

Commodity Futures Trading Commission
CEA CASES

NAME: JOHN S. MORRIS, EVERETT E. KLIPP, AND JOHN S. MORRIS AND CO., INC.

CITATION: 34 Agric. Dec. 316

DOCKET NUMBER: 205

DATE: FEBRUARY 17, 1975

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(No. 16,266)

In re JOHN S. MORRIS, EVERETT E. KLIPP and JOHN S. MORRIS AND Co., INC. CEA Docket No. 205. Decided February 17, 1975.

Allegation of violation of the Act -- unsustained by evidence of record -- Dismissal

Where the evidence of record fails to support the allegation that the provisions of the Act were in fact violated, the complaint herein is dismissed.

Richard W. Davis, for complainant.

Robert P Howington, Chicago, Ill., for respondents.

Decision by Dorothea A. Baker, Administrative Law Judge.

DECISION AND ORDER

PRELIMINARY STATEMENT

This is an administrative proceeding under the Commodity Exchange Act (7 U.S.C. Chapter 1), instituted by a Complaint and Notice of Hearing issued on January 18, 1973 by Assistant Secretary of Agriculture Richard E. Lyng. The Respondents are charged with willfully violating the provisions of Section 4b(2)(A) and (C) of the Act (7 U.S.C. 6b(2)(A) and (C)). Those provisions prohibit among others, any member of the Contract Market, or any correspondent, agent, or employee of any member from cheating, defrauding or attempting to cheat or defraud as well as:

"(C) willfully to deceive or attempt to deceive such other person by any means whatsoever in regard to any such order to contract or the disposition or execution of any such order or contract, or in regard to any act of agency performed with respect to such order or contract for such person; or * * *"

An oral hearing was held in Chicago, Illinois, on March 19, 20, 21, May 15, 16, 17, 1974 before Dorothea A. Baker, Administrative Law Judge, Office of Administrative Law Judges, United States Department of Agriculture. The Respondents were represented by Robert P. Howington, Jr., Esquire, Chicago, Illinois. Richard W. Davis, Jr., Esquire, Office of the General Counsel, United States Department of Agriculture, appeared as counsel for the Complainant. Both sides offered oral testimony and introduced documentary evidence. In addition, Complainant offered a number of documents as Offers of Proof in response to a suggestion by the Judicial Officer, in a ruling issued on May 8, 1974. In due course the parties hereto filed briefs, the Complainant's reply brief having been filed December 17, 1974.

FINDINGS OF FACT

After consideration of the entire record herein and based upon the probative, convincing and reliable evidence thereof, the following findings of fact are made:

1. Respondent John S. Morris and Co., Inc. ("Morris and Co."), an Illinois corporation, was at all times material herein a registered futures commission merchant under the Commodity Exchange Act and a clearing member of the Board of Trade of the City of Chicago.

2. Respondent John S. Morris was at all times material herein President of John S. Morris and Co., Inc.

3. Respondent Everett E. Klipp was at all times material herein Treasurer of John S. Morris and Co., Inc.

4. Mr. Joseph Grogan was at all times material herein a self-employed grain trader and a registered floor broker under the Commodity Exchange Act.

5. Mr. Charles E. Evans, Jr., opened a futures trading account with John S. Morris and Co., Inc., on or about March 10, 1971, in the name of Charles Evans, Jr. Trading was conducted in this account from time to time until October 8, 1971. Mr. Evans' account was introduced to Morris and Co. by Mr. Joseph Grogan pursuant to a Rule 222 Agreement between Morris and Co. and Grogan.

6. At the time Mr. Evans opened his account, he executed before a witness a customer's agreement which stated, in part:

"Gentlemen:

I hereby agree that all transactions executed for my account are subject to the rules and regulations of the exchange where executed. I further agree that I will at all times maintain and keep my account fully margined in accordance with your requirements. In case of my failure to maintain with you at all times such margin as you may deem adequate for your protection, you may, without prior demand or notice to me, Sell and/or Purchase such commodities as you may consider necessary."

7. Mr. Evans commenced trading in the account in March of 1971 after an initial deposit of \$ 5,000 was made to cover his margin requirements. From this time until the end of July 1971, Mr. Evans' account periodically became under-margined. Margin calls were made by Mr. Douglas Bullard, the margin clerk at Morris and Co., to Mr. Grogan who relayed them to Mr. Evans. In some instances, written notices were sent to Mr. Evans by Mr.

Bullard.

8. From time to time and in response to these calls, Mr. Evans deposited cash with Morris and Co. to cover his additional margin requirements. The following amounts were received by Morris and Co.:

3/11/71	\$ 5,000.00
4/09/71	1,600.00
6/10/71	3,600.00
6/26/71	1,464.30
7/06/71	1,350.00
7/14/71	5,600.00
Total	\$ 18,614.30

9. Mr. Evans, on his own initiative, met with Mr. Bullard a few times in July 1971, to discuss the margin requirements of his account and the possibility of Mr. Evans depositing securities with Morris and Co. as collateral against his margin requirements. During the course of these meetings, Mr. Bullard informed Mr. Evans that at times Morris and Co. would accept securities from customers as collateral against the margin requirements of the customers' trading accounts. Mr. Bullard also informed Mr. Evans that any securities deposited with Morris and Co. would only be used as collateral for margin to the extent of 75 percent of their market value and that, in any event, if his account got into a net deficit he would have to come up with additional funds.

