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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 RESPONDENTS

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QUESTION PRESENTED

Section 22(b)(1) of the Commodity Exchange Act prior to its amendment in December 2000 (7 U.S.C. § 25(b)(1) (1994)) created a private cause of action against futures contract markets and clearing organizations for "a person who engaged in any transaction on or subject to the rules of such contract market" seeking to recover "actual losses that resulted from such transaction and were caused" by the contract market or clearing organization's failure to enforce its rules or application of its rules in violation of the Act or the regulations or administrative orders thereunder.

The question presented is whether this cause of action was available only to persons who bought or sold futures contracts or options, or whether the cause of action also could be asserted by an entity that merely cleared another person's purchases or sales.

RULE 29.6 STATEMENT

Board of Trade of the City of New York, Inc. (NYBOT), formerly a New York Not-for-Profit Corporation, states that following a January 12, 2007 merger, NYBOT's successor in interest is ICE Futures U.S. Inc., which is a wholly owned subsidiary of IntercontinentalExchange, Inc., a Delaware corporation publicly traded on the New York Stock Exchange. Respondent New York Clearing Corporation, now known as ICE Clear U.S. Inc., a clearing organization, and respondent New York Futures Exchange, Inc., a dormant contract market, state that they are wholly owned subsidiaries of ICE Futures U.S. Inc. Respondent New York Cotton Exchange no longer exists as it was merged into NYBOT.

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STATEMENT

After a futures or options trade takes place on the floor of a futures exchange designated as a "contract market" under the governing statute, that trade is "cleared" by the clearing organization associated with the contract market. Clearing establishes a series of relationships, specified in the rules of the clearing organization, among the buyer, the buyer's "clearing member," the seller, the seller's "clearing member," and the clearing organization that are designed to guarantee the performance obligations of the buyer and seller.

As a clearing member, petitioner was obligated by clearing organization rules to make certain payments to the clearing organization based on the change in value of the futures contracts and options held by petitioner's customers. Petitioner went out of business when it was unable to make these payments as a result of the failure of one of its customers to meet a margin call made by petitioner. Petitioner commenced this action under 7 U.S.C. § 25(b)(1) against, among others, the contract market and the clearing organization where that customer's trades were executed and cleared respectively, alleging that they failed to enforce certain contract market rules in failing to prevent the principal of petitioner's customer from using his position on a contract market committee to understate improperly the customer's margin obligation.

Section 25(b)(1)[1] establishes a private right of action for a person who "engaged in any transaction on or subject to the

[1] We agree with the Solicitor General (Br. 3 n.1) that this case is governed by the version of the Commodity Exchange Act (CEA) in effect when this case was filed in July 2000. Like the government and petitioner we use "Section xx" to refer to the section of title 7 of the United States Code rather than the section of the CEA. Unless otherwise indicated, references to the C.F.R. and rules of the NYBOT, NYFE, and NYCC likewise refer to those rules in effect when this case was filed.

rules" of a contract market to the extent that he has suffered "actual losses that resulted from such transaction" and that those actual losses were caused by the failure of a contract market or its clearing organization to enforce its rules. Every court to consider the issue has concluded that the phrase "any transaction on or subject to the rules" of a contract market limits the cause of action to persons who buy and sell futures contracts or options. Congress used "on or subject to the rules of" a contract market repeatedly in the statute, each time to refer specifically to trading of futures contracts and options. Moreover, Section 25(b)(1) was enacted shortly after this Court's decision in *Merrill Lynch, Pierce, Fenner & Smith* v. *Curran*, 456 U.S. 353 (1982), which focused exclusively on claims asserted by traders in upholding the implied cause of action that Section 25 replaced.

Congress also strictly limited the damages recoverable under Section 25(b)(1) to the plaintiff's "actual losses that resulted from" its transaction, which must be caused by the defendant's alleged failure to enforce its rules or alleged violation of the law in enforcing those rules. Petitioner's claim fails that test as well: its alleged damages resulting from the collapse of its business did not result from a transaction, they resulted from the lack of creditworthiness of petitioner's customer. The court of appeals correctly concluded that petitioner's "loss was a credit loss, not a trading loss." Pet. App. 12a.

A. Statutory And Regulatory Background

1. A futures contract is an agreement between two parties to buy or sell an asset at a certain time in the future for a specified price. JOHN C. HULL, OPTIONS, FUTURES, AND OTHER DERIVATIVES 6 (6th ed. 2006). The practice of entering into futures contracts originated in connection with agricultural commodities. "When an entire crop was harvested and marketed within a short time-span, dramatic price fluctuations sometimes created severe hardship for farmers or for processors"; these risks were alleviated by "the practice of

'forward contracting'—the use of executory contracts fixing the terms of sale in advance of the time of delivery." *Curran*, 456 U.S. at 357.

As this Court explained in *Curran*, "[b]ecause the weather and other imponderables affected supply and demand, normally the market price would fluctuate before the contract was performed. A declining market meant that the executory agreement was more valuable to the seller than the commodity covered by the contract" because it permitted the seller to obtain more than the market price for his goods. *Curran*, 456 U.S. at 357. "[C]onversely, in a rising market the executory contract had a special value for the buyer, who not only was assured of delivery of the commodity but also could derive a profit from the price increase." *Ibid*.

The opportunity to profit from these market price fluctuations "motivated speculators to engage in the practice of buying and selling 'futures contracts'" and "led to the development of recognized exchanges or boards of trade." *Id*. at 357-358. The exchanges brought standardization to the practice of trading futures contracts, making contracts fungible by developing "standard terms describing the quantity and quality of the commodity, the time and place of delivery, and the method of payment; the only variable was price." *Id*. at 358.

Futures contracts for agricultural commodities and raw materials, such as metals, were long traded on futures markets, but in the 1970s trading began in futures contracts on Treasury bills and municipal bonds; in 1982, trading began on stock index futures. ROBERT W. KOLB, FUTURES, OPTIONS, AND SWAPS 25 (2d ed. 1997). Trading in stock index futures provides an opportunity to speculate on larger-scale future movements in the stock market, and also plays a crucial role in hedging portfolio risk. *Id.* at 221. Futures exchanges today also provide a market for trading options on futures contracts (similar to the trading in options on a company's stock).[2] In all respects relevant here, the rules governing trading of options on futures are essentially the same as those governing trading of futures contracts.

2. Futures trading has been subject to federal regulation since the predecessor to the Commodity Exchange Act (CEA), 7 U.S.C. § 1 *et seq*., was enacted in 1922. In the 1974 CEA amendments, Congress created the Commodity Futures Trading Commission (CFTC) to exercise regulatory authority in this area.

The linchpin of the CEA's regulatory scheme is Section 6(a)(1), which bans futures trading (with exceptions not relevant here) unless a "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." A "contract market" is a board of trade designated by the CFTC pursuant to 7 U.S.C. § 7. The subsidiary companies of the Board of Trade of the City of New York, including the New York Futures Exchange and New York Cotton Exchange, were contract markets. Other contract markets include the Chicago Board of Trade, and the Chicago Mercantile Exchange.

[2] "An option on a futures contract or a futures option is an option that takes a futures contract as its underlying good." KOLB, *supra*, at 4. With a futures option "the call owner receives a long position in the underlying futures at the settlement price prevailing at the time of exercise" and, upon exercise, "a payment that equals the settlement price minus the exercise price of the futures option." *Ibid.* A call seller "receives a short position in the underlying futures at the settlement price prevailing at the time of exercise" and, upon exercise, "pays * * * the futures settlement price minus the exercise price." *Ibid.* The exercise of a futures put option works as a mirror image, with the owner of the futures put option receiving a short position and a payment equaling the exercise price minus the futures settlement price, and the put seller receiving a long position and paying the exercise price minus the settlement price. *Id.* at 5.

Futures traders "broadly speaking * * * fall into two general classifications, i.e. 'trade' hedging customers, and speculators. All orders which reach the trading floor originate with one or the other group of traders." *Curran*, 456 U.S. at 359 n.11 (internal quotation marks omitted). "Hedgers" are "[t]hose who actually are interested in selling or buying the commodity"; "'speculators' or 'investors'" are "[t]hose who seek financial gain by taking positions in the futures market generally." *Id*. at 359. The CFTC rules use the terms "customer" and "commodity customer" to refer to futures traders. 17 C.F.R. § 1.3(k).

A futures trader that is not a member of a futures contract market may buy or sell futures contracts through a "futures commission merchant" (FCM). The CEA defines an FCM as a person "engaged in soliciting or in accepting orders for the purchase or sale of any commodity for future delivery on or subject to the rules of any contract market" who accepts funds or property "to margin, guarantee, or secure" trades or contracts. 7 U.S.C. § 1a(12).

The FCM generally will effectuate the customer's transaction by placing the customer's order through a "floor broker"—the person who in a "place provided by a contract market for the meeting of persons similarly engaged, shall purchase or sell for any other person any commodity for future delivery on or subject to the rules of any contract market." 7 U.S.C. § 1a(8).[3]

[3] The Futures Industry Association asserts (Br. 2) that "[i]ndividual customers * * * must carry out their transactions through brokerage firms called futures commission merchants," and that "[s]uch merchants arrange for the execution of customer orders either through floor brokers in a trading pit or on a computerized trading screen, as specified in the rules of the relevant exchange." Although Chicago-based futures exchanges may require customer orders to be placed through FCMs, on New York exchanges such as NYFE, orders may be placed by customers directly with floor brokers or may be initiated by floor brokers in accordance with discre-

A significant proportion of futures and options trading consists of proprietary trading by contract market members for their own accounts, acting in the capacity of a "floor trader," which the statute defines as a person who "in or surrounding any * * * place provided by a contract market for the meeting of persons similarly engaged, purchases, or sells solely for such person's own account, any commodity for future delivery on or subject to the rules of any contract market." 7 U.S.C. § 1a(9).

After a floor broker (on behalf of a customer) or a floor trader (on his own behalf) has executed the purchase or sale of a futures or options contract, that purchase or sale must be "cleared" by the "clearing organization" for the contract market on which the transaction occurred. NYFE Rule 306(i)(2) (Pet. Br. App. 14a). The mechanics of this clearing process are unique to futures and options markets. Clearing creates a series of new relationships, specified in the rules of clearing organizations, that provide guarantees for the performance obligations of the buyer and seller that facilitate trading—and therefore enhance the depth of the market—by substantially eliminating traders' concerns that a potential counterparty might not perform due to lack of creditworthiness or otherwise.

The clearing process is complex and varies among contracts markets.[4] We discuss the process specified for the customer trades at issue here—trades on the New York Futures Exchange (NYFE).

The NYFE rules provided that "[e]very 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." Rule 306(i)(2) (Pet.

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tion granted by their customers. See NYFE Rule 306(c) (Pet. Br. App. 12a).

[4] That is why petitioner's repeated references to the practices of the Chicago markets (*e.g.*, Br. 4-9) are inapposite here.

Br. App. 14a). The New York Clearing Corporation (NYCC) is the clearing organization that cleared contracts made on the NYFE.

A "clearing member" of the NYCC that has "assumed" a contract has "the privilege to clear with [NYCC] Contracts effected on or subject to the rules of an Exchange." NYCC Bylaw 1.1 (J.A. 94). The NYCC rules state that upon its acceptance of the contract for clearing, the NYCC:

> shall assume, in the place of each Clearing Member that is a party to such Contract, all liabilities and obligations imposed thereby to the Clearing Member that is the other party thereto, to the extent provided in [the NYCC rules], and shall succeed to and become vested with all rights and benefits accruing therefrom. ***Such assumption by the Corporation shall terminate all liabilities and obligations of the Clearing Member whose Contract is so accepted to the other Clearing Member which was a party to such Contract***.

NYCC Rule 401(a) (Resp. App. 6a) (emphasis added). The clearing organization's liability does not extend "to any customer of a clearing member." *Id*. Rule 401(b)(i).

The clearing process thus creates two new agreements—one between the NYCC and the buyer's clearing member and the other between the NYCC and the seller's clearing member—and eliminates any liability of a clearing member on the original contract between the buyer and seller. In return, each clearing member agrees to satisfy to NYCC the obligations of the clearing member's customer under the original contract. The clearing member thus becomes a party to an agreement different than the contract between the buyer and seller—an agreement between itself and the clearing organization in which the clearing member agrees to pay to the clearing organization in accordance with the clearing organization's rules the net amount due with respect to the contracts carried in the clearing member's customer account with the clearing organization. The buyer and seller remain the beneficial owners of their contract executed on the contract market floor, and remain entitled to that contract's benefits and subject to its obligations.

The obligation between a clearing member and the NYCC flows from the NYCC rule requiring clearing members to "deposit with or pay to [the NYCC] original margin, variation margin and option premiums for each cleared Contract" in amounts specified by the NYCC rules. NYCC Rule 502(a) (J.A. 171). The amount of original margin required to be on deposit with the NYCC from any clearing member is determined each day in accordance with a formula applied to the position in futures contracts and options carried by the clearing member. That amount may fluctuate from day to day depending on changes in the size and composition of that position (as a result of trading activities, contract expirations, etc.), together with profits or losses on short options positions occurring during the day.

