begins immediately thereafter. In a when-issued trade, no money changes hands; rather, sellers agree to deliver the securities on the date the Treasury settles with successful bidders, generally one week after the auction 'settlement''). At settlement, the Treasury transmits the new issue to the successful bidders in exchange for payment. On settlement day, whenissued buyers must pay for their purchases and when-issued sellers must deliver the securities they sold. Persons who sell short an issue in the whenissued market must deliver that issue to the purchaser at settlement; they cannot substitute another Treasury issue.1

After settlement, trading to buy and sell the issue continues in the secondary or "cash" market until the maturity date, when the issue is redeemed. In every when-issued or cash market trade, a seller who does not already own the issue is said to be "short," and the buyer "long." The "short" seller may obtain the securities it is required to deliver by purchasing them at the Treasury auction or in a when-issued or cash market trade. Alternatively, the short may borrow them in the "financing market," generally through a repurchase or 'repo'' transaction, and delivering the borrowed securities to the buyer.

Traders of Treasury securities frequently use repurchase agreements not only to effectuate delivery when they have "short" positions, but also to finance their "long" purchases. A repurchase transaction is the functional equivalent of a loan using Treasury securities as collateral, in which the owner of an issue sells it and simultaneously agrees to repurchase it on a specified date for a specified price. The repurchase price is somewhat higher than the sale price; the difference between the two prices represents an interest rate, and is often called the "repo" rate.

Treasury securities can be financed either through "special" repo agreements, in which the collateral is a particular, identified issue, or through "general" repo agreements, in which no particular issue need be specified for delivery. When there is specific demand for an issue because short sellers need to borrow the issue in order to deliver it to persons who have bought it, owners can lend the issue in a special repomarket transaction at a "special rate."<sup>2</sup>

The issue generally is said to be "on special" when the interest rate that owners (such as SMC and Caxton in the case of the April Notes) are required to pay to borrow cast against the issue is significantly lower than the "general" collateral rate." The general collateral rate is an overall rate for loans collateralized by Treasury securities, and usually fluctuates only in relation to short-term, money-market rates. Because the demand, as reflected by price, for a particular issue is unique in both the cash market and in the financing market (while the issue is on special), there are separate product markets for each Treasury security issue within the meaning of the antitrust laws.

If the supply of an issue is artificially constricted by agreement among the holders of the issue, both the price of the issue in the cash market and the cost of borrowing the issue in the financing market increase.<sup>3</sup> When the cost of purchasing an issue in the cash market or the cost of borrowing it in the financing market is significantly different than the cost of buying or borrowing securities of comparable maturities, a "squeeze" is said to occur.

## B. The Conspiracy

SMC and Caxton both manage investment funds-sometimes known as "hedge funds"—which generally make large, "leveraged" investments with borrowed capital. The hedge funds managed by the defendant entities compete with numerous other traders and investors in the when-issued, cash and financing markets to sell purchase and finance various Treasury security issues. Prior to their purchase of April Notes, the defendant entities had a history of interaction. Beginning in January 1990, Caxton became comanaging general partner of two of SMC's funds, and Caxton's chairman became the president of SMC. The formal affiliation of Caxton and its chairman with SMC ended after one

<sup>3</sup> Due to the manner in which the financing market works, the increased cost of borrowing the security occurs when short sellers earn *lower* interest rates on money they lend to holders in order to borrow the security overnight or for a short term. The cost of borrowing the securities increases when short sellers—who must borrow the security to avoid a default (failure to deliver or "fail") on their contractual obligations—receive say, only 4.25% on the money they land when, if the issue were not "on special," they would have been able to borrow the securities in the repo market and earn a higher interest rate, say, 5.75%. year, but employees and agents of the defendant entities continued to communicate regularly with each other, including during the period encompassed by the conspiracy.

As charged in the complaint, beginning in or about April 1991, the defendant entities agreed on a scheme to acquire control of the supply of April Notes and to limit the supply of the issue in the cash and financing markets in order to cause a squeeze. This scheme ensured that persons who had sold notes short in the when-issued market or the post-settlement cash market could obtain such notes only by purchasing them at artificially high and non competitive prices in the cash market or by borrowing them at artificially low and non-competitive special rates in the financing market. This course of conduct continued for a period of time during which the defendant entities, with the assistance of others, earned supracompetitive rates on transactions in the April Notes.

Through numerous purchases made through various dealers, in the whenissued market, the cash market and at auction, SMC and Caxton obtained substantial positions in the April Notes. Indeed, from May until mid-September 1991, the defendant entities controlled more than the "floating supply" of the issue, giving them the power to cause short sellers of the April Notes to fail to meet their security-specific delivery obligations.

As part of the alleged scheme, SMC and Caxton conferred on the subject of their activities or planned activities with respect to April Notes. They exchanged information about the size of their positions, the likely size of the short positions in the markets and ways to finance positions so as to keep their notes from becoming available to meet the demand for specials financing. The defendant entities gave tacit assurances to each other that they would continue to hold their substantial long positions in the April Notes, and would limit the supply of April Notes they would make available to the cash and financing markets from the positions they controlled.

The conspirators agreed to coordinate SMC's and Caxton's financing efforts so as to restrict the supply of April Notes available in the financing and cash markets. The conspirators began to implement their squeeze on May 23, 1991.<sup>4</sup> An essential part of the scheme

<sup>&</sup>lt;sup>1</sup>Each Treasury security of a particular issue is unique and bears an identification number (known as a "CUSIP number") which distinguishes it from all other securities. Thus, all April Notes (all of which were issued on the same date) bore the same CUSIP number.

<sup>&</sup>lt;sup>2</sup> A Treasury security may trade "on special" in the collateral markets for various reasons. Special

rates could be the result of ordinary market supply and demand, but could also be induced by persons acting together to distort normal market forces. Potentially, if the holders of an issue withhold enough of it from the "specials" market, unmet demand may cause come percentage of the issue to be financed at interest rates approaching zero.

<sup>&</sup>lt;sup>4</sup>The conspirators waited until May 23 to implement the squeeze because the subsequent issue of two-year notes was auctioned on the previous day. By waiting until the Treasury auctioned a succeeding issue, the conspirators minimized the risk that the Treasury would reopen