IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

U.S. COMMODITY FUTURES TRADING COMMISSION, **Plaintiff**, **v.** **KRAFT FOODS GROUP, INC. and MONDELĒZ GLOBAL LLC,** **Defendants.**	**Civil Action No. 15-2881** **Hon. John Robert Blakey**

DEFENDANTS KRAFT FOODS GROUP, INC. AND MONDELĒZ GLOBAL LLC'S MEMORANDUM OF LAW IN SUPPORT OF THEIR MOTION TO CERTIFY ISSUES FOR INTERLOCUTORY APPEAL PURSUANT TO 28 U.S.C. § 1292(B) AND TO STAY PROCEEDINGS

Defendants Kraft Foods Group, Inc. and Mondelēz Global LLC (collectively "Defendants" or "Kraft") respectfully move pursuant to 28 U.S.C. § 1292(b) to certify for interlocutory appeal two questions arising from this Court's December 18, 2015 Memorandum Opinion and Order ("Opinion") (Dkt. No. 87 ("Op.")). The first is whether a defendant's large futures position, coupled with an alleged intent to affect market prices but absent any other false communications to the market, constitutes "false signaling" market manipulation under §§ 6(c)(1) or 9(a)(2) of the Commodity Exchange Act ("Act") and corresponding Regulations 180.1 and 180.2. The second question is whether, when a defendant's purchases in the futures market cause cash and futures market prices to converge, those converging prices are "artificial" for purposes of those same statutory provisions and regulations.

The Court's Opinion reaches a holding on each of these issues, and each question readily satisfies the requirements for interlocutory appeal under § 1292(b)—each presents (1) "a

question of law" that (2) is "controlling" and (3) "contestable" and (4) whose "resolution . . . promise[s] to speed up the litigation." *Arenholtz v. Bd. of Trustees of the Univ. of Ill.*, 219 F.3d 674, 675 (7th Cir. 2000). The Court's decision denying Defendants' motion to dismiss Counts I and II of the Complaint turned entirely on these two controlling questions of law, and their definitive resolution now, before protracted and costly litigation, is essential to ensure not only that Kraft's motion to dismiss and later motion for summary judgment are properly decided, but also that jurors ultimately receive proper instructions at trial. Nor can there be any dispute that the legal issues these questions raise are contestable. The CFTC's novel legal theory in this case has drawn significant criticism, and the underlying legal issues have divided federal courts nationwide. Moreover, while the Seventh Circuit has yet to address the precise legal questions the case presents, there is substantial reason to believe that the Seventh Circuit would decide these issues consistent with its closely analogous decision in *Sullivan & Long v. Scattered Corp.*, 47 F.3d 857 (7th Cir. 1995) (holding manipulation requires a deceptive act beyond open market trading and that converging prices are not artificial). Immediate appellate review is essential to clarify these issues of first impression.

ARGUMENT

The legal questions presented in this motion meet the standard required for an interlocutory appeal under § 1292(b). The court of appeals may hear an interlocutory appeal if the district court certifies that the appeal presents "a controlling question of law as to which there is substantial ground for difference of opinion and that an immediate appeal from the order may materially advance the ultimate termination of the litigation." 28 U.S.C. § 1292(b).

Specifically, the Seventh Circuit holds that an interlocutory appeal under § 1292(b) is permissible upon the showing of four factors. The appeal must (1) present a question of law; (2)

that is controlling; (3) that is contestable; and (4) the resolution of which will expedite the resolution of the litigation. *Ahrenholz v. Board of Trustees of the Univ. of Ill.*, 219 F.3d 674, 675 (7th Cir. 2000).

The court in *Ahrenholz* "emphasize[d] the duty of the district court and of our court as well to allow an immediate appeal to be taken when the statutory criteria are met." *Id.* at 677; *see also Padilla v. Dish Network LLC*, No. 12 CV 7350, 2014 WL 539746, at *5 (N.D. Ill. Feb. 11, 2014) (finding that to certify a question for appeal under § 1292(b), a party must demonstrate "the existence of a difficult central question of law which is not settled by controlling authority"). Defendants meet the statutory requirements and, therefore, certification for interlocutory appeal should be granted.

