No. 04-198

In the Supreme Court of the United States

R.J. FITZGERALD & CO., INC., ET AL., PETITIONERS

v.

COMMODITY FUTURES TRADING COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether an extreme departure from the standards of ordinary care, that presents a danger of misleading customers that is either known to the defendant or so obvious that the defendant must have been aware of it, satisfies the scienter requirement for commodities fraud under 17 C.F.R. 33.10.

2. Whether the court of appeals applied an incorrect standard of appellate review or an incorrect legal standard in determining whether petitioners had a duty to disclose that at least 95% of their customers were losing money.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 3a-44a) is reported at 310 F.3d 1321. The opinion of the district court (Pet. App. 45a-76a) is reported at 173 F. Supp. 2d 1295.

JURISDICTION

The judgment of the court of appeals was entered on October 29, 2002. A petition for rehearing was denied on April 12, 2004 (Pet. App. 1a-2a). On June 29, 2004, Justice Kennedy extended the time within which to file a petition for a writ of certiorari to and including August 10, 2004, and the petition was filed on that date. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Petitioners Raymond Fitzgerald and Leiza Fitzgerald operated petitioner R.J. Fitzgerald & Co. (RJFCO), a commodities brokerage firm "designed specifically to deal with smaller, less experienced customers." Pet. App. 17a n.8. Petitioners attracted such customers in part through a television commercial and a seminar. The commercial, which ran on the cable network CNBC in March 1998, encouraged investors to reap large profits on commodity futures and options on commodity futures based on the weather:

> Investors, El Nino is upon us, and its effect on world crops could mean huge profits in the grain markets. With giant developing nations, such as China and Russia badly in need of grains and world grain supplies put to the test, conditions may exist for profits as high as 200 to 300 percent. * * *
>
> Thus far, El Nino has struck where expected, and if patterns continue, the effects could be devastating. Droughts, floods and other adverse conditions could dramatically alter the supply and demand dynamics of the corn market, but timing is the key. Call R.J. Fitzgerald now for all of the data on this potentially profitable investment.
>
> Option investing involves a high risk of loss and only risk capital should be used.
>
> The potential of the corn market may never be greater. Tight U.S. reserves coupled with domestic and worldwide demand could be the formula for a trade you won't want to miss. Find out how as little as $5,000 could translate into profits as high as 200 to

> 300 percent. Call R.J. Fitzgerald today, 1-800-881-1955.

Gov't C.A. R.E., Tab 5; see Pet. App. 7a-8a.

After the commercial stopped running, the National Futures Association (NFA), an industry self-regulatory organization, informed Raymond Fitzgerald that the commercial was misleading in that it overstated potential returns, gave the impression that weather events were inevitable, and downplayed the risk of loss. Raymond Fitzgerald responded that he had already discontinued the commercial. Pet. App. 8a.

At promotional seminars in 1998, RJFCO told potential customers that whether to invest in futures or options on futures depends on risk tolerance: "If you are highly aggressive and looking for unlimited profit potential as well as unlimited risk than [sic] it would be the futures. But most would like something less aggressive, something offering unlimited profit potential but limited risk—option trade [sic]." Pet. App. 9a-10a (brackets in original).

RJFCO illustrated this "unlimited profit potential" by explaining that over the previous 18 years, there had been an average increase "of 22 cents from the low to the high in the price range" of heating oil. Pet. App. 10a (internal quotation marks omitted). RJFCO represented that an investment of $5000 in a heating oil futures contract would result in $46,200 if there were a "22 cent move" in price. *Ibid.* In contrast, a customer who wanted "limited risk" through an options contract would receive "approximately 50% of that profit—46,200 divided by 2 equals $23,100." *Ibid.* (internal quotation marks omitted). With respect to risk, RJFCO explained that a " 'big reason' people lose money is 'greed,' and 'you will never go broke taking a profit, just take it one piece at a time.'" *Id.* at 10a n.5.

In the course of these solicitations, RJFCO knew but did not disclose that over 95% of its customers were losing money. Pet. App. 19a n.9. Ultimately, the customers lost substantially all of the money they invested in petitioners' schemes. Pet. 4.

