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 Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF OF *AMICUS CURIAE* FUTURES INDUSTRY ASSOCIATION, INC. IN SUPPORT OF PETITIONER

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Pursuant to this Court's Rule 37.2, *amicus curiae* respectfully files this brief in support of the petition for certiorari.*

STATEMENT OF INTEREST OF *AMICUS CURIAE*

The futures industry is a major engine of the American economy: every day, more than *$5 trillion* worth of futures contracts and related options are traded on the futures markets in this country. The Futures Industry Association (FIA) is a national trade association for that industry. Its regular membership consists of 35 of the Nation's largest futures brokerage firms, and its associate membership consists of approximately 150 firms involved in virtually all other segments of the industry. FIA regular members execute customer orders for, and provide the financial guarantees underwriting, more than 90% of all transactions on the United States futures markets. Petitioner Klein is not an FIA member; respondents Board of Trade of the City of New York and New York Clearing Corporation are associate members. Neither regular nor associate members are bound by the views taken by FIA as *amicus*.

FIA has a strong interest in any case that affects the futures industry, and has participated as *amicus curiae* in several such cases, including *eBay, Inc. v. MercExchange, L.L.C.*, 126 S. Ct. 733 (2005), *Dunn v. CFTC*, 519 U.S. 465 (1997), and *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353 (1982). FIA has a particularly strong interest in cases involving the interpretation of the Commodity Exchange Act (CEA), the federal statute that

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* Pursuant to this Court's Rule 37.6, *amicus* states that no counsel for a party authored this brief in whole or in part, and no person or entity other than *amicus* has made a monetary contribution to the preparation or submission of this brief. All parties have consented to the filing of this brief *amicus curiae*, and their consent letters are on file with the Clerk's Office.

establishes the regulatory framework governing the futures industry and the relevant regulatory agency, the Commodity Futures Trading Commission (CFTC).

This case presents such an issue. As explained below, the Second Circuit clearly misinterpreted the CEA's plain language to deprive futures commission merchants like petitioner of any cause of action against registered entities like respondents New York Futures Exchange, Inc., Board of Trade of the City of New York, and New York Clearing Corporation. That error affects the interests not only of the parties to this case, but of the entire futures industry, by exposing futures commission merchants to substantial financial harm resulting from bad faith misconduct by registered entities without any remedy. Because that decision threatens to destabilize those firms whose funds provide the financial backbone for this important industry, FIA sought (and obtained) leave to file a brief *amicus curiae* in the Second Circuit in support of the petition for rehearing and rehearing *en banc*, and now files this brief in support of the petition for certiorari.

REASON FOR GRANTING THE WRIT

The Second Circuit Clearly Erred, And Destabilized The Nation's Futures Industry, By Stripping Futures Commission Merchants Of Their Statutory Cause Of Action Against Registered Entities.

As a threshold matter, there can be no real dispute that the Second Circuit erred by construing the CEA to deprive futures commission merchants like petitioner of a cause of action against registered entities like respondents New York Futures Exchange, Inc., the Board of Trade of the City of New York, and New York Clearing Corporation. Such a cause of action is expressly conferred by Section 22 of the CEA, codified at 7 U.S.C. § 25, which authorizes claims against "[a] registered entity that fails to enforce any bylaw, rule, regulation, or resolution that it is required to enforce" by "a person who engaged in any

transaction on or subject to the rules of such registered entity 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." *Id.* § 25(b)(1).

That is the beginning and the end of this case. Respondents New York Futures Exchange, Inc., Board of Trade of the City of New York, and New York Clearing Corporation are "registered entit[ies]." *See id.* § 1a(29) (defining "registered entity" to include "a board of trade designated as a contract market" and "a derivatives clearing organization"). Petitioner is "a person who engaged in any transaction on or subject to the rules of such registered entit[ies]," *id.* § 25(b)(1); indeed, petitioner engaged in transactions subject to the rules of no fewer than *three* "registered entit[ies]," respondents Board of Trade of the City of New York, New York Futures Exchange, and New York Clearing Corporation. Petitioner alleges that respondents "fail[ed] to enforce any bylaw, rule, regulation, or resolution that [they are] required to enforce," and that as a result petitioner suffered "actual losses … caused by such failure to enforce or enforcement of such bylaws, rules, regulations, or resolutions." *Id.*