I. The Motion Presents Questions of Law.

Under *Ahrenholz*, a question of law for purposes of § 1292(b) is a question that asks the meaning of a "statutory or constitutional provision, regulation, or common law doctrine . . . ." The court goes further to state that a question of law under § 1292(b) means "an abstract legal issue." 219 F.3d at 676-77. Stated differently, a "question of law" should refer to a pure question of law that the court of appeals can "decide quickly and cleanly without having to study the record." *Id.*

Here, Defendants request certification for interlocutory appeal to decide two abstract legal issues that require interpretation of both statutes and regulations. *See, e.g.*, *Padilla*, 2014 WL 539746, at *6 (question of statutory interpretation presents pure question of law). Defendants ask "whether a 'false signaling' market manipulation claim under §§ 6(c)(1) or 9(a)(2) and Regulations 180.1 or 180.2 can be based on defendant's large futures position and alleged intent to manipulate in the absence of any other alleged false communication to the market?" The second threshold legal question asks, "where a defendant's purchases in the futures

market cause converging prices in the cash and futures market, can those converging prices be artificial under §§ 6(c)(1) or 9(a)(2) and Regulations 180.1 or 180.2?"[1]

As acknowledged by this Court, the interpretation of § 6(c)(1) and Regulation 180.1 is an issue of first impression. (Op. at 15.) The Court found that under §§ 6(c)(1) and 9(a)(2) Plaintiff was not required to plead that Defendants transmitted a message to the market concerning their intentions beyond taking a large long position in December 2011 wheat futures. (*Id.* at 27, 36.)

Likewise, this Court also found that under §§ 6(c)(1) and 9(a)(2), as well as Regulations 180.1 and 180.2, converging cash and futures prices could still be considered an artificial price. (*Id.* at 45.) Both issues present questions concerning the application of a legal standard and are therefore questions of law. "The Seventh Circuit has regularly granted interlocutory appeals reviewing denials of motions to dismiss where there was a contestable application of a legal standard." Order, *In re Potash Antitrust Litig.*, No. 08 C 6910, at 4 (N.D. Ill. Jan. 13, 2010) (Castillo, J.) (citing *Williams v. Sims*, 390 F.3d 958 (7th Cir. 2004)). The two issues presented are clearly questions of law as they involve abstract legal issues concerning the interpretation of statutes and regulations within the meaning of § 1292(b).

II. The Questions of Law Are Controlling.

The questions of law are "controlling" because the resolution of whether §§ 6(c)(1) and 9(a)(2), as well as Regulations 180.1 and 180.2, require an act to deceive the markets beyond taking a position in the futures market "is quite likely to affect the further course of the litigation, even if not certain to do so." *Sokaogon Gaming Enter. Corp. v. Tushie-Montgomery Assocs., Inc.*, 86 F.3d 656, 659 (7th Cir. 1996); *see also Johnson v. Burken*, 930 F.2d 1202, 1205-06 (7th Cir. 1991) (question is controlling if the further course of the case would be affected by its

[1] See Defendants' Proposed Order Certifying the Court's December 18, 2015 Memorandum Opinion and Order for Interlocutory Review submitted along with this motion.

resolution). Likewise, the question of whether a converging cash and futures price can be artificial under the above statutes and regulations is also controlling.

In the instant matter, the resolution of Defendants' questions of law would significantly affect the continuing course of the litigation. Plaintiff's Complaint alleges a manipulative scheme undertaken by the Defendants that does not include any outward signal to the market on the part of the Defendants besides Defendants' open market futures position. (Dkt. No. 1 ("Compl.").) If Plaintiff were required to allege an additional element of deception beyond Defendants' open market futures position, Plaintiff's Complaint would fail on its face as Plaintiff makes no such allegations. Likewise, if converging cash and futures prices could not be artificial, Plaintiff's claims concerning the existence of an artificial price would fail because Plaintiff's Complaint states that cash prices fell and futures prices rose, *i.e.*, converged as the contract neared expiration. (Compl. at ¶ 40.)