2. In 1999, the Commodity Futures Trading Commission (CFTC) commenced this enforcement action pursuant to the Commodities Exchange Act, 7 U.S.C. 1 *et seq.* (CEA or Act). The CFTC alleged, *inter alia*, that petitioners committed fraud by misrepresentation and omission of material facts in connection with the solicitation of commodity futures transactions, in violation of 17 C.F.R. 33.10, which provides:

> It shall be unlawful for any person directly or indirectly:
>
> (a) To cheat or defraud or attempt to cheat or defraud any other person;
>
> * * * * *
>
> (c) To deceive or attempt to deceive any other person by any means whatsoever in or in connection with an offer to enter into, the entry into, the confirmation of the execution of, or the maintenance of, any commodity option transaction.

3. In 2001, a bench trial was held before a magistrate judge. During the trial, the magistrate judge granted a "directed verdict" for petitioners on some of the CFTC's claims, including its claims that petitioners violated the Act by airing the commercial and failing to disclose the firm's loss record to potential customers. At the close of trial, the magistrate judge ruled in petitioners' favor on

the remaining claims, including the claim that petitioners violated the Act by conducting the seminars. Pet. App. 5a-6a.

4. The Eleventh Circuit reversed, and held that the undisputed facts establish fraud as a matter of law. Pet. App. 3a-44a. The court of appeals explained that to establish liability, the CFTC must prove three elements: a misleading statement or omission; materiality; and scienter. *Id.* at 12a. In analyzing these elements, the court was "guided by the principle that the CEA is a remedial statute that serves the crucial purpose of protecting the innocent individual investor—who may know little about the intricacies and complexities of the commodities market—from being misled or deceived." *Id.* at 13a.

The court first explained that "[w]hether a misrepresentation has been made depends on the 'overall message' and the 'common understanding of the information conveyed.'" Pet. App. 12a (quoting *Ham-mond* v. *Smith Barney, Harris Upham & Co.*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,617, at 36,657 & n.12 (Mar. 1, 1990)). Applying that standard, the court concluded that the television commercial aired by petitioners is deceptive as a matter of law because it "overemphasizes profit potential and downplays risk of loss, presenting an unbalanced image of the two." *Id.* at 13a. Specifically, the commercial suggests that "truly enormous profits (200-300%) can be made on options on futures contracts by looking at known and expected weather patterns," and "[a]gainst these highly alluring statements is only boilerplate risk disclosure language." *Id.* at 13a-14a.

The court of appeals held that petitioners' misrepresentations were material because "[i]t is too obvious for debate that a reasonable listener's choice-making process would be substantially affected by emphatic statements on profit potential ('200-300%') and the suggestion that known and expected weather events are the vehicle for achieving those enormous profits." Pet. App. 15a.

The court followed circuit precedent holding that "scienter is established if Defendant intended to defraud, manipulate, or deceive, or if Defendant's conduct represents an extreme departure from the standards of ordinary care." *Id.* at 12a. The court elaborated:

> [S]cienter is met when Defendant's conduct involves "highly unreasonable omissions or misrepresentations . . . that present a danger of misleading [customers] which is either known to the Defendant or so obvious that Defendant must have been aware of it."

Ibid. (quoting *Ziemba* v. *Cascade Int'l, Inc.*, 256 F.3d 1194, 1202 (11th Cir. 2001)). Under this standard, the court concluded that petitioners acted recklessly in airing the commercial because settled precedents left no doubt that the commercial was deceptive, and "Defendant, as a federally registered professional, knowledgeable in the nuances and complexities of the industry, deviated in an extreme manner from the standards of ordinary care." *Id.* at 15a.

The court of appeals then concluded that the promotional seminar was fraudulent for the foregoing reasons and an additional one: it "suggests that profits on options on futures contracts * * * are proportionately related to the cash market," when in fact they are not. Pet. App. 18a. Finally, the court of appeals held that petitioners fraudulently failed to disclose that more than 95% of the firm's clients lost money in the types of investments petitioners advertised. Pet. App. 19a. Relying on precedents holding that a "duty to disclose arises where a 'defendant's failure to speak would render the defendant's *own* prior speech misleading or deceptive,'" the court held that "[i]t is misleading and deceptive to speak of 'limited risk' and '200-300' percent profits without also telling the reasonable listener that the overwhelming bulk of firm customers lose money." *Id.* at 19a-20a (quoting *Ziemba*, 256 F.3d at 1206).

