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

OFFICE OF
PROCEEDINGS

GREGORY PAUL VIOLETTE, and PAMELA G. VIOLETTE, Complainants[1]	)	
v.	)	CFTC Docket No. 97-R020
FIRST AMERICAN DISCOUNT CORPORATION, SCOTT ALLEN WOLF, WOLF FUTURES GROUP, INC., and DAVID JUDE JAVOR, Respondents[2]	)	

INITIAL DECISION

This case involves charges of unauthorized trading by respondent Wolf and the firm Wolf controlled.[3] According to complainant, Wolf repeatedly traded numerous contracts on days when he had been authorized to trade only one contract. According to Wolf, complainant had authorized

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[1] Violette's ex-wife, Pamela G. Violette, signed the complaint. She was dismissed as a complainant by Order dated May 20, 1997, upon a finding by the undersigned that there was no evidence establishing that she had standing since the account was held in Gregory Violette's name only. "Complainant" when used in the singular refers to Gregory.

[2] David J. Javor had also been named by Violette as a respondent in the original complaint, and the complaint was served on him as well. By Order dated May 20, 1997, the complaint was dismissed as to Javor upon finding that the only allegation tying him to any of complainant's losses was a single reference in the original complaint alleging that Scott and Javor had lost his money. That Order should be considered incorporated herein. Accordingly, complainant should note that if he wishes to appeal the dismissal of Javor in the May 20 Order, he may now do so.

[3] Wolf was registered as an associated person and principal of Wolf Futures Group, Inc., an introducing broker guaranteed by respondent First American Discount Corporation ("First American" or "FADC"). The two Wolf respondents are referred to in this decision as "Wolf."

Wolf to engage in all the challenged trading by granting Wolf time and price discretion to trade the contracts traded.

An oral hearing was held in two parts, on February 12 and April 1, 1998. The following decision is based in large part upon my finding that in general complainant Violette was much less credible than Wolf.

Violette's Complaint and Addenda

The original complaint, sent by overnight courier on December 11, 1996, was convoluted and unspecific, with the narrative portion consisting only of the following two paragraphs:

> Some time in August 1996 I open [sic] an account with Wolf Futures Group, Inc. 1st American Discount Corp. open [sic] the account using monies from a joint account to fund the account with 1st American Discount Corp. and Wolf Futures Group, Inc. The first problem is that 1st American used one joint account monies to open a new individual account with them and Wolf.
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> Then Scott Wolf traded that account, making unathoried [sic] trades, churning the account and lossing [sic] the full amount put into the account along with put [sic] the account on a margin call of $8060.47.

(Complaint attachment, received December 12, 1996.) As for damages, Violette sought the amount of money he said he transferred to open the account, $17,697.33, plus the amount of the margin call, for a total of $25,757.80.

Because the complainant did not include any documents regarding the transactions, the Commission's Office of Proceedings called the complainant and requested him to send in his account statements (Note to File, December 13, 1996). A packet of statements thereafter sent in by Violette was incomplete, so he was called again and asked to send in several missing statements (Note to file, 12/23/96). He replied that he did not have the requested statements, including

monthly statements for the last three months his account was open (Violette fax letter, dated December 23, 1996).

On January 2, 1997, the Director of the Office of Proceedings instructed Violette to specifically identify trades that he claimed were unauthorized, and to provide additional information concerning the churning claim:

> . . . [Y]ou must produce a detailed chronological statement and damage calculation in support of your unauthorized trading allegation. This statement must identify each trade that you claim was unauthorized; and state the amount of the loss for each unauthorized trade.
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> You must also produce a detailed chronological statement and damage calculation in support of your churning allegation.....

(R.Britt Lenz letter, dated January 2, 1997; emphasis in original.) The Director asked Violette to provide information regarding three issues associated with his churning allegation (how respondents controlled the account, how he had communicated his trading strategy to respondents, and how the trading activity in the account was allegedly inconsistent with his trading strategy), and to calculate the amount of commissions attributed to the alleged churning. In a footnote, the Director encouraged Violette to continue searching for his missing statements.

Finally, the Director's letter informed Violette that cases involving unauthorized trading and churning often involve analysis of a complainant's investment experience. The letter noted that Violette had been involved in five previous reparations cases in which account statements and account-opening documents had been filed and suggested that Violette should be prepared to produce information regarding from those cases. The letter offered Violette the opportunity to request prior case documents from the Office of Proceedings in the event he had not kept copies.

Violette's reply to the Director's letter contained somewhat more information than his original narrative, but still offered few details:

> On or about the 13th, 14th, and 15th, of August 1996, is when Scott made trades that was [sic] not authorized by me. At one point on the 19th of August he told me that he had loss [sic] seven thousand dollars from trading my account and it ended up being around eight thousand dollars. Scott did get some monies back from the floor [--] he told me from their wrong doing. As far as I can understand what was loss [sic] at the end of this day of Scott making trades that I did not authorize, I was down from $17,906.93 to $9,129.47, after getting some fees returned. Making my loss to be $8,777.46, when my agreement between me and Scott was to use a stop and make sure the loss was keep [sic] at $450.00.
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> The next problem day was around the 26th or 27th of August 1996, and Scott still made trades in my account days after, the 28th, 29th maybe more. [Sic.] Again Scott make unathorize [sic] trades which brought my account from $8,961.49 to being on margin call for $8,060.47, which gave me a loss of $17,021.96.
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> I can not give a loss for each trade because Scott made many of trades [sic] and due to all of them being losing the total amount loss [sic] is from all of the trades me [sic; presumably, "he"] made. I am not able to understand the statements that well to give the loss per trade that Scott made.

In regard to the three questions asked about his churning claim, Violette for the first time raised the issue of Wolf's alleged trading beyond his permission to trade only a single contract at a time:

> 1) I did not sign any power of attorney to Scott or anyone else.
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> 2) Scott told me that he traded the S&P and used a really tight stop. We talk [sic] about using a $450.00 stop and Scott told that would be the LARGEST stop he would use. He told me he used the $200.00 range. Scott explained that in different times he would use up to the $450.00 stop.
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> 3) Scott traded more than one contract at a time, when we talked about one contract and ONLY after talking to me would he trade any more contracts that day. Giving me the chance to say yes or no if I wanted to do any more trades in a given day. From looking at the statements Scott traded a lot of contracts along with not using the $200.00 stop we talked about using every[ ]time. Scott did tell me that he would be using a $450.00 stop when he felt it was needed. As far as I can see he did not even us[e] the $450.00 stop as I did agree to when he felt it was needed.

> Commissions: I came up with a total of $6,639.72 in commissions. Plus any amount that was charged or credit [sic] after September 11, 1996. I remember Scott telling me at least two times that he was going to credit my account some money as a return of commissions because he had a bad day trading my account along with others. He also told me that he would give me a credit if I put more money into my account and gave him another chance to build my account back up. At which time he sent me a release to be signed and I was to send it back along with putting more money into my account. He wanted me to release him from all the things he had done wrong up to that point with my account. I did not sign the release nor did I add any money to my account.

(Violette faxed letter dated January 7, 1997; original received January 13, 1997.)[4] Violette also repeated his assertion that he had not received any other statements from First American.

The complaint, consisting of the initial filing and the several additional submissions, was served on the respondents on January 8, 1997.

Respondents' Joint Answer

Respondents (including Javor, *see* footnote 2) answered jointly. Their answer denied any unauthorized trading or churning, and sought sanctions against complainant on the grounds that the complaint was allegedly filed in retaliation for respondents' civil action filed against Violette in Illinois to collect a debit balance (Joint Answer, ¶3 and page 4).[5] Respondents sought clarification of the allegedly unauthorized trades, noting that complainant had still not specified exactly which

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[4] The return address sticker on the envelope contains the name "Dr-Mrs Gregory P. Violette." The record does not reflect what, if any, doctorate is held by Violette.

