UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

GREGORY VIOLETTE	:	
v.	:	CFTC Docket No. 98-R188
LFG, L.L.C. and REBECCA JILL PALM	:	OPINION AND ORDER

Respondents LFG, L.L.C. ("LFG") and Rebecca Jill Palm ("Palm") appeal from a Judgment Officer's decision awarding complainant Gregory Violette ("Violette") $17,300 plus interest and costs. The Judgment Officer found that Palm violated Section 4b of the Commodity Exchange Act ("Act") by failing to comply with Violette's instruction to liquidate an open short call option position when the market rose by one point.

On appeal, respondents primarily challenge the Judgment Officer's credibility determinations and factual assessments. They also contend that the judge's legal analysis is incompatible with the requirements of Commission Rule 1.35 and that his dismissal of their ratification defense is contrary to the record. Complainant did not file a responsive brief.

As explained below, we vacate the award and dismiss the complaint against LFG because it is the subject of a pending bankruptcy proceeding. As to Palm, we conclude that the Judgment Officer erred by failing to assess the reliability of Violette's testimony in support of his claim. Because our *de novo* review of the testimony in light of the record taken as a whole shows that it is insufficiently reliable to establish Violette's claims by the weight of the evidence, we vacate the award against Palm and dismiss the complaint. Finally, we undertake *sua sponte* review of

certain discovery issues and vacate the sanctions that the Judgment Officer imposed on Violette for seeking unduly broad discovery.

BACKGROUND

I.

In August 1998, Violette filed a reparations complaint seeking $17,300 in damages from LFG and his account executive, Palm.[1] The complaint alleged that on April 14, 1997, Violette established a two-contract long call option position in the June S&P futures contract at a price of 2.70.[2] On the same day, Violette and Palm discussed the open positions in complainant's account.[3] According to the complaint, Palm knew that Violette would be leaving that day for a vacation of more than two weeks and recommended that his open call position be liquidated if the price rose to 3.70 or higher. The complaint claimed that Violette accepted the recommendation and directed Palm to buy back his June S&P call position when the market moved one point against him.

The complaint noted that while Violette was away, Palm traded his account on April 15, 17 and 23, 1997. None of these trades, however, involved Violette's order regarding his June

[1] During the period at issue, LFG was registered as a futures commission merchant ("FCM") and Palm was registered as an associated person ("AP").

[2]Violette attached his April 14, 1997 account statement to his complaint. The statement indicates that the June S&P option position Violette established that day was a short call position rather than a long call position. The account statement shows that Violette also liquidated a four-contract short put position in the April S&P futures contract and established a two-contract short wheat futures position and a five-contract short corn position.

[3]The April 14, 1997 account statement indicates that as a result of the trades described above, Violette's account had open positions in wheat futures (a two-contract July/September spread and a two-contract May short position), corn futures (a five-contract short position), and June S&P call options (a two-contract short position) at the end of the day.

S&P call position.[4] According to the complaint, Violette eventually liquidated the June S&P call position and suffered a loss $17,300 greater than the loss he would have suffered if Palm had followed his April 14, 1997 instruction.[5]

LFG and Palm filed a joint answer and counterclaim seeking attorney fees in September 1998.[6] Their answer noted that Violette had experience trading both futures and options prior to opening his LFG account. It alleged that complainant was an active trader in a wide range of commodity markets and "generally followed a trade recommendation program regarding his grain trades." Answer at 2-3. According to the answer, aside from grain trades, all other trades in Violette's account "were initiated and liquidated at his sole discretion and on his explicit instruction." Answer at 3.

As for the specific allegations in the complaint, respondents noted that the June S&P call option position that Violette established on April 14, 1997 was a short position rather than a long position. The answer acknowledged that Palm discussed profit and loss parameters with complainant after this short position was established, but emphasized that Palm informed Violette that LFG's order desk was not accepting stop orders for S&P option positions. According to the answer, Violette neither entered an order to liquidate his June S&P call option position at a specific loss nor advised Palm that he was going out of town. Indeed, the answer alleged that Palm and Violette agreed that "Palm would contact [c]omplainant once the position

[4]Violette attached his April 1997 monthly account statement to his complaint. The monthly statement shows that on April 15, 1997, three July wheat futures contracts were sold and three December wheat contracts were purchased for complainant's account. It shows that on April 17, 1997, a two-contract short July wheat futures position was liquidated at a small loss in complainant's account. Finally, it shows that on April 23, 1997, a two-contract May short wheat position and a five-contract short corn position were liquidated and two July wheat futures contracts were sold for complainant's account. The liquidations resulted in a loss of almost $5,000 for complainant.

