No. 06-1265

In The
Supreme Court of the United States

KLEIN & CO. FUTURES, INC.,

Petitioner,

v.

BOARD OF TRADE OF THE CITY OF NEW YORK, INC., ET AL.,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Second Circuit

BRIEF OF PETITIONER

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QUESTION PRESENTED

Whether the court of appeals erred in concluding that petitioner, as a futures commission merchant (FCM), lacked statutory standing to invoke the right of action under 7 U.S.C. § 25(b)(1), because, in the court's view, it did not engage in "any transaction on or subject to the rules of" respondents, despite the statutory requirement that FCMs enter into and execute their transactions on, and subject to the rules of, respondents and the fact of FCMs' financial liability for the transactions.

PARTIES TO THE PROCEEDING

Petitioner is Klein & Co. Futures, Inc. The respondents were appellees in the court of appeals, and consist of the Board of Trade of the City of New York, Inc., the New York Clearing Corporation, the New York Cotton Exchange, Inc., and the New York Futures Exchange.

Mark D. Fichtel, Albert Weis, Jeff Soman, Charles Sweeney, Al Peres, Chris Meek, George Haase, Lawrence Gulitti, Bryan Sayler, Nitesh Trivedi, Joseph O'Neill, Walter Fair, Evan Thomas, Joseph Jach, Norman Eisler, and First West Trading, Inc. also were appellees in the court below, but petitioner does not seek review of the court of appeals' ruling affirming their dismissal from the case.

RULE 29.6 CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 29.6 of the Rules of the Supreme Court, petitioner Klein & Co. Futures, Inc. hereby states that it has no parent company, and no public company owns 10% or more of its stock.

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OPINIONS BELOW

The opinion of the United States Court of Appeals for the Second Circuit is reported at 464 F.3d 255 (2006). Pet. App. 1a-15a. The opinion of the United States District Court for the Southern District of New York granting respondents' motion for summary judgment is unreported. Pet. App. 16a-34a.

STATEMENT OF JURISDICTION

The court of appeals entered its judgment on September 18, 2006. A petition for rehearing and rehearing *en banc* was denied on November 14, 2006. Justice Ginsburg, on January 31, 2007, granted an extension of time within which to file a petition for a writ of *certiorari* to and including March 14, 2007. Petitioner timely filed its petition for a writ of *certiorari* on March 14, 2007. This Court granted the petition on May 21, 2007. This Court's jurisdiction is invoked under 28 U.S.C. § 1254(1).

STATUTE INVOLVED

Section 22 of the Commodity Exchange Act, 7 U.S.C. § 25(b)(1), as in effect when this case was filed on July 26, 2000, provides in relevant part as follows:

> **§ 25. Private rights of action**
>
> * * *
>
> **(b) Liabilities of organizations and individuals; bad faith requirement; exclusive remedy**
>
> (1)(A) A contract market or clearing organization of a contract market that fails to enforce any bylaw, rule, regulation, or resolution that it is required to enforce by section 7(a)(8) and section 7(a)(9) of this title,
>
> (B) a licensed board of trade that fails to enforce any bylaw, rule, regulation, or resolution that it is required to enforce by the Commission, or

> (C) any contract market, clearing organization of a contract market, or licensed board of trade that in enforcing any such bylaw, rule, regulation, or resolution violates this chapter or any Commission rule, regulation, or order,
>
> shall be liable for actual damages sustained by a person who engaged in any transaction on or subject to the rules of such contract market or licensed board of trade to the extent of such person's actual losses that resulted from such transaction and were caused by such failure to enforce or enforcement of such bylaws, rules, regulations, or resolutions.

7 U.S.C. § 25(b)(1) (1994). Additional provisions of the statute are set forth at App., *infra*, 1a-7a.

INTRODUCTION

This case arises out of the failure of respondent New York Futures Exchange (NYFE), its clearinghouse respondent New York Clearing Corporation (NYCC), and the other respondents to enforce their rules to ensure against gross misconduct by the Chairman of NYFE.[1] The failure to enforce the rules caused catastrophic loss to petitioner Klein & Co. Futures, Inc., and destroyed that business based on the fraudulent manipulation of settlement prices of certain positions in the commodity futures market by the NYFE Chairman.

[1] Respondent NYFE, as of May, 2000 when this action accrued, was a wholly-owned subsidiary of respondent New York Cotton Exchange (NYCE), which was a wholly-owned subsidiary of respondent Board of Trade of the City of New York (NYBOT). At that time, respondent NYCC also was a wholly-owned subsidiary of respondent NYBOT. NYCC cleared the trades for the various NYBOT exchanges, including NYFE. Petitioner was a member of each of the four respondent entities and thus was subject to the rules of each of them.

On January 12, 2007, IntercontinentalExchange (ICE) acquired NYBOT, making NYBOT a wholly-owned subsidiary of ICE and part of a for-profit, publicly traded corporation for the first time in its history.

The court of appeals erred in holding that petitioner did not have standing to bring this action against respondents under Section 22(b)(1) of the Commodity Exchange Act, 7 U.S.C. § 25(b)(1) (1994), to recover its actual losses caused by bad faith conduct of respondents. Section 25(b)(1) was designed precisely to authorize futures commission merchants (FCMs) like petitioner to bring such actions as part of the overall enforcement scheme created in the Commodity Exchange Act to protect the integrity of the nation's commodity futures markets from self-dealing or other malfeasance by exchanges and their clearinghouses. The court of appeals misread the plain text of the statute and relied on a fundamental misconception about the operation of the commodity futures markets to hold that only purchasers and sellers of futures contracts have standing under Section 25(b)(1).

Simply put, Section 25(b)(1) authorizes suit to be brought against respondents by a person who has "engaged in any transaction on or subject to the rules" of an exchange or its clearinghouse. *Ibid*. Petitioner plainly met this requirement. The rules of the exchange required that any contract made on the exchange "shall be made on behalf of a clearing member," such as petitioner, "who shall be the buyer or seller of said contract on the terms set forth therein" and that the clearing member shall assume as its own the futures contracts on the exchange. *See* NYFE Rule 306(i)(2) (App., *infra*, 14a). The clearing member then submits the contract for clearing on the clearinghouse, which consummates the transaction. Petitioner was financially liable to the clearinghouse for any losses on the clearing transaction, NYCC By-Law 5.5(a) (J.A. 131-132), and was an indispensable party to that transaction because clearinghouses allow only members like clearing FCMs to perform that function, *id.* at 5.1 (J.A. 119). As such, the court of appeals' holding that petitioner did not engage in a transaction on or subject to the rules of the exchange or clearinghouse defies all logic.

STATEMENT OF THE CASE

A. Overview Of The Commodity Futures Market

1. Futures contracts began trading on organized exchanges in Chicago in the mid-1800s. *See* Chicago Board of Trade, *Commodity Trading Manual* 5 (1994) (hereinafter *Commodity Trading Manual*). The Chicago Board of Trade was the first such organized exchange, established in 1848 by 82 merchants. The exchange provided a physical location for buyers and sellers to trade commodities, such as grain or cattle, through the use of forward contracts – *i.e.*, contracts for the future delivery of specified commodities. These early forward contracts had significant drawbacks, however, because they were not standardized according to quantity, quality, or delivery time, and merchants or traders often failed to fulfill their forward commitments because of their refusal or inability to make or to take timely delivery of the commodity on the agreed upon delivery date.

In 1865, the Chicago Board of Trade formalized trading by the creation of agreements called "futures contracts," which imposed a standardization that had been lacking. *Ibid.*; *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353, 358 (1982). In addition, the Chicago Board of Trade instituted a margin system, which required the deposit of funds to minimize counterparty risk and to help guarantee future performance. *See Commodity Trading Manual* 5.

A modern futures contract imposes an obligation to buy or sell a specified amount of a commodity at an agreed upon price on a certain date in the future. The seller of a futures contract (the short position) is obligated to make the delivery of the commodity, *i.e.*, sell, on the date specified by the contract. Conversely, the buyer of a contract (the long position) is obligated to take delivery of the commodity, *i.e.*, buy, on the date specified by the contract. All of the terms of a modern futures contract are standardized, except for price which is established or "discovered" by the buyers and sellers in the futures market.

Delivery rarely occurs on the futures market because the ongoing obligation of a buyer or seller of a futures contract is almost always "offset," and thus closed, through the purchase or sale of an equal and opposite contract. *See* Chicago Board of Trade, *Handbook of Futures & Options* 10 (2006) (hereinafter *Handbook of Futures & Options*); *Curran*, 456 U.S. at 357-358. For example, a purchaser of a futures contract in January for a 5000 ounce silver contract with a March delivery date can offset and close this position at any time between the January purchase and the March date by selling an identical 5000 ounce silver contract with the same delivery date.

2. The commodity futures market serves a well-recognized, important public interest. The purchase or sale of futures contracts on commodities markets helps to discover the cash price for goods and reflects a market price for the underlying tangible commodity. "The prices involved in [futures] transactions are generally quoted and disseminated throughout the United States and in foreign countries as a basis for determining the prices to the producer and the consumer of commodities and the products and byproducts thereof and to facilitate the movements thereof in interstate commerce." 7 U.S.C. § 3 (1994).

Futures contracts assist the participants in the cash market (*e.g.*, producers, middlemen, commercial users or processors of a commodity), who are known as "hedgers," to protect themselves from, *i.e.* hedge against, adverse price fluctuations of the physical commodity in which they deal. *Ibid.* ("[Futures contracts] are utilized by shippers, dealers, millers, and others engaged in handling commodities and the products and byproducts thereof in interstate commerce as a means of hedging themselves against possible loss through fluctuations in price.").

For example, a manufacturer of soybean oil who enters into a business contract to deliver its oil several months in the future can hedge against a price increase in the market for the soybeans that are its raw material. The oil producer need only buy a sufficient number of futures contracts in soybeans with a delivery date for when he will need to actually buy soybeans in the future. Thus, if the manufacturer knows it will need 5,000 bushels of soybeans in March, it can buy a 5,000 bushel futures contract of soybeans in January at $7 a bushel. Then, if the price of soybeans rises to $9 a bushel by March, the futures contract will likewise rise and can be sold to offset the increased price of the underlying commodity. In order to gain this protection against adverse price movements, the hedger must, however, surrender its ability for a greater profit than could be gained from favorable price changes. Thus, if the price of soybeans declines to $5 a bushel, the same futures contract prevents the manufacturer from realizing a greater profit (because the soybeans are less expensive at $5 a bushel, but offsetting the futures contract position at $7 a bushel will be more expensive). The oil manufacturer uses this hedging opportunity when the benefit of the protection against too great a price increase for its raw material outweighs the cost of sacrificing the possible greater profit. The National Futures Association (the congressionally authorized self-regulatory organization of the industry, *see*, *infra*, note 9) explains as follows:

> Whatever the hedging strategy, the common denominator is that hedgers willingly give up the opportunity to benefit from favorable price changes in order to achieve protection against unfavorable price changes.

National Futures Association, *Opportunity and Risk, An Education Guide to Trading Futures and Options on Futures* 19 (2006), *available at* http://www.nfa.futures.org/investor/OppRisk/OppRisk.pdf (last visited July 16, 2007).

In addition to hedgers, speculators participate in the commodity futures market. They do so as an investment strategy. Speculators "seek to profit from anticipated increases or decrease in future prices. In so doing, they help to provide the capital needed to facilitate hedging." *Ibid*.

3. Today, futures contracts are traded on various organized exchanges, which are boards of trade that are

designated as contract markets, *see* 7 U.S.C. § 7, such as respondent Board of Trade of the City of New York (NYBOT) and, at the time this action accrued, respondent New York Futures Exchange (NYFE).[2] Each exchange operates a market for trading in contracts in certain commodities. *See, e.g.*, http://www.nybot.com (last visited July 13, 2007). Trading on an exchange is limited to members of that exchange and affiliated persons.

The trading of futures contracts has long occurred through a competitive, open outcry bidding on the floors of exchanges. Members of the exchange and their brokers gesture with pre-defined hand signals and shout to each other bids and offers in trading pits located on the exchange floor. *See Commodity Trading Manual* 35.[3] In more recent years, bids and offers also are posted by electronic means so that they can be matched without face-to-face contact between the members on the exchange.