The Second Circuit could not, and did not, deny any of these straightforward points. Rather, the Second Circuit began its analysis by correctly noting that "Section 22 includes two types of claims": "Section 22(a) relates to claims against persons *other* than registered entities and registered futures associations," whereas "Section 22(b) deals with claims against [registered] entities and their officers, directors, governors, committee members and employees." Pet. App. 7a (emphasis added; citing 7 U.S.C. §§ 25(a), (b)). This case, as the Second Circuit recognized, involves a Section 22(b) claim: petitioner is suing registered entities and individuals affiliated with those entities. *See* Pet. App. 8-9a; 11a. Such a claim, as the Second Circuit again recognized, is "available only to

a private litigant 'who engaged in ... transaction[s] on or subject to the rules of' a contract market.'" Pet. App. 8a (quoting 25 U.S.C. § 25(b)(1)-(3)).

The Second Circuit, however, never analyzed the critical issue whether petitioner is "a person who engaged in any transaction on or subject to the rules of" a contract market or other registered entity, 7 U.S.C. § 25(b)(1), within the meaning of Section 22(b). Instead, the Second Circuit simply assumed without analysis that a person pursuing a claim under Section *22(b)* is subject to the limitations applicable to a person pursuing a claim under Section *22(a)*. *See* Pet. App. 7-8a ("The text of the two subdivisions requires that a putative plaintiff fall within one of the four required relationships set forth in § 22(a)(1)(A-D)."); Pet. App. 9a ("[Petitioner] does not fall within any of the required subdivisions of § 22(a)(1)(A)-(D).").

That is a complete non sequitur. Sections 22(a) and (b) create different causes of action by different plaintiffs against different defendants. Section 22(a) creates a cause of action against non-registered entities (*i.e.*, intermediaries like traders and brokers), *see* 7 U.S.C. § 25(a), whereas Section 22(b) creates a cause of action against registered entities, including futures contract markets, *see id.* § 25(b). The requirements of the cause of action under Section 22(a) are set forth in Section 22(a), while the requirements for the cause of action under Section 22(b) are set forth in Section 22(b). Nothing in the statute remotely purports to import the requirements for a Section 22(a) claim into Section 22(b), and there is no basis in law or logic for doing so. *See*, *e.g.*, *Russello v. United States*, 464 U.S. 16, 23 (1983) ("[W]here Congress includes particular language in one section of a statute but omits it in another section of the same Act, it is generally presumed that Congress acts intentionally and purposely in the disparate inclusion or exclusion.") (internal citation omitted); *see also Omni Capital Int'l, Ltd. v. Rudolf Wolff & Co., Ltd.*, 484 U.S. 97, 106 (1987)

(applying this principle to the CEA). The wholesale importation of Section 22(a) requirements into Section 22(b) is especially problematic because specific provisions of Section 22(b) expressly incorporate the provisions of Section 22(a), underscoring that Congress knew perfectly well how to accomplish such incorporation where it wished to do so. *See* 7 U.S.C. § 25(b)(2) (referring to "a person that engaged in any transaction specified in subsection (a) of this section"); *id.* § 25(b)(3) (same).

The Second Circuit did not dispute any of the foregoing canons of interpretation, or otherwise seek to justify its importation of Section 22(a)'s requirements into Section 22(b). Rather, the court appears to have taken that fateful step wholly by inadvertence. Needless to say, that is no way to construe any statute, much less the statute governing one of the most important industries in this Nation. If the Second Circuit had a reason for importing Section 22(a)'s requirements into Section 22(b), the court at a minimum should have disclosed that reason.

Respondents tried to confuse matters at the rehearing stage below by arguing that this case is governed by statutory provisions that were amended in 2000. But the 2000 amendments invoked by respondents did not alter the statute in any way material here: in relevant part, those amendments substituted the term "registered entity" for the previous term "contract market," but under settled pre-2000 law, each respondent that is now a "registered entity" was covered by the term "contract market." *Compare* 7 U.S.C. § 25(b)(1) (2007 ed.) with 7 U.S.C. § 25(b)(1) (1994 ed.). In any event, notwithstanding respondents' theory that this case should be decided under the pre-2000 statute, the Second Circuit clearly decided the case under the post-2000 statute, *see* Pet. App. 7-9a & nn.3, 4, which is precisely why the decision below has a continuing impact on the industry and why *amicus* is here.

