UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

In the Matter of:	:	
JERRY W. SLUSSER, FIRST REPUBLIC FINANCIAL CORPORATION, and FIRST REPUBLIC TRADING CORPORATION	:	CFTC Docket No. 94-14
	:	OPINION AND ORDER

In July 1999, the Commission found the three respondents[1] liable for multiple violations of the Commodity Exchange Act ("Act") and imposed sanctions that included cease and desist orders, registration revocations, permanent trading prohibitions, and a joint and several civil money penalty. *In re Slusser* [1998-1999 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,701 at 48,306 (CFTC July 19, 1999) ("*Slusser I*"). On review, the United States Court of Appeals for the Seventh Circuit endorsed the Commission's conclusion that respondents violated the Act in ways that amounted to "multiple frauds." *Slusser v. CFTC*, 210 F.3d 783, 784 (7th Cir. 2000) ("*Slusser II*"). In addition, the court affirmed the non-monetary sanctions that the Commission imposed on respondents. *Id*. at 788.

The Seventh Circuit refused to enforce the Commission's imposition of a civil money penalty, however, and remanded for further proceedings on this sanction. In this regard, the court held that, in the circumstances presented: (1) $600,000 was the maximum civil money penalty that the Act authorized the Commission to impose on each respondent; and (2) the Commission had the burden of demonstrating that any civil money penalty it imposed on Slusser

[1] During the period at issue, respondent Jerry Slusser ("Slusser") was the sole shareholder of respondent First Republic Financial Corporation ("FR Corp."). FR Corp. was the sole shareholder of respondent First Republic Trading Corporation ("FR Trading").

was appropriate to his net worth. *Id*. at 786-88.[2] In light of this holding, the court remanded to the Commission for further proceedings consistent with its opinion.

As explained more fully below, we conclude that a $600,000 civil money penalty is appropriate to the gravity of each respondent's violations. Because the record does not include sufficient evidence to permit us to evaluate the appropriateness of this level of civil money penalty either to Slusser's net worth or to the corporate respondents' size and ability to remain in business, we remand to the Administrative Law Judge ("ALJ") for further proceedings consistent with this Opinion and Order.

DISCUSSION

I.

The Commission responded to several aspects of the court's *Slusser II* opinion in a September 2000 decision. *In re Nikkhah*, [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 28,275 at 50,674-78 (CFTC Sept. 26, 2000) ("*Nikkhah II*"). *Nikkhah II* held that the Division of Enforcement ("Division") has both the burden of production and the burden of proof on issues relating to a respondent's net worth. It also emphasized that the Division has a right to discover information relevant to net worth-related issues, and that negative inferences could be drawn if a respondent fails to cooperate in the process.[3] Finally it specified a procedure that would provide respondents with an opportunity to protect the privacy of net worth information.[4]

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[2] The court's opinion referred to respondents FR Corp. and FR Trading as "defunct corporations," but noted that the Commission had the burden of demonstrating that civil money penalties imposed on these respondents were appropriate to both the size of each company's business and its ability to continue in business. The court said that consideration of these two factors involved a "collectibility condition." *Id*. at 786-87.

[3] We held that the ALJ must give the Division reasonable time to seek discovery, to subpoena witnesses, and to retain experts to review, analyze, and testify about the information obtained.

[4] *Nikkhah II* indicated that respondents should be given notice of the amount of a civil money penalty appropriate to the gravity of their violations and an opportunity to stipulate that this level of civil money penalty was also appropriate to net worth. *Id*. at 50,677-78.

Consistent with this procedure, a determination of the level of civil money penalty appropriate to the gravity of each respondent's wrongdoing is the first step in complying with the court's remand. In most cases, the presiding ALJ makes the initial determination on this issue. Given the age of this case and the benefits of simplifying the ALJ's task on remand, however, we are relying on our own *de novo* analysis.

As a general matter, Commission precedent recognizes that the level of civil money penalty appropriate to the gravity of a respondent's violations is not the same as the maximum permitted under the Act's $100,000 per violation test.[5] As we explained in *In re Incomco*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,198 at 38,535-36 n. 16 (CFTC Dec. 30, 1991):

> In enacting [then] Section 6(b) of the Act, Congress established a relationship between the number of violations a respondent commits and the maximum level of civil [money] penalty the Commission may impose. Nevertheless, our selection of appropriate sanctions in a particular case turns more on an examination of the overall nature of the wrongful conduct respondent has committed than a simple enumeration of the violations established on the record.

Because our precedent has generally focused on the overall gravity of respondents' violations rather than their number, we have not frequently commented on the appropriate method for counting violations. When we have commented on the subject, however, we have generally endorsed what might be characterized as a broad but common sense approach.