[5] The April monthly statement indicates that Violette's two-contract June S&P call position was liquidated on April 30, 1997 at a cost of $21,000.84.

[6] Violette's answer to the counterclaim denied that he had agreed to pay costs that respondents incurred in defending a reparations claim.

experienced a loss of one basis point and then [c]omplainant would instruct Palm on what was to be done regarding" his June S&P call position. Answer at 3.

According to the answer, the market for complainant's June S&P call position settled at 3.65 on April 14, 1997 and the settlement price rose to 5.15 by the end of the following day. The answer claimed that Palm repeatedly and continuously attempted to contact Violette by telephone but could not reach him and could not leave a message because complainant did not have either an answering machine or a voice-mail system. Respondents noted that because complainant's account remained properly margined, they were not in a position to liquidate the June S&P call position without complainant's specific authorization.

The answer alleged that Violette did not contact Palm until April 30, 1997. At that time, Palm informed complainant that the market had declined by over 8 points. According to the answer, complainant asked Palm why she had not liquidated the June S&P call position. Palm reminded Violette that she did not have discretion to trade his account and that he had not left specific orders on what to do if the market rose one basis point. The answer claimed that Violette responded that Palm should have placed the liquidation order regardless of whether she had discretion.

Respondents acknowledged that Palm made trades in Violette's account on April 15, 17, and 23, but insisted that those trades had been "specifically authorized" by complainant. Answer at 5. The answer also acknowledged that complainant's June S&P call position had been liquidated at a cost of $21,000, but argued that Violette's claim that his position could have been liquidated at a price of 3.70 was speculative. Respondents also argued that Violette had ratified any error by failing to notify LFG that his account statements disclosed an error.

On October 20, 1998, the Commission's Proceedings Clerk issued an order notifying the parties that the case had been assigned to a Judgment Officer for a determination under the Commission's summary proceedings rules. The Proceedings Clerk's order also provided information about the applicable procedures and the deadlines for taking discovery and filing verified statements of fact.

In November 1998, complainant and respondents exchanged discovery requests.[7] Complainant filed his discovery response in December 1998. Violette attached a group of documents to his response that he described as "every document in [his] file relating to [his LFG account]."[8] He also listed eight types of documents that he asserted LFG already had.[9] Finally, Violette indicated that he was enclosing:

> [E]verything I have as of this date and as of this date plan on using. As time moves forward and I plan for a hearing or other meeting I might come up with more things I might find as I prepare for meetings or hearing. If I do I will send everything to [r]espondents and [the Commission].

Complainant's Answers to Discovery at 2.

Violette also filed responses to respondents' interrogatories. Three of his responses related to his conversation with Palm on April 14, 1997. Violette indicated that he discussed his plans to be away with Palm and that she was to "follow the trades in the grains that LFG people and she [were] doing." He said that after he sold the call options they had discussed "us[ing] the same stop we had been using in the pas[t], a 1.00 point stop." Violette also stated that he did not

[7] Respondents' discovery requests are not in the record and there is no explanation for their absence. In a motion for protective order filed in December 1998, respondents claimed that they served discovery requests on Violette on October 15, 1998.

[8] These documents included the account statements that Violette attached to his complaint, some notes apparently prepared by Violette, and several documents Violette received from the Office of Proceedings.

[9] The listed documents included papers received from respondents or the Commission and paperwork Violette sent to the Commission and respondents.

feel he had to monitor the market while he was on vacation because Palm knew that "the grain trades [were] to be followed as given by the LFG person," and the "S&P [o]ption trade was to be followed with [our] 1.00 stop number." Complainant's Answers to Discovery at 3-4.

The discovery requests that Violette served on respondents were quite broad. For example, he requested all account statements for his account, a complete telephone record for all telephone calls between himself and respondents, a complete list of every trade in his account and an explanation for why the trade was made, a transcript of any recording of a telephone call between himself and respondents, an explanation of the method respondents used in selling options for his account, all correspondence and related documents between himself and respondents, all information provided to anyone about his complaint, a list of all complaints filed against respondents, and a copy of all documents respondents intended to submit or use in support of their defense.