The agreement to buy and the agreement to sell that occur on the exchange do not consummate a futures contract, however. A transaction for a futures contract is completed by the act of clearing the trade which takes place at the exchange's clearinghouse, such as respondent New York Clearing Corporation (NYCC). Trades can be cleared only by a clearing FCM, like petitioner Klein & Co. Futures, Inc., which must be well-capitalized and a member of the clearinghouse. Indeed, respondent NYFE's rules dictate that every contract made on the exchange shall be for the "clearing member who shall be the buyer or seller of said contract" and "shall be assumed" by that

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[2] Options contracts are traded on such exchanges as well. An option contract gives an investor the option (*i.e.*, the right, but not the obligation) to enter into a particular futures contract during a particular period of time at a particular price. The instant dispute involves both futures contracts and their options but, for the purposes of this Court's review, the distinctions between the two make no difference and we use the term "futures contracts" to refer to both.

[3] For a fuller description of the exchange floor and trading pits, *see Handbook of Futures & Options* 24-25.

clearing FCM within one hour of a trade's execution. *See* NYFE Rule 306(i)(2) (App., *infra*, 14a).

Through the clearing transaction, one clearing FCM becomes responsible to the clearinghouse for the short position in the trade, another clearing FCM becomes responsible to the clearinghouse for the long position in the trade, and the clearinghouse becomes the counterparty to both FCMs. Respondent NYCC has explained: "[i]n each mutually confirmed transaction, [NYCC] is substituted as the buyer to the selling clearing member and the seller to the buying clearing member." NYCC Statement (App., *infra,* 19a);[4] *see also Handbook of Futures & Options* 60. A

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[4] The NYCC Statement was previously available on NYCC's website, and was cited in the brief of the Futures Industry Association as *amicus curiae* in support of petitioner before the Second Circuit. The statement is not currently on their website, but is available online as it existed in August 2005 on a not-for-profit internet archiving site at http://web.archive.org/web/20050823002032/209.208.183.6/generalInformation/aboutNYCC/aboutNYCC.htm. It is also reproduced in the appendix to this brief. App., *infra,* 19a.

Descriptions by the Commodity Futures Trading Commission and the Chicago Mercantile Exchange (CME) clearinghouse are in accord with NYCC's statement. Specifically, the CME describes the act of clearing as follows:

> Clearing members assume full financial and performance responsibility for all transactions executed through them and all positions they carry. CME Clearing, dealing exclusively with clearing members, holds each clearing member accountable for every position it carriers regardless of whether the position is being carried for the account of an individual member, for the account of a non-member customer, or the clearing member's own account. Conversely, as the contra-side to every position, CME Clearing is held accountable to the clearing members for the net settlement from all transactions on which it has been substituted as provided in the Rules.

CME Clearing, *Financial Safeguards* at 2 (2006), *available at* http://www.cme.com/files/financialsafeguards.pdf (last visited July 16, 2007); *see also* Commodity Futures Trading Commission, *Glossary*, *available at* http:/www.cftc.gov/opa/glossary/opaglossary_c.htm (last visited July 16, 2007) (same).

clearing FCM is therefore at the center of a commodity futures trade.

4. The exchange's clearinghouse thereby protects other participants in the market from adverse financial consequences of a default by removing counterparty risk in a futures contract. This is accomplished by severance of any relationship between the buyer and seller on the exchange, so that a trade is comprised of several separate but coordinated transactions, including between the buyer or seller and its clearing FCM, and the clearing FCM and the clearinghouse. Through this series of transactions, clearing firms "do not create financial obligations to one another but, rather, to the clearinghouse" and "nonclearing firm buyers and sellers create obligations not to each other but to the clearing firm that clears their trades." *Handbook of Futures & Options* 60.

Under this system, the clearinghouse and its clearing member FCMs are financially responsible for every trade that occurs on the exchange. Therefore, clearinghouses require that their members, *i.e.,* the clearing FCMs, deposit with the clearinghouse performance bond money called "margin" to guarantee the clearing FCMs' performance. Clearing FCMs, in turn, require their customers to post similar margin with them to cover the customers' own market positions. *See id*. at 18.

The original margin, when the futures contract is first executed and cleared, is set to be consistent with the level of market risk in the commodity. But the price and risk of a futures contract in a particular commodity changes from day to day. Accordingly, after each trading session, the exchange, in accordance with its rules and bylaws, calculates a settlement price for each commodity, *see* NYFE Rule 315 (App., *infra*, 14a-15a), which is supposed to reflect that commodity's end of trading day market value. That settlement price is transferred to the clearinghouse, so that the clearinghouse can reconcile its clearing members' positions in the aggregate and the day's winners and losers in the market can be determined.[5]

It is the settlement price that is used to determine the gain or loss for each position open at the end of the day. If a clearing FCM's positions, in the aggregate, lose money on the day, a variation margin payment may be required, and the clearing FCM may be required to deposit additional margin to the clearinghouse, before the next day, or even earlier in times of significant market volatility. Conversely, if a clearing FCM's position gains money, the clearinghouse may return the excess margin to that FCM.

A clearing FCM undertakes a similar calculation based on the settlement price with respect to the buyers and sellers whose trades it cleared. Those customers will be required to deposit more funds into their account with the clearing FCM if they lose based upon the settlement price, and customers that win may be entitled to receive excess funds in their account.

Transactions in futures contracts differ significantly from the typical purchase of securities in this regard. Ownership of an underlying security is transferred in the typical securities transaction either through the payment of cash or by an extension of credit. By contrast, participants in the commodity futures market are required to post margin that is a performance bond – which is often

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[5] The CFTC explained in its administrative order addressing the misconduct by the NYFE chairman related to this case:

> For positions held since the previous trading day, the variation payment is the difference between the settlement price that day and the settlement price on the previous day. For positions acquired during the day and held at the end of the day, the variation payment is the difference between the trade price and the settlement price. Clearinghouses pay (or collect) variation payments to (or from) their members for the members' daily variation.

Matter of Norman Eisler, CFTC No. 01-14, at 3 (C.F.T.C. Jan. 20, 2004), available at http://www.cftc.gov/files/enf/04orders/enfeisler-order.pdf (last visited July 13, 2007).

only between 2 and 5 percent of the contract's face value – to ensure that they can fulfill their contract obligations in the future.

B. Federal Regulation Of Commodity Futures Exchanges Through Public And Private Enforcement

Organized commodity futures exchanges have relied upon self-regulation for more than one hundred and fifty years. The rules and by-laws of the exchanges and of the clearinghouses have been designed to support competitive, efficient, and liquid markets free from undue manipulation. Even though the commodity futures market is subject to extensive federal oversight, the primary responsibility for market surveillance and protection of the integrity of the futures market remains with the exchanges themselves. *See* 7 U.S.C. § 5(b) ("It is the purpose of this chapter to serve the public interests * * * of this section through a system of effective self-regulation of trading facilities, clearing systems, market participants and market professionals"); Comptroller General of the United States, Report to Congress, *Commodity Futures Regulation – Current Status & Unresolved Problems* 48 (1982); CFTC, *Conflicts of Interest in Self-Regulation and Self-Regulatory Organizations*, 72 Fed. Reg. 6936, 6938 (Feb. 14, 2007) (to be codified at 17 C.F.R. pt. 38) ("Congress established a statutory system of [exchange] self-regulation, combined with [federal] oversight, to promote 'responsible innovation and fair competition among boards of trade, other markets and market participants.'") (citations omitted).

1. Federal regulation of the commodity futures market began with the Grain Futures Act of 1922, Pub. L. No. 331, 42 Stat. 998 (1922), which mandated that futures trading in certain enumerated commodities, such as grain and flaxseed, could occur only on federally

licensed exchanges, *id.* at § 4(b).[6] Fourteen years later, Congress enacted the Commodity Exchange Act of 1936 (CEA), Pub. L. No. 74-675, 49 Stat. 1491 (1936), in order to strengthen the federal government's oversight of the market. The CEA extended government oversight to trading in cotton and certain other specified agricultural commodities. Importantly, the CEA also imposed federal regulation on the licensing of exchanges and registration requirements on other market participants, such as FCMs. *Curran*, 456 U.S. at 362.

In 1968, Congress amended the CEA to require exchanges to enforce their own rules as part of the self-regulatory process. The federal government also gained the power to disapprove any exchange rules that were inconsistent with the CEA. Commodity Exchange Act Amendment of 1968, Pub. L. No. 90-258, 82 Stat. 26 (1968); *Curran*, 456 U.S. at 364.

Significant expansion of the regulation of the commodity futures market occurred again in 1974 when Congress enacted the Commodity Futures Trading Commission Act of 1974, Pub. L. No. 93-463, 88 Stat. 1389 (1974). Under that Act, Congress extended federal regulation to *all* commodities. 7 U.S.C. § 1a(4) (1994). The 1974 law also created the Commodity Futures Trading Commission (CFTC), which is an independent federal agency comprised of five full-time commissioners and a staff. Commodity Futures Trading Commission Act, § 101, 88 Stat. at 1389.

Congress further amended the CEA in various respects, including in 1982 when it codified the private right of action set forth in 7 U.S.C. § 25(b)(1) (1994), which is at issue in this case.

2. Congress ensures that exchanges self-regulate and enforce their rules in a manner consistent with the

[6] Congress first authorized the regulation of the commodity futures market in 1921 with the Futures Trading Act, 42 Stat. 187 (1921), but that Act was held unconstitutional in *Hill v. Wallace*, 259 U.S. 44 (1922), as exceeding Congress's taxing power. *Curran*, 456 U.S. at 361.

public interest by requiring that the CFTC conduct investigations and initiate enforcement actions. *See, e.g.*, 7 U.S.C. §§ 7, 7a, 7a-1, 8; 7 U.S.C. §§ 7, 7a, 7b, 8 (1994). And this authority applies to the exchanges' clearinghouses because exchange rules include the rules of their clearinghouses. 17 C.F.R. § 1.41(a)(3) (1999); *see also* CFTC, *Contract Market Rules and Authority Delegation*, 41 Fed. Reg. 40,091, 40,093 (Sept. 17, 1976) ("a meaningful distinction cannot be drawn between the rules of the clearing organization and the contract market for purposes of" 7 U.S.C. § 7a).

In addition, the CFTC has authority to enjoin improper exchange behavior; to alter or to supplement an exchange's rules; to suspend or to revoke an exchange's designation as a contract market (*i.e.*, elimination of the ability to operate as a forum for the purchase or sale of futures contracts) if the exchange fails to enforce the statute, the agency's regulations, or the exchange's own rules; and to direct a contract market to take any action deemed necessary by the Commission in an emergency. 7 U.S.C. §§ 13a, 13a-1, 8, 12a(7), 12a(9) (1994).

Private enforcement is also explicitly provided for by Congress. The CEA grants an administrative remedy to individuals injured by any entity that is required to be registered by the CFTC, which includes members of the exchanges such as FCMs, although not the exchanges themselves. *See* 7 U.S.C. § 18. With regard to the exchanges, a private civil action against exchanges (and other market participants) was "routinely and consistently" recognized as an implied private right of action under the CEA. *Curran*, 456 U.S. at 379; *see also Leist v. Simplot*, 638 F.2d 283, 299-300 (2d Cir. 1980), *aff'd sub nom. Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353 (1982) (collecting cases).

In 1982, in *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, this Court held that the administrative remedies created under the CEA in 1974 had supplemented, not replaced, the previously recognized implied private rights of action under the CEA. 456 U.S. at 384-387. The Court emphasized that the private right of action differed substantially from the administrative remedies, including because the administrative remedies for private litigants, were "not available against the exchanges," but the private right of action was so available. *Id.* at 384. The Court acknowledged the significance of the continuing availability of the private right of action under the CEA, noting that the United States believed that "the private cause of action enhances the enforcement mechanism fostered by Congress over the course of 60 years." *Id.* at 387.

