

Commodity Futures Trading Commission
CEA CASES

NAME: ZENITH-GODLEY COMPANY, INC. AND JOHN MCCLAY, JR.

CITATION: 6 Agric. Dec. 900

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(A. D. 1602)

In re ZENITH-GODLEY COMPANY, INC., and JOHN MCCLAY, JR. CEA Doc. No. 42.
Decided September 3, 1947.

Suspension of Trading Privileges Held in Abeyance

Where respondents pursuant to agreement with Dairymen's association interested in supporting price of butter purchased for the association's account 97 percent of butter on the New York Mercantile Exchange at not less than the price fixed by the association, it is held, that respondents manipulated the price of a commodity in interstate commerce in violation of the act, and order entered suspending their trading privileges for 90 days, such suspension to be held in abeyance for two years conditioned upon observance of the act by respondents. *

* Reference to other points involved in this case will be found in Index-Digest in this issue of Agriculture Decisions. -- Ed.

Intrastate Aspects of Methods of Manipulating Prices Not Changing Character of Transactions in Interstate Commerce

Since under sections 6 (b) and 9 of the act and under the commerce clause of the Federal constitution it is not required that the methods of manipulating the price of a commodity in interstate commerce be themselves interstate, the act has been violated by respondents even though the manipulative transactions might be said to have been physically intrastate and, in any event, the New York Mercantile Exchange is a market interstate in character and the purchases made by respondents were transactions in interstate commerce. *

* Reference to other points involved in this case will be found in Index-Digest in this issue of Agriculture Decisions. -- Ed.

Interstate Commerce -- Intent of End of Movement of Commodity as Criterion of Character of Transaction -- Intermingling of Purchases, When Not Changing Interstate Character of Transaction

The general rule is that where transportation has acquired an interstate character "it continues at least until the load reaches the point where the parties originally intended that the movement should finally end" and the intermingling of such purchases or sales with intrastate transactions does not interfere with the federal power to regulate the entire transaction. *

* Reference to other points involved in this case will be found in Index-Digest in this issue of Agriculture Decisions. -- Ed.

Constitutional Law -- Fifth Amendment -- Use of Terms not Defined in Act

Although the words "manipulation", "manipulate", and "manipulating" are not defined in the act, these terms are not so vaguely used as to render the part of the act defining a violation in those terms unconstitutional under the Fifth amendment of the Federal constitution. *

* Reference to other points involved in this case will be found in Index-Digest in this issue of Agriculture Decisions. -- Ed.

Mr. Benj. M. Holstein for complainant. *Messrs. John W. Burke and Herbert A. Heerwagen, of Davies, Auerbach, Cornell & Hardy, New York City,* for respondents. *Mr. John J. Curry,* Hearing Examiner.

Decision by Thomas J. Flavin, Judicial Officer

DECISION AND ORDER

This is a disciplinary proceeding under the Commodity Exchange Act (7 U. S. C. Chapter 1) involving charges by the complainant (usually called the Government herein) that the respondents, Zenith-Godley Company, Inc., and John McClay, Jr., of New York City, manipulated the price of butter in interstate commerce in that on or about December 17, 1946, the Dairymen's League Co-Operative Association, Inc. (hereinafter called the League), engaged respondents' services to purchase butter for its account on the New York Mercantile Exchange, on December 18, 19, 20, 23, and 24, 1946, "at not less than 84 cents per pound", and that pursuant to such engagement the respondents during such period of time offered to purchase and did purchase approximately 668,000 pounds of butter on the New York

Mercantile Exchange for the account of the Dairymen's League at the price of 84 cents per pound. It is alleged that the price of 84 cents per pound paid for the butter thus purchased was an artificial and manipulated price which influenced or determined the price of butter in interstate commerce and constituted a violation of Sections 6(b) and 9 of the Commodity Exchange Act (7 U. S. C. 9, 13). n1

n1 "SEC. 6 (b). If the Secretary of Agriculture has reason to believe that any person (other than a contract market) is violating or has violated any of the provisions of this Act, or any of the rules and regulations made pursuant to its requirements, or has manipulated or is attempting to manipulate the market price of any commodity, in interstate commerce, or for future delivery on or subject to the rules of any board of trade, he may serve upon such person a complaint stating his charges in that respect, to which complaint shall be attached or contained therein a notice of hearing * * * requiring such person to show cause why an order should not be made directing that all contract markets until further notice of the Secretary of Agriculture refuse all trading privileges to such person. * *

"SEC. 9. Any person who shall * * * manipulate or attempt to manipulate the price of any commodity in interstate commerce, or for future delivery on or subject to the rules of any board of trade, * * * shall be deemed guilty of a misdemeanor, and upon conviction thereof, be fined not more than \$ 10,000 or imprisoned for not more than one year, or both, together with the costs of prosecution."