Respondents objected to the bulk of Violette's requests as unduly burdensome or seeking information that was irrelevant.[10] On December 14, 1998, respondents filed a motion for protective order noting that Violette's complaint related to a single trade but that his discovery requests: (1) sought information and documents relating to the entire life of his account; (2) sought privileged information; and (3) sought information regarding complaints against LFG that did not relate either to Violette or the trade at issue in the complaint. On this basis, respondents sought a protective order that limited Violette's discovery to the time period of the transaction at issue in the complaint and other material "specifically relevant" to that transaction. In addition, respondents sought all other relief "that the Honorable Judgment Officer deem[ed] just and reasonable." Motion for Protective Order at 4. Violette did not respond to the motion.

[10] The documents that respondents submitted in response to Violette's requests are not in the record.

On January 13, 1999, the Judgment Officer issued an order that prohibited Violette from taking discovery and required him to pay the costs that respondents incurred in preparing their protective order. The Judgment Officer emphasized that Violette had not attempted to defend his burdensome discovery requests. He also took official notice of the fact that Violette "or his fellow complainants previously have been sanctioned for tactics found to be abusive."[11] The judge indicated that this fact was an appropriate consideration because it related to Violette's "experience and sophistication" as a litigant.

On January 27, 1999, Violette filed a motion requesting the Judgment Officer to set aside his January 13, 1999 order. Violette claimed that he was not aware that he should answer the motion for protective order and expected the Commission to contact him and "explain what had to be done if something needs addressing." He also stated that he "was told" that the Judgment Officer would review the matter and get both sides together on the phone and determine what information should be exchanged. Violette also disputed the Judgment Officer's statement that he had been sanctioned in previous cases, insisting that it was his brother who had been sanctioned. Finally, Violette argued that it was unfair to deny him discovery. He urged the Judgment Officer to permit discovery but impose limitations based on a reasonable time before and after the transaction at issue.

The following day, the Judgment Officer denied Violette's motion. The Judgment Officer found that Violette's claim that he expected the Commission to contact him and explain what to do was not credible in light of Violette's extensive experience with the reparations

[11] The Judgment Officer was referring to sanctions imposed in a series of reparation cases involving complainant Gregory Violette and members of his family. *See, e.g., Violette v. First American Discount*, [1998-1999 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,419 at 46,980 (CFTC August 31, 1998) *citing Violette v. Kaiser,* [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,928 (Initial Decision Dec. 18, 1996); *The Violette Group, Inc. v. Ackerman*, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,729 (Initial Decision June 28, 1996).

process. The Judgment Officer also found Violette's claim that he had not been sanctioned for abusive tactics incredible.[12] Finally, the Judgment Officer concluded that in view of Violette's clear knowledge that abusive tactics would not be tolerated, a complete denial of discovery was "the only meaningful sanction available that will have an impact on Violette's disregard for the rights of other litigants." Order Denying Motion to Vacate Sanctions at 2. In this regard, the Judgment Officer noted that Violette's allegation did not depend on any documents or records but "solely on his contention that his broker failed to follow verbal trading instructions." *Id.*

Violette submitted a verified statement on February 26, 1999. In addition to reiterating his claims about the instruction he gave Palm on April 14, 1997, Violette asserted that he had previously given this type of instruction to Palm and she had followed it. In support, he alleged that Palm had liquidated an S&P option position at a loss of $1,414.16 on February 6, 1997 and had liquidated an S&P option position at a loss of $1,014 on February 13, 1997. Violette also indicated that he did not believe an oral hearing was necessary to resolve the complaint.[13]

On March 16, 1999, respondents submitted their verified statement. In an affidavit executed by Palm, respondents indicated that Violette's account was opened in December 1996 and was designated and treated as a non-discretionary account. Respondents acknowledged, however, that on occasion Palm placed trades for complainant's account based on a trading program. They indicated that these trades were entered "according to complainant's

[12] The Judgment Officer acknowledged that one of the cited cases involved Violette's brother but emphasized that in the other case Violette represented the complaining entity and was found to have acted in bad faith. *See The Violette Group, Inc. v. Ackerman*, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,729 at 44,013 (Initial Decision June 28, 1996).

