Supreme Court, U.S.
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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 Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

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COUNTERSTATEMENT OF QUESTION PRESENTED

Whether the court of appeals correctly held that a futures commission merchant ("FCM") that handled and cleared trades for its customer lacked standing to assert claims against a contract market and a clearing organization under former Section 22(b) of the Commodity Exchange Act (7 U.S.C. § 25(b) (1999)) to recover losses resulting from its customer's failure to pay margin calls, on the ground that the FCM's claims did not arise from its own trading losses as a result of any transaction on or subject to the rules of the contract market.

RULE 29.6 CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 29.6 of the Rules of this Court, respondent Board of Trade of the City of New York, Inc., a New York Not-for-Profit Corporation ("NYBOT"), states that, following a January 12, 2007 merger, NYBOT's successor in interest is Board of Trade of the City of New York, Inc., a Delaware corporation, a wholly owned subsidiary of IntercontinentalExchange, Inc. ("ICE"), a Delaware corporation publicly traded on the New York Stock Exchange. Respondents New York Clearing Corporation ("NYCC"), a clearinghouse, and New York Futures Exchange, Inc. ("NYFE"), a contract market, state that they are wholly owned subsidiaries of NYBOT. Respondent New York Cotton Exchange ("NYCE") no longer exists.

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OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI

OPINIONS BELOW

Respondents NYBOT, NYCE, NYFE and NYCC (collectively, the "NYBOT Respondents") submit this opposition to the petition of Klein & Co. Futures, Inc. ("Klein" or "Petitioner") for a writ of certiorari to review the opinion and judgment of the United States Court of Appeals for the Second Circuit, filed September 18, 2006, in *Klein & Co. Futures, Inc. v. Board of Trade of New York*, 464 F.3d 255 (2d Cir. 2006). The opinion of the court of appeals is set forth in the Appendix to the Petition at 1a-15a. The opinion of the district court is set forth in the Appendix to the Petition at 16a-34a.

STATUTORY PROVISION INVOLVED

Section 22 of the Commodity Exchange Act ("CEA"), 7 U.S.C. § 25 (1999), entitled "Private rights of action," as it existed in July 2000 when Petitioner commenced the underlying action, is set forth in the Appendix to the Petition at 37a-41a. Section 22 was amended in December 2000, and the subsection of the statute at issue here has been amended. *See* Point C, *infra.*

COUNTERSTATEMENT OF THE CASE

The Petition seeks review of the decision by the court of appeals affirming the district court's dismissal with prejudice of Klein's federal claims under the CEA against NYBOT, NYFE, NYCE and NYCC.

In the district court, Petitioner Klein, an FCM and a clearing member of NYCC, alleged that its customer, defendant Norman Eisler ("Eisler"), a member of the NYFE Settlement Committee, manipulated the settlement prices of P-Tech futures and options traded on NYFE, a contract market, and that in May 2000, when the settlement prices were recalculated, Klein incurred losses because its customer, Eisler, and his company, First West Trading, Inc. ("First West"), could not pay margin calls issued by Klein resulting from First West's trading losses. First West's default on its obligations to Klein triggered a series of events that, because of Petitioner's limited capital, led to Petitioner's collapse.

On July 20, 2000, Petitioner filed its complaint in the United States District Court for the Southern District of New York (Daniels, J.) against Eisler, First West and the NYBOT Respondents. In its complaint, Petitioner claimed that it was wrongfully injured as a result of Eisler's conduct and First West's margin default, and Klein's resulting collapse. *See* Pet. App. at 17a. Klein alleged that it "'had no equity or financial interest in the First West account nor did Klein &

Co. exercise control over the trading in said account.'" *Id.* at 24a.

Petitioner asserted claims for violations of the federal commodities laws and various state law claims. Count I of the Complaint alleged that the contract market NYFE violated CEA § 5b by failing to enforce its rules. Count II alleged that defendants violated the anti-fraud provisions in CEA § 4b and 17 C.F.R. §§ 33.9 and 33.10 thereunder. Count III alleged that defendants violated the insider trading provisions of CEA § 9. Counts IV-XI of the Complaint alleged a variety of state law claims against the defendants.[1]

The NYBOT Respondents moved before the district court to dismiss Petitioner's CEA claims on the grounds, among other things, that Petitioner was not a trader and thus lacked standing under CEA § 22(b).[2] Eisler and First West also moved to dismiss for lack of standing under Section 22(a). The NYBOT Respondents argued that Petitioner did not base its claims on any trading of futures contracts or options done for its own account and, therefore, lacked standing under CEA § 22.

On February 18, 2005, the district court dismissed Petitioner's federal claims with prejudice for lack of standing under CEA § 22. As to the NYBOT Respondents, the district

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[1] In a countersuit against Klein pending in the district court, NYBOT and the clearinghouse NYCC sought to recover from Klein over $4 million lost by the innocent customers of Klein whose assets were seized as a consequence of Klein's default, which customer losses NYBOT voluntarily paid to Klein's customers and seeks to recover from Klein. *See* Pet. App. at 17a.

