

Will the Merc Boss Make the Best of a Mess?

By LISA GREEN MARKOFF
National Law Journal Staff Reporter

WHEN NEWS OF a deep FBI probe into the conduct of Chicago futures traders sprang forth in January, Leo Melamed of the Chicago Mercantile Exchange reluctantly went to work.

"Our industry is prone to crises and crisis is part of my job, but that's really not what I want to do," says Mr. Melamed, who, as chairman of the executive committee of the "Merc" and special counsel to its board, ordinarily concentrates on the trading, strategic planning and power-wielding he prefers.

But if responding to a federal investigation wasn't a job Mr. Melamed chose to do, it was a task he did not put off. Employing the persuasiveness and political savvy that are more likely the product of his trading skills than his brief legal career, Mr. Melamed appointed a panel of nine powerful futures experts to review exchange rules.

The proposals it submitted last month, which address current trading practices, surveillance and sanctions, could lead to significant change in the industry Mr. Melamed once transformed in the early 1970s. They also could help the Merc combat calls for increased government control of the rowdy futures markets.

If Mr. Melamed is able to convince his members to accept the panel's advice, "most people will say he made the best out of a mess," says Thomas A. Russo, a commodities law expert and partner at New York's Cadwalader, Wickersham & Taft.

The time for nostalgic reflection about the trading probe has yet to arrive, however, and the energetic, 58-year-old Mr. Melamed can do little but wait for the completion of ongoing grand jury proceedings and the anticipated indictments against futures traders at the Merc and at its cross-town rival, the Chicago Board of Trade.

To be sure, the exchanges are unlikely to face criminal indictments or civil liability for any wrongdoing proved against their members. While the Commodity Exchange Act provides an express cause of action against a futures exchange, the plaintiff must prove that the exchange acted in bad faith, a standard that has been interpreted as near-malice in disregarding its own rules, commodity lawyers say.

But even if the Merc escapes liability, Mr. Melamed has a personal stake in the wide-ranging investigation. His futures firm, Dellsher Investment Co., was one of dozens slapped with a subpoena. "That was a joke," says Mr. Melamed abruptly, clearly uncomfortable about the topic. And a Merc trader, David Horberg, reportedly lost trading privileges with Dellsher after he received a subpoena.

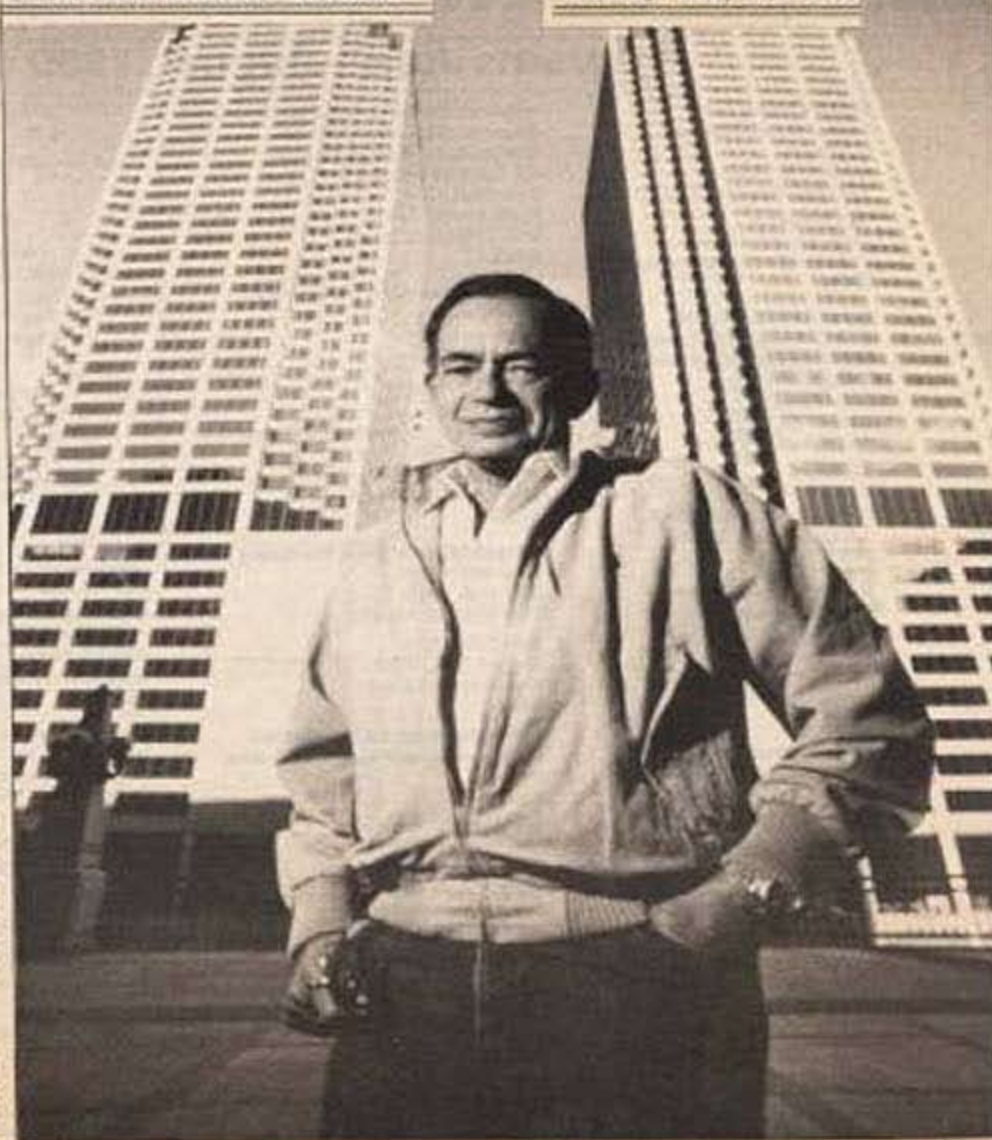
Meanwhile, the impact of the FBI probe on the hardly pristine reputation of the futures industry seems punishment aplenty for those who, like Mr. Melamed, have made the business their life's work. "It's given the industry a much blacker eye than it may deserve," he says.