[13] In early March, respondents moved to strike Violette's verified statement because he (1) failed to submit an affidavit of service, and (2) misstated the contract language material to respondents' counterclaim. On March 11, 1999, the Judgment Officer issued an order denying respondents' motion. The order admonished both sides to the dispute that "gamesmanship, vexatious conduct, and vituperative tactics" would not be tolerated and would result in strong sanctions such as dismissal or default.

instructions," and that the S&P trade at issue in this case was "wholly unrelated to the trading program." Palm Affidavit at ¶¶ 6-7.

Respondents reiterated their prior claims about Palm's conversation with Violette on April 14, 1997. For example, they indicated that Palm informed Violette that LFG was not accepting open stop orders for S&P option positions and that "he did not have any protective stop order in place to limit losses on [his June S&P call position]." Palm Affidavit at ¶ 12. Respondents indicated that Palm attempted to reach Violette by telephone on April 15, 1997 when she noticed that the market had moved one basis point against complainant's position. They stated that Palm was unable to leave a message for Violette because there was no answering machine or answering service available, but continued to try to reach Violette by phone. Palm Affidavit at ¶¶ 14-17. Respondents reiterated their prior claim that Violette did not inform Palm that he was leaving on an extended vacation. Palm Affidavit at ¶ 18.

Respondents acknowledged that the case involved a credibility dispute between Palm and Violette but contended that "[r]espondent Palm is clearly more believable when compared to the past and current practices of the complainant before this tribunal and this Judgment Officer." Respondents' Verified Statement at 5.

II.

The Judgment Officer conducted a telephonic hearing on April 29, 1999.[14] Violette and Palm were the only witnesses. Although respondents had counsel representing them, the Judgment Officer did almost all the questioning of the witnesses.

During his testimony, Violette acknowledged that during their conversation on April 14, 1997, Palm informed him that LFG was not accepting stop-loss orders for S&P option positions.

[14] The Judgment Officer had issued an order in late March indicating that a telephonic hearing was necessary to resolve credibility issues.

In this context, he indicated that "it wasn't like [Palm] took a stop order from me." Tr. at 9-10. He explained, however, that Palm had agreed to hold his order, monitor the market, and liquidate his open short June S&P call position when the market moved one point against the position. Tr. at 10.

When the Judgment Officer inquired about the specificity of Violette's order, complainant indicated that it was the same as similar orders that Palm had acted on in the past. The Judgment Officer then asked a series of questions about Violette's trades in S&P options. Tr. at 16-35. During these questions, both Violette and one of respondents' attorneys referred to several account statements that were not in the record. Palm also speculated about what some of the figures listed on these account statements might mean. Toward the end of this series of questions, the Judgment Officer explained that he had undertaken this review in order to evaluate Violette's claim that Palm had previously acted on complainant's instruction to liquidate an S&P option position at a one-point loss. The Judgment Officer then remarked that:

> The only options transactions I can find for those three months that you're involved in look like they were closed out at a profit to you, so it doesn't look like there was ever a dollar – at least in those February, March, April, there wasn't ever a $1 against you or one point against you, whatever it was, order that got triggered.

Tr. at 35. When the judge asked Violette whether he had anything indicating that Palm had liquidated an S&P options position after the market moved one point against the position, Violette said that he believed there was "one time" Palm filled such an order. Violette offered to try and find this trade, but the Judgment Officer indicated that he did not want to wait at that point.[15] Tr. at 36.

[15] Later in his testimony, Violette referred to two previous times that he "got hit with a loss" and estimated that the losses were about $1,100 to $1,200. Tr. at 56. Even later, he specified February 6 and 13 and the dates when Palm liquidated S&P option positions based on a one-point stop order even though LFG's trading desk was not accepting such orders. Tr. at 83-84.

The Judgment Officer then questioned Violette about the grain trades that Palm had made for his account while he was on vacation. Complainant explained that he did not give Palm instructions about the number of contracts to purchase and sell, but only told her to continue following the in-house trading system.[16] Tr. at 39. In this regard, he indicated that it was not Palm's practice to consult him before she made trades under the in-house system. *Id.*

Violette acknowledged that he did not try to contact Palm during his vacation even though he knew that the S&P market was volatile. In this regard, he explained that he was willing to accept risk in the range of $1,000 to $1,500 and felt that his instruction to Palm protected him from greater losses. Tr. at 56-57. Violette testified that the large loss he suffered was "devastating" but acknowledged that he waited until May 20, 1998 to file a written complaint with LFG. When the Judgment Officer questioned him about this delay, Violette said that filing a complaint earlier "probably did not cross [his] mind." Tr. at 69.