[5] The current version of the Act includes alternative tests for determining the maximum size of a respondent's civil money penalty and only requires that that the Commission's determination of the amount of a civil money penalty include consideration of the "appropriateness" of the amount to the "gravity" of respondent's violations. Because the conduct at issue in this case took place prior to 1992, the Commission's authority is more limited. The applicable version of the Act restricts the maximum size of a civil money penalty to "$100,000 for each . . . violation," and mirrors the current Act's requirement that the Commission's determination include consideration of the appropriateness of the amount to the gravity of the violations at issue. In addition, when a respondent's "primary business" involves use of the commodity futures markets, the applicable version instructs that the Commission's determination include consideration of the appropriateness of the amount to the "size" of respondent's business and the extent of respondent's "ability to continue in business." In all other cases, it instructs that the Commission's determination include consideration of the appropriateness of the amount to respondent's "net worth."

For example, in *In re Carr*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,933 (CFTC Oct. 2, 1990), the Commission considered the appropriate civil money penalty for a continuing violation of a cease and desist order and observed that "[e]ach day of noncompliance with a Commission rule may constitute a separate violation." *Id.* at 37,397 n.3. Similarly, in *In re Rosenthal & Co.*, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,221 (CFTC June 6, 1984), the Commission considered a dispute about the proper method for calculating the number of violations when the Complaint at issue alleged a nationwide solicitation fraud involving 25 offices and a sales force of 500. In this context, the Commission rejected respondents' claim that only one violation had been alleged and proven. Rather, it concluded that "multiple" violations had been proven, and, in support, cited to a recent court decision concluding that each mailing of a deceptive letter amounted to a separate violation of an FTC consent order. *Id.* at 29,191.

The application of this broad but common sense approach in the context of the circumstances underlying most enforcement proceedings results in a violation count that generally ranges from dozens to hundreds of violations. Consequently, it is rare that the level of civil money penalty appropriate to the gravity of respondent's violations approaches the level produced by multiplying the number of violations by $100,000. Indeed, it is not unusual for the Commission to dismiss certain allegations without detailed consideration because their determination "would not have a material effect on the sanctions [the Commission] would impose." *In re Nikkhah*, [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 28,129 at 49,887 n. 26 (CFTC May 12, 2000).

The allegations in this case involve the type of broad-based, repeated wrongdoing that we would normally view as involving hundreds of violations. Indeed, in its opinion in *Slusser II*,

the court acknowledged that the events described in the Complaint in this proceeding could be viewed in this manner. *Slusser II*, 210 F.3d at 786. In the circumstances presented, however, the court viewed the form of the Complaint, specifically its organization into six Counts, as the best evidence of the number of violations alleged.[6] Consequently, it held that $600,000 was the maximum civil money penalty we could impose on each of the respondents. *Id.*

We do not normally equate the number of violations at issue in an enforcement proceeding with the number of Counts included in a Complaint. *See*, *e.g.*, *In re JCC Inc.*, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,080 at 41,571, 41,583 (CFTC May 12, 1994) (affirming a $510,000 civil money penalty in the context of a Complaint including two Counts); *In re Grossfeld*, [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,921 at 44,461, 44,471 (CFTC Dec. 10, 1996) (imposing a $1.3 million civil money penalty in the context of a Complaint including three Counts). We recognize, however, that in this case we are bound by the court's finding that a "reasonable person in Slusser's position" would have viewed the proceeding as involving only six violations. *Slusser II*, 210 F.3d at 786. Consistent with our precedent, however, our evaluation of the gravity of respondents' violations looks beyond this bare number to the overall nature of the violations.

As we noted in our prior decision in this matter, respondents' violations involve fraud, and the statutory and regulatory prohibitions on fraudulent conduct are at the core of regulatory

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[6] The court noted that:

> Most of the violations narrated by the complaint [in this case] entail multiple acts or statutes; it would have been easy to separate the events into tens if not hundreds of violations, or to allege that each day of managing the funds without registration as a commodity pool operator was a separate violation. But the CFTC staff did not do any of these things . . . . Just as the sentence in a criminal case is limited by the number of counts alleged in an indictment times the maximum punishment for each offense, so the penalty in an administrative prosecution is limited by the number of violations alleged in the complaint times the maximum fine per violation. [In light of the number of Counts included in the Complaint, a] reasonable person in Slusser's position would have assumed that his maximum exposure was $600,000 and financed his defense accordingly.

Id.

provisions that the Commission enforces. The violations were intentional and extended over several months. Respondents made no attempt to cure their violations or to cooperate with the Commission's investigation of their conduct. The record permits us to reliably estimate respondents' gain from their wrongdoing at $6 million dollars and the net loss to pool customers at $6.5 million.

In view of this evidence, we conclude that a civil money penalty of at least $600,000 is warranted by the violations committed by each respondent.[7]

II.