3. Not long after the *Curran* ruling, Congress codified in 7 U.S.C. § 25, *see* Futures Trading Act of 1982, Pub. L. No. 97-444, § 235, 96 Stat. 2294, 2322-2324 (1983), the private civil action against various participants in the market, including against exchanges.

Section 25 provides multiple distinct causes of action against four different categories of defendants set forth in Sections 25(a)(1), 25(b)(1), 25(b)(2), and 25(b)(3), for violations of the CEA and/or failure to enforce rules, bylaws or regulations as required by the CEA. The persons who can bring suit against the different types of defendants are also different in each provision:

- Section 25(a) authorizes suit *against* FCMs, traders, or other persons or firms who are not an exchange or its clearinghouse.

  A suit under Section 25(a) can be *brought* only by persons who: (A) "received trading advice" from the putative defendant for a fee; (B) made a futures contract through the defendant or deposited money with an order to do so; (C) "purchased from or sold to" the defendant or placed through it certain futures options or contracts; or (D) "purchased or sold" a futures contract through the defendant "if the violation constitutes a manipulation of the price of any such contract or the price of the commodity underlying such contract." *Id.* § 25(a)(1)(A)-(D) (1994).

- Section 25(b)(1) authorizes suit *against* "a contract market [*i.e.*, an exchange] or clearing organization of a contract market," or "a licensed board of trade."

A suit under Section 25(b)(1), *i.e.*, the suit at issue here, can be *brought* only by a person "who engaged in any transaction on or subject to the rules of such contract market or licensed board of trade." *Id.* § 25(b)(1) (1994).[7]

- Section 25(b)(2) authorizes suit *against* registered futures associations.[8]

A suit under Section 25(b)(2), can be *brought* only by a person that engaged in "any transaction specified in subsection (a)," *i.e.* Section 25(a)(1)(A) to (D). *Id.* § 25(b)(2) (1994).

- Section 25(b)(3) authorizes suit *against* an officer or other specified individual at a contract market, clearinghouse, licensed board of trade, or registered futures association.

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[7] It has been clear since at least 1976, that, with respect to such a reference to the rules of a contract market, "[t]he term contract market includes a clearing organization that clears trades for the contract market." 17 C.F.R. § 1.41(a)(3) (1999); CFTC, Contract Market Rules and Authority Delegation, 41 Fed. Reg. 40,091 (Sept. 17, 1976). Accordingly, respondents cannot succeed on the argument (*see* Br. in Opp. 14-15, 21-22) that, despite the inclusion of "clearing organization" as an identified defendant, this provision somehow does not permit a suit for a transaction conducted on or subject to the rules of a clearing organization.

The 2000 amendment to Section 25(b)(1) neither expanded nor contracted the private rights of action under the CEA. It was a technical and conforming amendment that substituted the term "registered entity" in certain places for the terms "contract market," "clearing organization of a contract market," and "board of trade," *compare* 7 U.S.C. § 25 (present statute), *with* 7 U.S.C. § 25 (1994), in order to correspond with the new definition of "registered entity" added in 7 U.S.C. § 1a(29), that includes boards of trade designated as contract markets and clearing organizations, as registered entities. *See* Commodity Futures Modernization Act of 2000, Pub. L. No. 106-580, 114 Stat. 2763 (2000).

[8] A "registered futures association" is a self-regulatory organization, such as the National Futures Association, that regulates the firms and individuals who conduct futures trading with public customers.

> A suit under Section 25(b)(3), can be *brought* only by a person that engaged in "any transaction specified in subsection (a)," *i.e.*, Section 25(a)(1)(A) to (D), if the defendant is at a registered futures association. If the defendant is at a contract market, clearinghouse, or board of trade, the person must not only have engaged in a "transaction specified in subsection (a)," but that transaction must have been "on, or subject to the rules of" such contract market or board of trade. *Id.* § 25(b)(3) (1994).

C. FACTUAL BACKGROUND[9]

Petitioner Klein & Co. Futures Inc. was a member of each of the respondents. Thus, petitioner was a clearing FCM that executed trades on NYFE and also assumed trades made on NYFE and cleared those contracts with NYCC.

The chairman of respondent NYFE, Norman Eisler, was on NYFE's committee that set the settlement price each day for the futures contracts at issue here, "P-Tech" futures (which stands for Pacific Stock Exchange Technology Futures Contracts and Options). Eisler also was a floor broker on that exchange. 7 U.S.C. § 1a(16).

Eisler purchased, through his company First West Trading Inc., a number of futures contracts, including P-Tech futures. J.A. 17. Petitioner was Eisler's clearing FCM, thus the contracts were made on behalf of petitioner who was the "buyer or seller of said contract[s]," and petitioner assumed within one hour those contracts on the exchange, *see* NYFE Rule 306(i)(2) (App., *infra*, 14a), and cleared those same contracts with NYCC. Petitioner was responsible to NYCC for the P-Tech futures contract positions. NYCC's rules require as follows:

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[9] The facts set forth in this brief are based on the factual allegations in the complaint because the district court dismissed petitioner's complaint pursuant to Rule 12 of the Federal Rules of Civil Procedure and, therefore, those allegations, *see* J.A. 10-28, must be taken as true.

> If and to the extent a monetary default relates to a Contract carried in the customer account of a Defaulting Clearing Member, such margin, Guarantee Fund deposit and other assets (whether held for the proprietary account or the customer account) shall be applied to pay the Defaulted Obligation.

NYCC By-Law 5.5(a) (J.A. 131-132).

Unbeknownst to petitioner at the time, Eisler was using his position as a member of NYFE's settlement committee to fraudulently set the settlement prices of P-Tech futures from approximately August 1999 through May 12, 2000. He did so in a manner that ensured that his company's positions artificially appeared profitable, even when it was suffering losses on the market, so that it could avoid margin calls. When Eisler was unavailable to set the settlement price on any given day, another member of respondent NYFE's settlement committee would do so "according to instructions left by Eisler, or by using the procedures followed by Eisler." *Matter of Norman Eisler*, CFTC No. 01-14, at 4 (C.F.T.C. Jan. 20, 2004), *available at* http://www.cftc.gov/files/enf/04orders/enfeisler-order.pdf (last visited July 13, 2007).[10]

The CFTC has determined that this deliberate miscalculation, by Eisler and others at his direction, falsely inflated the value of the P-Tech futures positions held by petitioner with NYCC, and by Eisler with petitioner, by approximately $2 million each day. *Id.* at 2, 5. The CFTC also found that NYFE failed to enforce NYFE Rule 315, governing the setting of settlement prices, in violation of the CEA. *Matter of New York Futures Exch.,*

[10] NYFE settlement prices were generally set using a NYBOT computer system, in which "[a] NYBOT employee was responsible for entering the data into the system and checking the accuracy of the results." *Id.* at 3; *see also* J.A. 18 (alleging that "all responsibility for supervision, regulation, investigation and certain quasi-governmental duties of the NYFE were delegated to NYBOT and NYBOT assumed such duties and responsibilities").

Inc., CFTC No. 01-13 (C.F.T.C. July 11, 2001), *available at* http://www.cftc.gov/files/enf/01orders/enfnyfe.pdf (last visited July 13, 2007).

Petitioner did not know that Eisler was manipulating the settlement prices of P-Tech futures contracts. Petitioner therefore did not know that the positions in its account with NYCC were really losses, not gains, because these losses were masked by NYFE's fraudulently set settlement prices. J.A. 18. That bogus price, in turn, led petitioner to calculate a margin requirement for First West's account with petitioner that was not in line with the economic reality or risk of the value of P-Tech futures contracts. *Ibid.*

By March 2000, respondents received complaints from some members that the P-Tech futures contracts settlement price calculated by Eisler was incorrect. *Id.* at 18-19. But respondents did not investigate or take corrective action. *Id.* at 20.

Eisler began to lose the ability to fraudulently set the P-Tech futures settlement prices by May 2000, when the market for such contracts became too volatile. *Matter of Norman Eisler*, *supra*, at 6. On May 11, 2000, petitioner Klein & Co. Futures was subject to a margin call for NYCC based on the P-Tech futures positions it was responsible for with NYCC due to Eisler, and petitioner met this obligation. J.A. 21-23. Petitioner, in turn, computed a $700,000 margin call on Eisler's First West account, and ordered Eisler to either deposit more funds with petitioner or liquidate his position. *Id.* at 21.

On Friday, May 12, 2000, after Eisler indicated that he could not liquidate his P-Tech positions, *id.* at 22, petitioner requested that respondents take emergency action and suspend trading of P-Tech futures and liquidate all positions at the previous day's settlement price. *Id.* at 23. Respondents refused to do so, explaining that because petitioner had met its margin with NYCC no such emergency action was required. *Ibid.*

On Monday, May 15, 2000, however, Eisler's membership and privileges with respondent NYBOT and its affiliates, including NYFE and NYCC, were terminated, *id.* at 24, so he could no longer calculate the settlement price for P-Tech futures. *Ibid*. A correct calculation of the P-Tech futures settlement price occurred and petitioner's positions with NYCC in the P-Tech futures market due to Eisler's trades were subject to a margin deficit of $4.5 million. *Id.* at 25.

Eisler was not able to meet the margin call with petitioner to offset that deficit. Petitioner was not able to meet its margin call from NYCC, which meant that petitioner no longer met the minimum capital requirement for membership on NYBOT, NYCE, NYFE and NYCC. *Ibid.* This led to the suspension of petitioner's membership privileges, and the closing of petitioner's business that very day. *Id.* at 26, 28.

D. PROCEEDINGS BELOW

1. Petitioner brought the instant action on July 26, 2000, in the United States District Court for the Southern District of New York, under, *inter alia*, the Commodity Exchange Act, 7 U.S.C. § 25 (1994), against Eisler, First West, and the several respondents and their officers, directors or committee members. J.A. 9-57.

The district court dismissed the case, holding that petitioner lacked standing. Pet. App. 24a. The district court stated that Section 25 "provides that private remedies are available only to litigants who 'engaged in any transaction on or subject to the rules' of such contract market or licensed boards of trade." *Id.* at 23a (quoting 7 U.S.C. § 25(b)(1)-(3)). The district court interpreted that provision "to mean that only *purchasers or sellers* on the contract market have a right of action" under 7 U.S.C. § 25. *Id.* at 23a-24a (emphasis in original). The court thus concluded that petitioner lacked standing because it was not a "purchaser or seller" and did not "trade on its own account." *Id.* at 24a.[11]

2. The court of appeals affirmed. Unlike the district court, the court of appeals purported to recognize that 7 U.S.C. § 25 creates different private rights of action against different defendants, but it ignored the differences between the distinct types of actions arising under Section 25(a)(1), (b)(1), (b)(2), and (b)(3). *See* Pet. App. 7a (describing Section 25 as "includ[ing] *two* types of claims") (emphasis added).

The court of appeals held as a general matter that Section 25(a) and (b) "require[ ] that a putative plaintiff fall within one of the four required relationships set forth in" the various subparagraphs of the (a)(1) cause of action, 7 U.S.C. § 25(a)(1)(A) to (D) (1994). Pet. App. 7a-8a. And, in the court of appeals' view, the "common thread" of the subparagraphs of Section 25(a)(1) "is that they limit claims to those of a plaintiff who actually traded in the commodities market." *Id.* at 8a. The court of appeals concluded that petitioner did not fall within the requirements of Section 25(a)(1)(A) to (D), and thus could not bring any of its claims, including under Section 25(b)(1), because petitioner had not "purchased or sold" P-Tech futures contracts. *Id.* at 9a.

The court of appeals denied a petition for rehearing and rehearing *en banc* on November 14, 2006. *Id.* at 35a-36a.

SUMMARY OF ARGUMENT

I.

The plain language of the Commodity Exchange Act confers statutory standing on petitioner to bring this private right of action against respondents. Petitioner falls

[11] The district court characterized petitioner's obligation to NYCC as "inherited from First West," Pet. App. 21a, revealing the district court's mistaken view that First West could be a counterparty to a clearinghouse in a futures transaction, when in fact only a clearing member can hold such a position. *See*, *infra*, pages 37-41.

well within the requirement that it have "engaged in any transaction on or subject to the rules" of a commodity futures exchange or its clearinghouse, as required to bring an action under 7 U.S.C. § 25(b)(1) (1994).