Palm's testimony reiterated many of the points made in respondents' prior submissions. She said that she did not believe Violette gave her a valid order to liquidate his S&P call position on April 14, 1997. Tr. at 109. She also insisted that Violette did not give her advance notice that he was going on vacation. Tr. at 110. She characterized their agreement on April 14 as she "would contact [Violette] if [the market rose one point] and then [they] would discuss how [they] should exit the position." Tr. at 62.

Palm claimed that the process for entering grain trades in Violette's account was significantly different than the process for entering other trades. Tr. at 109. When the Judgment Officer questioned her about the grain trades she had entered while complainant was away, Palm explained that Violette had entered "good 'til canceled orders" that authorized these trades. Tr.

[16] Complainant explained that someone at LFG "was trading the grains and [Palm] was getting the information from them, what to get into, out of, long, short, and she had done well with it, very well." Tr. at 40.

at 41. Under further questioning, however, Palm acknowledged that these orders did not specify the contracts to be purchased or sold and that she determined the order terms by consulting an LFG-sponsored grain-trading program.[17] Tr. at 44-45. When the Judgment Officer informed Palm that this practice violated Commission Rule 166.2, she said that she had "cleared that up" quite some time ago. Tr. at 48-49.

The Judgment Officer later asked Palm whether she would be willing to hold an S&P order for a customer and transmit it to the trading floor when the market reached a specified point. Tr. at 86. Palm said that if such an order were placed, she would execute it "even though [she] couldn't place it to the floor as such." *Id.* Palm also acknowledged that it was possible that prior to April 14, 1987, she had exited S&P option positions in Violette's account at a loss, but insisted that, "as far as [she could] recall", they were in continuous contact on a daily basis regarding all positions and orders prior to that date. Tr. at 105-106.

Finally, the Judgment Officer questioned Palm about her reaction when she was unable to contact Violette and the accrued loss for his S&P call option continued to grow. Violette said that she was "very concerned" and spoke with two people within LFG. She testified that these people recommended that she leave the position alone since there was no liquidation order. Tr. at 79, 113. She acknowledged that despite her concern, she only tried to contact complainant by telephone during the workday. Tr. at 114.

[17] Palm testified that she time-stamped order tickets at the time she spoke with Violette but did not fill in the required trading information or transmit the order to the trading floor until LFG's analyst came out with his recommendation. Tr. at 85.

IV.

In June 1999, the Judgment Officer issued his Initial Decision awarding damages to Violette. *Violette v. LFG, L.L.C.*, [1998-1999 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,667 (June 11, 1999) ("I.D."). The Judgment Officer reviewed both Violette's and Palm's versions of the events at issue and concluded that Violette's was more credible than Palm's. In support of this conclusion, the judge offered a detailed analysis of apparent flaws in Palm's testimony. He noted that Palm's testimony was hesitant and marred by what the Judgment Officer termed "a Watergate-style denial."[18] I.D. at 48,157. In this regard, the Judgment Officer emphasized that Palm initially did not flatly deny that prior to April 14, 1987 she had accepted Violette's one point stop order to protect an S&P option position when LFG's trading desk was not accepting such orders. He noted that she first indicated that she did not remember doing that, and then amended that response by saying that she did not recall such an order in the context of an S&P position. *Id.*

The Judgment Officer then turned to Palm's testimony regarding the practices she followed in making grain trades in complainant's account. He noted that these practices involved the very activity at issue here – accepting an order from Violette that she held until certain conditions were met rather than immediately sending the order to the trading floor. The Judgment Officer found it plausible that Palm's willingness to accept and hold grain orders for Violette "confused her regarding whether she had taken such orders in S&P contracts as well." I.D. at 48,158. He found it unnecessary to pinpoint the reason for Palm's initial hesitancy in testifying on this point because Violette's testimony was "much more credible" due to its

[18] The Judgment Officer explained this reference by noting that Palm qualified her statements with comments like "[a]s far as I recall" and "I believe." *Id.*