The respondents in their answer denied the charges, and by way of affirmative defense set forth their version of the transactions involved and their participation therein. The answer also set up as affirmative defenses (1) that the transactions involved were not in interstate commerce as that term is defined in the act, (2) that the acts complained of did not constitute manipulation within the terms and meaning of the act and that the words "manipulation", "manipulate", and "manipulating" are so vague, indefinite and

uncertain as to render the part of the statute defining a violation in those terms unconstitutional under the Fifth Amendment to the Constitution of the United States, and (3) that the prohibition against manipulation of prices does not govern cash transactions under the act.

A hearing was held at 60 Beaver Street, New York, New York, on March 18, 1947, before John J. Curry, a hearing examiner duly designated by the Acting Chief Hearing Examiner, United States Department of Agriculture, to act as referee in the proceeding. Benjamin M. Holstein, Office of the Solicitor, appeared for the complainant. The firm of Davies, Auerbach, Cornell & Hardy, 1 Wall Street, New York, New York, John W. Burke and Herbert A. Heerwagen of Counsel, appeared for the respondents. At the close of the Government's case, respondents moved to dismiss the proceeding. The examiner denied the motion. Both parties offered testimony and introduced exhibits in evidence. By agreement the time for filing suggested findings of fact, conclusions, order, and briefs was extended to May 20, 1947, and both parties filed such documents within the time allowed. On June 20, 1947, the Government filed an amendment to its suggested findings of fact, conclusions, and order. The examiner issued his report on July

16, 1947. No exceptions were filed and no oral argument before the deciding officer was requested. Except for some rearrangement, this decision and order are, then, substantially the same as proposed by the examiner in his report.

The issues are (1) whether the butter prices established on the New York Mercantile Exchange on December 18, 19, 20, 23, and 24, 1946, were manipulated and (2) whether the prices of a commodity in interstate commerce were manipulated.

It is not disputed that respondent McClay, while acting as a broker, purchased on the Exchange during the above five-day period 668,060 pounds of butter for the account of the League. Respondent McClay, however, denied that he was aware of the purpose of the League in acquiring the butter.

FINDINGS OF FACT

1. Respondent Zenith-Godley Company, Inc. (hereinafter referred to as Zenith-Godley), is a New York corporation having its principal place of business and office in New York, New York. It is a wholesale dealer engaged in the business of distributing butter and eggs.

2. Respondent John McClay, Jr., New York, New York, during all the times material herein was and now is president of Zenith-Godley and enjoyed membership trading privileges on the New York Mercantile Exchange, a duly designated contract market under the act. The brokerage commissions realized by respondent McClay in connection with the transactions involved herein inured to the benefit of Zenith-Godley. The butter involved herein was in New York at the time of sale and ready for immediate delivery. All transactions were for cash. Prior to the date of the transactions involved herein, respondent McClay had not operated in the capacity of broker on the Exchange.

3. The Dairymen's League Co-Operative Association, Inc., is a cooperative association of milk producers with offices at 11 West 42d Street, New York, New York, and is engaged in the business of marketing fluid milk produced by its members. It does not have membership trading privileges on the New York Mercantile Exchange.

4. Under the provisions of an order of the Secretary of Agriculture issued under authority contained in the Agricultural Marketing Agreement Act, as amended (7 U. S. C. 601 *et seq.*), the price required to be paid by handlers for Class I-A or fluid milk during any month is determined by a formula based substantially upon prices paid for Grade A butter on the New York market. n2 On December 17, 1946, the

price of Grade A butter on the Exchange had declined to 82 1/2 cents per pound and on that date the League ascertained that, pursuant to the formula referred to above, the price of such butter would have to be quoted at 84 cents or higher from December 18 through December 24 for the price of Class I-A or fluid milk to remain at the same level during January 1947 as it had been during December 1946.