A. Petitioner engaged in numerous transactions that were conducted both *on* the exchange and its clearinghouse and *subject to their rules*. With respect to each futures contract trade, respondents' rules required that petitioner "shall be the buyer or seller of said contract" and shall assume that contract on the exchange as its own within one hour of the trade, NYFE Rule 306(i)(2) (App., *infra*, 14a), and petitioner cleared – *i.e.*, consummated – that same contract with NYCC, subject to such rules. NYCC By-Law 5.1 (J.A. 119-120).

B. The court of appeals ignored the significance of petitioner's integral role in these transactions, any one of which confers standing on petitioner under Section 25(b)(1). The court limited standing to those who "purchased or sold" futures contracts. But this ruling disregards petitioner's position as buyer or seller of the contract and is replete with error, contrary to a number of basic statutory tenets, including that the interpretation of a statute must begin with the words of the statute.

The plain text of Section 25(b)(1) and of its neighboring statutory provisions demonstrate that "any transaction on or subject to the rules" of the exchange and clearinghouse necessarily includes the transactions in which petitioner engaged. Had Congress meant to limit standing under Section 25(b)(1) to a subset of futures transactions, *i.e.*, purchases or sales of futures contracts, it would not have used the term "any" transaction – an expansive term not readily subject to such a limitation. *United States v. Gonzales*, 520 U.S. 1, 5 (1997).

Moreover, if Congress had intended to limit the remedy under Section 25(b)(1) to purchasers and sellers, it knew how to do so. In Section 25(a)(1)(D), Congress limited standing to persons only so long as they had "purchased or sold a contract" in certain circumstances.

7 U.S.C. § 25(a)(1)(D) (1994). Congress did not use such terminology in Section 25(b)(1).

The court of appeals also erred when it held that, as a general matter, plaintiffs under the various causes of action in Section 25(b) must have engaged in a transaction that fell within Section 25(a). There is no such cross-reference in Section 25(b)(1). And the cross-references to Section 25(a) in Sections 25(b)(2) and (b)(3) demonstrate that the absence of the cross-reference in Section 25(b)(1) was not inadvertent.

Section 25(b)(3), in particular, highlights that the requirement of Section 25(b)(1) that a plaintiff have engaged in "any transaction on or subject to the rules" of an exchange or clearinghouse is different from the requirement of Section 25(a) that a plaintiff have engaged in one of the transactions specified in Section 25(a)(1)(A) to (D). In Section 25(b)(3), Congress specified that certain suits are available only to persons that satisfy *both* the requirements. Thus, the former requirement cannot be read to mean the same as the latter.

C. The structure of the statute further establishes that "any transaction on or subject to the rules" of an exchange or clearinghouse encompasses petitioner's transactions at issue here. Indeed, 7 U.S.C. § 6(a) *mandated* that the clearing transactions be on or subject to the rules of the exchange and clearinghouse. Section 6(a) provided that the clearing transactions such as those in which petitioner engaged would have been unlawful unless conducted on or subject to the rules of the exchange and clearinghouse. Section 6(a) also uses "any transaction" as a term that is broader than just a purchase or sale contract, which cannot be squared with the court of appeals' statutory interpretation.

II.

A. The court of appeals' ruling was grounded in the view that trading in commodity futures contracts is nothing more than a contract of sale between a buyer of a futures contract and the seller. It thus held that petitioner was no more than a creditor of its customer. But that cannot be reconciled with the reality or rules of the exchange which make clear that it is petitioner as the clearing FCM who is the "buyer or seller of said contract" and assumed that contract as its own on the exchange, *see* NYFE Rule 306(i)(2) (App., *infra*, 14a), and then was financially liable to the clearinghouse for the clearing of that same contract. NYCC By-Law 5.5 (J.A. 131-132).

B. Indeed, far from being a mere creditor, an FCM is an indispensable party to a contract on the commodity futures exchange. Every trade must be consummated on the exchange's clearinghouse. Through those transactions, the clearinghouse becomes the buyer to the selling FCM and the seller to the buying FCM and serves the clearinghouse function of eliminating counterparty risk. Clearinghouses transact – *i.e.*, clear – only with their own members. Thus, only a clearing member like a clearing FCM may consummate the trade on the clearinghouse. NYCC By-Law 5.1 (J.A. 119).

III.

Both Congress and this Court have long recognized that the private rights of action under the Commodity Exchange Act enhance the public enforcement mechanisms. Congress explained "that the right of an aggrieved person to sue a violator of the Act is critical to protecting the public and fundamental to maintaining the creditability of the futures market." H.R. Rep. No. 97-565(I), at 56-57 (1982). Permitting FCMs like petitioner to bring an action against an exchange and its clearinghouse for violation of their obligation to enforce their rules consistent with the Act certainly serves such a public purpose and helps to ensure the integrity of the futures commodity market.

ARGUMENT

I. THE PLAIN TEXT AND STRUCTURE OF THE COMMODITY EXCHANGE ACT DEMONSTRATE THAT PETITIONER HAS A CAUSE OF ACTION AGAINST RESPONDENTS UNDER 7 U.S.C. § 25(b)(1)

A. Petitioner Is A "Person Who Engaged In Any Transaction On Or Subject To The Rules Of" The Exchange And Clearinghouse

Petitioner has statutory standing because it falls well within the class of plaintiffs vested with a cause of action under Section 25(b)(1). That provision permits "a person who engaged in any transaction on or subject to the rules of" an exchange or its clearinghouse to recover from the exchange or clearinghouse any "actual losses" resulting from that transaction, if the damages were "caused by" the exchange or clearing organization's "failure to enforce * * * bylaws, rules, regulations, or resolutions." 7 U.S.C. § 25(b)(1) (1994).

Petitioner, as an FCM, engaged in a number of transactions "on or subject to the rules of" NYFE and its clearinghouse, NYCC.

Petitioner was the buyer or seller of Eisler's P-Tech futures contracts at issue in the instant dispute, and was required to accept and assume those same contracts "*on*" the exchange, as set forth in Section 25(b)(1). NYFE Rules explicitly require that:

> Every contract made on the Exchange shall be assumed by a member of the Exchange who is a clearing member of the clearing organization which clears contracts made on the Exchange. Every such contract when made by a trading member shall be made on behalf of a clearing member who shall be the buyer or seller of said contract on the terms set forth therein. The clearing member shall assume said contract in writing within one hour after receipt of a report from the trading member identifying the terms thereof.

NYFE Rule 306(i)(2) (App., *infra*, 14a).

Those transactions were also "*subject to the rules of*" the exchange, as set forth in Section 25(b)(1). *See, e.g.*, *ibid*; NYFE Rule 121(f) (App., *infra*, 10a) (requiring a clearing member such as petitioner to be financially involved in every trade); NYFE Rule 315 (App., *infra*, 14a-15a) (prescribing how the settlement price is calculated for the positions); NYFE Rule 703 (App., *infra*, 15a-18a) (prescribing margin requirements); NYBOT Margin Rule XXX(a) (App., *infra*, 20a) ("[N]o carrying member shall carry an open position in a futures or option contract for an account, unless it collects the original margin required pursuant to the Rules within a reasonable time, except for good cause."). And those are rules that respondents were required to enforce. 7 U.S.C. § 7a(a)(8) (1994).[12]

Also, petitioner engaged in transactions on and subject to the rules of the exchange when, as a member of the exchange's clearinghouse, petitioner cleared those contracts it assumed on the exchange *on* the clearinghouse and *subject to* the rules of the clearinghouse. Through that clearing transaction, petitioner as a clearing FCM became the seller of the futures contracts to the clearinghouse. *See, supra*, pages 7-11 (explaining clearing process); NYCC By-Law 5.1 (J.A. 119) ("Only Clearing members shall be entitled to clear Contracts with the Corporation[.] * * * Each Clearing Member shall have the privilege of clearing with the Corporation all Contracts traded on or subject to the rules of each Exchange of which it is a member or member firm * * *, whether for customer or proprietary account"); NYCC By-Law 5.7 (J.A. 142-143) (proscribing margin).

Furthermore, as part of the open and ongoing position in P-Tech futures, petitioner engaged in transactions subject to the rules of the clearinghouse on a daily basis

[12] In addition, petitioner has alleged transactions that were "subject to the rules of" respondents NYBOT and NYCE, the parent companies of NYFE and NYCC, which had their own rules and bylaws with which members of their subsidiaries, such as petitioner, were required to comply. J.A. 17-18, 20-21, 25-26.

when petitioner settled its accounts and was required to maintain appropriate margin with NYCC. NYCC Rule 502(c) (J.A. 171) (proscribing variation margin requirements based upon settlement price).

Any one of these transactions was sufficient to confer standing on petitioner under the plain text of 7 U.S.C. § 25(b)(1), as a person who engaged in "any transaction on or subject to the rules of" the exchange or clearinghouse.

B. Core Principles Of Statutory Construction Demonstrate That Section 25(b)(1) Is Not Limited To Purchasers And Sellers

The court of appeals fundamentally erred by holding that, because petitioner had not purchased or sold the P-Tech futures contracts on its own behalf, petitioner had not met the Section 25(b)(1) requirement that it be a person who "engaged in any transaction on or subject to the rules of" the exchange or its clearinghouse. *See* Pet. App. 8a (court of appeals required plaintiff to have "traded" in the commodities market); *id*. at 9a (court of appeals concluded that petitioner could not meet standing requirement because it failed to "contend that it purchased or sold P-Tech contracts"); *id.* at 11a (court of appeals emphasized that "Klein was not an owner of P-Tech contracts traded by First West").

First, as explained above, that reasoning should not deny petitioner standing because petitioner is the "buyer or seller" of the futures contract that it "assumed" as its own under respondents' own rules. *See* NYFE Rule 306(i)(2) (App., *infra*, 14a). Second, that ruling cannot be squared with the statutory text, and thus the fundamental tenet that any interpretation of a statute must begin with the words of the statute itself, *see, e.g.*, *Estate of Cowart v. Nicklos Drilling Co.*, 505 U.S. 469, 475 (1992), which do not so narrowly limit the persons with standing under Section 25(b)(1) to only the purchaser or seller of a futures contract.

1. The term "any transaction" is not limited to a purchase or sale of a contract

Section 25(b)(1) confers standing on a person who engaged in "*any* transaction" on or subject to exchange or clearinghouse rules. It is not limited to a person who engaged in a transaction to purchase or sell futures contracts on its own behalf.

The term "any," of course, when "[r]ead naturally, * * * has an expansive meaning, that is, 'one or some indiscriminately of whatever kind.'" *United States v. Gonzales*, 520 U.S. 1, 5 (1997) (quoting *Webster's Third New International Dictionary* 97 (1976)). The only language that Congress added to limit the term "any" as it described "transaction" was that the transaction must have been "on or subject to" the rules of an exchange or clearinghouse. "Any transaction" thus unambiguously encompasses many different types of transactions, in addition to the purchase and sale of contracts, that are involved in commodities futures trading and are subject to such rules. Such transactions include, for example, the transaction between an individual or entity that executes a trade and its clearing FCM which must guarantee and assume the trade, and the transaction between a clearing FCM and the clearinghouse to clear the trade. *See, supra*, pages 24-26.

Reading Section 25(b)(1) consistent with its plain text does not lead to absurd results or "separate the statute from its intended purpose." *Lewis v. United States*, 523 U.S. 155, 159-160 (1998). Section 25(b)(1) does not create boundless liability. Indeed, the requirement that a plaintiff have engaged in an exchange or clearinghouse transaction ensures that only participants in the futures market can bring a suit and not others, even if they might experience economic consequences from a market participant's transactions on the futures market. *See, e.g.*, *American Agri. Movement, Inc. v. Board of Trade of the City of Chicago*, 977 F.2d 1147 (7th Cir. 1992) (holding that farmers who were not participants in the futures market did not have standing under Section 25(b)(1), (3) even though the exchange's actions with respect to its rules may have affected the price at which they could sell their crops). Congress thereby precluded actions "for speculative damages to assets that are affected by fluctuations in prices on the commodity market but which are not the subject of transactions on such market." H.R. Rep. No. 97-565(I), at 57 (1982).