[2] The NYBOT Respondents also moved to dismiss Petitioner's CEA claims on the ground that Petitioner did not allege conduct that amounts to bad faith on the part of the NYBOT Respondents as required by CEA § 22(b). The NYBOT Respondents also moved to dismiss Petitioner's state law claims on the ground that these claims were preempted by the CEA.

court held: "Quite simply, [Klein] did not suffer its damages in the course of its trading activities on a contract market. Klein, therefore, does not have standing to allege a private cause of action under Section 22(b)." Pet. App. at 25a.

On September 19, 2006, a panel of the United States Court of Appeals for the Second Circuit affirmed the district court's decision and held: "[E]nforcing 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." Pet. App. at 13a. On November 14, 2006, the court of appeals denied Petitioner's request for rehearing and rehearing *en banc*. Pet. App. at 35a-36a. On March 14, 2007, Petitioner filed its Petition for a writ of certiorari.

ARGUMENT

"A petition for writ of certiorari will be granted only for compelling reasons" such as where "a United States court of appeals has entered a decision in conflict with the decision of another United States court of appeals on the same important matter . . . [or] a United States court of appeals has decided an important question of federal law that has not been, but should be, settled by this Court." S. Ct. R. 10(a), (c).

Petitioner argues in error that the court of appeals' decision created a conflict with the decisions of other United States courts of appeals. Petitioner further argues in error that, if left undisturbed, the court of appeals' decision will have an adverse impact on the nation's economy by increasing futures trading transaction costs. As set forth below, neither of these arguments can withstand scrutiny. There is no reason for this Court to grant the writ.

CEA § 22 did not, as Petitioner claims, manifest a Congressional intent to expand private rights of action under the CEA. *See* Pet. at 7-8. Congress enacted CEA § 22 to limit private rights of action following this Court's decision in

Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran, 456 U.S. 353, 388 (1982), which recognized but did not define an implied private right of action under the CEA. In enacting Section 22, Congress sought to define and circumscribe the private rights of action under the CEA that could be brought against, *inter alia*, contract markets, licensed boards of trade and clearing organizations. 7 U.S.C. § 25.

Section 22(b)(1), as it existed when Petitioner commenced the underlying action, explicitly limited standing to those who "engaged in any transaction on or subject to the rules of [a] contract market or licensed board of trade" *and* sustained "actual losses that resulted from such transaction . . . ." 7 U.S.C. § 25(b)(1) (1999). These provisions, taken together, make it clear that the word "transactions," as used in Section 22(b), refers to exchange trades, and that the phrase "actual losses" refers to exchange trading losses. *American Agric. Movement, Inc. v. Board of Trade of Chi.*, 977 F.2d 1147, 1153 (7th Cir. 1992) (Section 22(b) "forecloses all other remedies, including any on behalf of non-traders"); *see FTC v. Ken Roberts Co.*, 276 F.3d 583, 589 (D.C. Cir. 2001) ("transactions" under the CEA means trades on a contract market), *cert. denied*, 537 U.S. 820 (2002). Thus, to have standing, Petitioner had to have traded futures or options on a contract market and suffered trading losses as a result. Petitioner did neither.

All of the economic gains or losses of the trading belonged to First West, not Petitioner. There is no dispute that Petitioner did not incur trading losses and is not seeking to recover for trading losses. Petitioner's own complaint pled that Petitioner did not own or trade the P-Tech options at issue. *See* Pet. App. at 24a. Instead, as the court of appeals held (*see id.* at 12a), Petitioner sought to recover credit losses that resulted from the failure of First West, its customer, to

pay margin calls issued by Petitioner as the result of First West's trading losses.[3]

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 caused by First West's failure to pay Petitioner the margin debts that it owed to Petitioner under its customer agreement.

Based on these fundamental facts of record, the court of appeals correctly held that Petitioner lacked standing to bring CEA claims against the NYBOT Respondents under Section 22(b) because Petitioner was not itself a trader, but merely "a broker or agent that earned commissions for handling its customer[s'] trades." Pet. App. at 9a. The court of appeals' holding thus affirmed the findings of the district court that "Klein does not claim that it traded for its own account." *Id.* at 24a. "Rather," the district court continued, "it is undisputed that *First West*, not Klein, traded . . . [and] Klein suffered damages because of its customer First West's inability to cover its margin call." *Id.* at 24a-25a.

Although the court of appeals held that the Petitioner had no standing based on the fact that Klein acted as an agent for its customers, Petitioner fails to address this issue altogether. In fact, the word "agent" does not even appear in the Petition. Petitioner's failure to acknowledge that the outcome below was controlled by the undisputed fact that Petitioner, as FCM, acted only as an agent for its customer undermines each of its arguments and indicates that the Petition should be denied.

