U.S. COMMODITY FUTURES TRADING COMMISSION
Three Lafayette Centre
1155 21st Street, NW, Washington, DC 20581

EDNA D. ANDERSON,

Complainant,

v.

DAVID M. BEACH,

Respondent.

CFTC Docket No. 05-R058

INITIAL DECISION

This case illustrates what can happen when parties do not follow our directives. Respondent David M. Beach was barred from introducing evidence at the oral hearing because he violated our order concerning prehearing document submissions. On the other hand, complainant Edna D. Anderson did enough, in the Commission's eyes, to preserve her right to a hearing. However, she preserved the right to introduce so little evidence that she failed to make a prima facie showing that Beach violated the Commodity Exchange Act or Commission regulations.

Background

On June 27, 2005, the Office of Proceedings received Anderson's complaint.[1] In its final form, the pleading contained charges that Beach[2] harmed Anderson by making fraudulent misrepresentations, churning her account and failing to disclose material information.[3] Beach filed an answer in which he admitted to having given Anderson financial advice and admitted suggesting that she trade options according to the signals generated by a trading program but denied wrongdoing.[4]

At the close of discovery, we scheduled a hearing and required the parties to submit: statements of intent to participate in the hearing, witness lists, prehearing memoranda, written direct testimony of the parties and their

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[1] Commodity Futures Trading Commission Reparations Complaint Form, received June 27, 2005.

[2] Beach is (or was) Anderson's son-in-law. Letter from David M. Beach to the U.S. Commodity Futures Trading Commission, dated August 25, 2005 ("Beach Answer"), at 1; Letter to the Office of Proceedings, dated June 17, 2005 ("June 17th Letter"), at 2.

[3] Memorandum, dated July 13, 2005, at 2; Letter from Edna D. Anderson to the U.S. Commodity Futures Trading Commission, dated July 6, 2005; June 17th Letter at 2. In addition, Anderson lodged a suitability claim, a claim that is not cognizable in this forum because neither the Act nor Commission regulations impose suitability requirements. Phacelli v. ContiCommodity Servs., Inc., [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶23,250 at 32,672-75 (CFTC Sept. 5, 1986) (reversing an initial decision that rested on suitability). She also named Peregrine Financial Group, Inc. as a respondent but subsequently settled with the firm and stipulated to its voluntary dismissal from the proceeding. See Order of Partial Dismissal, dated April 25, 2006; Order, dated April 18, 2006.

[4] Beach Answer at 1-5.

non-hostile witnesses, and proposed exhibits.[5] Neither Anderson nor Beach filed prehearing documents. Consequently, we issued a show cause order on April 24, 2006.[6] Anderson responded by filing her written testimony[7] and Beach did nothing. Lacking an explanation from either party, we found their violations of our prehearing directives to have been willful, barred them both from presenting evidence at the hearing and, given Anderson's burden of proof, dismissed the complaint.[8]

Anderson appealed and, on December 21, 2006, the Commission issued an opinion.[9] It found that Anderson substantially complied with our prehearing requirements by belatedly filing her testimony, vacated our dismissal and remanded the case with instructions to "schedule a hearing with

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[5] Order and Notice of Hearing, dated March 17, 2006 ("Notice of Hearing"), at 1-3.

[6] Show Cause Order, dated April 24, 2006 ("Show Cause Order"), at 2-3.

[7] Direct Testimony of Edna D. Anderson, filed May 4, 2006 ("Revised Direct Testimony"); Direct Testimony of Edna D. Anderson, filed May 1, 2006. She submitted no other proposed exhibits nor did her testimony incorporate, by reference, any other statements in the manner we required. Notice of Hearing at 2 n.2 ("Written testimony may incorporate by reference other statements that the witness has made and that have been reduced to writing. However, for each document incorporated by reference, such incorporation must be explicit and must either (1) state that the entire document is being incorporated by reference or (2) identify those portions that are being so incorporated with precision. Moreover, the incorporated statement(s) must be attached to the written testimony in which the incorporation by reference occurs.").