Moreover, Congress further limited the scope of Section 25(b)(1) to actions for "actual losses," and to require, in actions against exchanges and clearinghouses, that the plaintiff prove bad faith. *See* 7 U.S.C. § 25(b)(1), (4) (1994).

2. Congress limited a different cause of action to purchasers and sellers

If Congress had intended to limit liability under Section 25(b)(1) to purchasers and sellers of futures contracts, it knew how to do so. That is evident because Congress did so in Section 25(a)(1)(D).

Section 25(a)(1)(D) identifies one of the categories of plaintiffs who have standing to bring suit under Section 25(a)(1) against FCMs, floor brokers, or other persons or firms who are not an exchange or its clearinghouse. Congress specified that, in circumstances where the violation constitutes price manipulation, suit could be brought only by a person who "purchased or sold a contract." 7 U.S.C. § 25(a)(1)(D) (1994).

Congress obviously chose not to use that language in Section 25(b)(1) and did not so limit standing when it authorized actions against exchanges and their clearinghouses.

3. Section 25(b)(1) does not incorporate the limits of Section 25(a)

The court of appeals also erred when it held that, as a general matter, plaintiffs under the various causes of action in Section 25(b) must have engaged in a transaction that fell within Section 25(a). Pet. App. 7a-8a ("[t]he text of [subdivisions 25(a) and 25(b)] requires that a putative plaintiff fall within one of the four required relationships set forth in § 2[5](a)(1)(A-D)").

There is no such cross-reference anywhere in the text of Section 25(b)(1). Congress's failure to so limit Section 25(b)(1) is all the more obvious because Congress did limit Section 25(b)(2) and (b)(3). Both Section 25(b)(2) and (b)(3) provide that only a person who engaged in "any transaction specified in subsection (a)" can bring suit. The incorporation of that provision in Sections 25(b)(2) and (b)(3) demonstrates that its omission in the adjacent Section 25(b)(1) was not inadvertent.

Moreover, Section 25(b)(3) firmly establishes that Section 25(b)(1)'s reference to a person who engaged in "any transaction on or subject to the rules of" an exchange or clearinghouse cannot be read, as the court of appeals apparently did, to mean a person who engaged in a transaction specified in Section 25(a). Section 25(b)(3) grants standing under one prong of that provision only to a person who satisfies *both* the requirement that he have engaged in a transaction specified in Section 25(a), and *also* that that transaction have been "on, or subject to the rules of" a contract market, clearinghouse, or board of trade. 7 U.S.C. § 25(b)(3) (1994).

Certainly the fact that Section 25(b)(3) includes both requirements demonstrates that Congress did not intend that the two requirements be read to mean the exact same thing. Yet, that is, in essence, what the court of appeals did. It thereby rendered superfluous parts of Section 25(b)(3) because, according to the court, the requirement that the transaction have been "on, or subject to, the rules of" the exchange or clearinghouse means nothing more than the other requirement that the transaction have been one that is specified in Section 25(a).

The court of appeals' circular reasoning violates a number of core principles of statutory construction. It violates the basic canon that, "where Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion." *Russello v. United States*, 464 U.S. 16, 23 (1983) (quoting *United States v. Wong Kim Bo*, 472 F.2d 720, 722 (5th Cir. 1972)); *see also Lopez v. Gonzales*, 127 S. Ct. 625, 631 (2006); *Barnhardt v. Sigmon Coal Co., Inc.*, 534 U.S. 438, 454 (2002); *INS v. Cardoza-Fonseca*, 480 U.S. 421, 431 (1987).[13]

The court of appeals' ruling also runs contrary to the well understood fact that if phrases are to have the same meaning, "it would have been natural for Congress to write in like terms." *Johnson v. United States*, 529 U.S. 694, 704-705 (2000). And it cannot be reconciled with the "'cardinal principle of statutory construction' that 'a statute ought, upon the whole, to be so construed that, if it can be prevented, no clause, sentence, or word shall be superfluous, void, or insignificant.'" *TRW Inc. v. Andrews*, 534 U.S. 19, 31 (2001)) (quoting *Duncan v. Walker*, 533 U.S. 167, 174 (2001)).

4. The different standing requirements in Section 25(a) and 25(b)(1) reflect different types of private suits intended by Congress

Congress's imposition of different standing requirements for suits against different defendants under the various causes of action in Section 25 reflects the different purposes of those causes of action.

Suits brought under Section 25(a) are customer-driven lawsuits against the entities with whom futures customers conduct business – *e.g.*, FCMs. By contrast, it is not just

[13] Indeed, with respect to this *very* provision, this Court previously has refused to incorporate provisions that exist elsewhere in the statute but were omitted from 7 U.S.C. § 25. *Omni Capital Int'l, Ltd. v. Rudolf Wolff & Co.*, 484 U.S. 97, 106 (1987) (explaining that because "Congress expressly provided for nationwide service of process" in other CEA enforcement provisions, "[i]t would appear that Congress knows how to authorize nationwide service of process when it wants to provide for it" and "[t]hat Congress failed to do so here argues forcefully that such authorization was not its intention").

customers who would bring suits under Section 25(b)(1) against exchanges and their clearinghouses regarding their erroneous enforcement, or failure to enforce, their rules and regulations. In such instances, the entities that deal with the exchanges and clearinghouses and are subject to their rules and regulations, *i.e.*, the FCMs, have an economic interest and sophistication to bring such suits. Indeed, clearing FCMs financially guarantee all customer trades to the clearinghouse and therefore are susceptible to greater losses than any one customer if an exchange or clearinghouse fails to enforce its rules that ensure the integrity of the futures market. Congress thus authorized FCMs to sue an exchange or clearinghouse that causes them actual losses, in bad faith.

Moreover, it would make little sense to limit standing under Section 25(b)(1) to persons engaged in the customer-based transactions listed in Section 25(a)(1) because customers have no direct relationship with the exchanges and clearinghouses subject to suit under Section 25(b)(1).[14]

[14] None of this is to say that customers of FCMs lack standing under Section 25(b)(1), even though they are prohibited by Congress, the CFTC, and respondents' own rules from engaging directly in transactions *on* the exchange and are not known to the clearinghouse. This is because the Section 25(b)(1) cause of action is also granted to any person who engages in a transaction "subject to the rules of" the exchange. 7 U.S.C. § 25(b)(1) (1994). An FCM's dealings with its customers is subject to many of respondents' rules, *see, e.g.*, NYFE Rule 305 (App., *infra*, 10a-11a) (prohibiting a member from taking the opposite position of a customer's order), so that if an exchange were to fail to enforce those rules, to the detriment of the FCM customer, that customer also has an action under Section 25(b)(1) against the exchange or its clearinghouse for bad faith, actual losses. Thus, customers who are injured by a market manipulation that the exchange has failed, in bad faith, to prevent or stop likewise would have a cause of action against the exchange, just as this Court held in *Curran*.

C. The Structure Of The CEA Confirms That Congress Understood The Transactions By Petitioner To Be "On Or Subject To The Rules Of" The Exchange And Clearinghouse

The framework created by Congress in the CEA for the trading of commodity futures contracts requires that the transactions in which petitioner engaged be on or subject to the rules of an exchange and its clearinghouse.

1. 7 U.S.C. § 6(a)(1) *requires* that transactions in which clearing FCMs engage be on, or subject to, the rules of an exchange and its clearinghouse

Section 6(a) states, in relevant part, that it is unlawful for a person to "enter into, to execute, to confirm the execution of, or to conduct any office or business anywhere in the United States * * * for the purpose of * * * dealing in, any transaction in, or in connection with, a contract for the purchase or sale of a commodity for future delivery * * * unless –

> (1) such transaction is *conducted on or subject to the rules of* a board of trade which has been designated by the Commission as a "contract market" for such commodity;
>
> (2) such contract is executed or consummated by or through a member of such contract market; and
>
> (3) such contract is evidenced by a record in writing * * *."

7 U.S.C. § 6(a) (1994) (emphasis added).

The transactions enumerated in Section 6(a) include precisely the types of transactions in which Congress has authorized clearing FCMs to engage. For example, petitioner's assumption of the futures contracts at issue here on the exchange and its clearing of those trades, pursuant to NYFE Rule 306(i)(2) and NYCC By-Law 5.1, fall squarely within Section 6(a) as the conduct of business for the purpose of dealing in a transaction "in, or in connection with, a contract for the purchase or sale of a commodity for future delivery." Thus, Section 6(a)(1) required that petitioner's transactions be conducted on or subject to the rules of the exchange and clearinghouse in order to be lawful.

Of course, the transactions in which petitioner engaged here are typical of every clearing transaction that consummates every commodity futures contract trade. And to hold that petitioner did not engage in a transaction on or subject to the rules of the exchange under Section 25(b)(1) would mean that the transactions in which clearing FCMs always engage to consummate futures contracts are unlawful under Section 6(a).

Such a ruling would render superfluous other provisions of the statute. For example Section 6(a)(2) requires that a commodity futures contract be "executed or consummated by or through a member of such contract market." Under the rules of the exchange and clearinghouse, the only entity that can consummate a contract is a member of the exchange's clearinghouse like a clearing FCM. *See* NYCC By-Law 5.1 (J.A. 119). Therefore, if an FCM's consummation of a trade is unlawful, Section 6(a)(2)'s provision for consummation of a trade through a clearing FCM is left with no application. Congress plainly did not contemplate such a result, requiring reversal of the ruling below. *TRW Inc.,* 534 U.S. at 31 (2001).

2. 7 U.S.C. § 6(a)(2), (3) confirm that "any transaction" is broader than a purchase or sale contract

Section 6(a) refers at the outset to "*any transaction*" that is "in, or in connection with, a *contract for the purchase or sale* of a commodity for future delivery." Section 6(a)(1) then talks in terms of "such transaction," but Sections 6(a)(2) and (3) talk in terms of "such contract." This statutory text and structure thus confirm that Congress used the terms differently and intended that "any transaction" in the CEA be broader than only the purchase and sale of a commodity futures contract.

The court of appeals, however, ignored the distinction between "any transaction" and a "contract for the purchase or sale of a commodity for future delivery," contrary to well-settled understanding that if Congress considered terms to have the same meaning, Congress would not have used different terms for each. *See Johnson v. United States*, 529 U.S. 694, 704-705 (2000) (explaining that if the phrases were to have the same meaning, "it would have been natural for Congress to write in like terms. * * * But that is not what Congress did."); *Smith v. United States*, 508 U.S. 223, 235-236 (1993) (explaining that Congress "carefully varied the statutory language" so that "with respect to some crimes, the firearm is subject to forfeiture not only if it is 'used,' but also if it is 'involved in' the offense").

II. RESPONDENTS' RULES, THE CEA, AND CFTC REGULATIONS ARE ROOTED IN THE UNDERSTANDING THAT FCMS LIKE PETITIONER ARE PRINCIPALS TO TRANSACTIONS ON OR SUBJECT TO THE RULES OF THE EXCHANGE AND ITS CLEARINGHOUSE

In denying petitioner standing, the court of appeals concluded that petitioner's "loss was a credit loss, not a trading loss" so that, in the court's view, petitioner's injury did not result from a transaction on or subject to the rules of the exchange or its clearinghouse. Pet. App. 12a. The court of appeals thus treated a futures transaction as no more than a contract of sale between the buyer of a futures contract and that contract's seller, with the clearing FCM of the buyer or seller nothing more than an extender of credit to that customer. *Id*. at 11a.

Putting aside the fact that the difference between a credit loss and a trading loss is irrelevant to determining whether a person "engaged in a transaction on or subject to the rules of" an exchange or clearinghouse, the court of appeals' view is wrong under respondents' own rules and by-laws, as well as the CEA and the CFTC's implementing regulations.

Petitioner, in fact and in law, was a principal to the P-Tech futures contracts of Eisler on the exchange and it necessarily engaged in the transactions to consummate those contracts on the clearinghouse.