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[3] As the court of appeals stated, "whether the First West trading positions rose or declined in value, Klein had no interest in any of the resulting profits or investment losses." Pet. App. at 12a. FCMs, when acting as agents, may lose money when their customers fail to reimburse them for margin posted in respect of the customer's positions; FCMs may well fail to be reimbursed for margin, but an FCM does not itself suffer its customer's trading losses.

I. THE COURT OF APPEALS' DECISION DID NOT CAUSE A SPLIT AMONG THE CIRCUITS

Petitioner argues that the court of appeals' decision created some unspecified split among the circuits. *See* Pet. at 3, 15, 23-26. Petitioner asserts that "[t]he ruling below conflicts with decisions of other circuits . . . that correctly interpret the role of futures commission merchants as critical principals who engage in transactions on, and subject to the rules of, boards of trade." *Id.* at 23. Petitioner is in error for the simple reason that the courts below found that Klein in the transactions at issue acted merely as agent or broker. The court of appeals' decision denying standing to Petitioner under Section 22(b) is entirely consistent with the decisions of the other circuits that have interpreted Section 22(b).

A. The Petition Fails To Identify Any Decision By Any Court That An FCM As Non-Trader Has Standing To Pursue Claims Under Section 22(b)

The Petition fails to identify any decision, and we are aware of no decision, by any court holding that an FCM, like Petitioner, when handling trades for a customer, has standing under CEA § 22(b). Instead, Petitioner claims that the decision below created some attenuated "conflict," because the court of appeals lacked appreciation for the role of an FCM. The court of appeals, however, understood exactly what an FCM does and does not do. The court of appeals explained:

> As a[n] FCM, Klein facilitated the trading and fulfilled certain obligations of its customers who traded through the NYBOT. . . . Klein functioned merely as a broker or agent that earned commissions for handling its customer[s'] trades. As a clearing member, Klein cleared their trades and was obligated to post margins for them as required.

Pet. App. at 3a, 9a-10a.

This analysis and conclusion was plainly correct. Under Section 22(b), the issue before the court of appeals was whether the FCM engaged in the trades itself, *i.e.*, whether its exchange transactions caused the damages it seeks. Petitioner was not the trader, no trades caused its own losses, and therefore, Petitioner lacked standing.

B. The Court Of Appeals' Decision Is Consistent With The Decisions Of The Seventh Circuit And Other Courts

The court of appeals' holding that Petitioner was a non-trader that lacked standing is consistent with every court decision that has considered the scope of the private right of action under Section 22(b). *See, e.g., American Agric.*, 977 F.2d at 1153 (the CEA "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 **3-5 (S.D.N.Y. Oct. 17, 2002); *Vitanza v. Board of Trade of N.Y., Inc.*, No. 00 CV 7393, 2002 WL 424699, at **4-6 (S.D.N.Y. Mar. 18, 2002); *Unity House, Inc. v. First Comm'l Fin. Grp.*, No. 96C-1716, 1997 WL 701345, at *7 (N.D. Ill. Nov. 5, 1997) (adopting reasoning of *American Agriculture* in context of § 22(a) claim), *aff'd*, 175 F.3d 1022 (7th Cir. 1999); *de Atucha v. Commodity Exch., Inc.*, 608 F. Supp. 510, 522 (S.D.N.Y. 1985) (Section 22(b) "plainly limits the private remedy to market traders").

Passing by these decisions, Petitioner contends that the court of appeals' decision conflicts with other decisions of the Seventh Circuit. Pet. at 24. No such conflict exists. The Seventh Circuit, which interpreted Section 22(b) in *American Agriculture* consistently with the Second Circuit, held that the term "transactions," as used in Section 22(b), refers to exchange trades, and therefore that Section 22(b) creates a cause of action only for traders on a contract market who were

injured in the course of trading. 977 F.2d at 1153. Specifically, in *American Agriculture*, the Seventh Circuit held:

> 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.* To the extent (if any) that pre-1974 courts had implied private remedies against exchanges in favor of non-traders, Congress directed them to stop doing so in § 22(b).

Id. (emphasis added). The Seventh Circuit's decision in *American Agriculture* is entirely consistent with the court of appeals' decision below, which precludes non-traders like Petitioner from pursuing claims under Section 22(b).

Asking this Court to ignore the ruling in *American Agriculture* and limit its holding to its facts,[4] Petitioner seeks to rely on an outdated Seventh Circuit decision not even decided under Section 22 of the CEA, *Bernstein v. Lind-Waldock & Co.*, 738 F.2d 179 (7th Cir. 1984). In *Bernstein*, the Seventh Circuit, in describing the clearing (not the execution) of trades, stated that the clearing "contract of sale is actually between the floor trader's clearing member . . . and the buyer's clearing member," and referred to *Leist v. Simplot*, 638 F.2d 283, 286-87 (2d Cir. 1980), *aff'd sub nom. Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353 (1982), for an accurate and "more detailed description of commodities trading." 738 F.2d at 181. Judge Friendly,

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[4] Petitioner argues that the holding of *American Agriculture* should be limited to its facts because the farmers there, who sold the agricultural commodities underlying the futures contracts being bought and sold, were not as involved in the market as are FCMs like Petitioner. However, like the farmers in *American Agriculture*, Petitioner did not "engage[] in any transaction on or subject to the rules of such contract market" that resulted in "actual losses . . . from the transaction." 7 U.S.C. § 25(b)(1).

writing for the panel in *Leist*, observed (more accurately) that clearinghouses "treat" FCMs "as if" they were principals, recognizing thereby that FCMs are *not* the actual principals on exchange trades, because it is their customers, the traders, that are the principals.[5] 638 F.2d at 286-87.