Judge Tjoflat wrote a concurring opinion stressing that petitioners "knew that by trumpeting enormous returns and downplaying the risk involved, a reasonable (if unsophisticated) investor would be enticed to make a bet that he would not otherwise make were the full picture disclosed." *Id.* at 26a. The concurrence concluded: "Don't make an active attempt to instill in the investor a grossly inaccurate picture of the risk-to-reward ratio. That is the rule in this case—a rule I find to be abundantly clear." *Ibid.*

Judge Wilson dissented. Pet. App. 26a-44a. Noting that "[n]o customer suffered a loss beyond his or her initial investment," the dissent interpreted the evidence to show that petitioners "did not misrepresent or guarantee profits and in fact disclosed the amount of risk involved." *Id.* at 43a & n.6.

ARGUMENT

Although petitioners contend that the courts of appeals are divided on whether "objective" recklessness satisfies the scienter requirement for commodities and securities fraud, every circuit to address the question has adopted the identical legal standard. In this case, the undisputed facts demonstrate scienter under any plausible standard—petitioners intentionally employed practices that have repeatedly been recognized to be inherently deceptive, and intentionally withheld information that would have helped to warn their targets of the deception. Petitioners cite no case from any circuit that tolerates such misconduct, and their other assertions of error are based on misstatements of the record. Further review is not warranted.

1. a. There is no conflict regarding the scienter requirement for commodities or securities fraud. The court of appeals held that "scienter is met when Defendant's conduct involves 'highly unreasonable omissions or misrepresentations . . . that present a danger of misleading [customers] which is either known to the Defendant or so obvious that Defendant must have been aware of it.'" Pet. App. 12a (quoting *Ziemba* v. *Cascade Int'l, Inc.*, 256 F.3d 1194, 1202 (11th Cir. 2001)). The court also emphasized that to be reckless, a defendant's conduct must "represent[] an extreme departure from the standards of ordinary care." *Ibid.*

The petition (Pet. 11-17) recognizes that the Second, Sixth, and Seventh Circuits also follow this standard (which petitioners call "objective"), but contends that the District of Columbia, First, Fifth, and Ninth Circuits apply a different standard (which petitioners call "subjective"). Not so. Each of those circuits has expressly adopted the same standard applied here:

D.C. Circuit:

> The kind of recklessness required * * * is an "extreme departure from the standards of ordinary care, . . . which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious that the actor must have been aware of it."

SEC v. *Steadman*, 967 F.2d 636, 641-642 (D.C. Cir. 1992) (quoting *Sundstrand Corp.* v. *Sun Chem. Co.*, 553 F.2d 1033, 1045 (7th Cir.), cert. denied, 434 U.S. 875 (1977)).

First Circuit:

> Recklessness is a highly unreasonable omission, involving not merely simple, or even inexcusable[] negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers that is either known to the defendant or is so obvious the actor must have been aware of it.

SEC v. *Fife*, 311 F.3d 1, 9-10 (1st Cir. 2002), cert. denied, 538 U.S. 1031 (2003) (internal quotation marks omitted).

Fifth Circuit:

> Severe recklessness is limited to those highly unreasonable omissions or misrepresentations that involve not merely simple or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and that present a danger of misleading buyers or sellers which is either known to the defendant or is so obvious that the defendant must have been aware of it.

Broad v. *Rockwell Int'l Corp.*, 642 F.2d 929, 961-962 (5th Cir.) (en banc), cert. denied, 454 U.S. 965 (1981).

Ninth Circuit:

> [R]eckless conduct may be defined as highly unreasonable omission, involving not merely simple, or even inexcusable negligence, but an extreme departure from the standards of ordinary care, and which presents a danger of misleading buyers or sellers

> that is either known to the defendant or is so obvious that the actor must have been aware of it.

Hollinger v. *Titan Capital Corp.*, 914 F.2d 1564, 1569 (9th Cir. 1990) (en banc), cert. denied, 499 U.S. 976 (1991) (quoting *Sundstrand*, 553 F.2d at 1045).