10. On or about July 27, 1971, and after his meetings with Mr. Bullard, Mr. Evans forwarded to Morris and Co. a certificate representing 2,890.075 shares of

stock in Investors Mutual, Inc., and which at that time had a market value of approximately \$ 28,900. The certificate was in the following name:

Marion L. Maas
c/o Charles Evans, Jr.
6650 N. Damen Avenue, Apt. 1
Chicago, Illinois 60645
As trustee for Mrs. Irgard Vrla.

Mr. Bullard, as margin clerk for Morris and Co., allowed Mr. Evans' account credit for \$ 21,700 against margin requirements, said sum being approximately 75 percent of the market value of the stock on deposit. This was consistent with Regulation 1822 of the Chicago Board of Trade.

11. At a later and different date, Mr. Evans forwarded to Morris and Co. a letter of hypothecation bearing the handwritten names of "Charles Evans, Jr." and "Marion L. Maas." The letter,

bearing the date August 3, 1971, authorized Morris and Co. to sell or repledge the stock anytime Morris and Co. considered it necessary in order to satisfy the requirements of the account. The name "Marion L. Maas" was signed by Mr. Evans on the letter of hypothecation. Morris and Co. was unaware of this at the time. The letter carried an addendum to the effect that Morris and Co. could not offer the stock for sale until after first offering it to Mr. Evans. This was added by Mr. Evans.

12. The stock certificate was owned by Marion L. Maas. Mrs. Maas had endorsed it and given it to Mr. Evans to use as "collateral for some stock he had bought" and for which she had put in some money. It was not her intention in endorsing the stock certificate to authorize disposition of the stock. Mrs. Maas felt she still controlled it. At the time of the hearing she was 80 years old and did not believe she was well-informed on stock matters.

13. Through August and early September 1971, Mr. Evans continued trading in his account at Morris and Co. and both Mr. Evans and Morris relied upon the value of the certificate as margin security for Mr. Evans' trading. However, Morris and Co. looked to Mr. Evans to cover a cash deficit. During this period, the margin requirements for Mr. Evans' account were below the \$ 21,700 value of the stock on deposit as collateral for said requirements.

14. As of the close of the market on September 15, 1971, Mr. Evans' account reflected a net deficit in the amount of \$ 1,541. This deficit accelerated to \$ 3,416 on September 16, and to \$ 5,134.75 on Friday, September 17. On Monday, September 20, Mr. Bullard issued a written margin call to Mr. Evans for \$ 5,000 to cover the cash deficit in the account. At this time, based on the market at the close of business on September 17, the account's margin requirement was \$ 22,634.75, an amount in excess of the value of the stock attributable as collateral for the margin requirements.

15. On September 20, 1971, Mr. Evans changed his positions in the market and thereby reduced the margin requirements in his account to \$ 13,291, which was under the value of the stock held by Morris and Co. as collateral for margin. However, the account still had a cash deficit of approximately \$ 5,000.

16. On September 28, 1971, Mr. John S. Morris requested that Mr. Everett Klipp review the account of Mr. Evans because of the

cash deficit in the account and Mr. Evans' failure to respond to the margin call of September 20. Mr. Klipp did so on Wednesday, September 29 and discovered: that the stock deposited with Morris and Co. was not the name of Charles Evans,

Jr. for whom account No. 260-1 was carried, but rather was in the name of Marion L. Maas as Trustee for Irmgard Vrla; that the signatures of Mrs. Maas on the stock certificate and on the letter of hypothecation were different; and that the signature of Mrs. Maas on the stock certificate was not guaranteed.

17. After consultation with Mr. John S. Morris on Thursday, September 30, Mr. Klipp contacted Mr. Evans and informed him that he had failed to meet the margin call of September 20 and that the stock on deposit was not acceptable as collateral for margin. Mr. Klipp also told Mr. Evans that Morris and Co. would deliver the stock to him in return for an assignment of the proceeds. Mr. Klipp was informed by Mr. Evans that the matter would be taken care of the following Tuesday, October 5. Mr. Grogan was informed by Mr. Klipp that the account would be liquidated if Mr. Evans did not deposit cash margin. Mr. Grogan relayed this information to Mr. Evans.

18. Morris and Co. could not have secured a loan on the stock certificate from its bank because there was no guarantee of the signature endorsed on the reverse side on the certificate. Morris and Co. was unwilling to loan money to Mr. Evans on the stock because of the discrepancy of signatures of Marion L. Maas on the certificate and letter of hypothecation, and the lack of a signature guarantee.

19. On Tuesday, October 5, Mr. Klipp informed Mr. Grogan that Mr. Evans had not responded as promised. Mr. Klipp further informed Mr. Grogan that unless Morris and Co. received funds from Mr. Evans, the account would be liquidated. Mr. Grogan related this to Mr. Evans. Mr. Evans requested that Mr. Grogan try to hold off Morris and Co. for a few days. Mr. Evans informed Mr. Klipp on October 6 that he had tried to get a loan on the stock but could not. On Thursday, October 7, Mr. Grogan informed Mr. Klipp that Mr. Evans' account would be transferred to Paine, Webber, Jackson and Curtiss. Mr. Evans had stated this to Mr. Grogan.