The amount of variation margin to be paid or received by any clearing member is determined each day by any net losses or net profits on its futures contract positions during the day. NYCC Rule 502(c) (J.A. 171). The amount of option premiums to be paid or received by any clearing member is determined each day by the net amount of premiums on options purchased and sold during the day. Profits or losses on options and on futures contracts are determined by reference to "settlement prices" calculated as prescribed in the rules of either the contract market or the clearing organization. See NYFE Rule 315 (Pet. Br. App. 14a-15a). The CEA makes clear that a clearing organization may not treat funds deposited with it "as belonging to * * * any person other than the customers" of the depositing clearing member. 7 U.S.C. § 6d.

When a customer opens an account with a clearing member, the customer will be required to deposit funds into that account to assure his performance, which must at least equal the "original margin" required by the contract market.[5] The clearing member is required to treat all funds "received * * * to margin, guarantee, or secure the trades or contracts of any customer * * * or accruing to such customer as the result of such trades or contracts, as belonging to such customer." 7 U.S.C. § 6d(2); see 17 C.F.R. § 1.21 (specifically addressing funds received "from any clearing organization" with respect to customer trades). This ensures that the customer will obtain the economic benefit of its trades. The customer's agreement with the clearing member in turn makes the customer responsible to cover the full amount of any losses.

Under NYFE rules, the minimum required amount of such margin is initially determined in accordance with a formula applied to the position in futures contracts and options carried by the customer, and is adjusted daily to reflect changes in the size and composition of that position and to reflect profits or losses on the futures contracts and options in that position. NYFE Rule 703 (Pet. Br. App. 15a-18a). In the event that the net equity in a customer's account falls below a maintenance level prescribed in the exchange rules or in the customer's agreement with the clearing member (U.S. Br. 8), whichever is greater, the clearing member issues a margin call to the customer requiring the customer to deposit additional margin in an amount sufficient to restore the net equity to the minimum. The profits and losses on the futures contracts and options are determined by reference to the same settlement prices as are used in determining the original

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[5] The customer-clearing member relationship is regulated by the rules of the contract market. Only FCMs may act as clearing members for customers, because the statute permits only FCMs to hold customer funds to margin, guarantee or secure customer trades and contracts. See page 5, *supra*. A non-FCM clearing member may only clear that entity's proprietary trades.

and variation margin obligations of the clearing member to the clearing organization.

The statute and rules thus make clear that (a) floor brokers (on behalf of their customers) purchase or sell futures or options contracts on or subject to the rules of a contract market (7 U.S.C. § 1a(8)); (b) it is those contracts that a clearing member has the "privilege" to clear (NYCC Bylaw 1.1 (J.A. 94)); and (c) the clearing member's "assum[ption]" of the contract between the buyer and seller is quite transitory—it ends as soon as the contract is cleared, because at that moment any obligations by the clearing member to the opposite clearing member or opposite customer on that contract cease (NYCC Rule 401(a) (Resp. App. 6a)) and are replaced by the clearing member's obligations to the NYCC and to its customer.[6]

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[6] Petitioner states (Br. 7) that there is no completed contract until after a trade is cleared. But the NYCC Bylaws define "clearing member" as a person that has "the privilege to clear with [NYCC] ***Contracts effected on or subject to the rules of an Exchange***." NYCC Bylaw 1.1 (J.A. 94) (emphasis added); see also NYCC Rule 401(a) (Resp. App. 6a) ("[t]he [NYCC] * * * shall assume, in the place of each Clearing Member that is a party to ***such Contract***") (emphasis added). Petitioner's position is thus squarely inconsistent with the NYCC and NYFE rules. Indeed, NYFE Rule 306(i)(2), on which petitioner relies, refers to "[e]very ***contract made on the Exchange***" (emphasis added), thus recognizing that a contract exists before clearance takes place. Pet. Br. App. 14a.

Petitioner also asserts (Br. 24-25, 35-36) that the clearing members are the original parties to the contract made on the floor of the Exchange, pointing to the second sentence of Rule 306(i)(2). As we discuss in detail below (see pages 40-42, *infra*), petitioner's construction of the rule ignores the plain language of the other two sentences and is plainly wrong.

These conclusions are confirmed by the real-world operations of the NYFE and NYCC that are not addressed by petitioner. The Trade Input Processing System (TIPS) that existed in 2000 "auto-

3. In its 1982 decision in *Curran*, this Court held that "the private cause of action under the CEA that was previously available to investors [under judicial decisions implying a cause of action under the statute] survived the 1974 amendments" to the statute. 456 U.S. at 388. Eight months after this Court's decision, Congress amended the CEA to—among other things—replace this implied remedy with an express cause of action.

Section 25 created two separate, but related, causes of action. The first, set forth in subsection (a), provides that a private action may be asserted against "any person (***other than*** a contract market, clearing organization of a contract market, licensed board of trade, or registered futures association)" whose violation of the CEA causes "actual damages resulting from one or more" of four specified transactions (emphasis added). 7 U.S.C. § 25(a)(1). For example, a person "who received trading advice * * * for a fee" may sue a person who violated the Act for damages that resulted from the receipt of that advice and were caused by the violation. *Id.* § 25(a)(1)(A). And a futures trader may sue floor brokers and FCMs for actual damages resulting from trading caused by those defendants' violations of the Act. *Id.* § 25(a)(1)(B).

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mate[d] the entire process of trade matching, validation, verification and correction" upon the entry by a broker's clerk of "the trade data that appear on his broker's trading card." CFTC Div. of Trading and Markets, *Rule Enforcement Review of the New York Cotton Exchange* 5 n.12 (Sept. 26, 2001). After the close of trading each day, TIPS provided to NYCC a database showing all transactions where the data supplied by one trading member matched the data supplied by another trading member. NYCC then ran the information so provided through its system to generate reports to the clearing members showing the matched transactions for which they had assumed responsibility for clearing, whereupon those transactions were deemed as having cleared, pursuant to NYCC Rule 402(b). Resp. App. 8a.

The second, set forth in subsection (b), addresses claims against the entities excluded from the previous subsection; paragraph (b)(1) addresses claims against contract markets, clearing organizations of contract markets, and licensed boards of trades. It imposes liability 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" the defendant's enforcement of its rules in violation of the Act or CFTC regulation or order, or by the failure to enforce a rule that the Act or the CFTC required it to enforce. 7 U.S.C. § 25(b(1).

The question presented here requires the Court to determine whether the cause of action created by Section 25(b)(1) may be invoked only by futures traders—the customers and proprietary traders that purchase and sell futures contracts and options and that were the sole focus of the Court's decision in *Curran*—or extends broadly to include clearing members (and, under petitioner's theory, a variety of other actors) that merely facilitate trades entered into by others.

B. The Events Underlying This Case

1. This case arises out of trading on the NYFE by First West Trading, Inc., of Pacific Stock Exchange Technology Index futures contracts and options (P-Tech futures and options) during 2000. Norman Eisler, the principal of First West, directed the trading. Because Eisler was both a floor broker and a member of the NYFE, he executed those trades for First West on the floor of the exchange using the traditional "open outcry" system. Pet. App. 3a-4a; J.A. 17-18 (¶¶ 56-57 & 59); see also pages 5-6, *supra*.

First West had a customer account at petitioner Klein & Co. Futures, Inc. (Klein), which was a clearing member of the clearing organization for NYFE trades, the New York Clearing Corporation (NYCC). J.A. 17 (¶ 55). In its capacity as a clearing member, Klein cleared First West's trades, which had been executed by Eisler. J.A. 17-18 (¶¶ 55, 56, 59, 61).[7]

Pursuant to NYCC rules (see page 8, *supra*), the variation margin obligation of Klein, as the clearing member, was calculated on the basis of changes in "settlement price." See page 8, *supra*. For futures contracts and options on a stock index, such as those involved here, the NYCC rule regarding calculation of settlement prices references the procedure for calculating the settlement price established by the exchange (here, NYFE) on which the contract is traded. NYCC Rule 502(c) (J.A. 170). The relevant NYFE rule specified an arithmetic procedure for calculating the settlement price but in some circumstances allowed the exercise of discretion (if a written record was prepared "setting forth the basis for such settlement"). NYFE Rule 315(d) (Pet. Br. App. 15a).

Klein's NYFE membership obliged Klein to require that First West post a minimum amount of margin with Klein with respect to the futures contracts and options cleared by Klein. That amount too was dependent on the settlement price. NYFE Rule 703; J.A. 21 (¶ 81) (discussing First West's margin obligation).

2. Eisler was the chairman of the NYFE and, in addition, a member of the Exchange's settlement committee responsible for establishing the settlement price of P-Tech futures and options. Pet. App. 3a; J.A. 11 (¶ 10); NYFE Section 2.19 (Resp. App. 11a).

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[7] Klein also was registered with the CFTC as an FCM, which entitled it to solicit and accept orders for futures contracts. See page 5, *supra*. Klein did not act in that capacity with respect to First West's trades, however, because those trades were originated and executed by Eisler, not by Klein—with Eisler designating Klein as the clearing member with respect to his trades. J.A. 17 (¶ 57) (Klein acknowledging in complaint that it did not "exercise control over the trading in [First West's] account").

Petitioner alleges that Eisler abused his position on the settlement committee to misprice the P-Tech settlement prices each day, which had the effect of artificially inflating the value of First West's futures contracts and options and artificially depressing the amount of margin that First West owed to Klein and that Klein, in turn, owed to NYCC. J.A. 18 (¶¶ 60-62); Pet. App. 4a.

On May 11, 2000, the margin call for First West's account was calculated to be approximately $700,000 on the basis of the (erroneous) settlement price established by the settlement committee. Pet. App. 4a; J.A. 21 (¶ 80). Eisler told Klein "that he did not know if he had enough funds to cover the margin," and Klein instructed him to liquidate First West's position; the following day Eisler said "that he did not have the funds to cover the margin." J.A. 21-22 (¶¶ 81-84). Eisler's Exchange membership was suspended and he was removed from the settlement committee. "Once this occurred, the remaining Committee members recalculated the settlement prices and First West's margin deficit ballooned to $4.5 million." Pet. App. 5a; J.A. 24-25 (¶¶ 96, 99-101).

In accordance with NYCC rules, Klein was required to take a charge against its net capital to cover First West's failure to meet Klein's margin call to it. That reduced Klein's capital to less than the minimum amount required by the NYCC's rules. Thereafter, Klein's memberships in the NYFE and NYCC were suspended. J.A. 25-26 (¶¶ 102-107). Klein ceased business operations on May 16. J.A. 28 (¶ 116).[8]

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[8] The CFTC filed an administrative enforcement action against Eisler and First West, which was settled by entry of a consent order requiring payment of a civil penalty of up to $4.9 million. *In re Eisler & First West Trading, Inc.*, No. 01-14 (Jan. 20, 2004), at http://www.cftc.gov/files/enf/04orders/enfeisler-order.pdf. The NYFE consented to the entry of an order imposing a $75,000 civil penalty. The findings—which NYFE neither admitted nor de-

When Klein failed to pay the NYCC margin call, NYCC applied the funds held in Klein's customer margin account to meet the NYCC margin call. J.A. 26-28 (¶¶ 111-113). The New York Board of Trade (NYCC's parent), paid those customers an amount equal to that owed to them by Klein in return for assignment of those customers' claims against Klein. Pet. App. 28a-29a & n.13.

C. Proceedings Below

Klein in July 2000 commenced this action against Eisler, First West, NYFE and NYCC, the New York Cotton Exchange (at the time the parent of NYFE), and the Board of Trade of the City of New York (NYBOT, at the time the parent of the Cotton Exchange, NYFE, and NYCC) (collectively "the Exchanges and the Clearing Organization") and certain officers and directors of the Exchanges and the Clearing Organization. Klein alleged that some exchange officers had been aware of complaints regarding the P-Tech settlement prices and had failed to make a prompt inquiry into the matter or provide notice of the complaints. J.A. 18-19, 20 (¶¶ 64, 72-73). Klein also alleged that it had requested that the NYFE Board take emergency action to halt trading of P-Tech futures and options, but no such action was taken. J.A. 23-24 (¶¶ 90, 95). Finally, it claimed that exchange officers exempted Klein from depositing required funds in the NYCC guaranty fund in order to conceal Eisler's wrongful activities. J.A. 20-21 (¶¶ 75-79).

The complaint asserted claims under Section 25 of the CEA and state law. J.A. 29-53. Claiming that the alleged

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nied—stated that the Exchange's Settlement Committee had failed to comply with the rule for establishing settlement prices for P-Tech futures contracts and options by failing to prepare a written record setting forth the basis for such settlements. *In re New York Futures Exch., Inc.*, No. 01-13 (CFTC July 11, 2001), at http://www.cftc.gov/files/enf/01orders /enfnyfe.pdf.

violations caused it to go out of business, Klein sought compensatory damages of $25 million. J.A. 54-57.[9]

1. ***The District Court's Decision.***

The district court dismissed Klein's Section 25 claim against the exchanges and clearing organization and their officers and directors. Pet. App. 16a-34a.