Far from disagreeing with other circuits, these four circuits all derived their legal standard from the Seventh Circuit's decision in *Sundstrand*—which, according to the petition (Pet. 14-15), is on the *other* side of the supposed circuit split. See *Fife*, 311 F.3d at 9-10; *Steadman*, 967 F.2d at 641-642; *Hollinger*, 914 F.2d at 1569; *Broad*, 642 F.2d at 961-962. Conversely, the Eleventh Circuit has never disagreed with any of these four circuits, and indeed has favorably cited Fifth and Ninth Circuit cases on this point. See *McDonald* v. *Alan Bush Brokerage Co.*, 863 F.2d 809, 814 & n.10 (11th Cir. 1989); *Messer* v. *E.F. Hutton & Co.*, 847 F.2d 673, 678 (11th Cir. 1988).

b. Instead of reflecting the application of different legal standards, any differences in opinion writing among the cases reflect differences in the types of fraud alleged, and the facts adduced, in each case. In this case, petitioners intentionally made representations that are inherently deceptive. Pet. App. 13a-15a, 17a-19a. The thrust of both the commercial and the seminar was that investors could reap huge profits in reliance on weather patterns and seasonal demand shifts. *Id.* at 14a, 18a. CFTC and judicial precedents have repeatedly held that sales pitches along those lines are inherently deceptive because such facts are already incorporated into the prices of commodities futures. *Id.* at 14a (citing cases); cf. *Basic Inc.* v. *Levinson*, 485 U.S. 224, 246 (1988).

Petitioners compounded their deception by making profit illustrations that falsely assumed that changes in the price of a commodity produce proportional changes in the price of futures and options on futures of the commodity, again in the face of established legal precedent. See Pet. App. 18a. Petitioners even went so far as to hold out the allure of "unlimited profits" with only "limited risk," while failing to mention that 95% of their investors were losing money. *Id.* at 19a. Petitioners thereby engaged in blatant fraud.

On these facts, petitioners' protestations of good faith are unavailing, not because the court of appeals applied an "objective" instead of a "subjective" test, but because the deception was so obvious that petitioners—"federally registered professional[s], knowledgeable in the nuances and complexities of the industry"—must have known what they were doing. Pet. App. 15a; see *id.* at 26a (Tjoflat, J., concurring) ("The defendants in this case *knew* that by trumpeting enormous returns and downplaying the risk involved, a reasonable (if unsophisticated) investor would be enticed to make a bet that he would not otherwise make were the full picture disclosed.") (emphasis added).[1]

The cases cited by petitioners apply the same legal principles to different types of situations. In *CFTC* v. *Savage*, 611 F.2d 270 (1979), the Ninth Circuit explained that the defendant was "accused of prearranging trades that defrauded [a firm's] customers and of entering into offsetting trades with those customers' accounts. Such

[1] While petitioners contend (Pet. 6) that the court of appeals "did not address the testimonial and circumstantial evidence of subjective good faith," the court specifically addressed petitioners' evidence (Pet. App. 16a) and concluded that it could not overcome the obviousness of the deception here, as established by precedent.

action required that [the defendant] and [the firm] act in concert, concert that would require knowledge on the part of the participants." *Id.* at 283. Thus, the nature of the allegations required that the defendant have actual knowledge not only of his actions and representations (as here), but also that those actions were part of a broader manipulative scheme perpetrated by another.

Even so, the Ninth Circuit did not hold that a fact finder's evaluation of direct evidence of subjective intent is always "*essential*," as the petition suggests (Pet. 11). To the contrary, the court recognized that "[k]nowledge * * * exists when one acts in careless disregard of whether his acts amount to cheating, filing false reports, etc. That is, the element of knowledge cannot be precluded by ignorance brought about by willfully or carelessly ignoring the truth." *Savage*, 611 F.2d at 283. The court simply held, based on the record in that case, that "[w]e cannot say that the facts put forward in the CFTC affidavits raise inferences so reasonable as to defeat [defendant's] claims." *Ibid.*

A similar analysis applies to the D.C. Circuit's decision in *Steadman*, where the defendants, based on a faulty legal opinion, chose not to register under state Blue Sky laws. The SEC filed suit on the theory that the defendants fraudulently failed to disclose the illegality of their non-registration and to book contingent liabilities for penalties that might result from nonregistration. 967 F.2d at 638. Thus, the nature of the allegation required that defendants have actual knowledge not only of their bookkeeping, but also of their potential liability under state law. On the record in that case, the D.C. Circuit held that "the evidence does not permit a finding that [the defendant] actually knew the [legal] opinion was wrong *or was reckless in relying on it*." *Id.* at 642 (emphasis added). Nothing in *Steadman* is inconsistent with the Eleventh Circuit's conclusion that petitioners are liable for intentionally undertaking conduct that is inherently deceptive.