[5] The Illinois action resulted in a January 16, 1996, default judgment against Violette, who had not appeared (Joint Answer, ¶3f). That judgment has since been enforced in Maine by respondents, who apparently collected the amount of the judgment plus an amount of attorneys fees from the bank involved in the refinancing of Violette's house over his objection. This

trades were unauthorized despite being asked to do so in the Director's January 2 letter (Joint Answer, ¶6). Respondents raised affirmative defenses of ratification (based on failure to object to trades in timely fashion as required by the First American customer agreement, as well as failure to bring irregularities to First American's attention as warned on each statement); "unclean hands" (based on Violette's own participation in the transfer of funds from his previous broker); "latches" [sic] (based on an estoppel theory that Violette was aware of the trading in his account and accepted profitable trades); failure to state a cause of action against Javor (Joint Answer, pages 3-4); and what respondents termed "estoppel" but really more closely appeared to be a defense of *res judicata* (based on Violette's failure to assert his claims in the Illinois civil action) (Joint Answer, page 4).

Finally, the answer sought attorneys fees as a sanction for Violette's alleged bad faith in filing his reparations case (Joint Answer, page 4). The claim did not encompass any contract claim for attorneys fees.

Violette is Ordered to Clarify the Complaint

After the case was forwarded for adjudication, and after discovery requests had been filed by Violette (*see* April 8, 1997, filing), he was ordered to produce a listing of each trade that he claimed was unauthorized (Order Suspending Discovery and Order to Complainants to Produce Comprehensive Statement of Complaint, dated April 10, 1997) (referred to generally in this decision as "April 10 Order"). That Order included the following language:

> ...A review of the record indicates that complainants have never responded adequately to a January 2, 1997, letter from the Director of the Office of Proceedings in which complainants were directed to set out a detailed

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information was learned from the parties during the discussions prior to and during the oral hearing, when the civil litigation proved to be the sticking point preventing settlement.

chronological statement of events. Among other things, complainants have alleged that some trades in their account were unauthorized, but have never identified the specific trades that were not authorized. Furthermore, complainants have alleged churning, but they have not explained how their trading could be considered excessive or to what degree. Finally, it is noted that complainants have alleged that transfers of money were made from another account, but they have not submitted any documents showing the transfers themselves. The respondents and the complainants may have information indicating that they know when the transfers occurred, and when the account was opened (and with what amount), but that information has not been made available to the undersigned. The sum total of the several gaps listed above is that the record is not yet complete enough to allow the case to proceed any further.[footnote]

Accordingly, complainants are ORDERED to file a complete chronological history of their account, including a detailed listing of the trades that are alleged to be unauthorized AND a precise calculation of their damages from those trades. Simply pointing generally to dates on which allegedly unauthorized trades were made (as was done in response to the January 2 letter) will not be sufficient to comply with this Order. Each specific trade must be listed, with a breakdown of (1) when the trade was initiated; (2) when it was liquidated; (3) the circumstances surrounding each trade, including when the complainants became aware of it and their response to that information; (4) a full explanation of all communications between complainants and respondents concerning each of the alleged unauthorized trades, as well as any other communications with respondents on this issue; and (5) the amount of damages associated with that trade. Failure to provide this information will result in a conclusion that complainants are unwilling to present enough evidence to support a *prima facie* case of unauthorized trading. ***Under no circumstances will complainants be able to recover damages for any trade not specifically listed in response to this Order, to include all five matters set forth above.***

In addition, complainants are ORDERED to file an affidavit setting forth the particulars of their churning claim. Such an affidavit must include, at minimum, the following information: (1) an explanation of how they are alleging that respondents controlled the level of trading in the account since no power of attorney apparently existed; (2) an explanation of how complainants have concluded that the level of trading was excessive in view of complainants' trading objectives; (3) a full detailing of complainants' trading objectives, including an explanation of when and how those objectives were communicated to respondents; and (4) an identification of how much in commissions complainants are alleging is attributable to the alleged churning, including a detailed explanation of complainants' calculations.

> Finally, complainants are ORDERED to file a complete set of account documents showing all transactions in their account, from beginning to end. They are further ORDERED to file all documents of any other account showing the transfers of money to the account in question. No transaction for which all relevant documents are not provided will be allowed to be the basis of any award in this case in the event complainants prevail.

(April 10, 1997, Order; emphasis in original.) The footnote included at the end of the first paragraph took note of complainants' previous failures to provide specifics and warned of the consequences of failing to provide the information sought:

> [footnote] Complainants' failure to respond adequately to the January 2 letter lends some credence to the allegation by respondents that complainants expressed the desire to file a reparations complaint with awareness that doing so would cause increased expense to respondents, the implication being that complainants may have filed a frivolous suit. Complainants are hereby WARNED that failure to respond to this Order with a complete, detailed, and verified response will likely result in dismissal of their complaint and consideration of attorneys' fees.

Complainant's reply to the April 10 Order (labeled "Comprehensive Statement") was timely filed and was received in the Office of Proceedings on May 12, 1997. The specifics related by Violette regarding his complaint are summarized here:

> (1) On August 15, 1996, Wolf allegedly traded 33 more S&P 500 contracts than the single one Violette had authorized, with Wolf telling Violette about the trades the next day ("Scott told me that he was trying to make me some money and things got out of hand and he loss [sic] track of things for some time that day."), resulting in losses of $9,065.36;
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> (2) On August 20, 1996, Wolf traded ten call options and allegedly charged $750 in commissions when $500 in commissions was the agreed-upon rate;
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> (3) On August 23, 1996, Wolf purchased 5 soybean contracts when Violette had not ordered any ("I did not know about this trade until I saw my statement days later and the trade was over and I never got any credit as Scott told me was going to happen. Scott said this trade got into the wrong account."), with a net loss of $483.24;

(4) On August 27, 1996, Wolf allegedly took six S&P positions when Violette had again ordered only one ("Scott and I had talk [sic] and he was to trade ONLY one contract to a $250.00 stop."), losing $1,626.24;

(5) On September 3, 1996, Wolf allegedly traded 25 S&P contracts when Violette had given him no order ("Again Scott told me the next day that he loss [sic] track of what he was doing for some time that day and we were hit by a Mack truck. Scott told me that he was waiting for some credit from the floor and they never gave us any."), losing $13,438.50; and

(6) On several days fees and adjustments made to Violette's account amounted to $3,219.75 (but Violette did not specify why these fees were improper).

(Comprehensive Statement, pages 1-3.) All told, according to Violette's latest submission, he had suffered a total loss of $31,302.84, making that the *third* damages figure he had submitted in connection with his reparations case.

Attached to the list of trades was Violette's so-called Affidavit in which he provided more details about his expectations concerning the level of trading. According to this unnotarized "Affidavit" (the truth of which was only "affirmed" -- not under penalty of law -- "to the best of my ability"), Wolf was always supposed to trade only a single contract on any given day and would contact Violette for permission if Wolf wanted to trade more than that (Affidavit, ¶¶2 and 3). Violette averred that the multiple contracts traded on several days was excessive for a $17,000 to $19,000 account and was done simply to generate commissions. In contrast to the assertion in the listing of trades regarding Violette's expected *$250* stop, Violette's Affidavit contended that Wolf was supposed to use a *$200* stop and that this assurance led Violette to decide to go "on board" with Wolf (Affidavit, ¶3). Also attached was a more complete set of account statements.

Because the Affidavit was unsworn and not affirmed under penalty of law, Violette was ordered to swear to his affidavit or it would be considered unsworn (May 20, 1997, Order, Part I). As noted above in footnotes 1 and 2, that same Order dismissed Pamela G. Violette as a complainant and dismissed the complaint against David Jude Javor (*id.*, Parts II and III) and set a discovery schedule for the parties (*id.*, Part IV). Violette filed a new submission, this time with an affirmation under penalty of law, on May 28, 1997 ("Affirmed Statement").