5. On December 17, 1946, the Executive Committee of the League determined to support the price of butter in order to prevent a decrease in the price of milk, and on the afternoon of the same day its representatives conferred with respondent McClay regarding making purchases of butter on the Exchange. Pursuant to instructions from the League, respondent McClay on December 18, 19, 20, 23, and 24, 1946, purchased on the Exchange for the account of the League a total of 668,060 pounds of Grade A butter, or a total of 97 percent of all the Grade A butter sold on the Exchange during this period. During the same period respondent McClay sold to the League out of the inventory of Zenith-Godley 48,404 pounds of Grade A butter and 133,048 pounds of Grade AA butter. About 96 percent of all the butter purchased by McClay was purchased at 84 cents or higher. McClay's trading during this period was the equivalent of 40 percent of the volume of trading on the New York Mercantile Exchange during the immediately preceding 5 1/2-month period. During this period McClay stood ready to purchase all Grade A butter on the Exchange at the price of 84 cents or higher—and on December 18 and December 24, 1946, made bids for Grade A butter on the Exchange at prices of 84 and 84 1/2 cents, respectively, which bids remained unfilled at the close of trading.

6. The normal difference in prices between the Chicago butter market and the New York butter market ranges from zero to 2 cents, the New York price being generally higher than the Chicago price by the amount of the freight rate of 1 1/2 cents. On December 18 and 20, 1946, the spread was 4 1/2 cents, on December 23, 1946, it was 6 cents, and on December 24, 1946, it was 7 1/2 cents. As a result of the wide spreads, large quantities of butter were diverted during the five-day period from the Chicago market to the New York Mercantile Exchange.

7. The price of Grade A butter on the New York Mercantile Exchange declined from 87 cents on December 9 to 82 1/2 cents on December 17 and further declines in price were expected on the latter date.

8. The price of Grade A butter on the New York market rose from 82 1/2 cents on December 17 to 84 cents on December 18 and remained at 84 cents through December 24, 1946. After the League discontinued its purchases at the close of trading on December 24, the price of

Grade A butter dropped from 84 cents on December 24 to 74-75 cents on December 26, 1946. The rise in price to 84 cents and the 84-cent price through December 24 were due largely to the activities described in Finding 5. The price decline after December 24 was due largely to the cessation of purchases for the League.

9. The price of butter on the New York Mercantile Exchange determines the price of butter on the New York market, and the price of butter on the New York market determines the price of butter in Philadelphia and points in New Jersey and affects the price of butter in Boston and Chicago.

10. Most of the butter shipped to New York City originates in states other than New York.

11. Members of the New York Mercantile Exchange have customers located in states other than New York and butter is bought and sold on the New York Mercantile Exchange for shipment to other states.

12. Of the total quantity of butter purchased by respondent McClay during the five-day period, 208,319 pounds were at the time of purchase owned by out-of-state consignors and were sold for their accounts on the Exchange.

n2 Order No. 27, as Amended, Regulating the Handling of milk in the New York Metropolitan Marketing Area (7 CFR. Ch. IX, Part 927). Other factors that enter into the formula are the average price of skim milk for human consumption and the average price of skim milk used for animal feed.

CONCLUSIONS

I

The Government contends that price manipulation took place during the five-day period from December 18 through December 24, 1946, in that the respondents, the corporate respondent acting through respondent McClay, prevented the price of Grade A butter from going down to its natural price level during such period. In *In re General Foods Corporation et al.*, 6 Agric. Dec. 288 (6 A. D. 288), decided April 28, 1947, it is stated at page 305 that "To manipulate prices means . . . to cause prices to go up or down by means directed to either such end or to prevent prices from going up or down by means directed to either such end."

There seems to be hardly any doubt that the prices established during the five-day period were manipulated. On December 17 the League committed itself to a program of heavy purchases of Grade A butter during the five-day period that followed when during that period it was essential for its purpose that the price of such butter be 84 cents on December 18 and remain at that price during the remainder of the period. The record shows that by reason of the League's purchases it was the market and thereby fixed the price. The League succeeded in its purpose and on December 26, 1946, it issued a press release announcing the success of its undertaking.

Respondents claim that McClay was unaware of the purposes of the League in entering the butter market and that McClay was merely

purchasing butter for a customer. McClay was following instructions to buy butter at a predetermined price when the market price was declining. While it is possible that McClay was not entirely familiar with the technical provisions of Order No. 27 as amended, he could not help but know under the circumstances that the purchases were for a price-influencing purpose in connection with butter rather than merely to procure butter for a customer.

II

Respondents urge also that they did not manipulate the price of butter in interstate commerce in violation of the act. They argue that the butter McClay purchased had come to rest at the time of sale and that, therefore, whatever interstate character it may have had prior to that time was ended when the butter came to rest in New York.