Petitioners also rely (Pet. 7, 12) on a subsequent D.C. Circuit decision, *Saba* v. *Compagnie Nationale Air France*, 78 F.3d 664 (1996), which addressed an airline's liability for damaged baggage under the Warsaw Convention. Even setting to the side the inappositeness of that context, the *Saba dicta* is fully consistent with the decision in this case because it states that "if it can be shown that a defendant gazed upon a specific and obvious danger, a court can infer that the defendant was cognitively aware of the danger and therefore had the requisite subjective intent." *Id.* at 669. The court then held that the danger that cargo wrapped by one company at one place would later be damaged when left outside in the rain by a different company at a different place was not sufficiently obvious. *Id.* at 670. While petitioners are correct that the *Saba* court discussed "subjective" intent, they are wrong to suggest that the D.C. Circuit held that it would never infer such intent from obviousness.

Nor has the First Circuit made such a holding. In *Rodriguez* v. *Montalvo*, 871 F.2d 163, 165 (1989), and *SEC* v. *MacDonald*, 699 F.2d 47, 51 (1983) (en banc), the First Circuit held only that evidence of the defendants' states of mind was relevant, admissible evidence. The First Circuit did not hold that recklessness can never be based on objective facts, notwithstanding a defendant's protestations of subjective good faith. Quite to the contrary, the First Circuit later held that a plaintiff "must demonstrate that the defendants acted with a high degree of recklessness *or* consciously intended to defraud," and ruled in favor of the plaintiff based on objective evidence. *Fife*, 311 F.3d at 9-10 (emphasis added).[2]

The Fifth Circuit cases cited by petitioners (Pet. 13) are even less apposite. In *Southland Securities Corp.* v. *INSpire Insurance Solutions, Inc.*, 365 F.3d 353, 366 (2004), the Fifth Circuit addressed the question whether the scienter of "the individual corporate officer" or "the collective knowledge of all the corporation's officers and employees" is controlling—a question not presented in this case.[3]

The Fifth Circuit's decision in *Broad* v. *Rockwell Int'l Corp.*, *supra*, presented the question whether the issuer of an indenture committed fraud by failing to disclose in a prospectus that under the terms of the indenture, "the right to convert into Collins Common Stock could, in the event of a merger, be replaced with the right to convert into only that which the holders of Collins Common Stock received in the merger." 642 F.2d at 960. Because there was no evidence that the defendants even considered this "boilerplate" provision, which would apply only in "remote future contingencies," the court concluded that the defendants had not acted

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[2] Petitioners' citation (Pet. 13) of *Backman* v. *Polaroid Corp.*, 893 F.2d 1405 (1st Cir.) (withdrawn from bound volume), rev'd on reh'g, 910 F.2d 10, 14 (1st Cir. 1990), is especially unavailing, because the en banc court withdrew the opinion relied on by petitioners long before the First Circuit decided *Fife*.

[3] Petitioners' reliance (Pet. 11 n.3, 13) on *Southland Securities* and *In re Silicon Graphics Inc. Securities Litigation*, 183 F.3d 970 (9th Cir. 1999), is misplaced for an additional reason: those cases applied the *pleading standards* of the Private Securities Litigation Reform Act of 1995, Pub. L. No. 104-67, § 21D(b)(2), 109 Stat. 747. This is not a private securities fraud case, and it is not at the pleading stage.

recklessly by failing to refer to the provision specifically in the prospectus. *Id.* at 962. In other words, any deception was far from obvious on the facts of that case.