[8] Order of Dismissal, dated May 16, 2006, at 4-5.

[9] Anderson v. Beach, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶30,382 at 58,720-22 (CFTC Dec. 21, 2006).

reasonable promptness."[10] On February 21, 2007, we presided over a hearing in New Orleans, Louisiana, at which Anderson submitted her written testimony into evidence and we set a post-hearing memoranda schedule.[11] Anderson filed a timely post-hearing memorandum.[12] Accordingly, we now turn to the merits of Anderson's claims.

Anderson Did Not Meet The Burden Of Proof With Respect To Any Of Her Claims

We begin with the claim that Beach committed fraud by misrepresentation. To recover on the basis of this theory, Anderson must, among other things, prove by a preponderance of the evidence that Beach represented a material fact and the representation was false or misleading.[13] In order to classify Beach's alleged misstatements (factual or puffery, false or not, so obviously false as to support the inference that Beach acted with scienter or not, possibly leading to loss causation or not), we must determine their content. For this task, "the touchstone is not so much the words of the solicitations, themselves, but the message that those words actually convey"

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[10] Id. at 58,722.

[11] Transcript, dated March 5, 2007 ("Transcript"), at 6-11. Beach was barred from introducing evidence at the hearing. Order, dated January 23, 2007, at 2.

[12] Complainant's Proposed Findings of Fact and Conclusions of Law, dated March 21, 2007 ("Complainant's Memorandum"). Beach made no filing.

[13] Udiskey v. Commodity Research Corp., [1998-1999 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶27,599 at 47,848 n.67, 47,852 (ALJ Apr. 2, 1999), aff'd, [2002-2003 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶29,255 (CFTC Dec. 16, 2002).

(i.e., how a reasonable recipient of the communication would have understood the statement in light of its actual content and the surrounding circumstances).[14] When the alleged misleading statement was unrecorded, the complaint's description of it is, at best, a starting point from which we try to imagine the "objective" message conveyed.[15] However, when it is "sufficiently specific," testimony may be adequate to prove what was said even if does not include a verbatim account of the relevant conversations.[16]

With respect to the trading (and account-opening transactions) that form the basis of her case-in-chief, Anderson testified,

> Before mid-2004 and the filing of my complaint, I had never heard of Dynamic Trading Group Ltd. I still don't know what futures trading means, was never instructed about it, and if

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[14] In re First Fin. Trading, Inc., [2002-2003 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶29,089 at 53,682 n.39. (CFTC July 8, 2002).

[15] In the context of insider trading, Professor Kathleen Coles explained,

> The more remote a tippee is from the primary tipper and tippee, the more likely it becomes that the information received by the remote tippee is less specific and less accurate than the information that was originally possessed or conveyed by the primary tipper. This process has been anecdotally compared to the children's game of "telephone," but the attenuation in accuracy and specificity of information as it passes from one person to another has also been demonstrated in academic studies involving hearsay evidence and the psychology of rumors.

Kathleen Coles, "The Dilemma of the Remote Tippee," 41 Gonz. L. Rev. 181, 215-16 (2005) (footnotes omitted).

[16] Ferriola v. Kearse-McNeill, [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶28,172 at 50,153 n.18 (CFTC June 30, 2000).

someone told me how trades were made on program signals, I am sure that I would not have understood it. It certainly would have taken at least "several" meetings to explain futures trading and contracts to me and how the Dynamic Trading Group Ltd[.] program worked and how it would be implemented, but how many of the 26 calendar days before 7/24/04 and hours per meeting did it take an IB to teach commodity trading to a novice investor? Did it include the July 4th weekend?