Referring to Section 25(b)'s limitation of the cause of action to "a person who engaged in any transaction on or subject to the rules" of a contract market, the district court determined that "[c]ourts have interpreted this provision to mean that only ***purchasers or sellers*** on the contract market have a right of action pursuant to [the provision]. Non-traders have no such private right of action under the CEA." Pet. App. 23a-24a (emphasis in original). Observing that Klein "does not allege that it was either a purchaser or a seller of P-Tech Futures and Options" and that Klein "does not claim that it traded for its own account," the district court concluded that Klein's claim did not meet the statutory prerequisite for asserting the cause of action. *Id*. at 24a.

The district court further determined that Klein "suffered damages because of its customer First West's inability to cover its margin call after the settlement price was recalculated. Quite simply, it did not suffer its damages in the course

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[9] NYBOT and NYCC in 2001 commenced an action against Klein, asserting the assigned claims of Klein's former customers. Standing in the shoes of those former customers, NYBOT and NYCC alleged that Klein violated 7 U.S.C. § 6d(2) when it utilized its customers' funds to satisfy its own debts to the NYCC and did not reimburse its customers. Pet. App. 27a-28a. As assignees, NYBOT and NYCC sought to recover the $4.5 million that Klein failed to pay to its customers. See page 15, *supra*.

The district court concluded that the initial complaint in that action failed to state a claim, but granted NYBOT and NYCC leave to amend. Pet. App. 33a. An amended complaint was filed on April 14, 2005.

of its trading activities on a contract market. Klein, therefore, does not have standing to allege a private cause of action" under Section 25(b). Pet. App. 25a.

2. ***The Court of Appeals' Decision.***

The court of appeals unanimously affirmed. Pet. App. 1a-15a. The court observed that "Section [25(b)'s] remedies are expressly available only to a private litigant who 'engaged in any transaction on or subject to the rules' of contract markets or other registered entities" and Klein "was not an owner of P-Tech contracts traded by First West." *Id*. at 11a.

Klein argued that clearing members were "'forced' purchasers or sellers" when they "suffered damages arising from obligations to guarantee their customers' trades" as a result of activities regulated by federal law and the rules of the NYFE and NYCC. Pet. App. 11a. But, the court stated, Klein was neither a trader in nor an owner of the P-Tech contracts: "[i]ndeed, * * * Klein stated in its complaint that it had no financial interest in the First West trading activity and had nothing to do with its trading decisions. Consequently, regardless of whether the First West trading position rose or declined in value, Klein had no interest in any of the resulting profits or investments losses." *Id*. at 12a.

The court explained that "'Klein suffered damages because of its customer First West's inability to cover its margin call. . . .' Thus, Klein's loss was a credit loss, not a trading loss." Pet. App. 12a. "Enforcing the statute that Congress wrote, we conclude Klein lacks standing because it was not 'engaged in any transaction on or subject to the rules' of a contract market and did not suffer any 'actual losses that resulted from such transaction' as required by" Section 25(b). *Id.* at 13a.[10]

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[10] The district court declined to exercise supplemental jurisdiction over Klein's state law claims and therefore dismissed those claims

SUMMARY OF ARGUMENT

Congress's decision to limit the Section 25(b)(1) cause of action to buyers and sellers of futures contracts and options is clear from the language Congress employed, the legal background against which Congress acted, the legislative history, and the absurd results that would flow from the broad interpretation advanced by petitioner and its amici. The lower courts' unanimous view that the remedy may be invoked only by traders should be upheld by this Court.

First, in restricting the cause of action to persons who "engage in any transactions on or subject to the rules of" a contract market, Congress invoked terms—"transactions" and "on or subject to the rules of" a contract market—that it used repeatedly in the CEA when referring specifically to investors' trades of futures contracts and options on the floor of a contract market and, in addition, the trades that the statute allows to occur off the exchange floor. Those terms have the very same meaning in Section 25(b)(1).

Petitioner's argument that the cause of action is available to anyone who participates in any type of activity that is in any way regulated by contract market rules rests on an interpretation of "any transactions" that ignores the settled meaning of the words Congress chose to limit the scope of that phrase. The government takes a similar approach with respect to "engage in," asserting that a person who engages in activity that is in any way ***related to*** a previously-executed transaction is a person who engages in the transaction itself. That interpretation makes no sense: one cannot engage in a transaction that has already taken place; rather, such a person engages in activity that helps implement the transaction.

Second, Congress enacted Section 25(b)(1) just six months after this Court's decision in *Curran* holding "that the private cause of action under the CEA that was previ-

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as well (Pet. App. 26a-27a); the court of appeals affirmed that determination (*id*. at 13a-15a).

ously available to ***investors*** survived the 1974 amendments." 456 U.S. at 388 (emphasis added). Acting against that backdrop, Congress would have made clear any intent to expand the cause of action beyond the bounds indicated in *Curran*. Not only is there no such indication in Section 25(b)(1), but Congress instead employed the very terms that it used repeatedly in the CEA to reference futures trading.

Third, the legislative history of Section 25(b)(1) provides additional support for the conclusion that the cause of action is limited to traders of futures contracts and options. The committee reports repeatedly refer to protecting "investors" and characterize *Curran* as permitting claims by "investors," "speculators," and "customers."

Fourth, accepting petitioner's interpretation of the provision would lead to absurd results. Investors' ability to invoke the provision might be eliminated; at a minimum, investors' recoverable damages would be reduced. And contract markets and clearing organizations would be subjected to multiple—and duplicative—claims by any person whose actions are in any way regulated by contract market rules. The Court in other contexts has rejected interpretations of private causes of action that would lead to such duplication.

Affirming the settled interpretation of Section 25(b)(1) will not produce a gap in enforcement of the rules governing futures and options trading. To the contrary, the CFTC possesses extremely broad enforcement authority, including the ability to levy fines, issue cease and desist orders, and bar individuals and entities from any involvement in the commodities markets. Regulatory oversight and enforcement provide strong punishment and deterrence in this area.

Even if the Court rejects our position and decides to expand the scope of the cause of action to non-traders, it nonetheless should affirm the judgment below on the ground that petitioner's complaint does not allege "actual losses that resulted from" its activities "on or subject to the rules of" a contract market and that "were caused by" the contract market's failure to enforce its rules. If the Court overturns the settled understanding of Section 25(b)(1), lower courts will need guidance on the causation requirement so that they will be able to weed out the unduly remote claims that can be expected under a newly-expanded private cause of action. Here, the court of appeals properly concluded that "'Klein suffered damages because of its customer First West's inability to cover its margin call. . . .' Thus, Klein's loss was a credit loss, not a trading loss." Pet. App. 12a (internal citation omitted). Such damages are not recoverable under Section 25(b)(1).

ARGUMENT

I. SECTION 25(b)(1) CREATES A CAUSE OF ACTION ONLY FOR PERSONS ENGAGED IN TRADING FUTURES OR OPTIONS CONTRACTS.

Section 25(b)(1) creates a strictly limited private cause of action against contract markets. Claims may be asserted only by "a person who engaged in any transaction on or subject to the rules of" a contract market. 7 U.S.C. § 25(b)(1). The language Congress chose makes clear its intent to provide a cause of action only for persons who trade futures. Clearing a trade simply does not fit within the plain language of the provision. The legal context at the time the provision was enacted and the legislative history confirm that conclusion. The court of appeals correctly concluded that the Section 25(b) cause of action may be invoked only by those who trade futures contracts and options; because Klein "was not a trader of P-Tech contracts" and "did not own the P-Tech contracts at issue" it could not assert the cause of action. Pet. App. 12a.[11]

[11] Petitioner erroneously asserts (Br. 3) that the court of appeals' decision rests on a "misread[ing] of the plain text" of Section 25(b) because the court discussed the four categories of transactions for

A. The Plain Language Of Section 25(b)(1) Limits The Class Of Plaintiffs To Buyers And Sellers Of Futures Contracts.

Relying principally on the asserted breadth of the words "any transaction" when separated from the rest of the provision, and—indeed—from the rest of the statute, petitioner and the government assert that anyone who engages in any activity governed in any way by the rules of a contract market may invoke the cause of action created by Section 25(b)(1). That construction, which is inconsistent with every lower court decision interpreting the provision, is wrong. Congress in the CEA employed the phrase "person who engaged in any transaction on or subject to the rules of such contract market" to convey a particular, and limited, meaning—a person who engaged in the buying or selling of futures contracts.[12]

1. *Three aspects of the language Congress chose restrict the scope of the Section 25(b)(1) action.*

Congress's limitation of the private cause of action to buyers and sellers of futures contracts is manifest in (1) its use of the term "transactions on or subject to the rules of" a contract market; (2) its decision to exclude transactions "on or subject to the rules of" a clearing organization; and (3) the

which Section 25(a) provides a cause of action. But subsection (a) was relevant to that court's decision because petitioner had appealed the dismissal of its claims against Eisler and the Exchange and Clearing Organization officers and directors; those claims are limited to the four transactions specified by subsection (a). See 7 U.S.C. § 25(b)(3). And—as we have discussed—the court of appeals specifically explained the reasons why petitioner was not a "person who engaged in any transaction on or subject to the rules of such contract market" entitled to invoke Section 25(b)(1).

[12] The CFTC's views on the scope of the private cause of action are not entitled to deference. *Adams Fruit Co.* v. *Barrett*, 494 U.S. 638, 649 (1990).

statute's restriction of recoverable damages to "actual losses that resulted from such transaction."

a. "Transactions on or subject to the rules of" a contract market. Congress in the CEA normally used the word "transaction" when referring to a trader's purchase or sale of futures contracts or options. Thus, the provision granting exclusive jurisdiction to the CFTC refers to

> agreements (including any transaction which is of the character of or is commonly known to the trade as an "option", "privilege", "indemnity", "bid", "offer", "put", "call", "advance guaranty", or "decline guaranty"), and transactions involving contracts of sale of a commodity for future delivery, traded or executed on a contract market.

7 U.S.C. § 2(i); see also *id*. §§ 6c (identifying "prohibited transactions," all of which are purchases or sales), 13(c) (barring CFTC Commissioners and employees from engaging in specified "transactions," all of which are purchases or sales).

Similarly, in its legislative findings, Congress repeatedly used the word "transaction" to refer to trades in futures or options:

> Transactions in commodities involving the sale thereof for future delivery as commonly conducted on boards of trade and known as "futures" are affected with a national public interest. Such futures transactions are carried on in large volume by the public generally and by persons engaged in the business of buying and selling commodities and the products and byproducts thereof in interstate commerce. The prices involved in such transactions are generally quoted and disseminated throughout the United States * * *.

7 U.S.C. § 5 (emphasis added).

The CFTC's rules follow the same approach. "Transaction" is repeatedly used by the CFTC as a synonym for "trade." See, *e.g.*, 17 C.F.R. § 1.35(b)(2) (requiring each FCM to keep a record of "transactions," and then listing a number of "transactions" that are all trades); *id*. § 1.35(e) (requiring contract markets to keep records showing "for each futures or option trade: the transaction date, * * * whether the transaction involved a put or a call," and showing "any transaction which is made non-competitively in accordance with written rules of the contract market"); *id.* § 155.2(i) (requiring contract markets to have rules which among other things require "that every execution of a transaction on the floor * * * be confirmed promptly").[13]

Moreover, the word "transaction" does not stand alone in Section 25(b)(1). Rather, the provision provides a cause of action only with respect to transactions "on or subject to the rules of" a contract market.

Throughout the CEA, Congress employed the phrase "on or subject to the rules of [a] contract market" to refer specifically to investors' trades of futures contracts and options executed on the trading floor of a contract market together with the trades that the statute permits "ex-pit" (off the exchange floor)—such as "exchanges for physicals," transfer trades, and office trades—which may be executed "off exchange" only if they are subject to the rules of a contract market.[14]

[13] Like the statute and the Commission's rules, the NYFE rules repeatedly equate a "transaction" with a "trade." See, *e.g.*, NYFE Rules 14, 302, 303, 313, 601. Resp. App. 11a-21a. For example, NYFE Rule 303(e) refers to "[t]ransactions made in any contract at a price above that at which such contract is offered or below that which is bid for such contract." Resp. App. 12a.

[14] 7 U.S.C. § 6c permits "the exchange of futures in connection with cash commodity transactions or of futures for cash commodities, or of transfer trades, or office trades if made in accordance with board of trade rules applying to such transactions and such rules shall have been approved by the Commission." Exchanges of futures for cash commodities, otherwise known as exchange-

Congress's use of that very same phrase to modify "transactions" in Section 25(b) makes clear that it intended to provide a cause of action only to the buyers and sellers in these particular transactions. See *Gustafson* v. *Alloyd Co.*, 513 U.S. 561, 575 (1995) (in statutory construction, "a word is known by the company it keeps").

