This is unlike Sarao and Coscia, who held simultaneous orders on both the “buy” and “sell” sides of the market: a larger order on one side of the market that put pressure on prices, and a smaller order on the other side of the market that served as a “trap” to catch traders fleeing from the larger order. In addition, the buy and sell orders used by Sarao and Coscia were typically several ticks away from the market, and their strategies required prices to change at least once, and possibly twice, to create a profit.

This is why the complaints against Sarao and Coscia highlight the price-distorting actions of spoofing. In contrast, the complaint against Oystacher focuses on the “false impression of market depth and book pressure” created by his initial orders, and how flipping his orders to the other side of the market “before other market participants could assess and react to the disappearance of the false market depth and book pressure” allegedly gave Oystacher an unfair advantage.

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Just as the Coscia conviction broke new legal ground by showing that the design of a computer program can be used to prove a trader's intent, the Oystacher case will explore new territory. One potential area may be whether a trader must give other traders time to respond when he changes his plans. Individuals associated with two computer-based trading firms – Richard May with Citadel Securities and Matthew Wasko, formerly a trader with CGT Analytics (CGTA) – filed affidavits with the court in which both allege that trading methods like those attributed to Oystacher interfered with the operation of their algorithmic trading programs.

Misleading Market Signals

According to May, “[O]ur algorithms made trading decisions based on the assumption that large buy or sell pressure in the market was real and that other participants wanted to trade on those orders.” According to Wasko, when orders were flipped it “...did not allow us (or our algorithms) time to react to the fact that the stacked orders did not reflect genuine market interest before the aggressive order traded against us. We always want to trade on orders we put in the market, but we cannot do so profitably when the market conditions are distorted such that they do not reflect true demand and supply.”

Did Oystacher place orders on one side of the market, wait for them to be filled, and when nothing happened he simply moved to the other side of the market, much like fisherman might move to a new spot when the fish won't bite? Or did he intend all along to flip his orders and take advantage of a flaw in these computerized trading programs? Once again, "intent" will be the key to the outcome of this case, and it will be up to the judge and jury to decide what Oystacher really meant to do.

Information Content of Prices and Quantities

Prices are a source of market information; so are the quantities to buy or sell at a particular price. Posting fictitious bids or offers – without any desire to actually buy or sell at those prices, but instead to deceive other traders – sends false signals to the rest of the market and misleads market participants. This is why spoofing is treated like any other form of market manipulation, and few would argue with this basic premise.

But which are bona fide orders and which are not? Like so many things, the devil is in the details. Everyone wants to eliminate the bogus orders and related activities that only serve to distort the markets. At the same time, no one wants to discourage legitimate trading activity that may involve the cancellation or modification of orders, and especially not the legitimate trading activity that provides liquidity. Hopefully the Oystacher case will provide guidance on this matter, and lead to better markets for everyone.

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