The failure of Plaintiff's Counts I and II in the Complaint based on the above standard would effectively end the market manipulation aspect of this case. Moreover, appellate review is critical here to ensure the proper scope and focus of discovery, the proper standard for summary judgment, and that jurors receive proper instructions at trial. Thus, under the standard set forth in *Sokaogon Gaming*, resolution of Defendants' questions of law would be controlling. 86 F.3d at 659.

III. Defendants' Questions of Law Are Contestable.

The issues presented by Defendants are "contestable" as required under § 1292(b). An issue is contestable if there is "a 'difficult central question of law which is not settled by controlling authority.'" *In re Brand Name Prescription Drugs Antitrust Litig*, 878 F. Supp. 1078, 1081 (N.D. Ill. 1995) (quoting *In re Heddendoft*, 263 F.2d 887, 889 (1st Cir. 1959)).

As acknowledged by this Court, the interpretation of § 6(c)(1) and Regulation 180.1 is a matter of first impression. (Op. at 15.) Moreover, the Seventh Circuit has not yet spoken on Defendants' questions of law. There is thus a substantial likelihood that the district court ruling will be revised on appeal. *In re Text Messaging Antitrust Litig.*, 630 F.3d 622, 626-27 (7th Cir. 2010) (holding the court properly certified as an issue for interlocutory appeal the question of pleading standards under *Twombly* because the standards had not been specifically and conclusively addressed by the Seventh Circuit). As such, the issues are contestable since the "controlling appellate court" has not ruled on the question and substantial ground for a difference of opinion exists in this matter. *Padilla*, 2014 WL 539746, at *5.

A. Whether a "false signaling" market manipulation claim under §§ 6(c)(1) or 9(a)(2) and Regulations 180.1 or 180.2 can be based on defendant's large futures position and alleged intent to manipulate in the absence of any other alleged false communication to the market?

This Court determined that the proper standard for fraudulent manipulation was an issue of first impression in the Seventh Circuit. In its Opinion, the Court concluded that the additional provisions added to the Act in § 6(c)(1) and the supporting regulations were intended to parallel § 10(b) of the Securities Exchange Act and SEC Rule 10b-5, and, therefore, "case law interpreting Section 10(b) and Rule 10b-5 remains instructive here." (Op. at 17.)

The Seventh Circuit has not addressed "false signaling" manipulation in the commodities context, but it has confronted manipulation claims under § 10(b). In the closely analogous case of *Sullivan & Long*, the court held that short selling is neither deceptive nor manipulative absent other representations, actual or implicit, even where the trader intends to depress the stock price. *See* 47 F.3d at 864-65. The defendant in that case was not required to have enough stock to cover its short sales, so plaintiffs could not have been deceived by the defendant's failure to disclose its intent not to deliver. *Id.* at 863-64.

Rather than applying the principles articulated in *Sullivan & Long*, this Court relied on an out-of-circuit case, *ATSI Commc'ns Inc. v. Shaar Fund, Ltd.*, 493 F.3d 87, 101 (2d Cir. 2007), in holding that under §§ 6(c)(1) and 9(a)(2), Plaintiff was not required to plead an additional deceptive act beyond Defendants' buying futures with an alleged intent to manipulate. Yet other circuit and district courts—including district courts interpreting *ATSI*—have held that "[m]ere sales [or purchases] do not inject false information into the marketplace, nor can a party inject false information into the marketplace . . . simply by selling [or buying] stock on the open market." *Nanopierce Techs., Inc. v. Southridge Capital Mgmt.*, No. 02 C 0767, 2008 WL 1882702, at *2 (S.D.N.Y. Apr. 21, 2008) (following *ATSI*); *see also GFL Advantage Fund, Ltd. v. Colkitt*, 272 F.3d 189, 211 (3d Cir. 2011) (market manipulation requires "some other type of deceptive behavior in conjunction with [open market trades]" that injects inaccurate information into the marketplace).

Other courts, by contrast, hold that otherwise legitimate trading can constitute manipulation solely because of the actor's purpose. This Court opted to follow the pleading standard articulated in *In re Amaranth Natural Gas Commodities Litig.*, 587 F. Supp. 2d 513 (S.D.N.Y. 2008), a case that purported to rely on *ATSI*, but interpreted *ATSI* differently than other courts in the same district, *see Nanopierce*, 2008 WL 1882702, at *2. Thus, the *Amaranth* and other courts represent one side of the split of authority on the proper pleading standard for open market manipulation claims. *See Markowski v. S.E.C.*, 274 F.3d 525, 529 (D.C. Cir. 2001); *S.E.C. v. Masri*, 523 F. Supp. 2d 361, 372 (S.D.N.Y. 2007).