20. Prior to Thursday, October 7, Mr. Evans' position in the market was as follows:

50,000 bu. March beans (long)
 50,000 bu. November beans (short)

 75,000 bu. December corn (long)

On October 7, Mr. Evans bought in the 50,000 bushels of November beans by an order placed from Paine, Webber, Jackson, and Curtiss. This lifted the spread on the account and increased the position held in the account. Mr. Klipp informed Mr. Grogan that this was the last straw and that the account would be liquidated. Mr. Grogan requested Mr. Klipp to hold off because he and Mr. Evans were to meet with a representative from Paine, Webber, Jackson and Curtiss concerning transfer of the account. Mr. Grogan informed Mr. Klipp that a transfer was possible but that he would let Mr. Klipp know for sure at 11:00 a.m. on Friday, October 8, 1971.

21. On October 8, 1971, Mr. Evans put in an order through Paine, Webber, Jackson and Curtiss to sell his 50,000 bushels of March beans at \$ 3.26. Mr. Grogan informed Mr. Klipp around noon on that day that Paine, Webber, Jackson and Curtiss would not give a definite answer concerning transfer of his account. Mr. Klipp decided to liquidate the account and entered orders to sell the corn at market on close, and the beans at \$ 3.26 or market on close. Both positions were liquidated at market on close and Mr. Evans' account was left with a deficit of \$ 3,216. The closing out of the open futures position of Mr. Evans was not explicitly authorized by him.

CONCLUSIONS

The sole issue involved in this proceeding is whether or not the Respondents violated the provisions of the Commodity Exchange Act. In support of its contention that it did the Complainant sets forth that its witness Mr. Evans was deceived and that in essence fraud was perpetrated upon him. However, the

evidence of record fails to support the allegation that the provisions of the Act were in fact violated. The customer's agreement signed by the witness Evans was not superseded nor supplemented by the oral conversations which he subsequently had. The convincing evidence of record reflects that although the witness Evans believed that the stock was to be used for margin for any trades he would make, there apparently was not a meeting of the minds between him and Mr. Bullard or any of the Respondents in this respect. Absent a meeting of the minds in this regard there was no subsequent contract. Moreover, the Respondents were justified in questioning the negotiability of the stock which had been deposited.

The evidence likewise is not convincing with respect to whether or not the witness Evans was notified that the stock was no longer acceptable for margin. It appears that notification was given him although he may have not so interpreted it. In addition, it appears that the witness could have re-established his positions after having had his account closed.

Another matter in this proceeding which deserves attention relates to whether or not the Complainant has complied with the Act with respect to the issuance of a warning notice. The evidence of record fails to disclose that it has.

Section 558 of the Administrative Procedure Act provides for the issuance of a warning letter in instances of this kind. For a more detailed discussion on this point see *In re Henry Shatkin*, CEA Docket No. 211.

Moreover, there is no precedent in the cases previously decided under the Commodity Exchange Act for this type of action. The Complainant has failed to show that it has, in the past, considered the facts as alleged herein to be violative of the Act. Consideration of the entire record fails to disclose that a violation of the Act occurred or that institution of the Complaint was justified on the basis of Complainant's prior policy. Moreover, it should be noted that this is an administrative proceeding and not a rule-making proceeding.

Pursuant to production under the Jencks Act various statements were produced by Complainant. These statements are a part of the record: [For purposes of convenience they have been numbered chronologically] (1) Statements relative to witness Caldwell, Folder 1; (2) Two letter's produced at first part of hearing and two pamphlets utilized by counsel, Folder 2; (3) Documents produced pursuant to certification to Judicial Officer, Folder 3; (4) Additional statements furnished after resumed hearing, Folder 4; (5) Statements first produced for en camera inspection some of which were later produced pursuant to Judicial Officer's ruling, Folder 5. Also of record are those documents which constituted offers of proof.

During the course of the hearing numerous motions were made and also renewed on brief with respect to the dismissal of this action for lack of jurisdiction; to terminate the proceedings; to strike the witness Evans' testimony; to disqualify the witness; and to terminate the proceedings. All of these motions were disposed of on record.

In view of the findings of fact set forth above and the conclusions herein it is concluded that the Complaint herein should be dismissed.

ORDER

That this Complaint be dismissed. Pursuant to the amended Rules of Practice governing proceedings under the Commodity Exchange Act, this Decision and Order becomes final * without further procedure thirty-five (35) days after service hereof, unless appealed to the Secretary by a party to the proceeding within thirty (30) days after service, as provided in Sections 0.16 and 0.18 of the amended Rules of Practice published in the Federal Register of August 20, 1973 (38 F.R. 22381).

*The Decision and Order became final February 17, 1975. -- Ed.

A copy of this Decision and Order shall be served upon each of the parties.

LOAD-DATE: June 16, 2008