A. Clearing FCMs Are Not Mere Creditors Because They Are The Buyer Or Seller Of The Futures Contract And Assume As Their Own That Contract On The Exchange

At the outset, by describing petitioner as no more than a creditor of First West, the court of appeals mistakenly assumed that that entity traded on the exchange with another customer on the exchange. That is not the case.

Since the founding of the Chicago Board of Trade in 1848, only members of the exchange can lawfully conduct business – *i.e.*, trade – on the exchange. *See Board of Trade of the City of Chicago v. Christie Grain & Stock Co.*, 198 U.S. 236, 248 (1905) ("the contracts made in the pits are contracts between the members"). That was, and remains, true for trades occurring on respondent NYBOT's subsidiary exchanges, including NYFE and NYCE, because respondents' floor trading rules expressly concede that only members with floor trading privileges have access to the trading floor. *See* NYBOT Rule 4.02, *available at* http://www.nybot.com/aboutNYBOT/rulebooks/nybot/download/Ch%2027%20Electronic%20Trading%20Rules.pdf (last visited July 18, 2007); *see also* NYFE Rule 121(f) (App., *infra*, 10a) (requiring a clearing member such as petitioner to be part of the transaction).

Moreover, respondents' rules dictate that a clearing FCM is a necessary *party* in every commodity futures contract executed on the exchange. As previously discussed, *see, supra,* pages 24-26, NYFE Rule 306(i)(2) required petitioner, as a clearing member, to be the buyer or seller on whose behalf the contract is made and to assume the futures contracts on the exchange. NYFE Rule 306(i)(2) (App., *infra*, 14a).

These rules are not advisory. As demonstrated above in the discussion of 7 U.S.C. § 6(a), Congress has mandated that members of an exchange must "execute[ ] or consummate[ ]" a futures contract for it to be lawful. That mandate precludes the direct buyer-to-seller contractual relationship between the investors that the court below erroneously envisioned. 7 U.S.C. § 6(a)(2) (1994); *see also Ricci v. Chicago Mercantile Exch.*, 409 U.S. 289, 303 (1973) ("[T]he express will of Congress is that to deal in commodity futures one must either be, or deal through, a member of a board of trade having specified qualifications and carrying official designation as a contract market."); 17 C.F.R. § 1.3(q) (1999) (defining "member" of an exchange to be a person with "trading privileges" on the exchange).

The rules and bylaws restricting trading to exchange members are among those that respondents are required to enforce by virtue of the CEA. 7 U.S.C. § 7a(a)(8) (1994).

B. Clearing FCMs Necessarily Engage In Transactions Subject To Clearinghouse Rules Because Only Such Clearing Members Can Perform The Required Consummation Of A Trade On The Clearinghouse And They Become Financially Liable For The Same

The court of appeals' creditor theory further falters with respect to transactions on the exchange's clearinghouse. Far from being a creditor, the clearing FCM takes on the financial liability to the clearinghouse of the trade and that remains regardless of the customer's obligation to the FCM. Indeed, it is only a member of the clearinghouse like a clearing FCM, not a buyer or seller, who can engage in the required transaction to consummate a trade on the clearinghouse.

1. As discussed above, there is no contractual relationship formed between two customers who arrange

for members of the exchange to trade on their behalf. Even if such a contractual relation were to exist, however, it would be severed when the clearing FCMs assume the contracts and clear them.

The process of clearing substitutes the clearinghouse as the buyer to the selling FCM and the seller to the buying FCM. *See*, *supra*, pages 7-11 (detailing operation of clearing transactions). Respondent NYCC acknowledges this fact. App., *infra,* 19a; *see also* CME Clearing at 2 (explaining that CME Clearing deals exclusively with its members and "does not look to individual customers for performance").

Accordingly, the underlying financial obligations in the trade that was executed on the floor of the exchange become the obligations of the clearing FCM on one side of the agreement and the clearinghouse on the other side of the agreement. *Bankruptcy Act Revision: Hearings on H.R. 31 and H.R. 32 Before the Subcomm. on Civil and Constitutional Rights of the House Comm. on the Judiciary*, 94th Cong., 2380 n.8 (1976) (Statement of CFTC Chairman William T. Bagley) ("the clearing house is substituted into each contract * * * through a contractual agreement"; this involves the "simultaneous assignment of rights and delegation of duties under the contract to the clearing house by both parties to the contract upon its acceptance by a clearing house for clearance.").

In sum, the clearing FCM, not the exchange member that executed the contract nor its underlying customer, is the counterparty to the clearinghouse in the clearing transaction that consummates the contract.

2. Clearing FCMs must play this role in commodity futures contract trades because trades must be cleared and only members of the clearinghouse can do so.

The clearing of trades and the use of a clearinghouse are not voluntary. The CFTC has long-explained that "the essence of the integrity" of an exchange is the clearinghouse. The existence of a clearinghouse "is a necessary prerequisite to receiving and retaining designation as a contract market." 41 Fed. Reg. 40,091, 40,093 (Sept. 17, 1976); *see* *also ibid.* (a futures contract not cleared "would be 'contrary to the public interest' ").[15]

This construction by the CFTC of the CEA "must be accorded" "considerable weight." *CFTC v. Schor*, 478 U.S. 833, 844-845 (1986) (citing *Chevron U.S.A. Inc. v. Nat. Res. Defense Council, Inc.*, 467 U.S. 837, 844-845 (1984)).[16] And, not surprisingly, the rules of respondent NYCC are in accord with this federal mandate: "Only Clearing members shall be entitled to clear Contracts with the Corporation[.] * * * Each Clearing Member shall have the privilege of clearing with the Corporation all Contracts traded on or subject to the rules of each Exchange of which it is a member or member firm * * *, whether for customer or proprietary account." NYCC By-Law 5.1 (J.A. 119).

3. The reality of the contractual obligations of the parties involved confirm that a clearing FCM is financially liable for and a party to the underlying commodity futures contract transaction.

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[15] Until the decision below, the courts of appeals where the major exchanges are located had long-recognized this well-established and required practice of commodity trading. *See, e.g.*, *Bosco v. Serhant*, 836 F.2d 271, 273 (7th Cir. 1987), *cert. denied*, 486 U.S. 1056 (1988) (noting that a futures transaction cannot occur without the "services of both a clearing member of the Exchange * * * and a futures commission merchant"); *Bernstein v. Lind-Waldock & Co.*, 738 F.2d 179, 181 (7th Cir. 1984) (Posner, J.); (explaining that only clearing members can enter into contracts, thereby insuring that the contract will go through); *Leist v. Simplot*, 638 F.2d 283, 287 (2d Cir. 1980) (Friendly, J.), *aff'd sub nom. Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353 (1982) ("the clearing house treats FCMs as principals in trading transactions").

[16] The CFTC defines a "clearing member" such as petitioner as "any person who is a member of, or enjoys the privilege of clearing trades in his own name through, the clearing organization of a contract market." 17 C.F.R. § 1.3(c) (1999). And in defining a "clearing organization," the CFTC explains that a clearinghouse acts as a medium for "clearing transactions in commodities for future delivery * * * or for effecting settlements of contracts for future delivery * * *, for and between *members* of any contract market." *Id.* § 1.3(d) (1999) (emphasis added).

The submission and acceptance of a futures contract for clearing by a clearing FCM to the clearinghouse dictates that any losses arise not from the extension of any credit, but due to the contractual obligations in which the *clearing FCM* is bound to the clearinghouse. The CFTC has explained:

> [W]hile the clearing house recognizes the rights of commodity customers, it deals only with its clearing members. The actual contractual situation is much more complex. The clearing house is contractually bound to clearing members, not the customers on whose behalf clearing members present trades for clearing. The clearing member, not the clearing house, is contractually bound to its customers.

Bankruptcy Hearings at 2380 n.8.

Accordingly, when a default occurs in a clearing FCM's account with a clearinghouse, the clearinghouse may satisfy that default by taking from the FCM any funds in the account, including those *unrelated to* the actual futures contract(s) that led to the default. *See* CFTC, *Interpretive Statement No. 85-3*, Comm. Fut. L. Rep. ¶ 22,703, 30,987-30,988 (OGC Aug. 12, 1985) ("a clearinghouse deals only with its clearing members and thus does not know the specific customer on whose behalf a particular contract was entered into by one of its clearing members.") (*quoting* Bankruptcy Hearings at 2395).

The CFTC understands that, although an FCM is prohibited from using its customer's funds to satisfy other obligations, *see* 17 C.F.R. § 1.22 (1999), that prohibition does not extend to a clearinghouse. A clearinghouse can look to all of the funds in the FCM's account with the clearinghouse to satisfy the FCM's obligation to it. The clearinghouse does not treat the FCM's customer funds "as the property of the particular customers of the clearing member firm to whom they may ultimately be traceable." CFTC, *Segregation of Customer Funds*, 50 Fed. Reg. 36,049, 36,050 (Sept. 5, 1985) (to be codified at 17 C.F.R. pt. 1) (explaining technical amendment to 17 C.F.R.

§ 1.20(a)); *see also ibid* (clearinghouse's customers are its members). "[A] clearing house deals strictly with its clearing members," not with individual investors, "in a relationship well-defined by the exchange's or the clearing house's rule book." Bankruptcy Hearings at 2409.

Respondents' rules, which govern petitioner's clearing transactions at issue here, require that clearing FCMs be held liable in this manner. For example, respondent NYCC By-Law 5.5(a) states: "If and to the extent a monetary default relates to a Contract carried in the customer account of a Defaulting Clearing Member, such margin, Guarantee Fund deposit and other assets (whether held for the proprietary account or the customer account) shall be applied to pay the Defaulted Obligation." *See* J.A. 131-132. Moreover, if the clearing member lacks the funds to meet the defaulted obligation, "such Defaulting Clearing Member shall continue to be liable therefor[e]." NYCC By-Law 5.5(b) (J.A. 132).[17]

As such, when Eisler's manipulation was brought to light, respondents never even sought to satisfy the unmet margin obligations to NYCC in P-Tech futures from Eisler or First West. Instead, consistent with the exchange rules that governed the clearing transactions in which petitioner had engaged, respondents looked only to petitioner, as the counterparty to NYCC for those contracts.

[17] The absence of any contractual relationship between an FCM customer and the clearinghouse is underscored by respondent NYCC's Rule 802. Upon suspension of a clearing member of the exchange, all the open futures contracts are liquidated unless they are transferred and accepted by another clearing member. J.A. 191. This liquidation can occur even if the open contract is fully margined and the FCM customer wants to maintain the position.

III. Congress Intended For Private Rights Of Action, Including Under Section 25, To Serve As Important Enforcement Mechanisms Under The CEA

The background and history of 7 U.S.C. § 25 demonstrate that Congress intended for FCMs to possess a private right of action against exchanges and clearinghouses, as an important enforcement tool in the regulation of the commodity futures industry.

This Court has long recognized that a "private cause of action enhances the enforcement mechanism fostered by Congress over the course of 60 years." *Curran*, 456 U.S. at 387. Congress's decision to "strengthen the regulation of commodity futures trading" was not intended to eliminate private causes of action; rather, "Congress evidenced an affirmative intent to preserve this enforcement tool." *Ibid*.

Section 25 was enacted against the backdrop of this Court's *Curran* decision. Congress began consideration of the statutory cause of action before this Court had issued its decision in the case. H.R. Rep. No. 97-565(I), at 56 (1982) ("At the time the Committee considered the bill, the Supreme Court had not yet resolved the issue of whether a private right of action could be implied under the Act."). It was during that legislative consideration that the Court ruled in *Curran* that the private right of action that had been recognized by the lower federal courts since 1967 survived the 1974 amendments to the CEA. 456 U.S. at 388. And it was established at that time that the implied private right of action included FCMs as plaintiffs. *See, e.g.*, *Seligson v. New York Produce Exch.*, 378 F. Supp. 1076, 1084 (S.D.N.Y. 1974) ("brokers as well as customers suffer when an orderly market is not maintained. * * * [P]laintiff [futures commission merchant] has as great a right to be protected by maintaining this action as would a customer").