Nothing in *Bernstein* had anything to do with standing under the CEA. CEA § 22(b) was not yet in effect when Bernstein commenced his action. 738 F.2d at 185. Petitioner's reliance on *Bernstein* to support its circuit split argument is without merit.

Also without merit is Petitioner's reliance on language in other court decisions that make passing reference to FCMs and their role. Although these decisions state that FCMs participate in futures transactions (which they do by providing ancillary services), the very language relied upon by Petitioner is consistent with the court of appeals' holding that FCMs, when acting for customers, are not traders, but instead are merely brokers who act as agents on behalf of their customers, the parties who actually engage in the exchange transactions.[6] *See* Pet. at 23-26; *Bibbo v. Dean Witter Reynolds, Inc.*, 151 F.3d 559, 560 (6th Cir. 1998) ("[f]utures trades are executed *on a customer's behalf* by an FCM") (emphasis added); *In re Western Fin. Mgmt.*, CFTC No. 81-18, 1983 WL 29657, at *11 (C.F.T.C. Oct. 14, 1983) (noting

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[5] A clearing member therefore might be better characterized as an agent for undisclosed principals. The contract and the rights thereunder belong to the principal, not the agent. Claims by an agent based on conduct taken on behalf of another (*i.e.*, handling orders and clearing trades), do not provide the agent with the contract rights of its principal, and thus are outside the scope of the private right of action afforded under Section 22(a).

[6] Of course, when an FCM is trading for its own account it may be entitled to standing under Section 22. Here, however, Petitioner acted solely as an agent for its customer, and was not a trader. Therefore, Petitioner lacks standing.

that an FCM "trades futures *for the investing public*" and makes futures contracts "*on behalf of* any other person") (emphasis added); *Nagel v. ADM Investor Servs., Inc.*, 217 F.3d 436, 439 (7th Cir. 2000) (observing that "futures contracts [must] be sold *through* commodity exchanges and the futures commission merchants registered on those exchanges") (emphasis added); *Bosco v. Serhant*, 836 F.2d 271, 273 (7th Cir.) ("[t]o do the actual trading of the futures [one needs] *the services* of both a clearing member of the Exchange . . . and a futures commission merchant, *who acts as custodian* of the investors' funds") (emphasis added), *cert. denied sub nom.*, 486 U.S. 1056 (1988); *Scott v. Prudential Sec., Inc.*, 141 F.3d 1007, 1013 (11th Cir. 1998), *cert. denied*, 525 U.S. 1068 (1999). As the court of appeals observed here, an FCM like Klein was but an agent; "Klein was not a trader of P-Tech contracts; nor did it own the P-Tech contracts at issue." Pet. App. at 9a.

The conclusion that an FCM like Petitioner has no standing because it acted only as a broker or agent is entirely consistent with the statutory definition of an FCM. CEA § 1a(20) defines an FCM as any person who (A) "is engaged in soliciting or accepting orders . . ." and (B) "in or in connection with such solicitation or acceptance of orders, accepts any money, securities, or property (or extends credit in lieu thereof) to margin, guarantee, or secure any trades." 7 U.S.C. § 1a(20). In other words, FCMs solicit or accept "orders" on behalf of customers (*i.e.*, the FCM acts as an agent), and accept money, securities or property to guarantee the "trades or contracts" that result from those orders. In sum, the decisions below are entirely consistent with prior decisions under the CEA and with the statute itself.

C. Petitioner Cannot Base Standing On Section 4(a)(1)

In its effort to find an issue where one does not exist, Petitioner claims that the court of appeals' decision is incompatible with CEA § 4(a)(1), which generally prohibits off-exchange trading of futures and options.[7] Specifically, Petitioner claims that, as a result of Section 4(a)(1), virtually everything an FCM does for a customer "in connection with" that customer's trading activity must be done on or subject to the rules of a contract market. Otherwise, Petitioner reasons, Section 4(a)(1) would render the FCM's conduct "off exchange" and thus unlawful. Petitioner's arguments are erroneous. The customer agreement between an FCM and its customers is not an activity on or subject to the rules of a contract market. Nothing about the court of appeals' decision is inconsistent with Section 4(a)(1).[8]

An FCM like Klein that also acts as a clearing member may facilitate futures or options trading in different capacities: (1) as a principal who trades for its own account, or (2) as a broker or agent that handles customer orders and/or clears customer trades through the exchange clearinghouse (here NYCC). Both of the latter functions are as broker or agent. It is undisputed that Petitioner's claims here did not

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[7] Section 4(a) is codified at 7 U.S.C. § 6(a). The Petition erroneously refers to 7 U.S.C. § 6(a) as "Section 6(a)". *See* Pet. at 21.