In each of the many instances when Congress used the phrase "on or subject to the rules" it did so to modify a word or phrase that is synonymous with a trade. For example, Section 6i, which governs reports of transactions in excess of trading limits, reaches "any contract for the purchase or sale of any commodity for future delivery on or subject to the rules of any exchange." 7 U.S.C. § 6i; see also *id*. §§ 1a(5)(A)(i)(I) (defining "commodity trading advisor" with reference to advice regarding "trading in" contracts "made or to be made on or subject to the rules of a contract market"); 1a(8) (defining "floor broker" as person who "shall purchase or sell for any other person any commodity for future delivery on or subject to the rules of any contract market"); 1a(9), (12) & (14) (similar use of term in definition of floor trader, futures commission merchant, and introducing broker); 6a(a) (defining CFTC's obligation to issue rule prohibiting "exces-

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for-physical transactions or "EFPs," are used by parties to simultaneously close out their opposite hedges in futures. A buyer of a cash commodity (*e.g.*, corn, sugar, cocoa, etc.) transfers to the seller a corresponding amount of long futures contracts for that commodity, or receives from the seller a corresponding amount of the short futures for that commodity, at a price difference that is mutually agreed upon. CFTC Glossary, at http://www.cftc.gov/educationcenter/glossary/index.htm. Such exchanges occur "ex-pit" or off the exchange floor.

A second type of "ex-pit" trade is the transfer trade, which involves a book entry by an FCM for the purpose of: (1) transferring existing trades from one customer account to another within the same firm where no change in ownership is involved; or (2) transferring existing trades from the books of one FCM to the books of another FCM where no change in ownership is involved. See *ibid*.

sive speculation" by reference to contracts made "on or subject to the rules of any contract market"); 7a(a)(7) & (12)(A) (contract markets must require that "receipts issued under the United States Warehouse Act shall be accepted in satisfaction of any futures contract, made on or subject to the rules of such contract market" and submit to the CFTC for approval rules "that relate to terms and conditions in contracts of sale to be executed on or subject to the rules of such contract market"); 9 (authorizing the CFTC to issue an order prohibiting person found to have engaged in manipulating prices "from trading on or subject to the rules of any contract market"); 12b (barring person subject to a Section 9 order from causing to be made "any contract for future delivery of any commodity, on or subject to the rules of any contract market").

This lengthy—and not even exhaustive—list demonstrates that when Congress used the phrase "on or subject to the rules of" a contract market, as it did in Section 25(b), it meant to refer to trading. See *FTC* v. *Ken Roberts Co.*, 276 F.3d 583, 590 (D.C. Cir. 2001) (Congress's use of "transactions on contract markets" is "best understood to refer to the actual trading of futures contracts").

b. "Rules of such contract market or licensed board of trade." The version of Section 25(b)(1) that was in effect at the time of the events in this case expressly imposed liability on a "***contract market, clearing organization of a contract market, or licensed board of trade***" that failed to enforce its rules or enforced them in violation of the statute or Commission regulations, but provided a cause of action only to "a person who engaged in any transaction on or subject to the ***rules of such contract market or licensed board of trade***" (emphasis added). 7 U.S.C. § 25(b)(1). The statute conspicuously omits transactions subject to the rules of the "clearing organization of a contract market."

That omission provides important additional evidence that Congress intended to permit only the buyers and sellers of contracts to assert the private cause of action. Those trades may be accomplished only on or subject to the rules of a contract market or board of trade. Congress did not include transactions "on or subject to the rules of such clearing organizations" because futures trades do not occur "on" clearing organizations, and because traders do not themselves participate in transactions subject to clearing organization rules. That language therefore was not needed to define the scope of the cause of action that Congress sought to create.[15]

Petitioner and the government argue at length that, because the clearing activity in this case supposedly was subject to the rules of the contract market as well as the rules of the clearing organization, petitioner's "transactions" entitle it to invoke the cause of action. That argument misses the point. The question here is what Congress intended by the words it used. Its omission of any reference to "rules of a clearing organization" notwithstanding its reference to "clearing organization" just a few lines earlier in the very same provision, shows that it was not seeking to provide a cause of action for a broad range of plaintiffs, but only intended to cover investors.[16]

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[15] Petitioner apparently realizes the significance of this omission—it repeatedly (and incorrectly) uses the phrase "on or subject to the rules of an exchange or its clearinghouse" (*e.g.*, Br. 3, 21, 22, 24, 25, 27), which is not what the statute said before the 2000 amendments. See also FIA Br. 6-7 (utilizing "on or subject to the rules of a registered entity"—the language inserted into the CEA for the first time by the 2000 amendments adopted after the commencement of this case).

[16] Petitioner and the government also contend that when Congress wrote "rules of a contract market" it meant to encompass the rules of a clearing organization because 17 C.F.R. § 1.41, promulgated in 1976, requires clearing organization rules to be submitted to the CFTC for review by defining "contract market" to include "a clearing organization that clears trades for the contract market." Congress in 1982 should be deemed to have been aware of this administrative interpretation, the argument goes, and therefore meant to include clearing organization rules when it wrote only

c. "Actual losses that resulted from such transaction." The statute restricts the damages that may be recovered under Section 25(b)(1) to the plaintiff's "actual losses that resulted from" the "transaction on or subject to the rules of such contract market or licensed board of trade." Rather than employing the more general phrase "actual damages," Congress inserted the more specific term "actual losses."

To be sure, Congress did use the term "actual damages" in (a)(1) and in (b)(1). However, in (b)(1), Congress explicitly made clear that "actual losses" was a distinct subset of "actual damages." Section 25(b)(1) declares that "any contract market, clearing organization of a contract market, or licensed board of trade * * * shall be liable for actual damages * * * ***to the extent of*** * * * ***actual losses***" that resulted from the transaction (emphasis added). Congress's use of that narrower phrase indicates that it contemplated recovery of only one specific type of "damages" under this provision—trading losses—as compared with the different types of damages that could be recovered under subsection (a). Especially when coupled with "such transaction," Congress's use of that term therefore provides still more evidence that Congress's intent was to create a cause of action available only to buyers and sellers of futures contracts, and not to non-traders, such as petitioner, that merely cleared such transactions.

"rules of such contract market." That contention is wrong for three reasons. *First*, Section 1.41(a) expressly states that its definitions apply only "[f]or purposes of this section," and when the CFTC promulgated the regulation it emphasized the limited applicability of the "contract market" definition 41 Fed. Reg. 40091, 40093 (1976). *Second*, the CFTC in June 1982—when Congress was considering the bill that added Section 25(b)—issued an administrative interpretation confirming this limitation on Section 1.41. See CFTC Interpretive Letter 82-5 [1982-1984 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,964 (June 15, 1982). *Third*, under this theory, Congress never would have had to use the term "clearing organization" or its synonyms anywhere in the CEA; yet those terms appear in several provisions, including Section 25(b).

* * * * *

In view of the statute's clear language, it is not surprising that every court to consider the scope of Section 25(b)(1) has concluded that it is available only to traders of futures contracts. See *American Agric. Movement, Inc.* v. *Board of Trade of Chicago*, 977 F.2d 1147, 1153 (7th Cir. 1992) ("By its terms, then, § 22(b) creates the exclusive remedies available to those injured by violations of the CEA, and makes those remedies available only to persons injured in the course of trading on a contract market. It therefore forecloses all other remedies, including any on behalf of non-traders."); *DGM Invs., Inc.* v. *New York Fut. Exch., Inc*, No. 01 Civ. 11602, 2002 WL 31356362, at *2 to *5 (S.D.N.Y. Oct. 17, 2002); *Vitanza* v. *Board of Trade of N.Y., Inc.*, No. 00 CV 7393, 2002 WL 424699, at *4 to * 8 (S.D.N.Y. Mar. 18, 2002); *de Atucha* v. *Commodity Exch., Inc.*, 608 F. Supp. 510, 521-522 (S.D.N.Y. 1985) (Section 25(b) "plainly limits the private remedy to market traders"); see also *Unity House, Inc.* v. *First Commercial Fin. Group*, No. 96C-1716, 1997 WL 701345, at *7 (N.D. Ill. Nov. 5, 1997), *aff'd*, 175 F.3d 1022 (7th Cir. 1999).

No court has adopted the broad rule urged by petitioners.

2. ***Petitioner's interpretation of Section 25(b)(1) cannot be reconciled with the language Congress chose.***

Petitioner advances three arguments in support of its contention that the private cause of action extends broadly to any person who engages in any activity that is in any way governed by the rules of a contract market or clearing organization. None of those arguments provides any basis for rejecting the interpretation of the statute based on its plain meaning.

First, petitioner relies principally (Br. 27-28) on the asserted breadth of the phrase "any transaction" standing alone, but its argument totally ignores the manner in which Congress used the term "transaction" in the statute and—even more importantly—the limiting language with which Congress surrounded that term in Section 25(b)(1). In particular, the words "any transaction" are followed by "on or subject to the rules of" a contract market, a phrase that has a specific meaning in the CEA. See pages 22-25, *supra*. This Court has repeatedly rejected statutory construction arguments that rest on wrenching critical language out of its statutory context. *E.g.*, *Jones* v. *United States*, 527 U.S. 373, 389 (1999). It should reject petitioner's argument for the same reason.

Second, petitioner claims (Br. 28) that Congress's decision not to use the phrase "purchased or sold" in defining the class of persons entitled to sue under Section 25(b)(1)—when it used that phrase in Section 25(a)(1)(D)—shows that Congress intended to make the cause of action available to a broader class of plaintiffs. But the latter provision was referring to a specific category of transactions: purchases or sales of contracts referred to in subparagraph (B) "if the violation constitutes a manipulation of the price of any such contract or the price of the commodity underlying such contract." 7 U.S.C. § 25(a)(1)(D). It would have been awkward and unnatural for Congress to use the word "transaction" there when it was trying to accomplish three things—refer back to subparagraph (B), which uses the term "contract"; identify the person entitled to sue; and limit the claims to those involving manipulation of the price of the same contract or the same underlying commodity as the contract or commodity that the plaintiff traded.

Using "transaction" would have made the sentence much more convoluted. For example: "who engaged in a transaction on or subject to the rules of a contract market with respect to a contract referred to in subparagraph (B) hereof if the violation * * *." Not surprisingly, Congress used a phrase imposing the same limitation as "transaction on or subject to the rules of a contract market"—"purchased or sold a contract referred to in subparagraph (B)"—that permitted a much simpler sentence structure in view of the context. 7 U.S.C. § 25(a)(1)(D). In Section 25(b)(1), by contrast, where there was no definition of contract in an earlier subparagraph for Congress to refer to, and there was no need to define a specific type of violation, Congress could express its intent through the more generic words that it employed elsewhere in the statute.

Third, petitioner claims (Br. 32-33) that Section 6(a) of title 7 supports its broad reading of Section 25(b)(1). But Section 6(a) actually supports our construction of the statute.

Section 6(a) prohibits offering, entering into, executing, confirming the execution 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." Petitioner contends (Br. 32-33) that this prohibition encompasses clearing, that the authorization of prohibited activities in Section 6(a)(1) when "such transaction is conducted on or subject to the rules of a" contract market must encompass clearing activities in order to override the prohibition against clearing, and that the similar "transaction * * * conducted on or subject to the rules of" language in Section 25(b)(1) accordingly encompasses clearing activities as well. The argument fails because petitioner is wrong in asserting that the prohibitory language encompasses clearing activities.

All of the activities prohibited by Section 6(a)—offering, entering into, executing, confirming execution, soliciting, accepting, and otherwise dealing in futures contract transactions—occur as part of the futures trade itself. Offer, solicitation and acceptance are elements of every trade, execution is specifically defined as trading in the statutory definitions of floor broker and floor trader (7 U.S.C. §§ 1a(8) & 1a(9)), and "otherwise dealing in" these transactions similarly references trading activity. By contrast, clearing takes place only after the trade is completed. See pages 6-10, *supra*. See also pages 40-41, *infra*.

Moreover, the term "clearing" is conspicuously absent from Section 6(a)'s list of prohibited activities even though the clearing function is referenced elsewhere in the statute. See, *e.g.*, 7 U.S.C. § 6d(2). That omission is fatal to petitioner's argument.

Petitioner places considerable emphasis on the presence of "in connection with" in Section 6(a)'s prohibitory language. But that phrase does not bring clearing within the scope of Section 6(a)'s prohibition.

The purpose of the prohibitory language at the beginning of Section 6(a) is to reach the entire class of transactions that Congress wished to be conducted "on or subject to the rules of" a contract market. That included not simply futures contracts themselves, but also options on futures contracts and other instruments relating to futures contracts. See 7 U.S.C. § 2(i) (referring to "any transaction which is of the character of, or is commonly known to the trade as, an 'option', 'privilege', 'indemnity', 'bid', 'offer', 'put', 'call', 'advance guaranty', or 'decline guaranty'" in defining the CFTC's jurisdiction). The obvious purpose of the "in connection with" language was to ensure that the prohibition would reach options as well as other agreements that were the subject of trading on futures markets—simply referring to "any transaction in * * * a contract for the purchase or sale of a commodity for future delivery" would not fulfill that goal.[17]

If petitioner's argument were correct, moreover, Congress would not have had to enact specific provisions barring unregistered persons from "engag[ing] as futures commission merchant or introducing broker in soliciting orders or accepting orders for the purchase or sale of any commodity for future delivery" (7 U.S.C. § 6d) and barring unregistered per-

[17] Congress could not utilize Section 2's list of transactions in Section 6(a) because combining those nine terms with Section 6(a)'s list of prohibited actions would have produced an unwieldy provision. And it could not have referred to "transactions on or subject to the rules of" a contract market, because that would have made the prohibition identical to the authorization in Section 6(a)(1), and provided no guidance with respect to the scope of the prohibition.

sons from "act[ing] as floor trader in executing purchases and sales, or as floor broker in executing any orders for the purchase or sale of any commodity for future delivery" (*id*. § 6e). All of those activities already would be impermissible under petitioner's broad view of the Section 6(a) prohibition. Congress's decision to enact these provisions demonstrates conclusively that the Section 6(a) prohibition does not have the broad reach ascribed to it by petitioner.