I am not computer literate, have never had or used an "e-sign", nor sent or reviewed E-Mail on my own, nor accessed my accounts online (including my commodities account) without assistance. I am a bottom line investor who did not understand the statements that I received for my commodities account. Although I was willing to take a little more risk at this time with David Beach for potentially better returns, I don't believe that commodity trading was a suitable investment for me. Trust was the key in this and the Philippine investments. If we had had the same quality of communications for the commodities investment as we had for the Pershing, National Planning, and Pacific Life investments, I would have been out of the commodities investment, if I got into it at all, by September 2004. The only communications between me and David Beech about my commodities account were my telephone calls to him inquiring about my losses; not once did he suggest that I close my account. He did agree to my request in November, 2004, to close my account without comment. During an informal visit to my house after my account was closed, he suggested to my son that any formal complaint should be filed with the CFTC. David Beach called me once after I received a check for closing my account, and asked if I had any questions for him. I said no, but that I would like to have my account reviewed. This was done by a few experienced investors who all agreed that I should pursue my complaint.[17]

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[17] Revised Direct Testimony at 2. This was the only relevant evidence introduced at the hearing. Transcript at 6-8.

In her posthearing memorandum, Anderson rests her case on material that she did not introduce into evidence, her complaint. Complainant's Memorandum at 2-3. Having been warned that proposed exhibits not submitted as part of her prehearing filing would not be admitted as part of her case-in-chief, twice having had the opportunity to submit her complaint as a proposed exhibit (or as part of her testimony) and twice choosing not to do so, she waived the right to have the complaint admitted as evidence. See Show

(continued..)

This testimony lacks any specific description of what Beach said to induce her trading with Peregrine and Beach does not admit to having misled her. In addition, it comes nowhere close to establishing facts that would support the inference that Beach had a cognizable disclosure duty that he violated.[18] Thus,

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(..continued)

Cause Order at 1-2; Notice of Hearing at 3-4. See supra text accompanying notes 5-7. Thus, we will not consider it as such.

[18] In her complaint, Anderson did not clearly state what law(s) Beach's alleged disclosure failures violated. The duties to disclose that we can enforce have two sources, Commission regulations and the agency's case law. Codified obligations to disclose are generally absolute in the sense of imposing strict liability requirements. See, e.g., Udiskey, [1998-1999 Transfer Binder] ¶27,599 at 47,857. Case law-generated duties to disclose arise in the context of fraud and, thus, are not violated unless scienter is present (except in 7 U.S.C. §6o(1)(B) cases). See In re Slusser, [1998-1999 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶27,701 at 48,311-16 (CFTC July 19, 1999). The duties to disclose found in Commission regulations depend on one's acts and status. For example, 17 C.F.R. §1.55 disclosure obligations apply to futures commission merchants and introducing brokers but "do not extend to associated persons." Knight v. First Commercial Fin. Group, Inc., [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶26,942 at 44,554 n.16 (CFTC Jan. 14, 1997). Similarly, a registered associated person who provides trading advice need not register as a commodity trading advisor or comply with commodity trading advisor disclosure requirements if the associated person's "advice is issued solely in connection with its employment as an associated person." 17 C.F.R. §§4.14(a)(3), 4.31(a); Udiskey, [1998-1999 Transfer Binder] ¶27,599 at 47,856-61. Anderson's testimony, taken at face value and combined with the judicial admissions of Beach, does not support a finding that the respondent violated any of the express disclosure obligations imposed upon him by Commission regulations. In addition, the absence of evidence concerning Beach's statements and the parties' interactions precludes us from finding that Beach had a case law-based disclosure duty that he violated with scienter.

her fraud and non-disclosure claims fail. In addition, the absence of trading-related evidence precludes us from finding that Beach churned her account.[19]

Conclusion

Because Anderson has not satisfied the burden of proof relating to any of her claims against Beach, we **DISMISS** her complaint with prejudice.

IT IS SO ORDERED.

On this 24th day of April, 2007

Bruce C. Levine
Administrative Law Judge

[19] To establish that churning occurred, Anderson must prove, among other things, that Beach excessively traded her account in a manner that was contrary to her trading objectives. Ferriola, [1999-2000 Transfer Binder] ¶28,172 at 50,154. Anderson's testimony is completely bereft of information that would support an inference of excessive trading and Beach's admissions do not fill the gaps.