[8] The text of Section 4(a) confirms that the court of appeals reached the correct result. Section 4(a) is entitled "Restriction on futures *trading*" (emphasis added) and, in the context of discussing lawful futures contracts (*i.e.*, futures trading), it uses virtually the same language as Section 22(b) (*i.e.*, "transaction is conducted on or subject to the rules of a [contract market]"). *Compare* 7 U.S.C. § 6(a)(1) *with* 7 U.S.C. § 25(b)(1). We respectfully submit that this is not a coincidence.

arise out of its own trades. Thus, they must have arisen out of its role as broker and agent for its customer First West.[9]

Like the court of appeals' decision below, the text of Section 4(a)(1) itself recognizes the distinction between the conduct of trading principals and the conduct of FCMs as agents. In particular, Section 4(a)(1) makes it unlawful for an FCM, like Klein, to confirm the execution of a customer's futures contract if that *customer's trade* is not entered into on or subject to the rules of the contract market. 7 U.S.C. § 6(a)(1). Such conduct (and virtually any other conduct undertaken by an FCM for a customer in connection with a futures transaction), places the FCM in the position of an agent.

As such, when an FCM engages in conduct on behalf of its customer (*e.g.*, entering orders, handling orders, and clearing trades) that conduct does not constitute the FCM's own "transaction" that gives rise to claims for "actual losses that resulted from such transaction" as required by Section 22(b). Here Petitioner's losses arose from its customer's failure to pay for trading losses by posting margin required of the customer under Petitioner's customer agreement. That customer agreement is not an exchange transaction; it is a private contract exterior to the trading on the exchange. While Section 4(a)(1) prohibits off-exchange trading, it does not address or regulate the private contractual arrangement between the Petitioner and First West that caused Petitioner's losses here.

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[9] The Futures Industry Association ("FIA"), which intends to file an amicus brief with this Court in support of the Petition, filed an amicus brief in another CEA-related action that explicitly described its members as "FCMs [who] buy and sell futures . . . *as agents* on behalf of their customers." FIA Amicus Brief at 3, *in CFTC v. Eustace*, No. 05 CV 2973 (E.D. Pa. Jan. 18, 2006) (emphasis added), available at http://www.futuresindustry.org/downloads/FIAAmicusBrief_0106.pdf.

D. Petitioner's Clearing Activities Did Not Constitute Transactions On Or Subject To The Rules Of A Contract Market

In a further effort to find an exchange "transaction" that would give rise to standing, Petitioner points to its involvement in the trading process as a clearing broker. *See* Pet. at 24-25. As a clearing broker, Petitioner dealt with the clearinghouse NYCC and cleared customer trades, subject to NYCC's rules. *See* Pet. App. at 11a, 24a. However, this argument fails because NYCC is a clearing organization, not a board of trade or contract market.

Under Section 22(b) as it existed when this case began, transactions subject to the rules of a clearinghouse did not give rise to standing. In particular, the language of the CEA, as it then existed, demonstrates that, when Congress drafted Section 22, it deliberately distinguished between "contract markets" and "licensed boards of trade" on the one hand, and on the other hand, "clearing organizations" with which FCMs interact in their capacity as clearing members. Section 22(b)(1)(A) itself reflects this conscious decision by the 1982 Congress to distinguish between these entities.[10] *See* Pet. at 2.

In the first sentence of Section 22(b)(1)(A), Congress listed contract markets, clearing organizations, and licensed boards of trade as three distinct entities. *See* 7 U.S.C. § 25(b)(1)(A) (1999). However, later in the same subparagraph, Congress explicitly stated that plaintiffs only have standing if they "engaged in any transaction on or subject to the rules of such contract market or licensed board of trade." *Id.* By omitting "clearing organizations" from this latter clause, Congress

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[10] Other provisions contained in the pre-2000 version of the CEA make it clear that Congress distinguished clearing organizations from exchanges. *See, e.g.*, 7 U.S.C. §§ 2a(vi)(II), 6d, 10a (1999) (referring separately to contract markets and clearing organizations).

intentionally excluded FCM clearing activities from the term "transactions" as that term is used in the statute. This makes sense because "transactions on a contract market" refers to trades, not to clearing.

Congress' careful identification of parties in Section 22(b)(1)(A) further confirms that the same word "transactions," as used in Section 22(a)(1), also refers to trades (and not clearing activities), as trades are conducted on an exchange, and trades are not transactions on or subject to the rules of a clearing organization. Thus an examination of the statute itself demonstrates that Petitioner's clearing of its customer trades through the clearinghouse subject to NYCC's rules did not afford it standing under the CEA.