Although petitioners contend (Pet. 13 n.4, 18 n.8) that "the Eighth Circuit standard is unclear" and an intra-circuit split has developed in the Tenth Circuit, petitioners cite no case from either circuit that is in conflict with the decision below. In *SEC* v. *Kluesner*, 834 F.2d 1438 (1987), the Eighth Circuit relied on findings that the defendant did not believe, and "*should not reasonably have believed*," that his representations were misleading. *Id.* at 1439 (emphasis added). In *SEC* v. *Johnston*, No. 90-4189, 1992 WL 180130, at *2 (July 28, 1992)—an unpublished, non-precedential decision—the Tenth Circuit held that summary judgment cannot be predicated on a credibility determination, but did not address whether such a judgment can be predicated on obviousness.[4]

Petitioners are also wrong to contend (Pet. 14) that the CFTC itself disagrees with the legal standard applied by the Eleventh Circuit. The CFTC has long held that conduct is reckless if it "departs so far from the standards of ordinary care that it is very difficult to believe the [actor] was not aware of what he was doing."

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[4] The Third Circuit is also in full agreement with the standard applied by the Eleventh Circuit. See *SEC* v. *Infinity Group Co.*, 212 F.3d 180, 192 (2000), cert. denied, 532 U.S. 905 (2001). The earlier Third Circuit case cited by petitioners (Pet. 15 n.6, 17 n.8), reversed a district court for imposing the burden of proof on the defendant, instead of the plaintiff. *McLean* v. *Alexander*, 599 F.2d 1190, 1196 (1979). The court went on to stress that evidence of the obviousness of a misrepresentation "traditionally supported a finding of liability in the face of repeated assertions of good faith, and continue[s] to do so." *Id.* at 1198.

Do v. *Lind-Waldock & Co.*, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,516, at 43,321 (Sept. 27, 1995) (quoting *Drexel Burnham Lambert Inc.* v. *CFTC*, 850 F.2d 742, 748 (D.C. Cir. 1988)); see *Hammond* v. *Smith Barney, Harris Upham & Co.*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,617, at 36,659 (Mar. 1, 1990) ("[N]o amount of honest belief * * * can justify baseless, false or reckless misrepresentations or promises.") (quotation marks omitted). Indeed, the CFTC recently cited the decision in this case with approval. *In re First Investors Group of the Palm Beaches, Inc.*, No. 01-10, 2004 WL 1153331, at *7 (May 24, 2004). The earlier decision cited by petitioners remands to an administrative law judge for an evidentiary hearing because the CFTC was not persuaded that summary judgment was proper on the record in that case. See *In re Staryk*, [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,206 (Dec. 18, 1997).[5]

c. At bottom, petitioners raise a philosophical question: is recklessness actionable because it evidences a subjective state of mind, or is it actionable in and of itself, regardless of any contention of subjective good faith? Petitioners argue (Pet. 11-17) that language from some opinions could be construed to reflect the former

[5] The Securities and Exchange Commission (SEC) rulemaking cited by petitioners (Pet. 14 n.5) is fully consistent with the authorities cited in the text. The SEC defined recklessness to mean "an 'extreme departure from the standards of ordinary care, . . . which presents a danger of misleading buyers or sellers that is either known to the (actor) or is so obvious that the actor must have been aware of it,'" and determined that subjective good faith is *not* a defense under this standard. *Amendments to Rule 102(e) of the Commission's Rules of Practice*, [1998 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 86,052, at 80,844, 80,851 (Oct. 19, 1998) (quoting *Steadman*, 967 F.2d at 641-642).

rationale, while language from other opinions could be construed to support the latter. But notwithstanding this metaphysical point, the fact remains that all circuits and the CFTC apply the same legal standard. Petitioners cite *no* court of appeals precedent concluding that a defendant who intentionally engaged in obviously deceptive acts lacked the requisite scienter.