Because Section 6(a)'s prohibition reaches only futures and options trading, the phrase "transaction * * * conducted on or subject to the rules of" a contract market in Section 6(a)(1) also refers only to traders' purchases and sales of future contracts and options. Far from supporting petitioner's approach, therefore, Section 6(a)(1) confirms that the similar language of Section 25(b)(1) also is limited to trading.

Petitioner also asserts (Br. 33-34) that Congress's separate use in Section 6(a)(1)-(3) of the words "transaction" and "contract" demonstrates that "any transaction" in Section 25(b) encompasses more than trading of futures contracts. But petitioner's argument ignores that fact that Congress used these two words to describe different concepts. Section 6(a) uses "transaction" to refer to trading; the phrase "contract for the purchase or sale of a commodity for future delivery" refers to the contracts that are the subject of the trades. Thus, the trading of futures contracts must be "conducted on or subject to the rules of a contract market"; the contracts themselves must be "executed or consummated by or through a member of such contract market." 7 U.S.C. § 6(a)(1) & (2). Petitioner is simply wrong in arguing that Congress's use of the two phrases supports its interpretation of Section 25(b)(1).

The government does not endorse any of petitioner's statutory construction arguments. It instead proposes (Br. 20) a "plain language" argument different than those presented by petitioner. The government asserts that a buyer or seller of futures contracts could not consummate its trade without the assistance provided by petitioner, and that petitioner therefore is "an entity that 'engaged in' the relevant transactions." The government relies heavily on the dictionary definition of "engage in," claiming that it reaches broadly to encompass entities such as clearing members.

The flaw in the government's argument is that it analyzes the meaning of "engaged in" without considering the words that surround it. As we have discussed, the plain language of Section 25(b)(1) refers to traders' purchases and sales of futures contracts and options, not the subsequent clearing of those transactions. The statute and NYCC rules make clear that the trade itself "on or subject to the rules of" the contract market is distinct from the clearing of that trade. The trade, according to the statutory definitions of floor trader and floor broker, occurs on the floor of the exchange. And the NYCC rules expressly recognize that the contract is made prior to initiation of the clearing process. See pages 6-10, *supra*. See also pages 40-41, *infra*.

A clearing member may perform an activity that is ***related*** to the trade, but it is not ***the transaction*** to which Section 25(b)(1) refers. The trade occurs ***before*** it is cleared. It is not possible to engage in a transaction ***after*** the transaction has occurred. Including as part of a "transaction" any post-contract activity that aided in consummating a transaction would reach broadly, for example to the banks that transfer required payments or to the technology companies that provide necessary hardware and software.[18]

Because petitioner did not engage in the trades themselves, the only relevant question under Section 25(b)(1) is whether the clearing of the trades—the separate activity in which petitioner did engage—was "any transaction on or subject to the rules" of a contract market. What the govern-

[18] The government rests its contrary view in part (Br. 20-21) on its view of the role that an FCM plays forming the agreement on the floor of the exchange. But Klein did not perform that role here; it acted solely as First West's clearing member. See pages 12-14, *supra*.

ment obscures by focusing on petitioner's "essential role" (Br. 20) is that the only relevant question for statutory construction purposes is whether petitioner's clearing activity was "any transaction on or subject to the rules" of a contract market. The government's argument thus depends on the same flawed assumption as petitioner's position: that the term "any transaction on or subject to the rules of such contract market" refers to any activity that is subject to contract market or clearing organization rules.

When Congress sought to reach beyond trading of futures contracts and include ancillary activities, it did so explicitly by employing language different than "transactions on or subject to the rules of" a contract market. Thus, in prohibiting individuals from falsely representing themselves as contract market members, Congress barred such false representations "in connection with the handling" of "any order or contract for the purchase or sale of any commodity in interstate commerce or for future delivery." 7 U.S.C. § 6h.

Similarly, in Section 25(a)(1) Congress created a private action for damages resulting from violations of the Act in favor of a person "who made ***through*** [the defendant] any contract of sale of any commodity for future delivery" and "who purchased from or sold to [the defendant] or ***placed through [the defendant]*** an order for the purchase or sale of" specified types of futures contracts (emphasis added). Paragraph 3 of Section 25(a) makes clear that the reason for this language is to reach "violation[s] in the execution of an order on the floor of a contract market."

Congress thus knew how to write more broadly when it wanted to target the activities of brokers and FCMs in facilitating trades of futures contracts. But it did not include similarly broad language bringing clearing or other non-trading activities within the scope of Section 25(b)(1).[19]

[19] The government (Br. 21) places considerable emphasis on Klein's agreement with Eisler guaranteeing that Klein act as a clearing memember for Eisler's trades (under NYFE Rule 121

In sum, the arguments advanced by petitioner and its amici simply do not provide any basis for ignoring the plain meaning of the words Congress used in Section 25(b)(1). Moreover, as we next discuss, the legal background and legislative history confirm that Congress intended to make the private action available only to investors.

B. The Legal Background Against Which Congress Legislated Confirms That The Private Action Is Available Only To Investors.

Congress enacted Section 25(b)(1) shortly after this Court held in *Curran* that the 1974 amendments to the CEA did not eliminate the private cause of action that courts had implied under the Act before adoption of those amendments. The *Curran* Court summarized its conclusion by stating, "[w]e hold that the private cause of action under the CEA that was previously available to ***investors*** survived the 1974 amendments." *Curran*, 456 U.S. at 388 (emphasis added).

The Court's opinion consistently focused on traders and investors as the parties eligible to invoke the cause of action. See *id.* at 389 ("***purchasers or sellers*** of futures contracts—whether they be pure speculators or hedgers—[were] necessarily * * * protected by [the antifraud provision of the CEA]") (emphasis added); *ibid.* ("We are satisfied that ***purchasers and sellers*** of futures contracts have standing to assert both [fraud and manipulation] claims") (emphasis added); *id.* at 390 ("The [1974] legislative history quite clearly indicates that Congress intended to protect all ***futures traders*** from price manipulation and other fraudulent conduct violative of the statute * * * [as] legislation regulating future

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(Pet. Br. App. 9a-10a)). But Klein's obligation to pay margin to NYCC arose from its role as clearing member for First West, not because of its separate promise to act as clearing member of last resort for Eisler's trades. See pages 7-8, *supra*. The guarantee simply is not relevant in this case.

trading was for the 'especial benefit' of futures traders") (emphasis added).

Acting against that backdrop, Congress would have made clear any intent to expand the cause of action beyond the bounds indicated in *Curran*. Not only is there no such indication in Section 25(b)(1), but Congress plainly chose statutory language consistent with the *Curran* Court's focus on a cause of action for investors—employing the phrase ("on or subject to the rules of" a contract market) used repeatedly in the CEA to reference futures trading.

Petitioner attempts to blunt the impact of *Curran* by arguing that the cause of action recognized there extended to claims by clearing members against clearing organizations and contract markets. Petitioner is wrong about the scope of *Curran* and—even more importantly—it is wrong about the way Congress would have perceived the Court's decision.

Petitioner first asserts (Br. 41-42) that the fact that one of the plaintiffs in *Curran* was an FCM shows that Congress intended to extend the Section 25(b)(1) private action to FCMs claiming injury with respect to clearing activities. But the plaintiff to which petitioner refers—Incomco—was engaged in trading for its own account, not on behalf of its customers.[20] In that situation, of course, the FCM ***is*** the investor, and therefore may invoke the cause of action on that basis. Those facts therefore say nothing about whether a clearing member

[20] The court of appeals' description of Incomco's trading activities makes this plain: "***All the plaintiffs*** invested heavily on the long side of the May contract. In addition, Incomco developed a position in the cash market. It had accepted 1,500,000 pounds of Maine potatoes delivered to it pursuant to the March futures contract, and planned to sell these potatoes to those short the May contract who needed supplies to satisfy their delivery obligations. Anticipating a cash market shortage, Incomco expected to sell its potatoes at a handsome premium." *Leist* v. *Simplot*, 638 F.2d 283, 291 (2d Cir. 1980) (emphasis added), *aff'd sub nom.*, *Merrill Lynch, Pierce, Fenner & Smith* v. *Curran*, 456 U.S. 353 (1982).

is entitled to sue on the basis of its actions in clearing the trades of one of its customers.

Petitioner also points (Br. 41) to *Seligson* v. *New York Produce Exch.*, 378 F. Supp. 1076 (S.D.N.Y. 1974), a district court decision recognizing an implied private right of action under the CEA for brokers against exchanges. Based on the fact that this one decision was included in a list of cases cited in a footnote in *Curran* (456 U.S. at 392 n.94), petitioner reasons that Congress must have intended to permit clearing members to sue when it codified that private right of action in the wake of *Curran*.

This single decision, which addresses the extension of the cause of action to FCMs in a single paragraph (378 F. Supp. at 1084), is too slender a reed on which to premise an expansive interpretation of the express cause of action created by Congress. Cf. *F. Hoffman-LaRoche Ltd.* v. *Empagran S.A.*, 542 U.S. 155, 172-173 (2004) (rejecting argument that statute should be construed by reference to single decision that pre-dated congressional action: "[w]e do not see how Congress could have taken this case as significant support for the proposition that the Sherman Act applies in present circumstances").

The Court included *Seligson* in a footnote that lists ten decisions that "drew no distinction between an action ***against*** a broker and an action against an exchange." 456 U.S. at 391-392 & n.94 (emphasis added). The Court's citation of *Seligson* for that proposition provides no indication that the Court meant to endorse the extension of the implied cause of action to claims by non-traders such as brokers or clearing members.

Moreover, there is no basis whatever to believe that Congress would have understood *Curran* to encompass claims by plaintiffs other than investors. Congress would have focused on the language used by the Court in the text of its opinion—language that repeatedly focuses on investors.

The way Congress wrote Section 25(b)(1) evidences no intent to create a cause of action broader than the one described in *Curran*. Rather, Congress's use of a phrase—"any transaction on or subject to the rules of" a contract market—that it consistently employed to refer to purchases and sales of futures contracts and options, viewed in light of the legal context that Congress confronted, can only be construed as embodying the cause of action for "investors" discussed by the Court in *Curran*.

C. The Legislative History Of Section 25(b)(1) Demonstrates That Congress Intended To Create A Cause Of Action For Investors.

The legislative history of Section 25(b) provides still more support for the conclusion that the cause of action is limited to traders of futures contracts and options. When Rep. Dan Glickman, Chairman of the House Subcommittee on Wheat, Soybean and Feed Grains, proposed the amendments that became Section 25(b), he observed that "[t]he amendments would * * * allow commodity ***investors*** who suffer actual damages the right to sue both brokers and exchanges" for CEA violations. H.R. Rep. No. 97-565, part I, at 239 (1982) (emphasis added).

Congress's single-minded focus on protecting investors—the buyers and sellers of futures contracts and options—is evident throughout Section 25(b)'s legislative history. See, *e.g.*, H.R. Rep. No. 97-565, part I, at 240 ("***investors*** in futures markets will face potentially greater and greater uncertainty and risk") (emphasis added); *id.* at 57 (the "cause of action in these cases would be restricted to cases where the plaintiff had engaged in a regulated commodity transaction and could show that there was bad faith in failing to take the necessary action").

That focus is not surprising because Congress viewed *Curran* as recognizing a cause of action for investors in futures contracts. The Conference Committee Report described *Curran* as holding

> that implied private rights of action exist under the Commodity Exchange Act in cases brought by an investor against his futures commission merchant for violation of an antifraud provision of the Commodity Exchange Act, and by speculators in futures contracts against a contract market and its officials and against futures commission merchants or other market participants claiming damages resulting from unlawful price manipulation that allegedly could have been prevented by the exchange's enforcement of its own rules.

H.R. Conf. Rep. No. 97-967, at 53 (1982); see also S. REP. NO. 97-495, at 51 (1982) (describing *Curran* as finding "that ***purchasers and sellers*** of futures contracts have standing" and summarizing *Curran* as a case that "will allow actions * * * by commodity ***customers***" to be brought in federal district courts, "rather than proceeding in the Reparations Section of the CFTC") (emphasis added). The then-Chairman of the CFTC similarly described the decision in *Curran* as one where the Court found that "***purchasers and sellers***" of futures contracts have standing.[21]

There is no hint in the legislative history of any intent to extend the private action beyond the class of plaintiffs identified by the Court in *Curran*. The government, for example, points (Br. 28) to a reference to a "'regulated commodity transaction,'" but that phrase is a perfect description of futures and options trades. The legislative history too, therefore, weighs against petitioner's construction of Section 25(b).