The Petitioner apparently contends that its customer agreement with First West was somehow a "transaction" subject to the rules of the clearinghouse, NYCC, which Klein incorrectly seeks to characterize as a "contract market." *See* Pet. at 6, 7, 27. The argument is without merit. NYCC is a clearing organization, not a contract market. As was made perfectly clear in CEA § 5 as in effect at the relevant time, a "contract market" is a "board of trade" designated as a contract market by the CFTC. Similarly, Section 22(b)(1)(A) clearly distinguishes between a "contract market" and a "clearing organization."[11] 7 U.S.C. § 25(b)(1)(A). The only "contract market" at issue in this case was NYFE, which was where First West and Eisler did their trades. Klein then cleared its customers' trades through the clearinghouse NYCC, which was not then, and is not today, a contract market or a board of trade.

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[11] This distinction was preserved in the 2000 amendments to the CEA by explicitly creating a brand new regulatory regime specifically applicable only to clearing organizations in what is now Section 5b of the Act. *See* 7 U.S.C. § 7a-1 (2000).

Accordingly, any losses suffered by an FCM as a result of its role as a clearing broker for a customer, including the credit losses suffered by Petitioner, are not losses that "result from [a] transaction" that is subject to a rule of any contract market as defined by Section 22(b). Indeed, even if a "transaction" with a clearinghouse alone could support standing, here the Petitioner dealt with the clearinghouse as agent for its customer. Petitioner's losses were credit losses suffered as a result of its customer's failure to reimburse it for margin payments due to the Petitioner under its customer agreement.

E. The Legislative History Refutes Petitioner's Assertion That Congress Intended To Confer Standing On Market Participants Who Did Not Trade

The court of appeals held that Petitioner as a non-trader FCM lacked standing under Section 22(b) to pursue claims against the NYBOT Respondents. The court of appeals reached this result based on the plain language of the statute, without resort to legislative history. *See* Pet. App. at 11a. However, notwithstanding Petitioner's arguments, the court of appeals' holding is entirely consistent with the legislative history of Section 22.

Citing a House "Conference" Report, Petitioner contends that it should have standing as a "market participant," and that Congress intended to deny the private right of action only to "'members of the public who did not partic[ipate] in the market and claimed to be injured in commercial transactions by declines in commodity prices.'"[12] Pet. at 28-29 (*quoting*

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[12] It appears the Petition mis-cited the relevant page of the House Report (incorrectly identified as a "Conference" report), as the phrase "market participants" does not appear on page 57 of the House Report. The quote actually appears at page 145, which sets forth the Committee on Agriculture's report that summarizes amendments that became Section

H.R. Rep. No. 97-565(I), at 57 (May 17, 1982)) (emphasis omitted). Petitioner argues that because it engaged in clearing activities or otherwise acted as an agent for First West, it was a "market participant."

The legislative history of the 1982 amendments, however, makes clear that "market participants" refers to "commodity investors" and "investors in futures markets" (*i.e.*, customers or traders), and thus that traders are the only parties who may bring a private cause of action against a board of trade, contract market or clearing organization. Specifically, when the principal proponent of the legislation, Rep. Dan Glickman, proposed amendments to the CEA that became Section 22, the Congressman said he did so to "[a]llow *commodity investors* who suffer actual damages the right to sue both brokers and exchanges for violations of the Commodity Exchange Act." H.R. Rep. No. 97-565(I), at 239 (emphasis added). He went on to add: "Without [these amendments], I feel that *investors in futures markets* will face potentially greater and greater uncertainty and risk." *Id.* at 240 (emphasis added).

This legislative history thus accords with the court of appeals' holding, and confirms that Congress intended to limit the universe of potential plaintiffs to customers or traders who sustained losses as the result of their transactions on a contract market.[13] As the court of appeals stated, "Klein's loss was a credit loss, not a trading loss." Pet. App. at 12a.

22, which were proposed by Rep. Dan Glickman and ultimately enacted by Congress.

[13] Likewise, the legislative history states: "[t]he cause of action in these cases would be restricted to cases where the plaintiff has engaged in a regulated *commodity transaction* and could show that there was bad faith in failing to take the necessary action." H.R. Rep. No. 97-565(I), at 57 (emphasis added).

II. THE COURT OF APPEALS' INTERPRETATION OF SECTIONS 22(a) AND 22(b)(1) IS CONSISTENT WITH PRINCIPLES OF STATUTORY CONSTRUCTION

Petitioner argues that the court of appeals "plainly misread" Section 22(b) when it purportedly grafted the Section 22(a)(1)(A)-(D) enumerated categories standing requirements onto suits brought under Section 22(b)(1). *See* Pet. at 26. Specifically, Petitioner contends that unlike Section 22(b)(2) and (b)(3), Section 22(b)(1) omits the phrase "engaged in any transaction specified in subsection (a) of this section," and instead defines a proper plaintiff merely as "a person who engaged in 'any' transaction on or subject to the rules of such contract market or licensed board of trade." *Id.* at 27.