Under the procedure we established in *Nikkhah II*, our determination of the civil money penalty appropriate to the gravity of the violations established on the record sets the stage for a decision by each respondent. If one or more respondent wishes to preserve the confidentiality of the financial information necessary to determine whether a $600,000 civil money penalty is appropriate to his net worth (respondent Slusser), or to its size and ability to continue in business (respondents FR Corp. and FR Trading), they may submit a written stipulation indicating that a $600,000 civil money penalty is appropriate to the applicable factor or factors. Otherwise, they will be required to cooperate with the Division's efforts to develop the record on factual issues material to the applicable factors. As we noted in *Nikkhah II*, in the absence of an appropriate written stipulation:

> The ALJ shall draw appropriate adverse inferences against respondents who fail to comply with their discovery obligations or to either appear or testify at [a] supplemental hearing after receiving a request from the Division.

[7] The record does not establish an appropriate basis for ignoring the formal distinctions between the individual and corporate respondents for purposes of analyzing money sanctions. *Compare In re Armstrong*, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,657 at 40,145 (CFTC Feb. 8, 1993) (ALJ erred by treating separate individual and corporate respondents as a "single enterprise" for purposes of assessing liability and sanctions). In the circumstances presented, however, careful delineation of the roles the different respondents played in the violations established on the record is not necessary. FR Trading clearly played a lesser role than either Slusser or FR Corp. Even its wrongdoing, however, is sufficiently grave to warrant a civil money penalty of $600,000.

Nikkhah II, ¶ 28,275 at 50,678. We direct the ALJ to permit respondents 30 days from the date this order is served to file and serve an appropriate stipulation.

As noted above, in the course of its *Slusser II* decision, the court referred to FR Corp. and FR Trading as "defunct corporations." *Slusser II*, 210 F.3d at 787. The court apparently based this characterization on an affidavit that Slusser submitted in connection with a motion to stay sanctions. Because the affidavit is conclusory and the record raises significant questions about Slusser's credibility, we are reluctant to accord significant weight to the affidavit's assertions. On the other hand, the public interest will not be served by prolonging the proceeding so that civil money penalties may be imposed on firms that are effectively out of business. In the interest of expedition and minimizing the cost of further proceedings, the ALJ should explore the possibility of joint stipulations relating to the current status of the corporate respondents.[8]

III.

In the absence of respondents' written stipulations, the ALJ shall give the Division a fair opportunity to develop the record on the applicable factors. In this regard, the Division shall be given reasonable time to seek discovery pursuant to Commission Rule 10.42(e) and 10.44(b) through (f),[9] to subpoena witnesses to appear at a supplemental oral hearing on material issues of fact, and when necessary, to retain experts to review and analyze the information obtained through discovery and to testify at the supplemental hearing.

[8] As a matter of clarification, we note that we would normally evaluate the civil money penalty imposed on the corporate respondents in light of gravity and net worth rather than their size and ability to remain in business. Under the applicable version of the Act, the latter factors apply when a respondent's primary business involves the use of the commodity futures markets. In light of the registration revocations and trading prohibitions imposed on the corporate respondents, our precedent recognizes that their primary business will no longer involve the use of the commodity futures markets. *See, e.g., In re Lincolnwood Commodities, Inc.*, [1982-1984 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,986 at 28,260 (CFTC Jan.31, 1984). We apply a different analysis in this case in light of our interpretation of the holdings in the Seventh Circuit's *Slusser II* decision.

[9] For these purposes, we waive the requirements of Commission Rule 10.44(a)(1) through (3) and (b)(3).

Following the supplemental hearing, the ALJ shall provide a reasonable period for the parties to submit proposed findings of fact and conclusions of law on material issues. Within 60 days of the deadline for making such submissions, the ALJ shall issue a supplemental Initial Decision resolving disputed issues of material fact and determining the appropriate civil money penalty in light of the applicable statutory factors.[10]

CONCLUSION

We vacate the civil money penalty previously imposed on the three respondents and conclude that, in light of the gravity of their violations, each should pay a $600,000 civil money penalty. We remand this proceeding to the ALJ for further proceedings consistent with this Opinion and Order.

IT IS SO ORDERED.

By the Commission (Chairman NEWSOME, and Commissioners HOLUM, LUKKEN, and BROWN-HRUSKA)

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Jean A. Webb
Secretary to the Commission
Commodity Futures Trading Commission

Dated: February 28, 2003

[10] In *Slusser I*, we imposed a single civil money penalty and made each respondent jointly and severally liable for its payment. We interpret the court's decision, however, as requiring the ALJ to make an independent determination of the civil money penalty appropriate to each respondent. Consequently, the ALJ shall not impose a joint and several payment obligation.