Sections 6 (b) and 9 of the act prohibit the manipulation of prices of a commodity in interstate commerce. It would seem that under these statutory provisions, and certainly under the commerce clause of Article I of the Constitution, it is not required that the *methods* of manipulating the price of a commodity in interstate commerce be themselves interstate. In other words, if the price of a commodity in interstate commerce is manipulated, the act has been violated even though the manipulative transactions which brought about the result might be said to have been physically intrastate. But in any event, it is clear (1) that the New York Mercantile Exchange is a market interstate in character and (2) that much of the butter purchased was itself in interstate commerce and that such purchases were transactions in interstate commerce.

Over 90 percent of New York City's butter supply comes from other states, principally from the Middle West. Members of the Exchange have customers located outside of the State of New York. Accordingly, it would appear that in the common course of trade butter arrives in New York from the West, it is bought and sold on the New York market and some of it goes on to other states for ultimate consumption. Butter prices established on the New York Mercantile Exchange largely determine butter prices on the Philadelphia market and points

in the State of New Jersey. New York prices also affect prices on the Boston market and the Chicago market. Such facts are generally recognized by the trade. Moreover, the Exchange is a duly designated contract market subject to the provisions of the Commodity Exchange Act and the rules and regulations issued pursuant thereto. It would seem, then, that the New York Mercantile Exchange is a market interstate in character.

Chicago Board of Trade v. Olsen, 262 U. S. 1, 40 (1923). This market is similar to the markets such as stockyards regulated under the Packers and Stockyards Act, 1921, as amended (7 U. S. C. 201 *et seq.*), and the designated areas under Title V of the Packers and Stockyards Act, as amended (7 U. S. C. 218 *et seq.*), with respect to which the handling of live poultry is regulated. The constitutionality of these statutory provisions regulating these markets is well-established.

Any question on whether respondents manipulated the price of a commodity in interstate commerce is dispelled when it is seen that a substantial portion of the butter purchased, 208,319 pounds, was sold for the account of consignors located in Iowa, Illinois, Minnesota, and New Jersey. The New York vendors of this consigned butter were the consignees.

The courts have repeatedly held that purchases of live poultry by marketmen at the live poultry terminals in New York City are transactions in interstate commerce. *Local 167 v. United States*, 291 U. S. 293, 297 (1934); *Live Poultry Dealers Protective Ass'n v. United States*, 4 F. (2d) 840 (C. C. A. 2d, 1924); *Greater New York Live Poultry Chamber of Commerce v. United States*, 47 F. (2d) 156, 158 (C. C. A. 2d, 1931); cf. *Schechter v. United States*, 295 U. S. 495, 542 (1935).ⁿ³ The interstate character of the transaction is not changed by reason of the fact that the commission merchants may have purchased the shipments of poultry they had received from producers in interstate commerce and which later they sold to marketmen, instead of selling such poultry on commission. *Greater New York Live Poultry Chamber of Commerce v. United States*, *supra*; *United States v. Erie R. Co.*, 280 U. S. 98 (1929). It is well established that commerce includes the purchase and sale in connection with interstate transportation quite as much as it does the transportation. *Binderup v. Pathe Exchange*, 263 U. S. 291, 309 (1923); *Swift & Co. v. United States*, 196 U. S. 375, 398 (1905); *Mulford v. Smith*, 307 U. S. 38, 48 (1939); *Bahnke-Walker Milling Co. v. Bondurant*, 257 U. S. 282, 290, 291 (1921); *Lemke v. Farmers Grain Co.*, 258 U. S. 50, 54 (1922); *Stafford v. Wallace*, 258 U. S. 495, 519 (1922).

ⁿ³ In the case of *United States v. Independent Meat & Poultry Market*, 32 F. Supp. 317 (1940), the District Court for the District of New Jersey held that the sale to a marketman of live poultry owned by the seller, a receiver operating at the city market in Newark, New Jersey, was not a transaction in interstate commerce. This decision cites the *Schechter* case as authority and directs attention primarily to the activities of the marketmen subsequent to the purchase of live poultry at railroad terminals. It is believed that any statements of the Court which may indicate that the purchases of live poultry at a railroad terminal, such as the City Market, are not in interstate commerce, are inconsistent, not only with the holding of the Supreme Court in the *Schechter* case but with the decisions in the other cases cited.

The general rule is that where transportation has acquired an interstate character "it continues at least until the load reaches the point where the parties originally intended that the movement should finally end." *Illinois Central R. R. Co. v. Louisiana R. R. Comm.*, 236 U. S. 157, 163 (1915). The intermingling of such purchases or sales with intrastate transactions does not interfere with the Federal power to regulate the entire transactions. *United States v. Rock Royal Cooperative, Inc., et al.*, 307 U. S. 533 (1939); *Currin v.*

Wallace, 306 U. S. 1 (1939); *United States v. Wrightwood Dairy Co.*, 315 U. S. 110, 120 (1942).