The petition well explains how the Second Circuit's erroneous conception of the role of futures commission merchants conflicts with the understanding of the other circuit in which CEA cases tend to arise, the Seventh Circuit (which is home to the Nation's two largest futures exchanges, the Chicago Board of Trade and the Chicago Mercantile Exchange). *See* Pet. 23-25. But above and beyond that conflict, the petition warrants review (and possible summary reversal) given its impact on the stability of the Nation's futures markets.

To understand the gravity of the Second Circuit's error, it is necessary to understand the basic operation of the futures and related options markets. Individual customers generally do not buy or sell directly in those markets; rather, they necessarily carry out their transactions through a futures commission merchant, like petitioner here. The best capitalized of these merchants become "clearing firms" that deposit over $50 billion daily with clearing houses, like respondent New York Clearing Corporation, to ensure against defaults. Such clearing firms include some of the Nation's best-known financial institutions, such as Bear, Stearns & Co. Inc., Calyon Financial Inc., Citigroup Global Markets Inc., Fimat USA LLC, Goldman, Sachs & Co., J.P. Morgan Futures Inc., Lehman Brothers Inc., Merrill Lynch Pierce Fenner & Smith Inc., Morgan Stanley, and UBS.

The Second Circuit displayed a fundamental misunderstanding of the industry by asserting that futures commission merchants like petitioner have "no financial interest" in their trades, and do not "face[] essentially the same risks as a buyer or seller of commodities contracts." Pet. App. 12a. To the contrary, as this Court has recognized, such merchants are "essential participants" in futures markets precisely because they are required to guarantee their customers' performance and to honor the contracts if their customers default. *Curran*, 456 U.S. at 359-60; *see also Leist v. Simplot*, 638 F.2d 283, 287 (2d Cir. 1980) (Friendly, J.)

(describing futures commission merchants as "principals in trading transactions").

Because a futures commission merchant guarantees its customers' performance, it makes perfect sense for Congress to have given such merchants (as well as their customers) a cause of action against registered entities that cause them losses as a result of bad-faith misconduct. Indeed, this case underscores why it would make no sense to limit the cause of action to customers, since the customer here (Norman Eisler, then chairman of the New York Futures Exchange) is the very person who allegedly abused his exchange office to manipulate market prices and then defaulted on his obligations. *See* Pet. 9-11. Precisely because petitioner was required to honor the contracts it entered on Eisler's behalf, it suffered massive losses (and indeed was forced out of business) after Eisler defaulted. Given the financial liability of futures commission merchants in futures transactions, the futures markets in this Nation will be seriously undermined if such merchants can be left holding the bag as the result of bad faith misconduct committed by officials of registered entities.

The decision below, in flat disregard of Section 22(b), shifted the financial risk of misconduct away from the registered entities charged with enforcing the rules onto the futures commission merchants that are engaged in every futures transaction, thereby creating a disincentive for these firms to underwrite the very speculation and risk-taking upon which the futures markets depend. *See, e.g.*, *Curran*, 456 U.S. at 359-60 (noting that futures commission merchants "have an interest in maximizing the activity on the exchange"). If futures commission merchants are left without any meaningful recourse for losses caused by bad faith misconduct by registered entities, they will be less willing to risk their capital to finance needed trading activity. Since futures commission merchants are engaged in every transaction in the futures markets, this reluctance could decrease the

overall liquidity and depth of those markets, and result in greater fluctuations in the prices of basic commodities contrary to the national interest. *See, e.g.*, *id.* at 358.

Given that the decision below is indefensible as a matter of law and disastrous as a matter of policy, this Court should not allow the decision to stand. Accordingly, this Court should grant the petition and either set the case for plenary review or summarily reverse the decision below. At the very least, this Court should call for the views of the Solicitor General, who can speak for the CFTC on this issue of vital importance to such an important segment of the Nation's economy.

CONCLUSION

For the foregoing reasons, this Court should grant the petition for writ of certiorari, and either set the case for plenary review or summarily reverse the decision below.

Respectfully submitted,

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