Discovery

Discovery requests and productions were exchanged by the parties in June and July 1997. Respondents sought to discover Violette's personal bank records because they wished to determine the source of the funds used to open the account so that they could challenge his standing to bring this case (*see* Christopher M. Burky letter, dated June 20, 1997). Violette filed a motion to compel discovery after his requests were only partially answered by respondents (Motion to Compel, dated July 10, 1997).

A conference call was convened on July 15, 1997, to discuss the discovery issues. During that call, action on complainant's motion to compel was reserved because respondents' counsel had not yet received it since Violette had mailed it to an incorrect address. With regard to respondents' request for bank records, respondents averred that complainant might not have standing because he had filed a bankruptcy petition in late 1995, and that bankruptcy had been reopened some six months later. According to respondents' counsel, the cause of action here might legally belong to the bankruptcy trustee, if Violette had not revealed in the bankruptcy his ownership of the funds later used to open this account (Conference call tape recording, dated July 15, 1997, Side 1). The

undersigned rejected respondents' motion, as well as the "possible" standing issue, on the basis that respondents had made no showing whatsoever that the bankruptcy order discharging complainant's debts, which was issued some eight months before the opening of the account from which the funds were transferred to open this account, had any effect upon Violette's authority to open an account half a year later. Furthermore, the ruling continued, Violette's discovery responses regarding the source of his funds stated that his former wife Pamela was the source of his funds and therefore respondents already had their answer regarding the source of funds. Respondents' counsel then argued that if Pamela was the source of funds, then Gregory Violette did not have standing, but that argument was rejected because even respondents conceded that Gregory Violette was the true customer on the account (*id.*). Counsel next tried to argue that Gregory Violette could not have had damages if he did not personally own the funds, but that argument also failed because so far as respondents were concerned, Violette was the customer to whom duties under the Commodity Exchange Act were owed and thus any damages or losses suffered by him as a customer were his, not those of his funding source. Respondents' counsel's last gasp argument, based on the bankruptcy trustee's motion to reopen the bankruptcy so he could pursue another claim previously not known to exist, similarly was found to be unrelated to this account and therefore not a basis to allow fishing into Violette's bank records (*id.*). The final ruling was that Violette would be considered the customer, but if respondents wished to coordinate with the bankruptcy trustee to intervene as the only person with standing to pursue the claim here, they were free to do so by proper motion (*id.* and Side 2).

In the same conference, the undersigned notified Violette that he must file responses to respondents' remaining requests for documents, and that his unsworn interrogatory answers were unacceptable in view of the prior Order requiring him to swear to his affidavit -- especially in view of his prior litigation experience involving the five previous reparations cases. He was told to immediately file a properly sworn copy of his first set of answers, to be followed by the ordered supplemental productions. Notice was taken that judges in other CFTC cases had sanctioned Violette for litigation abuses and other misconduct, and Violette was expressly warned that such conduct would not be tolerated here, including his disingenuous claim that he innocently "overlooked" the document request and his refusal to answer legitimate discovery requests based on frivolous objections (*id.* at Side 1).[6] Violette was ordered to supplement his discovery replies with more complete answers, including substantiation of any objections based on burdensomeness.

The conference call also addressed the fact that Violette had sent his discovery replies (and his motion to compel) to respondents' attorneys using an old address despite having been given respondents' attorneys' proper address in other cases and in the Service List attached to the instant case's Notice of Summary Proceeding (dated March 6, 1996), as well as each of respondents' filings (*id.*). Violette contended that he had inadvertently used an old computer disk and was trying his

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[6] *See, e.g., Violette v. Kaiser*, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶29,728 (Initial Decision, Dec. 18, 1996) (attorneys fees and costs assessed as sanctions for frivolous filings, abuse of discovery, and vexatious litigation); *The Violette Group, Inc. v. Ackermann*, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶26,929 (Order of Dismissal, June 28, 1996) (dismissal as sanction for frivolous and vexatious filing of complaint, failure to substantiate allegations of misconduct, and disregard of orders).

best (prior filings had indeed been sent to the attorneys' correct address; *see* certificates of service dated May 7 and 28, 1997), but he was warned to remail his discovery replies and motion to compel by overnight delivery and to cease making such errors because they would only hurt him in the case (*id.* and Side 2).

At the end of the conference, respondents' counsel renewed their asserted need to explore complainant's source of funds in an effort to prove he had misled the bankruptcy court, and this time sought a subpoena directed to Pamela Violette (claimed by Gregory Violette to be the source of his funds in opening the account) (*id.* at Side 2). Counsel's arguments were rejected, but the undersigned offered respondents' counsel the opportunity to have a conference call with all parties *and* the bankruptcy trustee to determine whether the trustee wished to assert that he had the right to replace Violette as the complainant (*id.*). Respondents never requested such a conference or made any filings showing that the trustee desired to participate or intervene as the proper complainant in this reparations case. Accordingly, that issue is considered abandoned by respondents.

A copy of the tape recording was sent to each side in view of the number of oral rulings made in the conference (*id.* at Side 2).

Despite having been warned that he must file a properly sworn affidavit regarding his discovery responses, when Violette re-filed and re-served his first set of discovery answers he again sent a document that was neither notarized nor sworn/affirmed under penalty of law, but merely included the simple statement, "I attest that the above statements set forth are known or believed to be true." (Answer to Discovery, filed July 15, 1997). The document was, however, served on

respondents' attorneys at their proper address, and there is no indication in the record that Violette's address mistake was ever repeated.

Violette filed his supplemental discovery replies on July 23, 1997. Again, he failed to properly verify his submission, and he again made objections without substantiation of how particular questions were burdensome (Answer to Discovery and Request for Documents, dated July 23, 1997). Violette refused to provide copies of materials received from respondents, asserting that they had sent those documents in the first place (*id.*, reply to document request number 5). He also refused to provide documents from other cases he had been involved in because he said respondents' attorneys already knew about those other cases and could look in other case files for copies of documents if they wanted them (*id.*, numbers 8 and 9). The only document Violette provided was a partial copy of his divorce decree from Pamela Violette, dated September 13, 1996 (first and last pages only).

As noted above, the conference call had not addressed Violette's July 10 motion to compel because respondents had not yet received it. The July 10 motion by Violette asserted, among other things, that respondents had not produced telephone records of calls made to him, which was important because he would show that no one had talked to him prior to "many of the trades" made by Wolf (request 3); that respondents had not provided a requested "list stating every trades [sic] made" (request 4); that respondents had not provided a list matching each trade to the telephone calls made to him, nor had they provided tapes of those calls (request 5); and that respondents had not provided several other documents he had requested, not recounted here (requests 2 and 9-12).

On July 31, 1997, respondents filed a reply to Violette's motion to compel, and also moved to compel production of documents from Violette. Respondents' reply to Violette's motion renewed their objection to sorting through "thousands of pages" of telephone records to identify the calls made to Violette (response to request 3), and objected to the trade listings and telephone bill match-up lists requested by Violette as essentially a request that respondents be forced to "aid Mr. Violette in his campaign against them" (response to request 4). Respondents also asserted that they had no tapes of any conversations with Violette (response to request 5).

In a ruling on the motions to compel, complainant's motion to compel production of telephone records was granted, as was his request to have respondents answer an interrogatory explaining the basis of the trades in his account (Rulings on Discovery Motions, Discovery Order, and Schedule, dated August 27, 1997, at pages 1-2). Respondents' motion to compel further production of account documents was likewise granted (*id.*, page 2). Both sides had attempted to force the other to provide copies of documents from all other litigation in which the other side had been involved, but only the case names and docket numbers were ordered produced. Requests for documents themselves were denied to both sides upon a finding that any party wishing to examine other litigation records could access those records from the courts involved (*id.*). Finally, the Order found that neither side had abused discovery and therefore no costs were assessed on the motions to compel (*see* Rule 12.30(c)).