"factual reliability" and complainant's "more-convincing demeanor." *Id.*[19]

Finally, the Judgment Officer found several problems with Palm's testimony about her reaction to her inability to contact Violette while the market moved continuously against his S&P call option position. The judge contrasted Palm's testimony about her level of concern with her failure to testify that she made any extraordinary effort to contact Violette. In this regard, he noted that Palm did not clearly establish that she consulted her supervisors at LFG[20] and acknowledged that she had not taken steps to contact Violette during non-business hours. The Judgment Officer also found it significant that Palm had not provided Violette with written notification of the problem and did not make any written notes of her unsuccessful efforts to telephone him. *Id.* In light of these flaws, the Judgment Officer concluded that:

> Palm's testimony regarding her efforts to contact Violette [was] thoroughly incredible, as it was self-serving, unconvincing, and uncorroborated by any other witness or even the slightest amount of documentary evidence. Any remaining belief in Palm's credibility when compared to Violette's was laid to rest upon consideration of Palm's testimony regarding the alleged efforts to contact him after she failed to execute the order.

Id.

In light of Violette's testimony, the Judgment Officer found that Palm violated Section 4b of the Act by recklessly failing to execute complainant's one point stop loss order. The judge only discussed one apparent flaw in Violette's testimony – the unexplained conflict between his testimony that he was devastated by his loss and his acknowledged failure to complain about Palm's actions for over a year. In this regard, the Judgment Officer termed the delay in making a complaint "questionable" but emphasized that Violette had filed his reparation complaint within

[19] In explaining this remark, the Judgment Officer emphasized Violette's testimony defending his failure to either provide a telephone number where he could be reached or contact Palm while he was away. *Id.*

[20]The Judgment Officer found that Palm had made ambiguous statements about consulting with "two other individuals" and "two other people within the company." *Id.*

the applicable statute of limitations and there was no evidence that he had delayed in an effort to deprive LFG of notice that it should retain the tape recording of Palm's April 14, 1997 conversation with Violette. I.D. at 48,156 n.2

Because the record indicated that complainant was willing to lose $1,000 on his S&P call position, the Judgment Officer found that his actual damages were $17,300 -- the difference between the loss he actually suffered ($18,300) and the amount he would have lost if his position had been liquidated at 3.70. In this regard, the Judgment Officer found that "respondents have not contended that the one-point stop-loss order could not have been executed, nor have they asserted that it could only have been executed at a different level beyond a one-point loss." I.D. at 48,158. On this basis, the judge ordered respondents to pay complainant $17,300 plus prejudgment interest and costs.

On June 14, 1999, the Judgment Officer issued an amendment to his decision that reduced his award by $121.55. The judge indicated that this amount represented the costs that Violette owed respondents due to his discovery abuse.

V.

Respondents filed a timely appeal and followed up with an appeal brief in July 1999. The brief challenges the Judgment Officer's credibility assessment as one-sided, noting that he scrutinized Palm's testimony in detail but made no effort to explain why complainant's testimony was reliable. It emphasizes that the Judgment Officer failed even to discuss Violette's inability to corroborate his claim that Palm liquidated S&P option positions based on similar stop orders on both February 6 and 13, 1997.[21]

[21] As noted above, respondents' brief also challenges the Judgment Officer's legal analysis and rejection of respondents' ratification defense. Given the result of our analysis of the factual issues respondents raise, it is not necessary to address their other arguments in the context of this case.

On April 23, 2001, counsel for respondents filed a notice indicating that LFG was the subject of a bankruptcy proceeding filed on April 9, 2001 in the Northern District of Illinois.

DISCUSSION

I.

LFG's petition in bankruptcy prevents the Commission from continuing this proceeding against it. *See* 11 U.S.C. § 362(a)(1). Commission precedent establishes a policy of dismissing any pending reparations proceedings against a respondent subject to a bankruptcy proceeding "[i]n the absence of a showing of undue prejudice." *Levine v. Stotler & Co.*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,164 at 38,423-24 (CFTC Nov. 6, 1991). Because Violette has not made such a showing, we vacate the Judgment Officer's decision as to LFG and dismiss the complaint against it without prejudice.

II.

