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November 8, 2005

Jean A. Webb
Secretary
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, N.W.
Washington, DC 20581

Re: Proposed Rule Regarding the Definition of "Client" of a Commodity Trading Advisor

Dear Ms. Webb:

I am a practicing attorney who has represented persons, i.e., publishers of impersonal trading advice, who would be affected by the proposed amendment to CFTC Reg. § 1.3(bb) that has been published for comment at Fed. Reg., vol. 70, no. 187, p. 56608 (Sept. 28, 2005). This comment, however, is submitted on my own behalf and not on behalf of any other person.

The Commission should not adopt the proposed rule for two reasons. First, the proposed rule is inconsistent with the Commodity Exchange Act ("CEA"), and the Commission therefore lacks authority to adopt it. Second, even if the proposed rule were within the Commission's statutory authority, it should not be adopted, because it would infringe the First Amendment rights of freedom of speech and press of publishers of impersonal trading advice.

In proposing the amendment, the Commission has not addressed, and has failed even to acknowledge, the Supreme Court's landmark decision in Lowe v. SEC, 472 U.S. 181 (1985). In Lowe, the Supreme Court ruled that a publisher of impersonal trading advice was not subject to either the registration or the antifraud provisions of the Investment Advisers Act of 1940 ("Advisers Act"). Although the decision was based on a statutory construction of the Advisers Act, the statutory construction was driven by the Court's concern that the First Amendment rights of the publisher would be violated by a contrary construction.

The Lowe decision highlights why the Commission's proposed rule may not and should not be adopted. The Supreme Court articulated in Lowe the important distinction between clients and subscribers: i.e., that clients have a fiduciary relationship with their personal advisors, whereas subscribers do not have such a relationship with the publications to which they subscribe. Thus, the use of the term "subscriber" in the CEA is not an ambiguous reference that needs clarification, but rather expresses a significant substantive difference between two types of persons. Furthermore, this statutory distinction serves an important purpose in protecting First Amendment rights, because it distinguishes those persons, i.e., advisors giving personalized advice, who

can be regulated as fiduciaries, and those persons, i.e., publishers of impersonal advice, who cannot.

1. The Commission Lacks Authority to Adopt the Proposed Rule

It is well established that the Commission lacks authority to adopt a regulation that is outside the jurisdiction granted to the Commission by Congress. For example, in CFTC v. Mass Media Marketing, Inc., 297 F. 3d 1321 (11th Cir. 2002), the court ruled that the Commission could not enforce the antifraud provision in CFTC Reg. § 33.10 as to a person who did not enter into a commodity option transaction, because the authority for the regulation, namely Section 4c(b) of the Act, did not extend to that person.

The proposed rule amendment would similarly be beyond the authority granted to the Commission, because it would eliminate the important distinction between clients and subscribers that is currently in the Act, and that until now has been reflected by the Commission in its regulations.

The distinction between clients and subscribers in the highly analogous context of the Advisers Act, which formed a model for the provisions of the CEA relating to commodity trading advisors ("CTAs"), was emphasized by the U.S. Supreme Court in Lowe v. SEC, 472 U.S. 181 (1985). Despite its importance and relevance, Lowe is nowhere mentioned in the Commission's Federal Register Release.

The Supreme Court in Lowe construed the term "client" as not applying to publishers of impersonal advice in a virtually identical antifraud provision in a analogous statute. See Lowe, 472 U.S. at 201-02 n.45, 208 n. 54. Compare CEA section 4o, 7 U.S.C. § 6o, and Advisers Act section 206, 15 U.S.C. § 80b-6. One of the primary reasons that the Advisers Act was determined to exclude publishers was that it repeatedly referred to clients, whereas, according to the Supreme Court, publishers have subscribers rather than clients. See Lowe, 472 U.S. at 207-08, 208 n. 54. Therefore, it was the use of the term "client", rather than "subscriber," that led in large part to the Supreme Court's conclusion that the Advisers Act was limited to advisers with a personalized fiduciary relationship with clients, and did not apply to publishers who had an arm's-length relationship with subscribers.

The proposed rule assumes that the term "subscriber" has no independent meaning in the CEA and in its own regulations, so that it is surplusage. But this argument runs afoul of the Lowe majority's criticism of the Lowe concurring justices' similar suggestion that the provisions of the Advisers Act apply to publishers of impersonal advice, because the concurring justices failed to give effect to every word in the statute. Lowe, 472 U.S. at 207-08 n. 53.

The distinctions between "client" and "subscriber" have been carried through to the Commission's own regulations. CFTC Reg. § 4.33 and CFTC Reg. § 166.1(c) refer to both "client" and "subscriber," with section 4.33 requiring records concerning both types of customers to be kept by CTAs, and section 166.1(c) defining a

"customer" of a CTA to be a "client" or "subscriber" or "prospective client or subscriber." 17 C.F.R. §§ 166.1(c), 4.33. Similarly CFTC Reg. § 4.31, which specifies the disclosure necessary for accounts to be traded by CTAs on behalf of customers, refers only to a "client." 17 C.F.R. § 4.31. These references track the language of section 4n(3)(A) of the CEA. The use of two terms in one provision and only one in the other clearly demonstrates that Congress intended the reach of section 4o, which applies only to clients, to be narrower than the reach of section 4n, which applies to both clients and subscribers.