The Parties' Verified Statements

Both sides completed discovery without further controversy and thereafter submitted their final arguments and evidence. *See* Rule 12.208(a). In complainant's statement, he stated that the "file speaks for [itself]" in establishing churning. Violette noted the numerous trades made on August 13 (25 S & P contracts), August 14 (24 contracts), and August 15 (34 contracts), 1996, and contended that those trades were made after only a single conversation each day. He also expressed bewilderment that Wolf could trade 34 contracts with less than $1,000 left in the account (Violette Verified Statement, dated November 18, 1997, at page 1). He contended that First American was liable for allowing Wolf to churn his account (*id.* at page 2). The verified statement contained a proper "under penalty of law" verification (*id.* at page 3).

Respondents' two submissions are labeled "Verified Statements" but only one of those statement appears actually to have been sworn or affirmed. A statement submitted by Patrick G. King, an attorney for First American, appears unsworn and undated. King's statement detailed particulars of his conversations with Violette regarding First American's attempts to collect against Violette for the deficit that had remained in his account, including Violette's alleged statement that if First American filed suit against him he would just "plug in his personal computer and print up another complaint" in reparations (Patrick G. King Statement, undated, paragraph 4). According to King, he asked Violette on what basis a complaint would be filed, and Violette said he would simply assert a violation of the Commodity Exchange Act, and the resulting case would cost First American more than it could collect from his deficit (*id.*, paragraph 5). Thereafter, according to the

affidavit, First American assigned its rights to Wolf Futures Group, which obtained a default judgment against Violette on January 17, 1997, that remained unpaid (*id.*, at paragraphs 7-11).

Wolf's own verified statement was adopted by First American (*see* Christopher M. Burky letter, dated November 19, 1997). That statement recounts the events leading to the opening of complainant's account and is highly notable because it contains, for the very first time in this litigation -- some nine months after respondents filed their Answer -- Wolf's version of the specific facts associated with the trades he made. According to Wolf, on those days when numerous contracts were traded, Violette had granted to him "time and price discretion" after specifying the *maximum* number of contracts that Wolf could buy. In other words, Violette would authorize Wolf to go long or short "as many as" 25 or 35 contracts on a particular day, and Wolf would then use the "time and price discretion" to determine when those contracts should be taken and at what price (Scott Wolf Verified Statement, dated November 19, 1997, at paragraphs 12-13, 15-19, 26-28, 48-49). The statement also details Wolf's use of time and price discretion for trades involving smaller quantities, as well as single contracts (*e.g., id.*, paragraphs 29-33, 36-40). Wolf's statement ends by quoting the language of the First American customer agreement requiring Violette to report errors or differences within seven days of confirmation statements, and asserts that Violette never made any reports of the alleged unauthorized trades (*id.*, paragraphs 60-63).

Oral Hearing, Part One, February 12, 1998

The parties were notified of an oral hearing to be held in this case to examine the credibility of the parties concerning only the issue of unauthorized trading. As the Notice of Oral Hearing

explained, the written record was sufficient to dispose of the allegation of churning (the complainant would lose because there was no showing of control over the account by respondents), the alleged illegal transfer of funds (no evidence whatsoever that the funds were transferred improperly), and respondents' counterclaim (based contingently on possible liability to the now-dismissed complainant Pamela Violette stemming from the transfer of funds issue) (Notice of Oral Hearing and Order to Parties, dated January 16, 1998).

As noted above, the oral hearing in this matter was held in two parts, on February 12 and April 1, 1998, and a separate volume of transcript was prepared for each by the reporting service. Transcript references in this decision to pages 1 through 85 are to the February 12 session, and to pages 86 through 255 are to the April 1 session.[7]

At the beginning of the oral hearing, the undersigned stated that only those trades identified by Violette in response to the April 10, 1997, Order would be examined (Tr. at 3). Thus, the trades of August 13 and 14 would not be considered for liability purposes because Violette had omitted them from his list of challenged trades (Tr. at 6-7).[8]

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[7] As the parties were informed in the Notice of Oral Hearing (page 2), the practice of the Judgment Officer is to do the initial examining of all witnesses, followed by the parties' opportunity to present additional evidence and to cross-examine the other side's witnesses. In this case, the first session of hearing consisted primarily of the Judgment Officer's questioning and the parties' presentations generally occurred during the second session. Unless otherwise indicated, questioning in quoted sections is by the Judgment Officer.

[8] All references to trading dates are to dates in 1996.

At the hearing, Violette continued to display the discrepancies and contradictions he had shown in his written submissions. Although, as discussed above, he had stated in his verified statement that he had authorized a contract on August 15, Violette testified that he had not authorized *any* contracts on that date (Tr. at 8-9, 28). Asked about this contradiction, Violette stated that the general trading strategy was for single contracts on any given day, but that he had authorized no trades on August 15 (Tr. at 9). Violette was asked when he learned about the large numbers of trades that had occurred on August 13 and 14, and he denied knowing about the volume of trading until August 16 or later (Tr. at 11, 13, 26). He denied having authorized more than one contract on the 13th (Tr. at 16-17) and claimed Wolf only verbally reported to him the results of trading that day (loss of $413), not its volume (Tr. at 18, 20-22). Violette did not remember whether Wolf informed him he had made over a thousand dollars on the 14th with the same type of trading (Tr. at 22-23), but he said Wolf again had not reported how many trades had been made that day (Tr. at 23). According to Violette, on each day of trading Wolf was to make a single trade and report the results to Violette, who would then decide whether to trade more contracts that day, but Wolf never did so (Tr. at 23-24).

On August 15, the 34 contracts traded by Wolf lost approximately $9,065 (August 15, 1996, confirmation statement, page 2, attached to Violette's verified statement). Violette was asked how he could have thought this occurred in a single contract, and he said that this was when he first found out about the volume of trading engaged in by Wolf, but it might have been the next day (Tr. at 26-27). Eventually, Violette admitted this occurred on the 15th because on that day Wolf told

him that "we got hit by a Mack truck" (Tr. at 27). The loss was understood by Violette to have been about half of his account and, he claimed, he definitely found out about the trading volume in that conversation because he had thought he had a $450 stop (Tr. at 28).

The focus of questioning was directed to Violette's actions after learning of Wolf's alleged violations of their "one contract" agreement (Tr. at 28*ff.*). He said he continued trading with Wolf because of Wolf's "promises" and because he "had faith and trusted him" (Tr. at 29). Violette admitted that he had filed other reparations cases before this account had been opened, and that those cases if reviewed would show he knew he could get his money back for unauthorized trades (*id.; see also* 37-38). Violette was then asked whether he had ever complained to Wolf about the unauthorized trading, and the following colloquy occurred:

> A. I guess I can't use the exact words I did use. I believe my question was, why were we trading so many when he wasn't authorized, we would only trade one. I might not have put it in those exact words, but I definitely made it clear that that was not what we were supposed to be doing.
>
> Q. If we were to look at the words you used with Mr. Wolf when you first opened your account and developed a trading strategy, is it possible that Mr. Wolf could have misunderstood your directive about trading one contract as allowing him to trade one contract at a time?
>
> A. No. That is why I wanted the tapes. He tape recorded on, I believe, the 13th, maybe even prior to. He was taping the conversation of our game plan, what he was to do, what I was getting myself into. I never received those tapes, though.
>
> Q. So on the 15th, he does this type of trading. You continued trading with this guy.
>
> A. Yes, Your Honor.

Q. Now, did he ever tell you that the $9,000 had been credited to your account?

A. No, no.

Q. But you continued trading with him anyway?

A. Yes, I did, Your Honor.

Q. So, because he said I'll look into getting you some money back? That's what you put in your initial complaint, "I'll look into trying to get you some money back, try to do a commission" --

A. Yes, I believe --

Q. Get some money from the floor, because they may have made a mistake.

A. If we are using the $9,000 as the number, --

Q. Right.

A. -- I believe the statement was something like, that some of that you're going to get back because of errors from the floor. We shouldn't have got stopped out so far from where the stop was, some things like that. But no way did he say he was getting $9,000 back.