As noted above, in light of his review of Violette's and Palm's testimony, the Judgment Officer concluded that Violette's version of events was more credible than Palm's version of events. In recognition of presiding officers' opportunity to assess demeanor-based factors in determining credibility, the Commission generally defers to their credibility determinations in the absence of clear error. *See Ricci v. Commonwealth Financial Group, Inc.* [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶26,917 at 44,444 (CFTC Dec. 20, 1996). Indeed, we have noted that when the testimony of two or more witnesses is in conflict and a presiding officer finds one witness to be more truthful than any of the others, the circumstances are rare when that determination will amount to clear error. *Secrest v. Madda Trading Co.*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,627 at 36,696 (CFTC Sept. 14, 1989).

The Commission, however, has repeatedly emphasized that factual findings cannot be based on one party's testimony simply because the presiding officer finds that party's testimony more believable than the testimony of an opposing party. *See, e.g. Sommerfeld v. Aiello*, [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 28,271 (CFTC Sept. 29, 2000). The presiding officer must independently evaluate the reliability of a witness's version of events "in light of the record as a whole." *McDaniel v. Amervest Brokerage Services*, [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 28,264 at 50,589 (CFTC September 26, 2000). As explained in *Secrest*, ¶ 24,627 at 36,696:

> [W]hile accepting the judge's finding that the testimony of one witness was more truthful than that of another witness, we may conclude that the judge committed clear error in finding that the testimony was sufficiently reliable to serve as an adequate basis for findings of fact that must be supported by the weight of the evidence.

The record before us establishes a significant shortcoming in the Judgment Officer's approach to reviewing Violette's testimony in the context of the record as a whole. We have previously found that a presiding officer committed clear error by giving close scrutiny only to the testimony offered by one side to a dispute. *Sommerfeld*, ¶ 28,271 at 50,651. The Initial Decision in this case reflects a similar disparity in the level of scrutiny accorded to Palm's and Violette's testimony. The Judgment Officer closely analyzed different facets of Palm's testimony and raised legitimate questions about both the credibility and reliability of her version of events. His analysis of Violette's testimony, however, was mostly general and conclusory. This approach is particularly puzzling in light of the Judgment Officer's skeptical statements

about Violette's credibility both at the hearing and in declining to revise the discovery sanctions that he had imposed.[22]

Our independent review of the record discloses several problems that undermine the reliability of Violette's version of events. First, his verified statement clearly and unequivocally claimed that Palm accepted similar one point stop loss orders for S&P positions in the past and acted on them by liquidating S&P positions at a loss on February 6 and 13, 1997. Nevertheless, Violette did not submit the account statements that would establish the existence of these losses.[23] Moreover, during his testimony, Violette contradicted himself on this issue. At two points, he essentially reiterated the claim in his verified statement that Palm had twice accepted and acted on similar one point stop orders. Tr. at 56, 83-84. At another point, he said that he "believe[d] there was one time" a similar order was triggered. Tr. at 36.

Second, Violette essentially offered no explanation for his delay in making a written complaint about Palm's alleged breach of duty.[24] Under Violette's version of events, he went on vacation with the understanding that he was risking $1,000 to $1,500 and came back to learn that he faced a loss of $21,000. If this were true, one would normally expect an immediate and vigorous protest from the affected customer. Moreover, Violette's history of bringing reparations claims extends back to 1995, well before the time of the conduct at issue here.

[22] We recognize that a credibility assessment expressed at a hearing is tentative and may change after more careful reflection on testimony taken as a whole. If a presiding officer finds it necessary to express tentative views about credibility at the hearing, however, we would expect an explanation in his Initial Decision for the change in view.

[23] During his testimony, Violette acknowledged that account statements bearing on this issue were in his possession. Tr. at 22 (February monthly statement), 32 (February 13 statement).

[24] Indeed, Violette never specifically claimed that he made an oral complaint to Palm. Respondents' answer is the only document that purports to set forth the discussion between Violette and Palm at the time Violette returned from his vacation.