Section 4l of the CEA is not a justification for the proposed rule. Section 4l does not use the term "subscriber," but rather uses the word "subscriptions." In addition, section 4l merely contains a laundry list of undifferentiated relationships applying to both CTAs and commodity pool operators ("CPOs"), so it is not clear which items on the list pertain to CTAs and which pertain to CPOs. Section 4l refers "contracts, solicitations, subscriptions, agreements, and other arrangements with clients" as activities which take place in interstate commerce so as to provide a jurisdictional basis for Congress to legislate. This provision does not impose any substantive regulation, and therefore it does not use the precise terms for the customers of registrants that are used in the provisions which impose substantive regulation: i.e., participants for CPOs, and clients and subscribers for CTAs. There is no basis for the Commission to assume that this general jurisdictional provision overrides the precise terminology used in substantive provisions of the CEA.

There are additional reasons why the use of the term "subscriptions" in section 4l does not justify an elimination of the distinction between clients and subscribers in other sections of the CEA. First, there is no basis for construing the phrase "other arrangements with clients" as necessarily referring back to the term "subscriptions" in this sentence. Thus, the provision could be read to state that subscriptions are a category of activities that is independent of "other arrangements with clients." Second, the word subscription in this context could refer to a subscription other than a subscription to an advisory publication, such as a subscription for an investment in a commodity pool, and have nothing to do with CTAs.

In Commodity Trend Service, Inc. v. CFTC, 233 F. 3d 981 (7th Cir. 2000), the Seventh Circuit ruled that the term "client" in section 4o could apply to a person receiving impersonal advice. Courts in other Circuits, however, could come to a different conclusion on this question. Rather than allowing additional courts to review the issue, and possibly disagree with the Seventh Circuit, the proposed rule seeks to cut off the debate and prevent litigants from even making the argument that section 4o is limited to advisors giving personalized advice. Because the Commission lacks the authority to change the CEA in the manner which is proposed, this issue should be left for the courts to decide as a matter of statutory construction of the CEA.

Finally, there is no relevance whatsoever to the reference, in the Commission's Federal Register release, to a 1978 statement by the Commission equating clients and subscribers. That statement occurred prior to Lowe, and prior to other constitutional litigation against the Commission, e.g., Taucher v. Born Comm. Fut.

L. Rep. (CCH) ¶ 27,677 (D.D.C. 1999), and Commodity Trend Service, Inc. v. CFTC, Comm. Fut. L. Rep. (CCH) ¶ 27,777 (N.D. Ill. 1999), aff'd on other grounds, 233 F. 3d 981 (7th Cir. 2000), in which courts recognized a constitutional distinction between personalized advisors and publishers of impersonal advice in applying the registration provisions of the CEA. The separate references in the CEA to clients and subscribers reflect that distinction. Any pre-Lowe statements by the Commission to the contrary are therefore irrelevant and superseded by these more recent developments in the law.

2. The Commission's Proposed Rule Would be Unconstitutional.

In Lowe, the Supreme Court ruled that the distinction between the term "client" and the term "subscriber" has significance. See Lowe, 472 U.S. at 208 n.54. The Court indicated that to prevent constitutional infirmities in the Advisers Act, Congress repeatedly used the term "clients" rather than "subscribers" to limit the coverage of the Act to persons giving personalized advice attuned to a client's specific concerns, and to exclude publishers of impersonal advice. Id. at 207-08, 208 n.54. More pointedly, the Court stated that the repeated use of the term "client" in the Advisers Act contradicts the suggestion that a publisher has the kind of fiduciary relationship that the Act was intended to regulate. Id. at 201-02 n.45. The provisions referred to in Lowe included antifraud provisions in the Advisers Act that use language that is essentially the same as that in the antifraud provisions in the CEA. See id. at 208 n.54, citing 15 U.S.C. §§ 80b-6(1), 80b-6(2); compare 7 U.S.C. §§ 6o(1)(A), 6o(1)(B). See also Lowe, 472 U.S. at 210 (holding that dangers of fraud that motivated enactment of Advisers Act are present in personalized communications but not in publications sold in an open market).

The dictionary also gives distinct meanings to the terms "client" and "subscriber." A client is "[o]ne for whom professional services are rendered." See, e.g., The American Heritage Dictionary (3d ed. 1994). To subscribe is "[t]o contract to receive and pay for a subscription, as to a publication." Id. The Latin roots of these two words are also distinct in that "client" comes from the word for dependent, and "subscribe" means to write one's name. Id. In other words, the plain meanings of these terms indicate that "client" refers to a fiduciary relationship with a professional, and "subscriber" refers to an arm's-length contractual relationship with a publisher. But regulation that is constitutionally permissible when applied to fiduciary relationships, even when the regulation has an incidental impact on the fiduciary's speech, is constitutionally impermissible when applied to pure speech by a non-fiduciary. See Thomas v. Collins, 323 U.S. 516, 544-48 (1945) (Jackson, J., concurring) (stating that regulation of a profession is constitutionally permissible whereas regulation of speech is not).