The fact that the State of New York may have been the final destination of all the butter purchased by Mr. McClay is immaterial. As above indicated, its interstate movement had not ended prior to its purchase by him and could not, therefore, be affected by its disposition after such purchase. The precise point was covered in the *Greater New York Live Poultry Chamber of Commerce* case, *supra*, at page 158, where the court recognized the circumstance that in the livestock cases, the cattle, after sale and processing in Chicago, resumed their interstate journey as finished products. The court conceded that this feature was absent in the case then before it, but held such absence immaterial and stated that the result in the livestock cases would not have been different "had the steers shipped from the West to Chicago been bought for butchering and sale in the Chicago market."

We may conclude that since the New York Mercantile Exchange is an interstate market, and particularly since the transactions in this case involved the purchase of butter which, at the time of such purchase was moving in interstate commerce, the manipulation which occurred was manipulation of the price of a commodity in interstate commerce.

III

Respondents also insist that the words "manipulation", "manipulate", and "manipulating" are so vague and uncertain as to render the part of the statute defining a violation in those terms unconstitutional under the Fifth Amendment to the Constitution of the United States. Similar objections were raised and overruled in *In re General Foods Corporation et al.*, *supra*. In *Bartlett Frazier Co. v. Hyde*, 65 F. (2d) 350 (C. C. A. 7th, 1933), *cert. denied*, 290 U. S. 654 (1933), a proceeding under the Grain Futures Act, it was contended that the statute made use of the term "manipulate" without defining what was meant by it and that for this reason the statute was void. In the course of its opinion, the court stated (at page 354) that "Even if we were disposed to attribute to the term undue uncertainty or indefiniteness, *Chicago Board of Trade v. Olsen* would forbid." Accordingly,

it is concluded that there is no substance to respondents' contention on this point.

IV

Little need be said concerning respondents' contention that the act does not cover cash or spot transactions. The Supreme Court in the course of its opinion in *Chicago Board of Trade v. Olsen*, *supra*, indicated clearly (page 39) that cash transactions were covered by the Grain Futures Act (predecessor to the Commodity Exchange Act) and added that "A futures market lends itself to . . . manipulation much more readily than a cash market." The plain import of the language of the statute shows that cash transactions are subject to regulation. Section 6 (b) of the act forbids manipulation of the price of any commodity in interstate commerce [of a cash nature] or for future delivery. Sections 4 (b) and 9 contain similar prohibitions. The act and the legislative history preceding its enactment make it clear that both types of transactions come within the purview of the statute.

It should be stated that most of the suggested findings and conclusions presented by each of the parties have been discussed or ruled upon in the course of this decision. If any of such matters have not been ruled upon specifically, the decision shall be considered as having overruled all findings or conclusions inconsistent with it.

The violations found herein are serious and warrant remedial measures. As McClay was a responsible officer of the corporate respondent, the latter must be held equally liable for the violations. The Government in its suggested findings and conclusions and order made the following recommendation:

"As above indicated, these violations were wilful because Mr. McClay intended his acts to have result which they in fact did have. However, it does appear that he may have been led to believe by his principals that no irregularity on his part would be involved in making such purchases. While we recognize the fact that, having chosen to trade on a contract market he was under the duty of doing so in accordance with law, we believe that in view of this mitigating circumstance the purposes of the Act will be served in this case by a suspension of the trading privileges of both respondents for a period of ninety (90) days, such suspension to be held in abeyance for a period of two years conditioned upon their observance of all provisions of the Act and regulations during that period."

There is nothing in the record which would cause us to dissent from the recommendation thus made and it is therefore adopted herein.

ORDER

All contract markets shall refuse the respondents Zenith-Godley Company, Inc., and John McClay, Jr., all trading privileges for a

period of ninety days; provided, however, that this sanction shall not become effective unless within a period of two years from the date of this order the said Zenith-Godley Company, Inc., or John McClay, Jr., after complaint and hearing in accordance with established procedure, should be found to have again violated the act, then and in that event and without further notice to the said Zenith-Godley Company, Inc., or John McClay, Jr., the Secretary of Agriculture or his duly authorized delegates may issue a supplemental order in this proceeding vacating such suspension and making effective forthwith the aforesaid denial of trading privileges for such 90-day period.

A copy of this order shall be sent by registered mail to each of the parties and to each contract market.

LOAD-DATE: March 12, 2008