Consequently, there is no basis to infer that complainant was an innocent or uninformed customer unaware of the importance of protesting alleged misconduct.[25]

Finally, in rejecting complainant's motion to set aside the discovery sanctions he had imposed, the Judgment Officer found that Violette's explanations for his conduct were not credible. While, as discussed below, we take issue with the sanctions the Judgment Officer imposed, the record supports his conclusion that Violette's explanations were incredible. In the circumstances presented, Violette's decision to dissemble in the context of this discovery dispute raises a substantial question about the reliability of the version of events set forth in his testimony.[26]

These flaws are comparable to the flaws the Judgment Officer noted in Palm's version of events. Nevertheless, they are outcome determinative in the context of this case because Violette had the burden of establishing the facts material to his claim by the weight of the evidence. The record taken as a whole establishes that neither his testimony nor Palm's testimony is sufficiently reliable to support fact-finding that meets the weight of the evidence standard. Because the record does not include documentary evidence or other reliable testimonial evidence that supports Violette's claim, the Judgment Officer's decision must be vacated and the complaint against Palm dismissed.

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[25] The Judgment Officer noted that the statute of limitations in Section 14(a)(1) of the Act gave Violette two years to file his reparations complaint. While we agree that Violette's delay in complaining had no significance for purposes of applying the statute of limitations, the Judgment Officer failed to consider its significance in the context of Violette's credibility -- whether there was no immediate protest because Violette knew that he had not actually instructed Palm to liquidate if the market moved one point against his position.

[26] It is possible for a party to be incredible in one context but not in another. The record before us, however, indicates that Violette knew that his explanation for his discovery-related conduct was false when he offered it. Moreover, nothing in the record suggests that Violette took his obligation to tell the truth more seriously in the context of the testimony he offered at the hearing.

III.

In the unusual circumstances presented on this record, we conclude that it is appropriate to undertake *sua sponte* review of the discovery sanctions that the Judgment Officer imposed on Violette.[27] Commission precedent indicates that sanctions imposed for discovery abuses must be commensurate with the nature of the abuse at issue. *Radden v. Futures Trading Group*, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,281 at 42,425 (CFTC Dec. 12, 1994). The abuse at issue here, making overbroad requests, is fairly common in reparations cases. In general, the appropriate response to this abuse is the relief respondents specifically requested – an order imposing reasonable limits on the scope of the opposing party's production. The Judgment Officer's response to Violette's abuse went well beyond this. We think it was appropriate for the presiding officer to consider Violette's prior experience with the reparations forum in determining whether his discovery abuse was more likely a product of ignorance than an attempt to gain tactical advantage. Proper consideration of Violette's experience, however, does not justify the Judgment Officer's conclusion that only such a severe sanction would have a meaningful impact on Violette.

We conclude that the Judgment Officer abused his discretion when he denied Violette discovery and ordered him to pay respondents' costs for preparing a motion for a protective order. Discovery may have helped Violette develop a better record to attack Palm's credibility, but there is no basis to infer that discovery would have played a substantial role in bolstering Violette's own credibility. Consequently, we conclude that this aspect of the Judgment Officer's error was harmless. Violette, however, should not be required to pay respondents' costs.

[27] Commission Rule 12.401(f) indicates that the Commission retains the discretion to consider "any issue arising from the record." As noted above, Violette is appearing *pro se*. Because the Judgment Officer made a substantial award in his favor, he had little incentive to appeal the Initial Decision in order to challenge the discovery sanctions.

CONCLUSION

For the foregoing reasons, we vacate the Initial Decision as to LFG and dismiss the complaint against it without prejudice, vacate the Initial Decision as to Palm and dismiss the complaint against her with prejudice, and vacate the discovery sanctions that the Judgment Officer imposed on Violette.

IT IS SO ORDERED.[28]

By the Commission (Acting Chairman NEWSOME and Commissioners HOLUM, SPEARS, and ERICKSON).

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Catherine D. Dixon
Assistant Secretary to the Commission
Commodity Futures Trading Commission

Dated: September 6, 2001

[28] Under Sections 6(c) and 14(e) of the Act, 7 U.S.C. §§ 9 and 18(e) (1994), a party may appeal a reparation order of the Commission to the United States Court of Appeals for only the circuit in which a hearing was held; if no hearing was held, the appeal may be filed in any circuit in which the appellee is located. *See also* 17 C.F.R. § 12.209 (telephonic hearings in reparations proceedings are held in Washington, D.C.). The statute also states that such an appeal must be filed within 15 days after notice of the order and that any appeal is not effective unless, within 30 days of the date of the Commission order, the appealing party files with the court a bond equal to double the amount of any reparation award.