Q. He didn't offer to give you the whole amount of money back?

A. He never offered to give me the $9,000 back.

Q. I'm saying, he never said, look, I'll get all this money back for you?

A. Well, in trading, yes, I guess his --

Q. No. Did he or did he not say he would get the money back for you --

A. In trade?

Q. -- to compensate you for your losses, because it was unauthorized trading?

A. No, he was never going to compensate me for the loses. He talked about doing more trading, doing better at it, and getting the account back, built up over and doubling.

Q. So you found out that he violated your trading strategy, exposed you to 20 times the loss that you had agreed to face, doesn't offer to reimburse you those losses, says that the way to get it back is to do more trading, and you still continued to trade with him?

A. Yes, I did, Your Honor.

Q. So what promises did he make? At this point, he has lost a total of $9,400 or something, and gained a total of $1,095, for a net pretty dismal trading performance in three days. What did he say that caused you to think that all he had to do was trade your account some more in order to get money back for you?

A. I would say him referring back to how well he has done prior. I guess my belief in him being sincere and honest, in what he had done as a track record. There was no promises, those times we talked. There was no guarantee I'd make the money back. It was just in good faith and believing him that he was going to follow my orders, and we were going to build the account back up.

(Tr. at 30-32.)

Violette testified that in his other accounts, his trading would have been profitable except that unauthorized trades were made, and that is why he filed complaints (Tr. at 38). Following some questions that dealt with those accounts, which were held with members of Violette's family, Violette again admitted knowing he was not liable for unauthorized trades:

Q. What I am really trying to get an understanding for is why you believed Mr. Wolf, who had just managed to basically deep-six half of your account -- it seems like in the other cases, you said things had been profitable until people did things that were unauthorized, is that what you said?

A. The two I was in with [my] brother, it wasn't as much unauthorized, it was just the wrong trade. And because of --

Q. Well, if it is the wrong trade, it is unauthorized.

A. Well, it was like --

Q. The net result is that it is unauthorized, it was not what you wanted.

A. That is true, Your Honor, yes.

Q. When that happens, you know you can get your money back, or you can try to get your money back. But you know that you're not liable for it, right?

A. Yes, Your Honor.

Q. I mean, you know the brokerage firm is liable for it.

A. Well, as you just said, you can try to make them stand good for their error or what they had done wrong.

Q. But you weren't willing to ask Mr. Wolf to do that on the 15th, apparently.

A. I believe on the 15th -- again, I emphasize that maybe it was some greed on my part but because maybe he was a good talker. I just had faith and confidence, because of his past track record, he led me to believe. I don't know how to say -- I realize, you lose half of an account, I guess when you made -- I don't want to use the word "promise," but when you're told, here is the picture, this is what we're going to do, I guess I still wanted to move on.

(Tr. at 41-42.)

Violette testified that he suffers from an ongoing mental disability that he believes makes him very gullible and that is why he believed Wolf when he allegedly promised to make the money back through better trading (Tr. at 44-46). This testimony led to additional inquiry as to why Violette continued trading with Wolf even after getting statements showing that the trading on the 15th was not an aberration, but was instead the way Wolf was trading every day:

Q. . . . So then eventually you started getting these statements. The statements for the first three days of trading show many, many more contracts, even though the third day is the only one that you suffered a sizable loss. But by, you know, let's say a week later, you've gotten at least one statement. Okay?

A. Yes.

Q. So when you found out about the loss on the 15th, he acknowledges to you that he is trading more contracts than you wanted. Within a week after that, you would have received at least one of the statements from the other days, the other two days, from the 13th or 14th.

A. Yes.

Q. Where you hadn't suffered sizeable losses. Now, did that confirm to you that this guy is just off on his own? Or did you have some sense that he was going to restrain his trading at that point?

A. Well, after talking about the 15th and coming to light upon -- again, this here is a large number. I don't know if we ever came to the exact number of trades, or -- there weren't supposed to have been that many. Example, the 15th, there was supposed to have been no trades, but, yes, when it finally came to light, I confronted him again to the best of my ability. I think his response was, we're going to stick to our game plan.

Matter of fact, I remember at times him telling me that it wasn't just me, it was other customers. I think his numbers were three, four, five other people, the same thing he was doing for. He had now fine-tuned the trading. It was one contract, as we first agreed to, and call back if you want to trade another one that day with authorization.

So I believed him. I felt that he now was going to start following our plan and do as he said.

Q. You knew you could report him to the CFTC, right?

A. I would say at that time, it wasn't at the top of my list of things to do.

Q. But you said you were angry --

A. Definitely.

Q. -- that he had departed --

A. But I felt I was looking at a person --

Q. But didn't you know he was committing a violation of the law?

A. Again, I guess it didn't come through my mind that way. I felt I was looking at a person that was probably, as he explained, trying to do good for me.

Q. You thought he was trying to help you?

A. Well, that's the way he put himself off to me. Example, that I was only trying to make us money. I felt I accepted that concept, and that we were going to go to our game plan. . . .

(Tr. at 47-48.)

Violette continued trading through the end of August, but those days only involved smaller numbers of contracts (Tr. at 49; *see also* Wolf Verified Statement at ¶¶ 22-47, *and* daily confirmation statements attached to Violette's Verified Statement). Violette admitted that those days involved more than single contracts, and agreed that several of those trades were authorized (Tr. at 51).

Wolf was examined about the allegations Violette had made (Tr. at 52*ff.*). His testimony began with comments concerning one of the last conversations he had with Violette, on September 6, several days after the last multiple-contract trading on September 3. In that conversation, Wolf admitted offering to try to obtain a commission adjustment for Violette, but stated that he did not offer to continue trading unless Violette would make his account "whole" by depositing more money (Tr. at 55-56). Wolf testified that he and Violette spoke several more times after that, but he did not know Violette had complaints about how Wolf traded the account until months later (Tr. at 57).

Wolf also testified that he had told Violette to contact someone at First American if he ever had problems with Wolf (Tr. at 58). This led to a re-examination of Violette concerning

whether he complained to First American. Violette read into the record the paragraphs on the backs of the confirmation statements providing the telephone number for First American if any problems occurred (Tr. at 60-61). Violette was asked if he had ever called First American, and he claimed he had done so on August 28 (Tr. at 62). However, what he was calling about was to ask questions regarding how so many contracts could be traded in an account the size of his (Tr. at 62, 66). He also talked to employees of the exchange about margin requirements (Tr. at 68).[9]

The questioning returned to Wolf, who was asked about his understanding of the trading agreement he had made with Violette (Tr. at 72*ff.*). He testified concerning how the number of contracts was determined:

> Your Honor, Mr. Violette came to me saying that he only wanted to day trade S&Ps, and he wanted to be aggressive. That was the whole idea. He heard that the S&Ps offered dramatic opportunities. I have been in the business long enough to know, when I start hearing that, to overstate situations as far as risk.
>
> Mr. Violette picked the number of -- after discussing with him for a while how many contracts to trade, 25 was first picked, up to 25 for the account. I said we wouldn't be trading 25 of one contract because that is insanity; that we would be going in much smaller increments.
>
> After the first two days of trading, after his first day of profits, when he saw he could make some money, he said, what could be done if we increased the size? I said, well, you know, it can't go much heavier with the amount of money in there. He says, well, right now I can't really add much more money, but what can you do? He says, why don't you go up to 35? That's what went down.

---

[9] At the second session, Violette claimed that he talked to First American and the exchange about his account being "over-traded" (Tr. at 131). Asked if he had called about unauthorized trading, Violette again stated that his questions had been about the margin (Tr. at 132-133; *see also* Tr. at 193). He admitted that he had not called after receiving the statement for the 15th when he lost $9,000, and acknowledged that his call occurred when he was not as upset as he claimed to have been on the 15th (Tr. at 152).

Every single trade was authorized. This man was spoken to every day in the morning and every afternoon virtually, and was given the best estimate of profit or loss at the end of every day that we could manually do, so that he could get some kind of idea where he was. . . .