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[21] *SEC/CFTC Jurisdictional Issues and Oversight, Part 1: Hearings Before the H. Subcomm. On Telecommc'ns, Consumer Prot., and Fin. and H. Subcomm. on Oversight and Investigations*, 97th Cong. 208 (1982) (emphasis added).

D. The NYCC And NYFE Rules Confirm That Clearing Members Do Not Engage In Transactions "On Or Subject To The Rules Of" A Contract Market.

Klein acknowledged in its complaint that it did not purchase or sell any P-Tech futures or options for its own account. It alleged that the trades executed for First West's account were "unsolicited trades," made "without input, counsel, advice or any type of recommendation whatsoever" from petitioner, and that Klein "had no equity or financial interest in the First West account nor did Klein exercise control over the trading in said account." J.A. 17 (¶¶ 56-57). Because petitioner was not engaged in buying or selling futures—but rather was acting solely as a clearing member in clearing First West's trades—petitioner is not entitled to invoke the private action created in Section 25(b).

The NYCC Bylaws and Rules themselves establish that the clearing process occurs *following* the transaction "on or subject to the rules of" the contract market. "Clearing member" is defined as a person who may clear "Contracts effected on or subject to the rules of an Exchange" (NYCC Bylaw 1.1 (J.A. 94), demonstrating that the contract has already been made before the clearing process begins. That description, of course, accords with the CEA's description of floor brokers and floor traders as the persons who effect purchase and sales on or subject to the rules of a contract market. See page 24, *supra*; see also U.S. Br. 5-6 (acknowledging that clearing process occurs after the buyer-seller contract is formed); S. Rep. No. 97-384, at 187 (1982) (stating that "[t]he actual trading of futures contracts takes place in the noisy, boisterous setting of an auction-type market"); *id*. at 188 (clearing process occurs "[a]fter a trade has been executed").

Perhaps recognizing that its status as a clearing member places it outside the congressionally-protected class, petitioner in this Court for the first time invokes NYFE Rule 306(i)(2), asserting (Br. 24) that the rule's statement that a contract "shall be made on behalf of a clearing member who shall be the buyer or seller of said contract" renders petitioner the buyer or seller of the P-Tech futures contracts and options.

As a threshold matter, an exchange rule cannot change the scope of a federal statute. Congress's determination that the cause of action extends only to investors cannot be overridden by a rule declaring that a clearing member that clears a contract thereby becomes the buyer or seller for purposes of Section 25(b). Clearing members perform an important role (see pages 6-9, *supra*), but clearing a trade does not place the clearing member in the same position as the buyer or seller. Indeed, NYCC Rule 401 (Resp. App. 6a-7a) makes clear that the clearing member's assumption of the buyer-seller contract is extremely brief: once the contract is cleared, the clearing members' "liabilities and obligations" under that contract are "terminate[d]." See pages 7-8, *supra*. The clearing member's obligations then flow from the NYCC rules, not from the contract formed on the floor of the exchange.[22]

Moreover, the text of Rule 306(i)(2) taken as a whole does not have the meaning ascribed to it by petitioner. The first sentence of the provision states that "[e]very contract made on the Exchange ***shall be assumed by a [clearing]***

[22] As respondents demonstrated in their opposition to the petition, the decisions relied upon by petitioner to suggest that clearing members, like petitioner, were principals to such transactions are not to the contrary. See Br. in Opp. 9-10. First, as *Leist* makes clear, FCMs are treated "as if" they were principals, recognizing that they were *not* the actual principals. 638 F.2d at 286-287. Second, with respect to *Bernstein* v. *Lind-Waldock & Co.*, 738 F.2d 179 (7th Cir. 1984), it is important to note that in addition to relying on *Leist* for a "more detailed description of commodities trading," (*id.* at 181) it also concerned trading in Chicago. As noted above (see note 3, *supra*), there are significant differences between trading rules in Chicago and in New York. Thus, *Bernstein's* description of the Chicago market mechanics is inapposite here.

member" (emphasis added). The sentence following the one on which petitioner relies says that "[t]he clearing member ***shall assume said contract in writing within one hour*** after receipt of a report from the trading member identifying the terms thereof" (emphasis added). Pet. Br. App. 14a. These two sentences thus recognize–consistent with the NYCC By-laws—that the contract is made prior to the clearing process.[23]

Petitioner's view that the second sentence of the rule (that a contract "shall be made on behalf of a clearing member who shall be the buyer or seller of said contract") establishes that the clearing member is a party to the trade, is squarely inconsistent with the other two sentences of the provision as well as with the NYCC Bylaws. The sentence on which petitioner relies therefore is most logically read to refer to the clearing members' agency relationships with their customers—that one clearing member must act for the buyer and another for the seller.

Because a contract must be made before it can be assumed by another, the only way to give meaning to all three sentences is to conclude that a contract made on the Exchange between the buyer and seller is then assumed by the clearing members, who (by virtue of the second sentence) must be identified by the floor brokers within some period of time after the transaction is executed. The rule does not and cannot confer the status that Congress established as the precondition for invoking the Section 25(b)(1) cause of action.

E. Petitioner's Construction Of Section 25(b)(1) Would Produce Absurd Results.

The meaning of Section 25(b)(1) propounded by petitioner should be rejected for the additional reason that it

[23] The TIPS automated process confirms this conclusion, because the trade data is input into the system in order to initiate the clearing process, making clear that the trade is complete before the clearing process begins. See note 6, *supra*.

would produce an interpretation of the statute plainly inconsistent with Congress's aim.

First, if the Court were to accept petitioner's contention that "on or subject to the rules of" a contract market reaches any interaction regulated by contract market rules, the other provisions of the CEA that use that phrase would apply much more broadly. Section 6i's requirements governing transactions in excess of trading limits would apply to clearing and other activities; the statutory definitions of "floor broker" and "floor trader" would encompass a wider variety of transactions than floor trades, and the CFTC would be obliged to expand the reach of its rules prohibiting "excessive speculation." See pages 24-25, *supra*.

Second, petitioner's approach would substantially vitiate the cause of action available to investors—the principal focus of Congress's concern. Thus, petitioner argues (Br. 31 n.14) that customers "are prohibited by Congress, the CFTC, and respondents' own rules from engaging directly in transactions *on* the exchange." It asserts that the "transaction" entitling investors to invoke Section 25(b)(1) is the transaction between the customer and the FCM, which, according to petitioner, is "subject to the rules" of a contract market.

But Section 25(b)(1) limits recoverable damages to "actual losses that resulted from" the transaction that is on or subject to the rules of contract market. The statute thus requires a causal connection between the actual losses and the transaction that is the basis of the suit. If a customer suffers trading losses as a result of a contract market's failure to enforce rules, it would be difficult to argue that such losses "resulted from" the customer's relationship with the FCM. See page 5, *infra*.

Under petitioner's reading of the statute, therefore, the party that Congress most clearly sought to protect—the customer directly investing in the futures markets—would be left without the ability to recover trading losses caused by an exchange's failure to enforce its rules, even though such losses were at the forefront of Congress's concern.

If, on the other hand, investors retain the ability to recover losses predicated on their exchange trades, allowing non-traders (such as petitioner) to recover will produce a significant risk—even a certainty—of multiple recoveries. Any trade of futures contracts would subject a contract market or clearing organization to potential claims by the investor, the FCM, the floor broker, the introducing broker (see 7 U.S.C. § 1a(8)), the commodity trading advisor (see *id*. § 1a(5)), and commodity pool operator (see *id*. § 1a(4)), all of whom like clearing members can claim to be "essential" participants in futures and options trades and most of whom participate in trades that are not proprietary trades by a contract market member. (The government recognizes (Br. 24 n.13) that this will be the result of its approach.) These multiple claims, which would become routine, inevitably would produce duplicative recoveries.

This Court repeatedly has refused to construe federal statutes in a manner that will subject a defendant to multiple liability. See *Holmes* v. *Securities Investor Protection Corp.*, 503 U.S. 258, 287 (1992); *Illinois Brick Co.* v. *Illinois*, 431 U.S. 720 (1977). It should reject that approach in this context as well.

Fourth, the structure of Section 25 indicates that Congress intended to limit the liability of contract markets and clearing organizations. Thus, the private cause of action created in Section 25(a)—which excludes claims against contract markets, clearing organizations, and their officers and directors—supplements the administrative action for recovery of actual damages set forth in Section 18 and the remedies that Section 7a(11) required contract markets to create. See 7 U.S.C. § 25(a)(2) ("the rights of action authorized by this subsection ***and by sections 7a(11), 18, and 21b(10) of this title*** shall be the exclusive remedies * * *") (emphasis added).

The private action against a contract market and its officers and directors, by contrast, is "the exclusive remedy under this chapter available to any person who sustains a loss as a result of" a contract market's enforcement of its rules in violation of the Act. 7 U.S.C. § 25(b)(5). Neither the administrative action nor the remedies created by contract markets' rules extend to such claims.

Moreover, a claim under subsection (a) is available only to persons who participated in one of four specified transactions—some of which plainly are not transactions "on or subject to the rules of" a contract market—a standard that also applies to claims against the officers and directors of contract markets and clearing organizations. 7 U.S.C. § 25(b)(3). Contract markets and clearing organizations, by contrast, are subject to suit only by a person who engaged in a transaction "on or subject to the rules of" a contract market.

Under petitioner's theory, however, the liability of contract markets and clearing organizations would be extremely broad—extending to any damages related to any activity that is in any way subject to the contract market's rules. That result is sharply inconsistent with the statutory design. That could open the door to Section 25(b) lawsuits involving membership issues (on the ground that membership is a "transaction"), administration of financial requirements, indeed, virtually any interaction between a contract market or clearing organizations and any other person or entity. That would threaten to impose a crippling financial burden on contract markets and clearing organization given the millions of interactions that take place each year—plainly the result that Congress sought to avoid by sharply circumscribing their liability.

Finally, contrary to the assertions of petitioner (Br. 42) and the Futures Industry Association (Br. 11), the integrity of the futures markets will not be threatened by interpreting Section 25(b)(1) in accord with Congress's intent. The principal safeguard of the proper functioning of the markets is the

CFTC's expansive enforcement authority, which extends broadly to contract markets and clearing organizations and their officers and employees. See 7 U.S.C. §§ 12a, 12c, 13a. The CFTC has broad authority to issue cease and desist orders, impose fines, bar individuals or entities from engaging in any regulated activity, and issue orders requiring contract markets to remedy deficiencies. *Id*. §§ 9, 9a, 12e, 13, 15.

The assertion that a broad interpretation of Section 25(b)(1) would play a critical role in deterring wrongful conduct is undercut by petitioner's inability to point to a single example of a decision upholding a claim by anyone other than an investor in the 24 years since the statute was enacted. Moreover, in the five years that have elapsed since the New York federal district courts dismissed each of the three lawsuits arising out of petitioner's collapse, the futures markets have grown substantially. Some commodity and futures exchanges have become public companies. Others have been acquired by or merged with public companies. These developments make clear that there is no reason whatever to believe that confidence in these markets would be affected adversely by a decision affirming the dismissal of these claims.

II. PETITIONER HAS NOT ALLEGED "ACTUAL LOSSES THAT RESULTED FROM" ITS TRANSACTIONS AND WERE CAUSED BY RESPONDENTS' FAILURE TO ENFORCE THEIR RULES.

If the Court accepts petitioner's invitation to expand substantially the scope of Section 25(b)(1) to encompass claims by non-traders, the Court should decide whether harm such as that allegedly suffered by petitioner has a sufficiently close causal connection to respondents' alleged misconduct and to the damages that petitioner claims to have suffered to give petitioner standing to maintain this action. Broadening the scope of the cause of action will open the door to many more lawsuits; clear guidance from this Court regarding the statutory causation requirement will help the lower courts weed out remote claims.

The courts below clearly understood that petitioner's alleged damages were too remote to satisfy the strict causation standard that Congress specified. This Court should so rule, and affirm the judgment of the court of appeals on that basis.

Section 25(b)(1) authorizes recovery of "actual damages sustained by a person who engaged in any transaction on or subject to the rules of" a contract market but only "to the extent of such person's actual losses that resulted from such transaction and were caused by" the contract market's failure to enforce its rules. Both courts below found that petitioner's claim failed to satisfy this standard.

The court of appeals stated:

> [R]egardless of whether the First West trading position rose or declined in value, Klein had no interest in any of the resulting profits or investments losses. As the district court observed, "Klein suffered damages because of its customer First West's inability to cover its margin call. . . ." Thus, Klein's loss was a credit loss, not a trading loss.