The statute and the parties who were defendants-appellants in the court of appeals make that court's holding readily understandable. Petitioner Klein named various categories of defendants in its complaint: its customer First West, several individuals (Eisler and other exchange officials), contract markets (NYFE, NYCE), the clearing organization (NYCC), and the exchange holding company (NYBOT). Notably, the Petition fails to address the fact that the court of appeals' ruling applied to all of these different individual and corporate defendants, including Eisler, First West, and the NYBOT Respondents and the individuals who worked for them.[14]

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[14] Klein twice makes the erroneous assertion that it did not appeal to the court of appeals from the district court's decision dismissing the action against Eisler and First West. *See* Pet. at ii, 12 n.5. We assume counsel's error is the result of confusion, not craft. In particular, we trust that counsel on the Petition is not attempting to advance its Section 22(a)(1)(A)-(D) enumerated categories argument by misleading this Court as to whether the appeal below included Eisler and First West (who Klein concedes may only be sued by a plaintiff that falls within the enumerated categories) and thus attempting to obscure the fact that the reference by the court of

It is undisputed that the enumerated categories in Section 22(a)(1)(A)-(D) applied to Klein's claims against Eisler and First West; indeed, Klein does not seek review of that decision. The text of the court of appeals' holding did not distinguish with any precision between Eisler, First West, the individual defendants, the exchange and the NYCC. *See, e.g.*, Pet. App. at 8a-12a. Instead, the opinion broadly stated that "[t]he text of [Sections 22(a) and (b)] requires that a putative plaintiff fall within one of the four required relationships set forth in [Section 22(a)(1)(A)-(D)]." *Id.* at 7a-8a. Placed in context, it is apparent that the court of appeals was addressing the defendants as a whole.

Contrary to Petitioner's statutory construction analysis, by omitting an explicit reference to the subsection (a)(1)(A)-(D) categories in subsection (b)(1), Congress did *not* signal an intention to broaden the class of potential plaintiffs who can bring claims against exchanges to include non-trading FCMs. Instead, Congress, by its omission of a cross-reference, deliberately *narrowed* the class of plaintiffs who can bring claims against contract markets, clearing organizations and licensed boards of trade, and in pursuit of this goal, protected these entities from suits by non-traders.

The legislative history of Section 22 and the court of appeals' decision (even as described by Petitioner) is consistent with this reading of Section 22(b) and the conclusion that Congress intended to require prospective plaintiffs to clear *both* the hurdles established by Section 22(a)(1)(A)-(D) *and* the requirement of an exchange transaction when pursuing a claim against a board of trade, contract market or clearing organization under Section 22(b). *See* H.R. Rep. No. 97-565(I), at 145. Specifically, the legislative history explains that the Glickman Amendment, which Congress ultimately

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appeals to those categories included reference to Eisler and the other individual defendants.

adopted and enacted as Section 22, "authorized an action for damages by a person *who engaged in the transactions listed above* [referring back to the Section 22(a)(1)(A-D) categories] against . . . a contract market (or clearing organization) that failed to enforce rules that served as a basis for its designation." *Id.* (emphasis added). Thus the construction advanced by the court of appeals is not inconsistent with the statute; rather, it is consistent with both the statutory text and the legislative history.[15]

Finally, even if this Court were to disagree with this aspect of the court of appeals' statutory construction, the result reached below is still correct. As set forth above and as numerous courts have held, Section 22(b) creates a cause of action only for traders on a contract market who are injured in the course of trading. *See American Agric.*, 977 F.2d at 1153. As a matter of law, non-traders like Petitioner lack standing to pursue claims under Section 22(b). *See* Point I.A.2, *supra*.

III. GRANTING THE PETITION WOULD BE IMPROVIDENT AS THE STATUTORY PROVISION THAT IS THE SUBJECT OF THE PETITION HAS BEEN AMENDED

In an effort to turn a decision dismissing a complaint by one failed business into an event that altered the legal landscape, Petitioner argues that the court of appeals' decision, if left unreviewed, would have an adverse effect on futures markets because the decision shifts market risk away

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[15] For example, a Section 22(a)(1)(A) plaintiff could be a person who held a futures position but did not engage in further trading based on trading advice from the defendant for a fee. Such a plaintiff could sue a trading advisor but could never be a plaintiff with standing to sue an exchange, because such plaintiff did not engage in any transaction on or subject to the rules of the exchange. In the alternative, a trader would have standing to sue a clearinghouse, if bad faith conduct by the clearinghouse caused the plaintiff's trading losses.

from the boards of trade and clearinghouses, and on to FCMs.[16] *See* Pet. at 14-19. Petitioner argues that these developments will adversely affect the national economy by increasing investors' trading costs. *Id.* Petitioner further argues that the "ruling below makes commodity exchanges unaccountable to futures commission merchants for bad faith violations of law." *Id.* at 17.