Indeed, one of the consolidated cases before the Court in *Curran* involved a suit by an FCM against an exchange. *See Leist v. Simplot*, 638 F.2d 283, 285 (2d Cir. 1980), *aff'd sub nom. Merrill Lynch, Pierce, Fenner & Smith, Inc. v.*

Curran, 456 U.S. 353 (1982). In *Leist*, an FCM was among the plaintiffs that alleged it suffered losses for transactions conducted on the exchange after the exchange acted in concert with others to manipulate the potato futures market in violation of the CEA, and that the exchange failed to follow its own rules that would have prevented the market manipulation. *Leist*, 638 F.2d at 292. In permitting the cause to go forward, the court of appeals found no reason to preclude it merely because it was filed by a member of an exchange rather than one of the member's customers. *Id.* at 300-301. By affirming this decision, this Court recognized that "Congress viewed [such] private litigation against exchanges as a valuable component of the self-regulation concept." *Curran*, 456 U.S. at 385.

When Congress enacted 7 U.S.C. § 25(b)(1), shortly after *Curran*, it did not diverge significantly from the pre-existing implied private rights of action. As demonstrated above, the text of the statute makes clear that Section 25(b)(1) vests a broad cause of action against exchanges by a person who engaged in "any transaction" that is conducted "on or subject to the rules of" the exchange or its clearinghouse. *See, supra*, pages 24-34. The limited legislative history surrounding the enactment of Section 25 evinces no intent by Congress to make FCMs ineligible to bring suit, or to disavow the right that they had possessed in the past. If anything, the contrary is true because Congress began its consideration of Section 25 before *Curran* was decided, with the specific intent to codify the private right of action. This intent was consistent with the belief "that the right of an aggrieved person to sue a violator of the Act [was] critical to protecting the public and fundamental to maintaining the creditability of the futures market." H.R. Rep. No. 97-565(I), at 57 (1982). Permitting FCMs such as petitioner to sue wrongdoers such as respondents similarly furthers the public interest in ensuring the integrity of the market.

CONCLUSION

For the foregoing reasons, the judgment of the court of appeals should be reversed.

Respectfully submitted,

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APPENDIX A

The relevant provisions of the Commodity Exchange Act, 7 U.S.C. §§ 6(a), 25 (1994), as in effect when this case was filed on July 26, 2000, provide:

§ 6. Regulation of futures trading and foreign transactions

(a) Restriction of futures trading to contract markets

Unless exempted by the Commission pursuant to subsection (c) of this section, it shall be unlawful for any person to offer to enter into, to enter into, to execute, to confirm the execution of, or to conduct any office or business anywhere in the United States, its territories or possessions, for the purpose of soliciting or accepting any order for, or otherwise dealing in, any transaction in, or in connection with, a contract for the purchase or sale of a commodity for future delivery (other than a contract which is made on or subject to the rules of a board of trade, exchange, or market located outside the United States, its territories or possessions) unless –

(1) such transaction is conducted on or subject to the rules of a board of trade which has been designated by the Commission as a "contract market" for such commodity;

(2) such contract is executed or consummated by or through a member of such contract market; and

(3) such contract is evidenced by a record in writing which shows the date, the parties to such contract and their addresses, the property covered and its price, and the terms of delivery: Provided, That each contract market member shall keep such record for a period of three years from the date thereof, or for a

longer period if the Commission shall so direct, which record shall at all times be open to the inspection of any representative of the Commission or the Department of Justice.

*   *   *

§ 25. Private rights of action

(a) Actual damages; actionable transactions; exclusive remedy

(1) Any person (other than a contract market, clearing organization of a contract market, licensed board of trade, or registered futures association) who violates this chapter or who willfully aids, abets, counsels, induces, or procures the commission of a violation of this chapter shall be liable for actual damages resulting from one or more of the transactions referred to in subparagraphs (A) through (D) of this paragraph and caused by such violation to any other person –

(A) who received trading advice from such person for a fee;

(B) who made through such person any contract of sale of any commodity for future delivery (or option on such contract or any commodity); or who deposited with or paid to such person money, securities, or property (or incurred debt in lieu thereof) in connection with any order to make such contract;

(C) who purchased from or sold to such person or placed through such person an order for the purchase or sale of –

(i) an option subject to section 6c of this title (other than an option purchased or sold on a contract market or other board of trade);

(ii) a contract subject to section 23 of this title; or

(iii) an interest or participation in a commodity pool; or

(D) who purchased or sold a contract referred to in subparagraph (B) hereof if the violation constitutes a manipulation of the price of any such contract or the price of the commodity underlying such contract.

(2) Except as provided in subsection (b) of this section, the rights of action authorized by this subsection and by sections 7a(11), 18, and 21(b)(10) of this title shall be the exclusive remedies under this chapter available to any person who sustains loss as a result of any alleged violation of this chapter. Nothing in this subsection shall limit or abridge the rights of the parties to agree in advance of a dispute upon any forum for resolving claims under this section, including arbitration.

(3) In any action arising from a violation in the execution of an order on the floor of a contract market, the person referred to in paragraph (1) shall be liable for –

(A) actual damages proximately caused by such violation. If an award of actual damages is made against a floor broker in connection with the execution of a customer order, and the futures commission merchant which selected the floor broker for the execution of the customer order is held to be responsible under sections 2, 2a, and 4 of this title for the floor broker's violation, such futures commission merchant may be required to satisfy such award; and

(B) where the violation is willful and intentional, punitive or exemplary damages equal to no more than two times the amount of such actual damages. If an award of punitive or exemplary damages is made against a floor broker in connection with the execution of a customer order, and the futures commission merchant which selected the floor broker for the execution of the customer order is held to be responsible under sections 2, 2a, and 4 of this title for the floor broker's violation, such futures commission merchant may be required to satisfy such award if the floor broker fails to do so, except that such requirement shall apply to the futures commission merchant only if it willfully and intentionally selected the floor broker with the intent to assist or facilitate the floor broker's violation.

(b) Liabilities of organizations and individuals; bad faith requirement; exclusive remedy

(1)(A) A contract market or clearing organization of a contract market that fails to enforce any bylaw, rule, regulation, or resolution that it is required to enforce by section 7a(8) and section 7a(9) of this title,

(B) a licensed board of trade that fails to enforce any bylaw, rule, regulation, or resolution that it is required to enforce by the Commission, or

(C) any contract market, clearing organization of a contract market, or licensed board of trade that in enforcing any such bylaw, rule, regulation, or resolution violates this chapter or any Commission rule, regulation, or order,

shall be liable for actual damages sustained by a person who engaged in any transaction on or subject to the rules of such contract market or licensed board of trade to the extent of such person's actual losses that resulted from such transaction and were caused by such failure to enforce or enforcement of such bylaws, rules, regulations, or resolutions.

(2) A registered futures association that fails to enforce any bylaw or rule that is required under section 21 of this title or in enforcing any such bylaw or rule violates this chapter or any Commission rule, regulation, or order shall be liable for actual damages sustained by a person that engaged in any transaction specified in subsection (a) of this section to the extent of such person's actual losses that resulted from such transaction and were caused by such failure to enforce or enforcement of such bylaw or rule.

(3) Any individual who, in the capacity as an officer, director, governor, committee member, or employee of a contract market, clearing organization, licensed board of trade, or a registered futures association willfully aids, abets, counsels, induces, or procures any failure by any such entity to enforce (or any violation of the chapter in enforcing) any bylaw, rule, regulation, or resolution referred to in paragraph (1) or (2) of this subsection, shall be liable for actual damages sustained by a person who engaged in any transaction specified in subsection (a) of this section on, or subject to the rules of, such contract market, licensed board of trade or, in the case of an officer, director, governor, committee member, or employee of a registered futures association, any transaction specified in subsection (a) of this section, in either case to the extent of

such person's actual losses that resulted from such transaction and were caused by such failure or violation.

(4) A person seeking to enforce liability under this section must establish that the contract market, licensed board of trade, clearing organization, registered futures association, officer, director, governor, committee member, or employee acted in bad faith in failing to take action or in taking such action as was taken, and that such failure or action caused the loss.

(5) The rights of action authorized by this subsection shall be the exclusive remedy under this chapter available to any person who sustains a loss as a result of (A) the alleged failure by a contract market, licensed board of trade, clearing organization, or registered futures association or by any officer, director, governor, committee member, or employee to enforce any bylaw, rule, regulation, or resolution referred to in paragraph (1) or (2) of this subsection, or (B) the taking of action in enforcing any bylaw, rule, regulation, or resolution referred to in this subsection that is alleged to have violated this chapter, or any Commission rule, regulation, or order.

(c) Jurisdiction; statute of limitations; venue; process

The United States district courts shall have exclusive jurisdiction of actions brought under this section. Any such action shall be brought not later than two years after the date the cause of action arises. Any action brought under subsection (a) of this section may be brought in any judicial district wherein the defendant is found, resides, or transacts business, or in the judicial district wherein any act or transaction constituting the violation occurs. Process in such action may be served in any judicial district of which the defendant is an inhabitant or wherever the defendant may be found.

(d) Dates of application to actions

The provisions of this section shall become effective with respect to causes of action accruing on or after the date of enactment of the Futures Trading Act of 1982 [January 11, 1983]: Provided, That the enactment of the Futures Trading Act of 1982 shall not affect any right of any parties which may exist with respect to causes of action accruing prior to such date.

APPENDIX B

The By-Laws and Rules of the New York Futures Exchange, as in effect when this case was filed on July 26, 2000, provide in relevant part:

Officials of the
New York Futures Exchange, Inc.
4 WORLD TRADE CENTER, 8th Fl.,
NEW YORK, N.Y. 10048
(212) 742-5001
NORMAN EISLER, CHAIRMAN
JOSEPH J. O'NEILL, PRESIDENT
THOMAS J. GREENE, SENIOR VICE PRESIDENT
TERRENCE H. MILLER, VICE PRESIDENT
ANGEL MOTISI, SECRETARY
New York Futures Exchange, Inc.

Board of Directors
1999-2000
NORMAN EISLER, CHAIRMAN
DAVID A. BAKER
RICHARD S. DEWLING
WALTER E. FAIR
A. GEORGE GERO
KEITH W. HOCHSTIN
GARY KNAPP
ROBERT LAKE
M. SCOTT MANOLIS
ANTHONY MANORY
ROBERT MARSH
CHRISTOPHER MEEK
ALFRED PERAS
TOM PETERS
THOMAS SANCHEZ
DAVID SCHELHORN
MELISSA SCHRAMM

JEFFREY M. SOMAN
CHARLES SWEENEY
JOHN M. WALSH

* * *

Trading Members

Rule 121 (a) The approval of an applicant shall not qualify said person to execute contracts on the floor of the Exchange unless said person is also approved by the Committee on Membership as a trading member. Each trading member, upon approval as such, shall receive a trading badge with a unique number and/or letter symbol, which badge must be displayed at all times by the trading member when on the trading floor.

(b) No person shall be approved as a trading member who is not registered or licensed with the Commodity Futures Trading Commission as a floor trader or floor broker, and no holder of a membership interest shall act as a floor trader or floor broker, as those terms are defined under the Commodity Exchange Act, without being currently registered or licensed as such.

(c) No person shall be approved as a trading member who has not successfully completed an ethics training course as required by the Commodity Futures Trading Commission. Such ethics training must be under the auspices, or meet the approval, of the Exchange.

(d) No person shall be approved as a trading member who has not demonstrated to the satisfaction of the Committee on Membership the capability of performing the functions of a trading member by reason of floor experience of at least six months and/or successful completion of an Exchange-authorized floor-trading training program.

(e) No person shall be approved or shall act as a trading member who does not have a net worth (defined herein as an excess of current assets over current liabilities) of at least $20,000, or who does not file with the Exchange a certified financial statement in such form and at such time as the Exchange may request.

(f) No person shall be approved or shall act as a trading member whose obligations on the Exchange are not guaranteed, in such form as may be prescribed by the Committee on Membership, by a clearing member of the Exchange. A guaranteeing clearing member shall be obligated to promptly accept and clear any trades that have been matched trader-to-trader on the Exchange by a trading member with whom the clearing member guarantees, which trades have not been cleared by another clearing member, and, whenever directed by the Exchange, to accept, by transfer or otherwise, any transaction effected by or for the account of such trading member.