Section 4o of the CEA, which is the statutory authority for CFTC Reg. § 4.41, is an antifraud provision that may be violated without a showing of fraudulent intent. See Commodity Futures Trading Commission v. Savage, 611 F. 2d 270, 285 (9th Cir. 1979). This is because section 4o "implements the fiduciary capacity that characterizes the advisor's relationship to his clients." Id. But the First Amendment does not allow fiduciary fraud standards to be imposed on non-fiduciary publishers of

impersonal advice, because such publishers cannot be held liable for false statements that are innocently or negligently made. See Gutter v. Dow Jones, Inc., 490 N.E.2d 898, 900-02 (Ohio 1986); Ginsburg v. Agora, Inc., 915 F. Supp. 733, 738-40 (D. Md. 1995). The First Amendment requires breathing space for speech, and the imposition of liability for innocent or negligent misstatements causes an impermissible chilling effect on speech. Gutter, 490 N.E.2d at 900-02; Ginsburg, 915 F. Supp. at 738-40.

In Gutter, the Ohio Supreme Court ruled that a newspaper publisher could not be liable to one of its subscribers for a negligent misrepresentation of fact that the subscriber relied upon in making a securities investment which resulted in a financial loss. Gutter, 490 N.E.2d at 902. According to the court, liability for a misrepresentation may not be imposed on a publisher in the absence of a contract, fiduciary relationship, or intentional design to cause injury. Id. at 900. The court explained that although accuracy in publications is to be desired, the chilling effect on free speech that would result from imposing liability for negligent misstatements is unacceptable under the Constitution. Id. at 901; accord, Jaillet v. Cashman, 139 N.E. 714 (1923) (absent special relationship, supplier of stock market quotes and financial news could not be held liable to investor for unintentional mistake in its financial news report); Demuth Development Corp. v. Merck & Co., 432 F. Supp. 990, 993 (E.D.N.Y. 1977) (holding that publisher of information on chemicals and their manufacturers could not be held liable for negligent misrepresentation, as it would have chilling effect on the right to disseminate knowledge); MacKown v. Illinois Pub. & Printing Co., 6 N.E.2d 526, 530 (1937) (ruling that newspaper can be held liable for misrepresentation only if contract or fiduciary relationship exists, or if mistake was intentional).

In Ginsburg v. Agora, Inc., 915 F. Supp. 733 (D. Md. 1995), the court ruled that the publisher of an investment newsletter could not be held liable for negligent misrepresentations to an investor who lost money on futures contracts traded on the basis of the erroneous advice. Id. at 740. The court stated that a contrary rule would run counter to the First Amendment, as follows:

> A contrary rule, allowing liability for negligent errors, would impose on the press the "intolerable burden" of demonstrating to the finder of facts that its efforts to determine the accuracy of any given report were reasonable. This "intolerable burden" would necessarily run counter to "the societal right to free and unhampered dissemination of information" embodied by the First Amendment.

Id. at 739 (citing Gutter, supra, and Daniel v. Dow Jones & Co., 520 N.Y.S. 2d 334, 339 (N.Y. Civ. Ct. 1987) (internal citations omitted).

The CFTC's antifraud provisions have been held to require affirmative disclosures. See, e.g., Hahn v. CIC International, Comm. Fut. L. Rep. (CCH) ¶ 21,163, at 24,753 (CFTC ALJ 1981) (ruling that section 4o was violated by failure of advisor to explain mechanics and risks of trading options); Reese v. Pattison, Comm. Fut. L. Rep. (CCH) ¶ 21,689, at 26,633-34 (CFTC ALJ 1983) (finding that section 4b was violated by failure of broker to make additional disclosures in connection with factually accurate

performance record). These disclosure requirements are constitutionally permissible to apply to fiduciaries, who have wide-ranging disclosure obligations. With respect to persons engaged in speech and press activities, however, these requirements of affirmative disclosure violate the First Amendment, which prohibits the government from imposing "forced speech" requirements on persons engaged in protected expression. See Miami Herald Publishing Co. v. Tornillo, 418 U.S. 241, 256-58 (1974) (holding that law requiring newspaper to give reply space to persons it criticizes is unconstitutional content-based regulation); Turner Broadcasting System, Inc. v. FCC, 512 U.S. 622, 641-42 (1994) ("Government action ... that requires the utterance of a particular message favored by the Government contravenes [the First Amendment].").

Section 4o of the CEA is thus a fiduciary fraud provision which cannot constitutionally be applied to impersonal advice. Because the proposed rule would place an unconstitutional burden on the speech of publishers of impersonal advice, it should not be adopted.

3. The Proposed Rule Should Not be Adopted

For the foregoing reasons, the Commission should not adopt the proposed rule.

Very truly yours,

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