These concerns are highly speculative at best, but in any event they do not address the fact that Congress in the version of Section 22(b) in effect at the relevant time provided that standing was limited to "a person who engaged in any transaction on or subject to the rules of such contract market." 7 U.S.C. § 25(b)(1). Petitioner's assertion that the court of appeals' decision will have a profound adverse impact on the national economy falls flat, especially because Congress in late 2000 amended the statutory provision that Petitioner claims the court of appeals misconstrued.

In December 2000, Congress amended Section 22(b), and recast the category of persons with standing to bring an action under Section 22(b) to include those "who engaged in any transaction on or subject to the rules of such registered entit[ies]."[17] 7 U.S.C. § 25(b)(1) (2000). At the same time, Congress defined "registered entities" to include clearing organizations, like the NYCC. This amendment was not, as Petitioner contends, "merely technical." Pet. at 1 n.1. Rather, this amendment renders moot any general need to review the court of appeals' decision, because the decision's precedential significance is highly limited. Any FCM in an action commenced under the statute as revised in December 2000 may

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[16] Of course, in this case, Klein's losses stemmed not from market risk but from customer credit risk.

[17] Similarly, 7 U.S.C. § 7(b)(3)(C), to which Klein cites to describe Congress' vision of the role of an FCM, *see* Pet. at 5, 22, was added in December 2000, *after* this action was commenced. Thus, it does not say anything about how Congress regarded FCMs prior to December 2000.

argue that its clearing activities are "subject to the rules of a registered entity" (which now include clearing organizations), and therefore can be the basis for a private right of action against a board of trade, contract market or clearing organization.[18]

Other policy arguments made by Petitioner are based on modern concerns, and are irrelevant, as they are advanced in support of Petitioner's strained interpretation of statutory language enacted by Congress twenty-five years ago. For example, the Petition states that "today" exchanges face conflicts of interest issues because, among other things, they must "generate returns for their owners." Pet. at 20. The circumstances that exist today, however, had no bearing on the scope of the private right of action that the 1982 Congress enacted in Section 22(b), at a time when virtually all commodity futures exchanges were not-for-profit membership organizations. Petitioner's policy arguments therefore have no substance, particularly because the statute at issue no longer provides what it did when this action was commenced.

Petitioner's final argument, that the court of appeals' decision absolves exchanges of liability for wrongdoing, ignores the role of the Commodity Futures Trading Commission (the "CFTC") in policing the futures industry. Enforcement of the CEA is the primary function of the CFTC. In fact, in 1982, at the same time it added CEA § 22, Congress enhanced the powers of the CFTC to take action against violations.[19] As demonstrated by the three separate proceed-

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[18] The NYBOT Respondents submit that the term "transaction" as used by Congress in the amended version of Section 22(b) is still limited to trades, and that Congress did not intend to broaden the categories of plaintiffs who could bring claims under the CEA to include clearing members who suffered credit losses.

[19] For example, in the case of contract markets and their officials, the CFTC was empowered in Sections 5b and 6(b) to suspend for six months and even terminate the designation of a contract market. *See* 7 U.S.C.

ings initiated by the CFTC in the wake of Petitioner's collapse, the CFTC's enforcement role served its appropriate function in this case.[20]

In sum, the precedential effect of the court of appeals' interpretation of the prior version of Section 22(b) is minimal. Standing for potential plaintiffs under the CEA is now governed by a revised version of the statute, and future plaintiffs must satisfy the standing requirements under the statute as amended. A decision so limited in scope is not a matter of importance requiring a writ of certiorari. For this reason as well, Klein's Petition should be denied.

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§§ 7b, 8 (1999). In Section 6b, the CFTC was empowered to impose fines against contract markets and their officials of up to $500,000 per violation and impose cease and desist orders. *See* 7 U.S.C. § 13a (1999). In Section 6c, the CFTC was empowered to bring court actions for injunctions and civil penalties in an amount equal to the greater of $100,000 or triple the monetary gain that resulted from the violation. *See* 7 U.S.C. § 13a-1 (1999).

[20] *See* Div. of Trading & Markets, *Report on Lessons Learned from the Failure of Klein & Co. Futures, Inc.* (C.F.T.C. July 2001), available at http://www.cftc.gov/files/tm/tmklein_report071101.pdf; Order Instituting Proceedings Pursuant to Section 5b, 6(b) and 6b of the Commodity Exch. Act, Making Findings and Imposing Remedial Sanctions, *In re New York Futures Exch., Inc.*, Docket No. 01-13 (C.F.T.C. July 11, 2001), available at http://www.cftc.gov/files/enf/01orders/enfnyfe.pdf; Order Making Findings and Imposing Remedial Sanctions, *In re Eisler & First West Trading, Inc.*, Docket No. 01-14 (C.F.T.C. Jan. 20, 2004), available at http://www.cftc.gov/files/enf/04orders/enfeisler-order.pdf.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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