(g) Notwithstanding the provisions of subdivision (f), above, an existing qualifying clearing member agreement may be used instead of a guarantee to qualify a member for trading privileges.

* * *

Trading Against Customer's Order

Rule 305 No member (other than a floor broker whose transactions are governed by Rule 306) having an order from a customer may take the opposite side of the transaction for himself, directly or indirectly, or for an account of any firm or corporation of which he is a partner, officer, or employee, or for account of any partner, officer, or employee of such firm or corporation, unless the member taking the opposite side or the clearing member has on file the prior written consent of the customer. Such consent need not be given for each transaction but may be given in general terms; provided, however, that the customer consent must be evidenced by an instrument separate from any customer's agreement with the clearing member. If the requisite prior consent is so filed, the transaction may be effected in accordance with the Rules of the Exchange, including, but not limited to, Rule 308, notwithstanding the provisions of subparagraph (e) thereof.

Members shall use due diligence to insure compliance with this Rule.

* * *

Trading Standards for Floor Brokers

Rule 306 (a) No floor broker shall purchase any contract (including a purchase of a futures contract, or a purchase of a call or sale of a put on the same future) for his own account, or for any account in which he has an interest, while holding an order of another person for the purchase of the same contract (including a purchase of a futures contract, or a purchase of a call or sale of a put on the same future) which is executable at the market price or at a price at which such purchase can be made for the floor broker's own account or for an account in which he has an interest.

(b) No floor broker shall sell any contract (including a sale of a futures contract, or a sale of a call or purchase of a put on the same future) for his own account, or for any account in which he has an interest, while holding an order of another person for the sale of the same contract (including a sale of a futures contract, or a sale of a cotton options call or purchase of a put on the same future) which is executable at the market price or at a price at which such sale can be made for the floor broker's own account or for an account in which he has an interest.

(c) No floor broker shall execute any transaction for any account of a customer for which buying and/or selling orders can be placed or originated, or for which transactions can be executed by such floor broker, without the prior specific consent of the customer (hereinafter referred to as "discretionary orders") regardless of whether the general authorization for such orders or transactions is pursuant to a written agreement, except that discretionary orders may be placed with another member for execution.

Within the meaning of this subsection, an order which gives the floor broker discretion only as to time and price shall not be deemed to be a discretionary order. The restrictions set forth in this subsection shall not apply to discretionary orders for:

(1) members of the floor broker's immediate family, which is defined to mean a spouse, parent, parent of a spouse, child, or spouse of a child;

(2) a member of the Exchange; or

(3) a proprietary account of the floor broker, as that term is defined in §1.3(y) of the Regulations of the Commodity Futures Trading Commission.

(d) No floor broker shall disclose at any time that he is holding an order of another person or shall divulge any order revealed to him by reason of his relationship to such other person except to execute an order or except pursuant to paragraph (c) of this Rule or at the request of an authorized representative of the Commodity Futures Trading Commission or the Exchange.

(e) No floor broker shall take, directly or indirectly, the other side of any customer order revealed to him by reason of his relationship to the customer except with the customer's prior written consent and in conformity with the Rules of the Exchange applicable to such transactions. Such consent need not be given for each transaction but may be given in general terms and must be filed with and retained by the floor broker or the clearing member by an instrument separate from any customer's agreement with the clearing member.

If the requisite prior consent is so filed, the transaction shall be effected in accordance with Rule 308, notwithstanding the provisions of subparagraph (e) thereof.

(f) No trading member shall make any purchase or sale which has been directly or indirectly prearranged.

(g) No floor broker shall allocate trades among accounts except in the sequence in which the orders for such accounts has been received. The sequence of time stamping of orders when received on the floor shall be prima facie evidence of the sequence in which such orders were received by a member. Trades executed for orders received at the same time shall be allocated on an equitable basis among the orders received; provided, however, that all orders received after the close on one trading day and prior to the opening on the next trading day shall be considered as received at the same time.

(h) No floor broker shall withhold or withdraw from the market any order or part of an order of another person for the convenience of another member.

(i)(1) Every execution of a transaction on the floor shall be confirmed promptly with the opposite trading member. Such confirmation shall identify price, quantity, and future or option.

(2) Every contract made on the Exchange shall be assumed by a member of the Exchange who is a clearing member of the clearing organization which clears contracts made on the Exchange. Every such contract when made by a trading member shall be made on behalf of a clearing member who shall be the buyer or seller of said contract on the terms set forth therein. The clearing member shall assume said contract in writing within one hour after receipt of a report from the trading member identifying the terms thereof.

*   *   *

Settlement Price Computation

Rule 315 The settlement price for each contract, other than expiring contracts on the last trading day, shall be determined as follows:

(a) The settlement price shall be the average of all prices of the closing range of the contract involved. When an average is a fraction, the settlement price shall be the next full trading point above or below the fractional average depending on which is nearer to the last price recorded.

(b) If, for any contract, no transactions have been executed during the respective closing period, the settlement price for such contract shall be the average of the highest bid and the lowest offer during such closing period; provided, however, that a bid or offer which is out of line shall not be considered.

(c) If there are no bids and offers for a contract during its closing period, the settlement price shall be determined by reference to the prevailing differences between such contract and the nearest active month of the respective contract market during the day in the case of a future, and the nearest active strike price of the same series in the case of an option.

(d) If a settlement price derived by employing the foregoing procedures is not consistent with trades in other months during the closing range or with market information known to the Futures and Options Contracts Committee, the Committee may establish a settlement price at a level consistent with such other trades or market information and shall prepare a written record setting forth the basis for such settlement.

(e) Notwithstanding the foregoing provisions of this Rule, on any day on which a cessation of trading of the NYSE Composite Index Futures contract pursuant to the Rule governing trading halts and daily price limits shall be in effect at the close of trading, the settlement price for each NYSE Composite Index Futures contract shall be at such expanded price limit as is applicable pursuant to said Rule.

*   *   *

Margins

Rule 703 (a) The Exchange shall determine and notify members and member organizations of the minimum amount of initial margin and option margin which must be obtained by all members and member organizations from customers, the amount of margin that must be maintained by customers, and the terms and conditions under which margin must be required and accepted from customers. The Exchange may establish different minimum initial option and maintenance margins for different classes of customers, and for different commodity interest transactions, accounts or positions.

(b) No member or member organization shall accept any order for new trades for any account to purchase or sell a futures contract or to grant an option contract unless the minimum initial margin and option margin established by the Exchange in the new trades is on deposit or is forthcoming within a reasonable time and unless the margin in that account's pre-existing open positions complies with applicable maintenance margin requirements established by the Exchange or is forthcoming within a reasonable time; provided, however, that if an account is under margined for an unreasonable time, a member or member organization may accept orders that only serve to reduce the risk of existing positions in the account.

(c) The member or member organization may call for additional margin at his or its discretion, but whenever a customer's margin is below the maintenance margin required by the Exchange, the member or member organization must call for such additional maintenance margin as will bring the account up to Exchange minimum initial margin and option margin requirements, and if within a reasonable time the customer fails to comply with such demand (the member or member organization may deem one hour to be a reasonable time), the member or member organization must close out the customer's position or sufficient contracts or options to restore the customer's account to required margin status.

(d) The terms and conditions under which margin must be required and accepted from customers shall be as follows:

(i) On each Exchange business day, each member or member organization shall compute, for each account with an open position in an Exchange futures contract or option contract, the open trade equity, total equity, initial margin required, initial margin on deposit, option margin required, option margin on deposit, and maintenance margin required for the account. The open trade equity in an account shall be calculated using the settlement prices published by the Exchange and any other contract market, as may be required.

(ii) Initial margin and option margin may be deposited by customers with a member or member organization only in one or more of the following forms:

(A) Cash.

(B) Obligations of the United States, provided, however, that such obligations shall not be accepted as initial margin or option margin for an amount not to exceed market value less applicable haircuts as described in Regulation 240.15c3-1 of the Securities and Exchange Commission.

(C) Securities listed for trading on the New York Stock Exchange, Inc. or the American Stock Exchange, Inc.; provided, however, that such securities shall not be accepted as initial margin or option margin for an amount not to exceed market value less applicable haircuts as described in Regulation 240.15c3-1 of the Securities and Exchange Commission.

(D) Irrevocable letter of credit.

(E) Credit in the customer's account arising from a loan made by the member or member organization for the collateral value of purchased options; provided, that the amount of credit extended by the member or member organization shall not exceed the collateral value of the purchased options determined in accordance with such procedures as may from time to time be established by the Exchange.

(e) No member or member organization shall accept any order for the purchase of an option contract unless the premium for that option contract is on deposit or forthcoming within a reasonable time.

(f) Premiums on purchased options may be deposited by customers with a member or member organization only in the form of cash.

APPENDIX C

The Statement of the New York Clearing Corporation, as was available when the Futures Industry Association filed its brief as *amicus curiae* in support of petitioner before the court of appeals on October 10, 2006, provides in relevant part:

Clearing Corporation Acceptance and Liability for Trades

The details surrounding all matched trades that have been accepted by a clearing member are submitted to the clearinghouse at the end of each day, where a confirmation process is conducted. By approximately, 10:00 p.m., the clearinghouse generates to each clearing member a report showing all of the trades that the clearinghouse has accepted for the account of the clearing member. In each mutually confirmed transaction, the clearinghouse is substituted as the buyer to the selling clearing member and the seller to the buying clearing member. Once substituted as the counterparty to a transaction, the clearinghouse may not reverse its acceptance of a trade. The Clearing Corporation has no liability to the customers of a clearing member or to any Exchange member that acted as broker for a clearing member. The Clearing Corporation has no liability to make or accept delivery under a futures contract.

APPENDIX D

The By-Laws and Rules of the Board of Trade of the City of New York, as in effect when this case was filed on July 26, 2000, provide in relevant part:

Margin Rule XXX Margin Requirements

(a) Except as hereinafter provided, no carrying member shall carry an open position in a futures or option contract for an account, unless it collects the original margin required pursuant to the Rules within a reasonable time, except for good cause.

(b) Except as hereinafter provided, no carrying member shall accept any order for a futures or option contract if the execution of such order would result in an increase in the account's position, except for risk reducing trades, unless:

(i) the original margin and premium required for all existing futures and option contracts carried in the account has been deposited in accordance with the Rules (or the rules, if any, of the exchange where such futures contracts or options are traded) or the carrying member has issued a call for any margin or premium required and such call has not been outstanding more than a reasonable time, except for good cause; and

(ii) the net liquidating value of the account exceeds the maintenance level required pursuant to the Rules or the carrying member has a call for any margin required and such call has not been outstanding more than a reasonable time, except for good cause.

(c) No carrying member shall be required to obtain or call for original margin on new positions that are liquidated on the same Exchange business day.

(d)(i) No member of the Exchange with floor trading privileges shall execute a trade or place an order for the purchase or sale of any futures contract or the purchase or grant of any option if a debit or deficit balance exists in the account of such member or in any account in which such member directly or indirectly has an interest, except for the liquidation of existing positions, or with the prior approval of the President. A member of the Exchange with floor trading privileges shall immediately notify the Secretary of the Exchange if a debit or deficit or deficit balance of ten thousand dollars ($10,000) or more exists in any account or all accounts, combined, in which such member, directly or indirectly, has an interest.

(ii) A carrying member may not knowingly accept any trade or order which is violative of paragraph (d)(i) of this Rule, except for trades which the carrying member is obligated to accept as the clearing member guarantor of a member with floor trading privileges. A clearing member guarantor shall immediately advise the Exchange of any trades which it accepts pursuant to this paragraph.

(iii) A carrying member shall immediately notify the Secretary of the Exchange if a debit or deficit balance of ten thousand dollars ($10,000) or more exists in the account of a member with floor trading privileges or in any account in which such member, directly or indirectly, has an interest of which the carrying member has knowledge.

(e) No carrying member may release margin funds from an account unless such funds are in excess of the account's minimum original margin requirements.

(f) Each member firm which carries an account for a Futures Commission Merchant or a foreign broker on an omnibus basis, shall collect the original margin and maintenance margin required of such account on the basis of the gross position carried for such account.