(Tr. at 73-74.)

The end of the first hearing focussed on Wolf's understanding of "time and price discretion":

Q. Now, you say he gave you the authority to trade up to a certain number of contracts?

A. That's correct.

Q. But you didn't have to trade that many?

A. No, I didn't have to. But once he started making money that second day, he wanted to increase that number.

Q. But whether or not you actually made the transaction was up to you?

A. That's a good question. I was not held to do that amount of money -- I mean, that amount of trades. In other words, if he gave me a position to do 25, I didn't have to do 25.

Q. Could you have done 10?

A. Yes.

Q. Could you have done five?

A. Yes.

Q. Could you have done one?

A. Yes. I could have done none.

Q. You could have done none. On what basis were you to make that decision?

A. Based upon opening and closing ranges and based upon the moving averages and chart formations.

Q. What would trigger the decision to not trade, for example?

A. Volatility, sometimes; news events, if a number was coming out, like an unemployment number.

Q. If you talked to him the day before, for example, and he said do 25 the next day, and then something happened that morning, like a news report said something was happening, you could then decide not to trade?

A. Right, correct.

Q. Without contacting him?

A. Well, it was normally understood, because we always discussed everything. That, and the only other time is rollover of the months.

Q. Oh, wait a minute. When you say you discussed everything, I'm talking about if something unanticipated happened.

A. Unanticipated?

Q. Yes. In other words, you're saying that you might have expected something to happen that morning, and whether it did or it didn't would trigger the decision?

A. If --

Q. Like you talked to him about it might or might not happen, and then if it did or didn't, that might make the difference in terms of whether or not you traded?

A. Let me try to put it --

Q. I guess what I'm trying to say is, like what if there had been -- what if there was an overnight report after you talked to him.

A. Right.

Q. An overnight report of, you know, a major attack on Iraq, for example.

A. Right.

Q. And prices would go up and the stock market might take a hit.

A. Right.

Q. Could you have decided on the basis of an unanticipated thing that you had not discussed with him to not enter the market that day because you were afraid of volatility?

A. If I understand you correctly, you are asking me whether I was going to trade or not trade? I guess I'm just saying --

Q. Right. I mean, if he'd authorized you to go up to 25 the next day, --

A. Right.

Q. -- and then something that you had not talked with him about, like for example, intervention in the Gulf --

A. Okay.

Q. -- might threaten -- you know, nobody might know what's going to happen.

A. I was not forced to trade.

Q. Okay. In that case, you could still decide not to --

A. Correct.

Q. -- until you talked to him again?

A. Correct.

(Tr. at 81-84.)

At that point in the first hearing, the parties were informed that in the Judgment Officer's view, the type of trading engaged in by Wolf seemed to violate CFTC rule 166.2 (Tr. at 84-85).

The hearing was then adjourned to a future date to allow the parties the opportunity to consider settlement in light of that suggestion, as discussed on the record during the second part of the hearing on April 1, 1998 (Tr. at 88*ff*.).

Oral Hearing, Part Two, April 1, 1998

Much of the second hearing involved discussions with the parties about the legal theories of each side's case, as well as attempts by all participants to understand the voluminous phone records and order tickets. Eventually, Violette was cross-examined by respondents' counsel, and claimed he did not recall when he confronted Wolf about the alleged unauthorized trading (Tr. 150-56). He also admitted knowing that unauthorized trading was a violation of the law by Wolf (Tr. at 160). He denied knowing about losses on August 27 until he received the statement for that day, despite being confronted with records of telephone calls between him and Wolf (Tr. at 161).

The next day on which voluminous trading occurred was September 3, and Violette lost $13,000 that day (Tr. at 164). He still did not close his account, however, and lost over one thousand dollars more two days later (Tr. at 166). The latter trades are not considered compensable in this case, however, since Violette failed to list them on his "Comprehensive Statement" in reply to the April 10, 1998, Order requiring him to specify allegedly unauthorized transactions.

Wolf testified that he and Violette had a pattern of talking on one day about the trading of the next day (Tr. at 195-96). On the afternoon of August 14, Wolf stated, Violette decided he wanted to trade more contracts, and authorized up to 35 for the 15th, because he "was here to be

aggressive" (Tr. at 197-98). In the same vein, Wolf testified that Violette authorized the trades on August 27 (Tr. at 201-202). He was fairly sure that Violette had authorized more S&P contracts than the six traded (Tr. at 203). As to the trades on the 3rd of September, Wolf testified that he and Violette had talked that morning when Violette called him, and that he and Violette discussed the "parameters" he would use that day in trading (Tr. at 205-206). Wolf testified that Violette decided to go back to the 25-contract limit that he had used at the beginning of the account (Tr. at 208). In Wolf's testimony, he also provided background information explaining his trading decisions based on certain market prices and why he thought his trading was not exercising what he termed "undue" discretion (Tr. at 209-224). However, he admitted that there was a bit of judgment and experience involved (Tr. at 225). Finally, Wolf also admitted that he had been informed in an audit by the National Futures Association that his type of trading was really discretionary trading (Tr. at 228-32).

Why Wolf's actions were not viewed by the Judgment Officer as exercising "time and price discretion" was discussed extensively with respondents' counsel at the oral hearing:

> MR. KING: Judge, if I could ask you a question, I want to be clear on something.
>
> JUDGMENT OFFICER MAILLIE: Yes.
>
> MR. KING: And I'm not saying that we're accepting Mr. Wolf's testimony or Mr. Violette's testimony, but if we assume for the sake of argument that Mr. Wolf is telling the truth, that they said trade up to 25, are you indicating, or are you saying -- are you holding that if you have time and price discretion and the customer authorizes up to a certain number of trades, that you absolutely have to place that number of trades?
>
> JUDGMENT OFFICER MAILLIE: No, no, no. I said that there is a question as to what the numbers mean. But it's my view that the broker can only

make the choice of up to a number if it depends on -- okay, liquidate my bellies, see how much we get, and then buy as many wheat contracts as we can get. Okay?

To me, that would be legitimate, because it is based on the uncertainty of how much money you've got available. Okay? You know, it could be, buy up to five if you can get them. But that is an instruction to buy as many as you can get, and the risk there is not going to be determined by the broker. That is going to be determined by the customer.

But I don't think the customer can place an open number type of order, as open as buy up to 25. I don't think that that -- I think that is the type of order that a broker has to look at, just as the customer -- you know, as he would look at any other illegitimate order placed by a customer and say, I'm sorry, we can't accept that type of order.

I mean, how do you transmit an order like that, buy up to 25? Can you transmit that to the floor? No, everything gets stuck in the broker's head.

The order is supposed to be reflected on order tickets when entered by the customer. In that case, there might never be an order ticket even prepared. I think that a broker takes that type of order at his own risk, because what happens if the market just goes completely in the customer's favor if he had been in the market, and the broker had decided, ah, time and price discretion allows me to decide never to enter an order here?

MR. KING: Well, that's the issue.

JUDGMENT OFFICER MAILLIE: If he had decided to do that and the customer never gets into the market, -- no, no, what I'm trying to say is, I don't know how you set the damages there. What I'm trying to say is that means -- if it's impossible to figure out the damages, that means there is something wrong with the order, and the broker has to reject it and ask for a specific number. The obligation is on the broker to figure out what the exact number is that the customer is willing to face -- I mean, to find out.

If the customer said buy soybeans -- I mean, do you want a market order? No. Well, what kind do you want? I don't know, you figure it out. And then the customer hangs up. That wouldn't be a legitimate order. The broker couldn't enter an order based on that, and would not be held to have violated anything by not accepting that order, because he didn't have a price, and he didn't have a number.

Under those circumstances, he would undoubtedly attempt to get the customer back on the phone and explain the problems with the order. But it would be no different than trying to place an order for one and a half contracts. It's a number that you can't accept.

As to how you set the damages associated with that, I guess that's something I'll have to figure out. In that respect, I may well end up finding that the customer authorized one.