Pet. App. 12a (internal citation omitted). The district court not only described First West's inability to cover its margin call as being the cause of Klein's alleged damages, it also observed, "[q]uite simply, [Klein] did not suffer its damages in the course of its trading activities on a contract market." *Id*. at 25a. That determination is correct and should be upheld by this Court.[24]

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[24] Respondents argued below that petitioner "suffered no investment loss whatsoever as a result of the decline in value of First West's positions. [Petitioner's] only connection to 'transactions in a contract market' was entirely secondary." Brief for the NYBOT Defendants-Appellees-Cross-Appellants, 2005 WL 5352926, at *21 (July 25, 2005). And respondents raised the issue in their brief in opposition (at 6): "Customer credit losses sustained by a broker are simply not losses arising from exchange transactions as described by CEA § 22. The losses Petitioner seeks to recover were

A. Section 25(b)(1) Requires A Close Link Between The Transaction, The Plaintiff's "Actual Losses," And An Exchange's Failure To Enforce Its Rules.

This Court has consistently held that language similar to that included in Section 25(b)(1) imposes a strict proximate cause requirement. See, *e.g.*, *Holmes*, 503 U.S. at 271 (construing the RICO statute to embody the "general tendency of the law, in regard to damages at least, is not to go beyond the first step"); *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*, 429 U.S. 477 (1977).[25]

Holmes provides a particularly strong analogy. The case arose out of an alleged stock-manipulation scheme that harmed two broker-dealers who, because of losses attributable to the alleged manipulation, could not satisfy their obligations to their respective customers. The failure of the broker-dealers triggered Security Investor Protection Corporation's (SIPC's) obligations under the Securities Investor Protection Act of 1970 to advance funds to reimburse the customers of the failed broker-dealers.

After reimbursing those customers, SIPC commenced an action against the alleged manipulators, asserting claims under RICO (18 U.S.C. § 1964(c)), and sought to be reimbursed for the funds paid to the customers. Notwithstanding

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caused by First West's failure to pay Petitioner the margin debts that it owed to Petitioner under its customer agreement." The proximate cause issue has thus been raised repeatedly at every stage of litigation in this proceeding, and it animated the decisions of the courts below.

[25] To be sure, Congress can mandate damage awards for all injuries caused by unlawful conduct. But the Court has "insist[ed] upon a clear expression of a congressional purpose" before attributing such an intent to Congress. *Brunswick Corp.*, 429 U.S. at 488. Section 25(b) manifests Congress's intent to strictly limit recoverable damages.

its allegations of "but for causation," and despite the fact that RICO conferred standing on "[a]ny person injured in his business or property," this Court held that SIPC's allegations did not fit within the terms of the statute. 503 U.S. at 265.

The Court determined that even if SIPC was assumed to stand in the shoes of the broker-dealers' customers, its injury was too remote because "the conspirators have allegedly injured these customers only insofar as the stock manipulation first injured the broker-dealers and left them without the wherewithal to pay customers' claims." 503 U.S. at 271. The same attenuated causation chain would be impermissible under the strict "actual loss" standard of Section 25(b)(1).

B. Petitioner's Claim Of Damages For The Collapse Of Its Business Fails To Satisfy The "Actual Loss" Standard.

Petitioner alleges that it was injured when its business collapsed in the wake of First West's failure to provide additional margin. It seeks damages resulting from the collapse of its business.

Thus, petitioner alleges that, "[a]s a direct result of the actions of the defendants, on May 16, 2000, Klein & Co. ceased to operate as a FCM, closed its offices, terminated its employees and commenced to wind up its business, which ceased to operate as of the close of business May 15, 2000." J.A. 28 (¶ 116); see also J.A. 39 (¶ 156). Its complaint seeks recovery of $25 million in compensatory damages. J.A. 54-57.

Petitioner's alleged damages resulting from the collapse of its business are not "actual losses that resulted from" any transaction in which petitioner "engaged" "on or subject to the rules of [a] contract market." Rather they are a classic example of consequential damages that are not recoverable under a strict proximate cause standard. *Associated Gen. Contractors of Cal., Inc.* v. *Carpenters*, 459 U.S. 519, 540, 545 (1983) (holding allegations of "consequential harm" insufficient as a matter of law by reference to the "indirectness of the injury"—the fact that the chain of causation between the injury and the alleged conduct by defendants "contains several somewhat vaguely defined links").

Indeed, the government appears skeptical that Section 25(b)(1)'s "actual loss" standard permits recovery of damages relating to the collapse of petitioner's business. It says that "petitioner's claims of pecuniary injury cannot be dismissed as speculative" because "petitioner's [NYCC] margin account deficit was approximately $4.5 million" (Br. 17) and declines to express a view on petitioner's damages claim based on the collapse of its business (Br. 29 n.17).

But the margin deficit cannot satisfy the "actual losses" requirement for the simple reason that the complaint does not seek recovery of the margin deficit. Not a single damages allegation refers to this amount.

That omission of such an allegation is intentional, because petitioner did not bear the financial burden of the margin deficit; $4.5 million was paid to Klein's customers by respondent NYBOT, which is now suing petitioner as the assignee of those customers to recover that amount from Klein. See page 15, *supra*. The record thus demonstrates that petitioner never paid one dollar of the loss on which the Solicitor General predicates petitioner's standing. The absence of such an allegation establishes that petitioner cannot satisfy Section 25(b)'s "actual losses" requirement.

CONCLUSION

The judgment of the court of appeals should be affirmed.

Respectfully submitted.

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SEPTEMBER 2007

APPENDIX

The relevant provision of the Commodity Exchange Act, 7 U.S.C. § 25 (1994), as in effect when this case was filed in July 2000, provides:

§ 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 insubparagraphs (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 section 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(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 al-

leged 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.

*   *   *

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

Rule 401. ***Acceptance for Clearance***

(a) The Corporation, by accepting a Contract offered to it for clearance by or on behalf of a Clearing Member, shall assume, in the place of each Clearing Member that is a party to such Contract, all liabilities and obligations imposed thereby to the Clearing Member that is the other party thereto, to the extent provided in Rule 401(b), and shall succeed to and become vested with all rights and benefits accruing therefrom. Such assumption by the Corporation shall terminate all liabilities and obligations of the Clearing Member whose Contract is so accepted to the other Clearing Member which was a party to such Contract.

(b) THE LIABILITIES AND OBLIGATIONS OF THE CORPORATION ARISING PURSUANT TO RULE 401(a) SHALL BE SUBJECT TO THE FOLLOWING LIMITATIONS:

> (i) SUCH LIABILITIES AND OBLIGATIONS SHALL EXTEND ONLY TO CLEARING MEMBERS. WITHOUT LIMITING THE GENERALITY OF THE FOREGOING, THE CORPORATION SHALL NOT HAVE ANY LIABILITY OR OBLIGATION ARISING OUT OF OR WITH RESPECT TO ANY CONTRACT TO ANY CUSTOMER OF A CLEARING MEMBER OR ANY EXCHANGE MEMBER WHICH ACTED AS A BROKER FOR A CUSTOMER OR A CLEARING MEMBER;
>
> (ii) IF ANY SUCH LIABILITY OR OBLIGATION ARISES OUT OF A FAILURE BY A CLEARING MEMBER TO MAKE OR ACCEPT DELIVERY OF A COMMODITY UNDER A CONTRACT WHEN

AND AS REQUIRED UNDER THE RULES OR ANY APPLICABLE EXCHANGE RULES:

(A) EXCEPT AS PROVIDED IN RULE 603, THE CORPORATION'S SOLE LIABILITY OR OBLIGATION SHALL BE TO PAY ANY DAMAGES AND PENALTIES PROVIDED FOR UNDER APPLICABLE EXCHANGE RULES FOR SUCH FAILURE, AND THE CORPORATION SHALL HAVE NO OBLIGATION TO MAKE OR ACCEPT DELIVERY OF ANY COMMODITY IN FULFILLMENT OF SUCH CONTRACT;

(B) IF SUCH FAILURE OCCURS AFTER THE DELIVERY NOTICE UNDER SUCH CONTRACT FOR THE PURCHASE OR SALE OF SUCH COMMODITY WAS ISSUED BY OR ASSIGNED TO SUCH CLEARING MEMBER, THE LIABILITY OF THE CORPORATION SHALL BE LIMITED, IN THE AGGREGATE, TO THE AMOUNT OF ORIGINAL MARGIN ON DEPOSIT WITH THE CORPORATION FROM SUCH CLEARING MEMBER FOR SUCH CONTRACT; AND

(C) ANY CLAIM AGAINST THE CORPORATION IN RESPECT OF SUCH FAILURE MUST BE MADE IN WRITING AND DELIVERED TO THE CORPORATION WITHIN ONE BUSINESS DAY AFTER SUCH FAILURE TAKES PLACE, OR SUCH CLAIM SHALL BE WAIVED AS AGAINST THE CORPORATION.

(iii) All such liabilities and obligations shall terminate after delivery of and payment for a commodity are made pursuant to these Rules and any applicable Exchange rules.

Rule 402. ***Trade Data Submission***

(a) The Corporation shall accept for clearance any Contract which has been matched by the Listing Exchange and has been submitted for clearance by or for such Exchange on behalf of the Clearing Members that are the parties thereto. The Corporation shall not accept for clearance any Contract or any transaction submitted to it by any person other than the Listing Exchange or its designated agent, except for transfers of Contracts and mechanical adjustments effected in accordance with any rules of the Listing Exchange, these Rules or the procedures of the Corporation permitting the submission thereof by persons other than the Listing Exchange.

(b) A Contract which has been matched by the Listing Exchange and has been submitted for clearance by or on behalf of any Clearing Member shall be deemed accepted by the Corporation for clearance when all processing of the day's trades have been completed and reports of cleared trades shall first have been made available to the Clearing Members. The Corporation shall have no liability or obligation to any Clearing Member or other person with respect to any Contract which has not been accepted by it for clearance.

(c) The Corporation shall be entitled to rely conclusively on the accuracy and authenticity of any information regarding any Contract submitted to the Corporation by the Listing Exchange on behalf of any Clearing Member, whether or not the Clearing Member in fact authorized the submission of such Contract for clearance.

(d) All Contracts accepted for clearance by the Corporation shall be subject in all respects to the By-Laws and these Rules.

(e) Any trade in a Contract which, on any day, is matched by the Listing Exchange but not accepted for clearance by the Clearing Member designated to clear such Contract, shall be automatically cleared to the account of the

Clearing Member which has guaranteed the Listing Exchange member who executed such trade on the day the trade was matched, provided that such guarantee has not been terminated in accordance with the rules of such Listing Exchange.

Rule 403. ***Daily Reporting of Open Contracts***

(a) Each Clearing Member shall report to the Corporation, by such time on each Business Day and in such manner as may be prescribed by the Corporation, such information as the Corporation may require with respect to Contracts which are open on such Clearing Member's books as of the close of business on the previous Business Day.

(b) If a Clearing Member discovers an error in any report made pursuant to this Rule 403, such Clearing Member shall as soon as practicable submit to the Corporation a correction and a written statement as to how the error occurred.

Rule 404. ***Reporting of Exchange Positions Carried by Other Firms***

(a) If a Clearing Member has customer or proprietary positions in any Contract carried for it by another Clearing Member or by a futures commission merchant which is not a Clearing Member, the Clearing Member first referred to shall:

(i) Give written notice to the Corporation of the name of such other Clearing Member or futures commission merchant not later than the close of business on the first day any such position is carried by such other Clearing Member or futures commission merchant; and

(ii) If any such position is being carried or maintained by a futures commission merchant which is not a Clearing Member, provide to the Corporation, on each Business Day, by the time specified by the Corporation for the purpose, the information specified in Rule 404(b) concerning any such position.

(b) Each Clearing Member shall report to the Corporation, on each Business Day, by the time specified by the Corporation for the purpose, in such manner as may be prescribed by the Corporation, the number of long and short open positions in each Contract for each expiration month which such Clearing Member is carrying for any other Clearing Member as of the close of business on the preceding Business Day. Each such report shall separately specify positions carried for such other Clearing Member's proprietary account and customer account.

Rule 405. ***Transfers of Open Positions***

Any transfer of a Contract shall be subject to the following:

(a) if the transferor shall have been declared to be in default, transfers may only be effected at the current day's settlement price unless the Corporation in its discretion determines that, because of excess margin on deposit or for other sufficient reason, accepting the transfer at other prices permitted by Exchange rules would not jeopardize the Corporation; and

(b) if, in any case, the Corporation in its discretion determines that it would be contrary to the best interests of the Corporation to accept a transfer at a price other than the current day's settlement price, it may, notwithstanding any provision to the contrary in the Exchange rules, require such transfer to be effected at such settlement price.

* * *

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

Futures and Options Contracts Committee

Section 2.19 (a) The Board shall appoint a Futures and Options Contracts Committee, consisting of not less than 3 nor more than 15 members of the Exchange, as determined by the Board. The Committee shall have a Chairman and Vice Chairman, one of whom shall retire at the end of each month, and may act by multi-person panels appointed by the Chairman

(b) Each panel, so appointed, shall meet each day at the close of trading in the contracts over which it has jurisdiction and determine the tone of the market and the settlement prices of such contracts. Each such panel shall determine the settlement prices in the respective market in accordance with the procedures set forth in Rule 415.