This latter point is significant, not only because it shows that this case does not present a circuit conflict, but also because it demonstrates the practical unimportance of any disagreement regarding the philosophical underpinnings of the recklessness test. Under petitioners' view (Pet. 11, 17), the circuits have been divided since at least 1979, when the Ninth Circuit decided *Savage*, supposedly in contravention of *Rolf* v. *Blyth, Eastman Dillon & Co.*, 570 F.2d 38 (2d Cir.), cert. denied, 439 U.S. 1039 (1978). If any such disagreement were outcome-determinative in any case, surely petitioners could have found one from the past quarter century.

d. The reason petitioners cannot do so is that they are asking for a legal standard that makes little sense as a practical matter. While petitioners assert (Pet. 19) a right to make blatant misrepresentations in "good faith," such "[r]eckless behavior hardly constitutes good faith." *Rolf*, 570 F.2d at 46 n.15; see *Infinity*, 212 F.3d at 193 n.16. Thus, "[t]he civil law generally calls a person reckless who acts * * * in the face of an unjustifiably high risk of harm that is either known *or so obvious that it should be known*." *Farmer* v. *Brennan*, 511 U.S. 825, 836 (1994) (emphasis added).

Nonetheless, petitioners claim (Pet. 10-11) that a trial is required every (or nearly every) time that a defendant claims to have lacked scienter. In addition to being wasteful and inefficient in cases where the deception was so obvious that the defendant must have been aware of it, this approach would also impose an unrealistic burden of proof. "Proof of a defendant's knowledge or intent will often be inferential * * * and cases thus of necessity [are] cast in terms of recklessness. To require * * * that a factfinder must find a specific intent to deceive or defraud would for all intents and purposes disembowel the * * * cause of action." *Rolf*, 570 F.2d at 47 (citation omitted); see *McLean*, 599 F.2d at 1198. Reliance on the legal standard applied here constitutes "a legitimate substitution for intent to do the proscribed act because, if shown, it is a proxy for that forbidden intent. If it were not used as a proxy, it might be all too easy for the wrongdoer to deliberately blind himself to the consequences of his tortious action." *Saba*, 78 F.3d at 668.

e. At a minimum, the issue petitioners raise does not warrant review at this time. If petitioners are correct, a court of appeals may eventually hold that a broker's subjective good faith relieves him of liability for making inherently deceptive statements, and this Court can consider whether this subtle issue warrants certiorari at that time. If petitioners are not correct, this Court's review will never be required.

It would also be best to consider recklessness for the first time in the context of a securities fraud case. The number of securities fraud cases dwarfs the number of commodities fraud cases. Indeed, almost all of the cases cited by petitioners as the basis for the supposed circuit split are securities cases. While the CFTC has followed securities law precedents in adopting a recklessness standard, see *Hammond*, *supra*, it has also sought to discourage the "uncritical application of security law principles." 40 Fed. Reg. 26,505 (1975). If this Court were to re-interpret this area of law, a legitimate question would arise whether the securities law standard should continue to apply under 17 C.F.R. 33.10.[6]

2. There is no merit to petitioners' contention (Pet. 20) that the court of appeals departed from decisions of this Court and other courts in holding that petitioners misled their customers.

a. Petitioners contend (Pet. 21) that they had no duty to disclose that at least 95% of their customers were losing money, but they admit that a duty to disclose arises when a defendant makes statements "that would be misleading unless qualified by such a disclosure." That is precisely the reason the court of appeals held that petitioners had a duty to disclose in this case. The court cited authorities for the proposition that a "duty to disclose arises where a 'defendant's failure to speak would render the defendant's *own* prior speech misleading or deceptive,'" and determined:

> Such a disclosure would have gone a long way in balancing out, for example, the affirmative representation in the Commercial that the grain market was ripe for "huge" profits of "200-300 percent" and to telephone RJFCO "now" because such a corn market opportunity may "never" exist again. It would also have done much to counteract the assertion of

[6] Petitioners are wrong to argue (Pet. 27) that this case presents a good vehicle for considering these issues because the CFTC "expressly waived any claim that the trial court's findings were clearly erroneous" at oral argument before the Eleventh Circuit. CFTC counsel stated that the commission did not challenge the magistrate judge's *credibility* findings, but did not acquiesce in any other findings. Petitioners also overstate the relevance of the magistrate judge's findings. While the magistrate judge found (Pet. App. 59a, 60a, 64a) that petitioners lacked an "intent to mislead," it made no specific findings on recklessness.

> "limited risk" in the Seminar. It is misleading and deceptive to speak of "limited risk" and "200-300" percent profits without also telling the reasonable listener that the overwhelming bulk of firm customers lose money.