So I don't have any trouble finding that the customer did not authorize specifically 24 or 34, or whatever the numbers were on these various days. If the customer authorized one, then the damages will be whatever the loss was, minus the one that he did authorize.

In any event, go ahead. I hope that answers your question. I'm sure you don't agree with it, but that's going to be the foundation for how I'm analyzing it.

MR. KING: Well, I just want to make sure that I have a correct understanding of 166.2 as you understand it. If a customer places an order -- let's assume that Mr. Violette places a one-lot on the morning of August 26, and he says, take time and price discretion on a one-lot in S&Ps, are you saying if the broker has a set of parameters that he's looking for, or even a set of parameters that he and the customer discussed, and the price doesn't reach that parameter that day, that he still has an obligation to place that order?

JUDGMENT OFFICER MAILLIE: Well, you've just given me two different scenarios. You said he has time and price discretion, and then you went ahead and said that the customer had given him parameters on those prices.

MR. KING: Let's take the first one. If he only had time and price discretion, the customer doesn't say anything about price, he says --

JUDGMENT OFFICER MAILLIE: Right, he says, I want to take one pork belly tomorrow, you use time and price discretion.

MR. KING: But I definitely want to trade one tomorrow.

JUDGMENT OFFICER MAILLIE: Right.

MR. KING: Is there an obligation -- if you don't see a time and price that you think is appropriate at any time during the day, is there an obligation to place an MOC order?

JUDGMENT OFFICER MAILLIE: I think he's got a definite order. I think he's got a definite requirement to buy something the next day.

The question isn't whether to buy. That is not reserved to the broker under that order. The question is when and at what price.

MR. KING: But if he is using his discretion with respect to when and price, if in his -- if he thinks it's in the best interests of the client --

JUDGMENT OFFICER MAILLIE: He didn't ask him to do what is in my best interests. See, that is where you are making your mistake in analyzing this. And you're flat-out wrong.

If there is a question of whether to enter the market, then it's a discretionary trade. If the question is when to enter the market, then that may be up to the broker, but he has still got an obligation to get the customer into the market.

If he ends up at a less favorable price because he still has a definite order and the market is becoming unfavorable as it goes on, and he thinks it is going to keep going, the broker can decide to not enter the order at his own risk. The customer might be grateful if it turns out that he's right. But if it turns out that he's wrong, then the broker is going to have to face the consequences of not putting the customer's order in, because the customer wanted to be in the market. Presumably, a good broker would contact the customer and try to get a clarification once the market started going badly.

* * *

MR. KING: Let's put it this way. If the broker is using his discretion, regardless of what the customer's best interest is, and if the broker says, I'm going to wait until the market rises five points or I'm going to wait until the market rises seven points, that is the discretion that I am going to use in connection with this trade.

JUDGMENT OFFICER MAILLIE: Right.

MR. KING: Because the customer gave me time and price discretion. If the market doesn't reach that point that day, and he doesn't place that trade, what you're saying is, he violated 166.2.

JUDGMENT OFFICER MAILLIE: Well, you have given me the second scenario now. I told you the two scenarios are different. There, you have a specific trigger point. He says, I'll enter the order five points above the opening.

MR. KING: But he doesn't tell the customer this. I'm saying this is completely at his discretion.

JUDGMENT OFFICER MAILLIE: It doesn't matter. That doesn't matter. That is not discretion. That is not time and price discretion. That is the discretion as to whether to enter the market.

MR. KING: And you're saying he can't do that?

JUDGMENT OFFICER MAILLIE: I'm saying that he can't do that -- that that violates 166.2.

MR. KING: Judge, that seems to me to be saying he has got an absolute obligation to place a trade to generate a --

JUDGMENT OFFICER MAILLIE: When a customer places an order? Yes.

MR. KING: That he has got to generate a commission from the account when the customer says, use time and price discretion, and if it never arrives at that place that you would have executed an order, you've got an absolute obligation to generate a commission from that client.

JUDGMENT OFFICER MAILLIE: But he doesn't say anything about -- if the customer doesn't know the condition that you have just put it on --

MR. KING: Because it is time and price discretion.

JUDGMENT OFFICER MAILLIE: No, it is not.

MR. KING: But Your Honor --

JUDGMENT OFFICER MAILLIE: That is not. That is a trading strategy discretion, and that's an entirely different matter. . . . Anything that involves whether to enter the market is more discretion than time and price gives you. . . .

(Tr. at 180-89.)

At the end of the second session of the oral hearing, respondents were directed to file their bill of attorneys fees (Tr. at 246-53), and they have done so, claiming $12,431.17 in fees and costs (*see* April 15, 1998, Affidavit of Attorney's Fees and Expenses signed by Christopher M. Burky, Esq.). Violette did not file a reply despite being given an opportunity to do so (Tr. at 253).

DISCUSSION

As a general matter, I find respondent Wolf to have been by far the more credible witness. Violette repeatedly in this proceeding -- from his scant complaint onward -- has changed his allegations, has failed to provide details when pressed, has revised his versions of events every time he has been asked for one, and has provided unconvincing justifications for his self-serving selective memory. I find that in most material respects, Violette is an unreliable witness whose testimony alone cannot be the basis of any finding of violations by Wolf. Accordingly, I reject Violette's numerous attempts to claim that he had no knowledge that Wolf would engage in trading beyond single contracts and I likewise reject Violette's charges that he did not authorize any disputed trades involving single contracts, as well as his claims that he did not authorize the trades of August 23 and 26.

Oddly, it is Wolf's relatively greater credibility that gives rise to the only issue in which I must find in Violette's favor, that being Wolf's pattern of engaging in trading where he, not Violette, determined both whether to enter the market and the actual number of contracts traded.

Rule 166.2 clearly requires the broker to obtain from the customer the "precise" amount of a commodity to be traded. As noted during the hearing, and as Wolf admitted he has been informed by the NFA, the rule does not allow a broker to obtain oral authority to trade a *maximum* number of contracts and then to make judgmental decisions as to whether the maximum, or a lesser number, will be traded. Contrary to the Herculean efforts of Wolf's counsel, "time and price discretion" does not include the decision whether to enter the market at all, which Wolf admitted was his decision under his trading agreement with Violette. Although Violette denied in his own testimony that he ever gave Wolf such permission to trade a maximum number of contracts, I find Violette's testimony unconvincing and suspect that he chose that particular distortion in order to further his overall unauthorized trading claim.

Based on *Wolf's* testimony, therefore, I find that of the trades complained of by Violette and listed on his "comprehensive statement" (with the exception of the August 23 and 26 trades disposed of above), -- *i.e.*, the S&P contracts traded on August 15 and September 3 -- were all traded under an oral trading authorization granted by Violette to Wolf in violation of Rule 166.2.

As to Violette's claims of churning and unauthorized transfers of funds, those allegations are without merit. Under the trading agreement with Wolf (Joint Answer, Exhibit E), Violette knew he was authorizing "aggressive" trading. Furthermore, I specifically credit Wolf's testimony that Violette determined the maximum number of contracts to be traded on any particular day, and that Violette, not Wolf, decided to increase that amount on August 15 when he wanted to become even more aggressive (Tr. at 74). Violette was highly experienced not only in trading but also in commodity futures litigation prior to opening this account, and he was

highly capable of voicing his opinion and demonstrating his full control over the account. Thus, a vital element required to find churning -- control over the level of trading in the account -- is lacking. Even if, however, the trading agreement were to be viewed as establishing that Wolf controlled the volume of trading, churning would still not be found here because (1) that volume reflected Violette's expressed wishes from the beginning; (2) the trading was done in furtherance of the high-volume trading strategy chosen by Violette *in writing* when he opened his account; and (3) there is no indication that Wolf's trading was done to maximize commissions -- in fact, he testified credibly that he chose certain contracts to *reduce* commissions to be paid by Violette (Tr. at 206).