(c) Each such Panel shall take cognizance of the questions arising in the regular course of business on the Exchange with respect to the market price properly obtaining at the time transactions within its respective jurisdiction are made and the recording of such transactions in the record of transactions; and it shall have authority to settle immediately disputes involving such questions.

(d) In performing its functions, no notice of meeting shall be given and the action of such number of members of the Committee who are present on the floor at the time, although a single member of the Committee, shall be deemed that of the Committee.

* * *

Customer

Rule 14 The term "customer" means a person for whom a member or member organization carries an account (other than such member or member organization) or from whom any member, member organization or nominee solicits or accepts any order to effect any transaction involving a futures contract or an option contract.

* * *

Offers to Buy or Sell

Rule 303 (a) No contracts shall be made or recorded for any month except those months authorized in the Rules governing said contracts.

(b) All offers to buy or sell contracts made on the floor of the Exchange shall be open to the member first accepting such offer, for the whole or any part of such offer; in case of simultaneous acceptances, that for the whole quantity shall take precedence over that for any part.

(c) All offers to buy or sell a contract shall be quoted in such terms as are set forth in the Rules governing said contracts.

(d) The time and price at which every contract is made shall be reported by the seller and/or buyer promptly, Transactions not so reported shall not be recorded in the record of transactions, except on the written consent of the Futures and Options Contracts Committee and provided that the posting or recording thereof shall not be later than ten minutes after the close of trading.

(e) Transactions made in any contract at a price above that at which such contract is offered or below that which is bid for such contract, until what is offered shall be taken or what is bid for shall be supplied, shall not be deemed made at the market price for such contract and shall not be reported or recorded in the record of transactions. No transaction that is not made competitively by open outcry in the trading ring of the Exchange shall be permitted, reported, or recorded in the record of transactions except:

(1) transfers of open contracts of a clearing member or member firm necessitated by the death of the only member of such firm who had held membership in the Exchange;

(2) transfers of open contracts of a client, made at the request of such client, from one member to another member;

(3) transfers of open contracts of a client at the request of the original clearing member to another member;

(4) transfers of open contracts from one account to another within the same office of a clearing member, or between different offices of one clearing member, where no change in ownership is involved. The transferred contracts in the transferee account must be recorded at the original date and price;

(5) transfers of futures contracts in exchange for the underlying or comparable commodity, or exchange of futures in connection with spot transactions in the underlying commodity or a comparable instrument;

(6) transfers occurring after the close of trading on the last trading day of any delivery month in any contract (but not later than noon of the following business day) to rectify errors.

For purposes of this subsection (6), a clearing member carrying one or more open contracts for that delivery month for its own account or the account of any other person as the result of an error may, by consent, transfer any or all of such contracts to any other account carried by such clearing member or to any other clearing member; provided, however, that:

(i) for any delivery month, no clearing member may so transfer for its own account to the account of any other person more than 20 contracts in the aggregate; and

(ii) not later than noon of the business day following such last trading day, the clearing member effecting the transfer, in addition to other reports made in the manner and time required by this Rule shall deliver to the clearing house written notification of such transfer (in such form as the clearing house may prescribe), specifying the parties thereto and the prices at which such transfers were effected.

Such trades may be effected between or in the offices of the clearing member or clearing members but must be reported to the Exchange for recording, clearly showing the exception above justifying the trade and stating whether the transaction has resulted in a change of ownership, the quantity, if any, of the spot commodity involved, the kind and quantity of the contracts, the price, the name of the other clearing member, if any, and any other pertinent data. The clearing member must in its records clearly label all such trades. The names of the purchaser and seller shall be given when required.

Acceptances of offers or parts of offers to buy or sell shall be binding upon the acceptor at the price named by the member offering.

(f) Disputes arising in the regular course of business on the Exchange from bids, offers or acceptances, made at any other time than on a call, shall be settled by a member of the Futures and Options Contracts Committee submitting the question to the members present. The decision of the majority voting shall govern. When such a dispute arises on a call, the question shall be decided on the spot by the Caller.

(g) Disputes involving questions of the time and price at which contracts were made, or of the market price properly obtaining at the time such contracts were made, or of the recording of transactions in the record of transactions, shall be referred to the Futures and Options Contracts Committee which, after hearing both parties, shall render a decision that shall be final.

(h) If an error or dispute arises between members as to a claim of a purchase or a sale of a contract, the party claiming the sale or purchase shall, unless otherwise mutually agreed upon, liquidate the same as soon as possible and the loss resulting shall be the subject of arbitration. Any claim of a purchase or sale of a contract must be made promptly after discovery and no later than five minutes before that contract's next opening.

For purposes of subsections (h) and (i), if the transaction is claimed to have occurred

(i) during original hours, "next opening" shall mean the first opening of the contract which takes place between 8:00 A.M. and 11:00 A.M. in New York on the next trading day.

(ii) during extended hours, "next opening" shall mean the 7:00 P.M. opening on the next trading day in New York.

(i) If a member claims to have bought or sold, or has bought or sold, a contract and the member with whom the trade has been made, or is claimed to have been made, is absent or cannot be found, the trade shall be closed at the contract's next opening, and notice of such closing of the trade shall be filed with the Exchange, and the resulting loss, if any, shall, if the trade is disputed, be subject to arbitration, and if not disputed, shall be immediately paid.

* * *

Straddle Transactions

Rule 313 (a) Members of this Exchange are permitted to execute futures or options contract orders to purchase one futures contract and sell another futures contract at a stated price difference ("futures straddle") or to effect one options transaction in conjunction with another options transaction as set forth in paragraph (b) below ("options spread"), to effect one options transaction in connection with a futures transaction as set forth in paragraph (c) below ("futures/options spread"), or to effect a transaction on this Exchange simultaneously with a transaction on another exchange as set forth in paragraph (d) below ("Inter-Exchange transaction") in such configurations of such contracts as may be recognized by the Exchange. Such transactions must be for the account of one customer except in the case of a transfer of interest in an authentic commercial transaction. These orders are to be executed competitively by public open outcry in the ring with at least one side of the futures straddle or options spread at the market price prevailing at the time of the trade.

In the case of futures/options spreads, the futures side shall be priced at the futures price prevailing at the time of the trade. In inactive futures months or options series or classes in which there are no prevailing market prices because there have been no trades, bids or offers in either futures month or in the respective options series or class, the prices must bear a reasonable relationship to the respective prevailing market prices of active futures or options. It shall be the trading member's responsibility to insure that orders executed in this manner be properly recorded in writing permitting identification of these transactions and the parties thereto, and that straddles and spreads are posted and announced in such manner as the Exchange may direct.

(b) For purposes of this Rule, options spreads are options transactions in the same or comparable class, all sides of which are executed in conjunction with one another and that fit into one or more of the following definitions or multiples thereof:

(1) *Vertical and Horizontal Options Spreads:* Short one call (put) and long another call (put) with a different strike price and/or expiration month.

(2) *Options Straddles:* Short (long) puts and calls in a generally accepted spread ratio.

(3) *Options Butterflies*: Two vertical spreads which share one common strike price.

(4) *Option Boxes:* Long a call and short a put at one strike price and short a call and long a put at another strike price.

(5) *Option Ratio Spreads:* Long calls (puts) and short calls (puts) in a generally accepted spread ratio.

(6) *Options Synthetic Futures:* Long calls (puts) and short puts (calls in a generally accepted spread ratio.

(c) For purposes of this Rule, futures/options spreads are transactions all sides of which are executed in conjunction with one another consisting of options and a future concerning which:

(1) The execution takes place in a location designated by the Exchange.

(2) The sides of the resulting transactions generally offset one another.

Examples of futures/options spreads which would qualify are:

(A) Synthetic Straddles: Long (short) futures and short (long) calls or long (short) puts in a generally accepted spread ratio.

(B) Conversions and Reverse Conversions: Long (short) puts, short (long) calls, and long (short) futures,

(C) Such other configurations of futures/options spreads which the Exchange determines to be generally offsetting.

(d) For purposes of this subsection, the term Inter-Exchange transaction means a straddle or spread transaction in which one leg is executed on this Exchange and the remaining leg is simultaneously executed on any other exchange.

Inter-Exchange transactions are permitted provided that:

(1) the trading member has current trading privileges on both exchanges; and

(2) the Inter-Exchange transaction is of a class and quantity authorized by the Exchange.

(e) Nothing in this Rule shall be construed to prevent the execution of futures straddles by individual purchases and sale or of futures/options spreads or options spreads by individual transactions.

* * *

Definitions

Rule 601 The following terms shall, for the purpose of these Arbitration Rules, have the following meanings, unless otherwise indicated:

(a) Controversy. Any claim, grievance or dispute which arises out of any transaction on or subject to the Rules of the Exchange executed by or effected through a member of the Exchange or employee thereof, which does not require for adjudication the presence of essential witnesses or third parties over whom the Exchange does not have jurisdiction and who are not otherwise available. The term “controversy” does not include a claim, grievance or dispute arising from cash market transactions which are not a part of, or directly connected with, any transaction for the purchase or sale of any contract effected on the Exchange.

(b) Statutory Controversy. Any controversy between a customer and a member or employee of a member.

(c) Inter-Exchange Transaction Controversy and Procedure

(1) Inter-Exchange Transaction shall mean a straddle or spread transaction (or order) recognized by the Exchange in which one leg of the straddle or spread transaction is executed (or is intended to be executed) on the Exchange and the

other leg is simultaneously executed (or is intended to be simultaneously executed) on another futures contract market ("Other Exchange") with respect to a futures or options contract in which that Other Exchange has been designated by the Commodity Futures Trading Commission.

(2) Controversy. Any controversy involving an Inter-Exchange Transaction.

(3) Procedure. The procedure to be followed in Inter-Exchange Transaction Controversies shall be as set forth by written agreement between this Exchange and such Other Exchange(s). Those agreements together with these Rules shall govern the arbitration of claims arising out of Inter-Exchange Transactions as defined herein. A listing of those agreements currently in effect, as well as the agreements themselves, are available upon request to the Secretary's office. Parties who are involved in an Inter-Exchange Transaction Controversy should consult those agreements as well as these Rules.

(4) Nothing set forth herein or in any agreement with Other Exchange(s) shall limit a customer's right (as claimant or respondent in arbitration) to a choice of forum under CFTC Reg. 180.1(b)

(d) Non-Statutory Member Controversy. Any controversy between a member and another member. For the purpose of this paragraph a controversy shall include any claim, grievance or dispute relating to a transaction on the Exchange or to a transaction to be made on the Exchange or to the relations or obligations to each other of the parties to a transaction which is governed by the By-Laws or Rules of the Exchange.

(e) Customer. A person other than a member of the Exchange who has a controversy with a member of the Exchange or an employee thereof.

(f) Member. A member of the Exchange or a partnership, corporation or association on which the benefits of membership have been conferred pursuant to the Rules of the Exchange, including former members to the extent set forth in the By-Laws.

(g) Claimant. A person who asserts a claim under these Arbitration Rules.

(h) Respondent. A person against whom a claim is asserted under these Arbitration Rules.

(i) Panel. A three member panel appointed to hear and determine a controversy under these Arbitration Rules. Except where a Mixed Panel is appointed, a Panel shall consist of a subcommittee of three members of the Arbitration Committee.

1. the 3 person Panel provided for in Rule 601(i) or (j);

2. in the case of a small claims matter assigned to a sole arbitrator, the arbitrator;

3. before a Panel has been appointed by the Chairman of the Arbitration Committee, the Chairman of the Arbitration Committee.

(j) Mixed Panel. A Panel consisting of one member of the Arbitration Committee and two persons who are not members of any contract market or associated with any member of a contract market or employees thereof, and who are not otherwise associated with a contract market (a "non member"). If the matter is a statutory controversy and a small claim as provided in (m)(l) below, the Panel shall consist solely of one person who is a non-member.

(k) Counterclaim. A claim which falls within the definition of a controversy asserted by the respondent against the claimant.

(l) Service. The delivery of pleadings and other documents to and from the Exchange and the parties. For purposes of these Arbitration Rules, service can be accomplished by hand delivery, mail, including express mail (by private or public courier), or by facsimile transmission (fax).

With respect to any such method employed, it is the responsibility of the sender to have and maintain proof of service. With respect to any time period required within these Rules, service shall be deemed to be made on the day that a pleading or document has been hand delivered, faxed or deposited with an express mail service; in the event of service by regular mail, service shall be deemed to have been made three days after deposit with the postal service.

(m) Small Claims

1. Any claim together with any counterclaim, if any, which aggregates less than $5,000 shall be decided by one arbitrator without a hearing, subject to 2 below.

2. If the Chairman of the Arbitration Committee or sole arbitrator, when appointed, determines that a hearing before a three person panel would be appropriate, then the small claim shall be so heard. The Chairman (or sole arbitrator) may make such decision at the request of any party or on his own motion.

3. If a small claims procedure occurs, the sole arbitrator shall be empowered at any time before he closes the proceedings to request documents and clarification including, but not limited to, written and/or oral testimony from the parties and others within the jurisdiction of the Exchange, as well as publicly available records from the Exchange staff, all on written notice to each of the parties.