Pet. App. 19a-20a (quoting *Ziemba*, 256 F.3d at 1206). Thus, the court did not abandon a nexus requirement, as petitioners contend (Pet. 22). Instead, it explained that petitioners' duty to disclose arose precisely because they made misrepresentations that would have been counteracted by the withheld information.[7]

b. Nor did the court of appeals "contraven[e] the standards for appellate review established by this Court." Pet. 24. The court of appeals stressed that it did not "second guess what the District Court concluded with regard to witness demeanor and credibility," and instead held that the "undisputed facts demonstrate fraud and deception as a matter of law." Pet. App. 13a; see *id*. at 16a-17a.

None of the cases cited by petitioners (Pet. 24) holds that this question cannot be decided as a matter of law. To the contrary, *Silver* v. *H&R Block, Inc.*, 105 F.3d 394, 397 (8th Cir. 1997), affirmed a grant of summary judgment because the statements at issue were not misleading as a matter of law. In *Isquith* v. *Middle South Utilities, Inc.*, 847 F.2d 186, 210-211, cert. denied, 488 U.S. 926 (1988), the Fifth Circuit recognized that it

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[7] Contrary to petitioners' representation (Pet. 21), the CFTC has not conceded that petitioners had no duty to disclose. See Gov't C.A. Reply Br. 24 n.20. Although petitioners also dispute (Pet. 23 n.9) whether 95 percent of their customers lost money during the relevant time period, petitioner Raymond Fitzgerald himself testified to that fact, and the district court found his testimony to be credible. See Gov't C.A. Reply Br. 11-12 & nn.8 & 9 (citing R44-2603, R45-2704).

had "the power to make such an independent evaluation," but chose to remand for the district court to determine in the first instance whether summary judgment was appropriate as a matter of law.[8]

c. Ultimately, the petition boils down to the record-based assertion (Pet. 23) that the Eleventh Circuit "ignored substantial contextual evidence" and "selectively extracted testimony from the record to support its reasoning." In reality, the court considered the contextual evidence of petitioners' deception, including the following facts: (i) petitioners were "federally registered professional[s], knowledgeable in the nuances and complexities of the industry," Pet. App. 15a; (ii) petitioners designed their business "specifically to deal with smaller, less experienced customers," *id.* at 17a n.8; (iii) petitioners employed practices expressly prohibited by settled precedents, *id.* at 16a; and (iv) petitioners knew that more than 95% of their customers were losing money, *id.* at 19a.

The court of appeals also considered and rejected other contextual evidence relied on by petitioners. For example, the court rejected petitioners' reliance on risk disclosures because "a general risk disclosure statement does not automatically preclude liability under the CEA where the overall message is clearly and objectively misleading or deceptive." Pet. App. 14a; see *id.* at 17a n.8. The court also acknowledged petitioners' assertion that some investors had, in the past, made profits as large as 200-300%, but held that "just because such profits are possible, or have happened to some degree in

[8] *TSC Industries, Inc.* v. *Northway, Inc.*, 426 U.S. 438, 450 (1976), which addressed the materiality of an omission, as opposed to the misleading nature of a statement, likewise recognized that summary judgment can be appropriate.

the past, does not mean that the Commercial's total message is not misleading." *Id.* at 17a n.7.[9] Because the Eleventh Circuit applied correct legal principles to the record in this case, further review is not warranted.

3. This case certainly does not present a serious First Amendment issue. While petitioners express concern that the Eleventh Circuit's decision will chill brokers' speech (Pet. 28-29), the very point of the CEA is to deter deceptive speech. The "First Amendment * * * does not prohibit the State from insuring that the stream of commercial information flow[s] cleanly as well as freely." *Virginia State Bd. of Pharmacy* v. *Virginia Citizens Consumer Council, Inc.*, 425 U.S. 748, 771-772 (1976).

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[9] The record does not support petitioners' contention (Pet. 23) that profit illustrations used in the commercials were substantially similar to illustrations used by the Chicago Board of Trade (CBOT) and NFA. Leiza Fitzgerald testified that she created the heating oil illustration on her own, and no one ever testified that the CBOT or the NFA attempted to link increases in *options* prices to winter weather or changes in cash market prices. See Gov't C.A. Reply Br. 20-21 (citing R41-2296, R41-2312).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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