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BP Initial Decision: The Significance of Change

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On August 13, 2015, the administrative law judge ("ALJ") assigned to hear evidence in *BP America Inc. et. Al* (Docket No. IN13-15) issued an ***Initial Decision*** in which she found that BP America Inc., and certain of its affiliates (collectively "BP") engaged in market manipulation by intentionally trading to influence index prices to benefit a related financial position. Putting aside the merits of the BP case, the Initial Decision is a good reminder of the kind of circumstantial evidence that regulators might interpret as indicia of manipulation. The reoccurring theme is CHANGE. Whether it be changes in the timing, location, size or the nature of trades, or changes in the profitability or transportation associated with trades, regulators are looking for changes in trading patterns and will call upon market participants to explain the changes. The following is a short list of changes highlighted in the BP case that may warrant special attention by market participants:

- **Price Setting Mechanism**
  - Alleged Change: increased the volume and percentage of fixed-price sales at a single location
  - Inference: shift to high percentage of fixed-price sales viewed as "marker" for manipulation
- **Timing**
  - Alleged Change: changed from selling on average approximately 20 minutes after the first trade to selling on average within 27 seconds of the first trade
  - Inference: "early bid hitting" was intended to "mark" or "frame" the open as part of an attempt to influence the direction for the day
- **Bid/Offer Behavior**
  - Alleged Change: increased number of trades resulting from hitting bids
  - Inference: hitting bids more frequently viewed as "effective way of selling at the lowest possible price" and signaling "anxious" seller
- **Volume**

- Alleged Change: increased market share in next-day, fixed-price market (especially early)
- Inference: a trader seeking to manipulate prices likely "will trade as much volume at fixed-price and on one side of the market as possible to establish a large market share"

- **Positions**
  - Alleged Change: increased related, financial positions
  - Inference: absent a "valid explanation," increased financial exposure viewed as part of scheme when paired with physical trading believed to benefit the position

- **Transportation**
  - Alleged Change: increased usage of transport and increased losses associated with transport
  - Inference: transporting "excess" gas to market furthered manipulative scheme to depress prices

- **Profit & Loss (P&L)**
  - Alleged Change: increased percentage of losses on physical trades compared to before and after the time in question
  - Inference: P&L showed capable of consistently making money in physical market, so losses suggest intentionally traded uneconomically

None of these changes alone is evidence of wrongdoing, but market participants can benefit from being aware of perceptions and recognizing that any of these changes might bring regulatory scrutiny.[1] Vetting new strategies prior to execution and recognizing changes in trading patterns as triggers for compliance reviews can help mitigate the risk of an investigation and reduce the risk of an actual or perceived violation. [1] Although the BP case stems primarily from an incriminating voice recording and a related referral to a special market monitor at BP, the circumstantial case built against BP highlights the types of changes in trading behavior that market participants should treat as red flags "“ not necessarily illegal, but worth vetting. Both the Division of Analytics and Surveillance (DAS) at the Federal Energy Regulatory Commission (FERC) and the Division of Market Oversight (DMO) at the Commodity Futures Trading Commission (CFTC) are looking for these patterns. They also consider suspicious any failure to change behavior in the face of persistent losses or changes in market conditions, but that might be best identified by a negative change in P&L.