The injury to the industry was ill-timed for exchange officials preparing for the quadrennial congressional review of the Commodity Futures Trading Commission, the agency that monitors the exchanges. Its new chairman, Wendy Lee Gramm, is a champion of free markets, but may find her hands-off position challenged in the wake of the investigation. "This will be the most thorough reauthorization the CFTC has seen," predicts Mr. Russo.

Mr. Melamed professes optimism that regulation will continue to be lightly administered to his indus-

THE NATIONAL LAW JOURNAL

Monday, May 8, 1989



CRISIS MANAGER: Special Counsel and Chairman of the executive committee Leo Melamed of the Chicago Mercantile Exchange accepts crises as a part of the job, but he says it's something he'd rather not deal with.

Richard Devit

try. "I believe Wendy Gramm's position will win out, but in order for that to happen, I believe exchanges must do the right thing by proving they can self-regulate," he says.

Within the hectic world of futures trading, where characters and legends abound, Mr. Melamed has managed to stand out as one of the industry's more colorful figures.

Born in Bialystock, Poland, Mr. Melamed emigrated to Chicago with his schoolteacher parents in 1941. A 1956 graduate of John Marshall Law School, he abandoned his general law practice after five years, returning to the trading floor he first visited while trying to earn some cash as a law student.

As he toiled in the egg, then pork bellies, pits, Mr. Melamed also ascended the political ranks of the exchange, becoming Merc chairman in 1969.

During his tenure, Mr. Melamed radically changed the product mix of the futures markets. Aided by economist Milton Friedman, Mr. Melamed convinced exchange members that, after the demise of fixed exchange rates in 1971, currency prices would fluctuate enough to make futures on those rates a popular product.

The success of currency futures spawned a host of financial futures products, including contracts based on interest rates and stock indexes, which now eclipse the traditional commodities in trading volume.

Mr. Melamed's creative thinking isn't limited to matters financial. For years, he was an enthusiastic Yiddish theatre actor, "an amateur rank-and-file, all the way," he says modestly. In 1987, he published "The Tenth Planet", a science fiction book about the fantastic destination of an Earth-launched space probe. Writing, and jogging, may constitute Mr. Melamed's hobbies, but trading is his obsession, and he's been known to interrupt interviews with frequent breaks to check prices and telephone instructions to the trading floor.

Computers are Mr. Melamed's latest cause. The Merc, in partnership with Reuters Holdings PLC, the powerful financial communications company, has created Globex, a system that allows exchange members to interact electronically when U.S. trading is closed for the day.

According to Mr. Melamed, the Globex system is the best response to the pressures of overseas compe-

tion for futures customers. After all, the concept of futures trading is easy for foreign financial centers to duplicate. "We think that [Globex] is the only realistic response to the demands of globalization and internationalization," he says. Other exchanges seem to agree: Exchanges in Paris and New York have joined the Globex system, and the Chicago Board of Trade, after criticizing the Merc's plan, has created its own computer network.

But Mr. Melamed wasn't always a resolute advocate of change. In a 1977 Hofstra Law Review article, he denounced computerization as "ominous" and declared that "an automated trading system would be detrimental to futures markets."

Twelve years later, Mr. Melamed denies that he has totally reversed his views. "I do not believe that Globex suggests we can do away with trading floors or the open outcry system," he says, adding that the computer helps "marry automation with open outcry."

But if computerized trading catches on, the traders Mr. Melamed represents might do well to consider another line of work. "If it works as well as people think it will, it will have an impact on the floor," says Kenneth M. Raisler, a former commodities regulator and a partner at New York's Rogers & Wells.

As exchange leaders such as Leo Melamed await the outcome of the federal probe, they undoubtedly find some consolation in the robust business the exchanges continue to attract. In March, volume at the Merc set an all-time record, with 9,369,441 futures and options contracts traded, a 38 percent jump against year-ago levels. The price of a seat on the exchange also remains dear: In March, a full membership cost \$550,000 up from \$520,000 in January, the month the probe became public.

Probe or no probe, the financial markets have no choice but to rely on futures for their strategies as long as interest rates and other economic barometers remain volatile, says Mr. Melamed.

So, the father of financial futures was asked, will interest rates remain turbulent? "Rates will stay high for most of 1989," he says. "We are facing some difficult times because of the deficit, and I'm afraid recessionary times will hit by late this year."

As to the reliability of Mr. Melamed's forecast, a former regulator's thoughts seem relevant. "History would not make anyone wise to second-guess this man," says Rogers & Wells' Mr. Raisler.

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EXCHANGES UNDER FIRE