The alleged illegal transfer of funds is simply an example of Violette's refusal to take responsibility for his own actions since he authorized that transfer when he opened the account (Joint Answer, Exhibit D).

Respondents' defense of ratification is the next issue to be determined. It is an affirmative defense, with the burden of proof on the respondents. As applied to unauthorized trading in general, respondents must show that a customer, with full awareness of the relevant facts, spoke or acted in such a fashion as to demonstrate that the customer intended to accept the trades as his or her own. *Stoller v. Siegel Trading Co.*, [1984-86 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,224 (CFTC June 6, 1984). Contrary to respondents' repeated arguments and their strong reliance on the language of their customer agreement and confirmation statements (Joint Answer, pages 3-4), mere failure to object to a completed trade is not sufficient to prove ratification. With regard to Rule 166.2 violations stemming from a grant of oral trading

discretion, the Commission has explicitly held that the existence of the oral agreement itself should not be considered as evidence of ratification -- it is the customer's conduct *after* the trades that is relevant, not the agreement that preceded the trading. *See Wolken v. Refco, Inc.*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,509 at page 36,188 (CFTC July 19, 1989), *and cases cited therein.* In *Wolken*, the customer made margin deposits to cover existing positions taken in violation of Rule 166.2, and the Commission found that those deposits showed ratification. *Id.*

Unlike *Wolken*, this case presents that rare situation where the allegedly ratified trades were complete and thus the broker is attempting to show that a customer has ratified a known *losing* transaction that could have been voided. This issue was discussed in the hearing (Tr. at 175-176). Although ratification of losing trades seems unlikely, here it is determined that respondents indeed have carried their heavy burden with respect to the August 15 trading. First, it is clear that Violette was fully aware of all relevant facts and that he did not make any decisions based on misrepresentations from Wolf. *Compare Troni v. Prudential-Bache Securities, Inc.*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,508 (CFTC July 18, 1989). Secondly, he knew at all times that he could object to any trades he had not authorized in advance. His testimonial admissions about his litigation to recover losses from unauthorized trading in other accounts established that he was well aware that he could object to unauthorized trades and have them reversed. Although he may not have known that Wolf's agreement with him violated a particular CFTC rule, Violette definitely knew that he had not *specifically* authorized each of the many day trades engaged in by Wolf pursuant to their

agreement. Indeed, that lack of specific authorization (which lies at the heart of Rule 166.2) has been Violette's obsession in this case as he has focussed throughout on obtaining telephone records and tape recordings (*see, e.g.,* Tr. at 96, 100, 101-114, and 118*ff.*). He clearly knew that the lack of twenty or thirty conversations when that many trades occurred would show that he had not specifically authorized them and that he could have them voided. Despite Violette's awareness that he could object, he chose not to do so, and then evinced his approval of Wolf's trading by continuing to authorize the very same activity. Thus, it is not merely from his failure to object that we can infer his acceptance of the trades, but instead from his affirmative conduct of (1) continuing to call Wolf to invite the type of trading, (2) continuing to place more single and multiple-contract transactions, and (most importantly) (3) continuing to specify the maximum contracts to be traded, that demonstrates Violette wanted to accept the results of his trading. He may have been thinking he was reserving the opportunity to later file a complaint based on unauthorized trading, but in so doing he was too clever for his own good because his conduct expressed his satisfaction that the trades now complained of were done pursuant to his wishes. Accordingly, Violette is considered to have ratified the transactions of August 15, 1996.

That analysis does not hold, however, for the September 3 trading engaged in by Violette. There is no evidence that he ever again gave Wolf permission to trade up to a maximum number of contracts following his receipt of the statements showing the huge losses on September 3. Although respondents would have the burden shift to Violette to demonstrate that he objected to the trades, as noted above the burden of proof for ratification rests upon respondents for every trade allegedly ratified and they cannot carry that burden simply through showing a failure to

object. In the absence of evidence showing that Violette acted affirmatively in any fashion to accept the trading of September 3 as his own, and in view of the fact that he declined Wolf's offer to continue trading and to deposit more money, it is determined that respondents have failed to demonstrate that Violette ratified the trades of September 3, 1996. Accordingly, Violette is entitled to damages stemming from the trading engaged in on that date.

In *Wolken*, the Commission found that the trading engaged in in violation of Rule 166.2 proximately caused the losses associated with those trades. *Accord, Troni v. Prudential-Bache Securities, Inc., supra.* Although that rule seems unduly harsh since it is conceded even by Violette's falsified version of events that he desired at least *one* contract on the days in question, nevertheless the rule of *Wolken* must be applied. Therefore, the reparation award in this matter reflects the total of losses suffered by Violette on September 3 from the trades engaged in by Wolf under his admitted program that has been found to have constituted a Rule 166.2 violation.

The account statements for September 3, 1996 (attached to Violette's Verified Statement), show that Violette lost a total of $13,438.50 from the day trading in the S&P index futures contract. The account statement also shows that the losses took the account value into a deficit position ($3,210.47). Normally, when trading takes an account into deficit, the customer is entitled only to the amount he lost of the equity he had deposited, and he does not obtain an award including the deficit unless he shows he paid the deficit. Here, Violette did not voluntarily pay the deficit that remained in his account, but the record establishes that it was collected from him from a mortgage company refinancing complainant's house in order to release a lien filed upon that house based on a default judgment obtained by respondents in civil litigation (Tr. at

234-42). Respondents also obtained an amount reflecting their attorney's fees. That amount is not, however, a loss from the trading but instead is attributable to Violette's failure to participate in the civil litigation. Since Violette has now "paid" the deficit, his award will be for the amount of losses stemming from the trades as reflected on the September 3 statement.

As to attorney's fees, such fees are DENIED. Although Violette may have made the statements to King as alleged in King's submission with respondents' verified statements, Violette's comments reflected therein, while flippant, do not establish that he believed he did not have a valid cause of action. Furthermore, the conduct engaged in by Violette during the course of the proceeding, as frustrating and deleterious to the orderly processing of this case as it has been, has resulted in more harm to his own case than to respondents. Violette's refusal to provide specifics, his convoluted argumentation, and his discrepancies in testifying have all undermined most of his charges. Finally, it is noted that respondents themselves have vigorously pressed as many issues that could be considered as frivolous as the allegations raised by complainant, including the abandoned bankruptcy and standing issues -- and especially the argument that Wolf did not exercise discretion *despite knowing full well that NFA had already audited Wolf and found that his conduct indeed required written trading authorization*. Moreover, while Violette was uncooperative in providing details of his allegations, respondents' own version of events was not provided until the submission of verified statements, long after Rule 12.18 required respondents to file a specific chronology of events. Thus, Violette's litigation conduct and strategies do not stand in isolation and, under the circumstances, are found NOT to be of the egregious sort as would entitle respondents to attorney's fees.

First American is liable for the acts of the Wolf respondents by virtue of its status as guarantor of Wolf Futures Group, its introducing broker (NFA registration records).

REPARATION AWARD AND ORDER

Violations having been found, it is ORDERED that respondents First American Discount Corporation, Scott Allen Wolf, and Wolf Futures Group pay reparations to complainant Gregory Paul Violette in the amount of $13,438.50, plus prejudgment interest compounded annually at the rate of 5.271% from September 3, 1996, to the date of payment, plus costs of $125 for the filing fee. LIABILITY IS JOINT AND SEVERAL.

It is further ORDERED that: (1) the complaint by Pamela G. Violette is DISMISSED for lack of standing; (2) the complaint against respondent David J. Javor is DISMISSED; (3) all other claims by Gregory Paul Violette are DENIED and DISMISSED; (4) respondents' counterclaim is DENIED and DISMISSED; and (5) respondents' request for attorneys' fees is DENIED.

Finally, it is ORDERED that all other oral and written rulings made during the course of this proceeding, except as modified herein, shall be deemed incorporated into this Order.

Dated: August 31, 1998

Joel R. Maillie

JOEL R. MAILLIE
Judgment Officer