This Court's decision to follow the latter line of authority presents a question on which there are substantial grounds for a difference of opinion. Even under *ATSI*, relied on by *Amaranth* and this Court, "buying and holding large positions" without "legitimate demand" is

insufficient to allege manipulation under §§ 6(c)(1) or 9(a)(2). (Op. at 26-27, 38.) Notably, *ATSI* relied on the Seventh Circuit's decision in *Sullivan & Long* and the Third Circuit's decision in *GFL* in determining that "[t]o be actionable as a manipulative act, [otherwise legal, open market activity] must be willfully combined with *something more* to create a false impression of how market participants value a security." 493 F.3d at 101 (emphasis added). "Mere sales [or purchases] do not inject false information into the marketplace, nor can a party inject false information into the marketplace . . . simply by selling [or buying] stock on the open market." *Nanopierce*, 2008 WL 1882702, at *2 (following *ATSI*). Thus, under the *GFL*, *ATSI*, and *Nanopierce* line of authority, purchasing a security—even in high volume and with the intent to increase or decrease the price—is not alone manipulative. There are likewise substantial grounds to believe that the Seventh Circuit would extend its closely analogous holding in *Sullivan & Long* to open market manipulation claims in the commodities context.

B. Where a defendant's purchases in the futures market cause converging prices in the cash and futures market, can those converging prices be artificial under §§ 6(c)(1) or 9(a)(2) and Regulations 180.1 or 180.2?

The second issue presented by Defendants is also contestable. The Court held that lawful, open market transactions—specifically a large long position—could create artificial prices for wheat on both the futures market and the cash market despite the fact that those prices moved towards convergence at the time of contract expiration and delivery. The Court held that an artificial price could exist based on Defendants' alleged lack of legitimate demand supporting its large long futures position despite the fact that Plaintiff's alleged wheat cash and futures prices converged as they were supposed to do.[2] However, an "essential point" of *Sullivan & Long* is

[2] Although the CME and CFTC regulations permit commercial users to take positions equal to twelve months' demand for wheat, this Court concluded—again as a matter of first impression—that Defendants' position equal to six months' demand represented "illegitimate demand." *See* CFTC

that conduct that causes convergence as the contract nears expiration and the delivery period does not create artificial prices—it eliminates them. *See* 47 F.3d at 862, 865.

In *Sullivan & Long*, the defendant engaged in substantial naked short selling, selling more shares than were outstanding so that it was not possible to deliver all the shares it sold short. 47 F.3d at 863. The Seventh Circuit held that this conduct did not constitute market manipulation and that even by engaging in such a large volume of naked short selling, such that the defendant could not possibly deliver on its obligations, the defendant did not create an artificial price. *Id.* at 862 (finding that defendant's conduct "eliminate[d] artificial price differences").

The Seventh Circuit also instructed that it "would think twice before concluding that [securities] laws prohibit 'schemes' that accelerate rather than retard the convergence between the price of a stock and its underlying economic value and therefore promote rather than impair the ultimate goals of public regulation of the securities markets." *Id.* at 861. The same basic principle applies to commodities futures markets, where the effective functioning of that market depends on the cash and futures prices converging as the contract expiration nears.[3] While this is an issue of first impression, there are substantial grounds to believe that the Seventh Circuit

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Speculative Limits, *available at* http://www.cftc.gov/IndustryOversight/MarketSurveillance/SpeculativeLimits/speculativelimits.

[3] The economic utility of deliverable futures markets is predicated on the notion that the delivery mechanism forces convergence between the cash and futures markets because they are substitutes. *See In re Soybeans Futures Litig.*, 892 F. Supp. 1025, 1056 n.33 (N.D. Ill. 1995)*; see* Senate Perm. Subcomm. on Investigations, Excessive Speculation in the Wheat Market at 61 (June 24, 2009) ("Senate Wheat Report") (quoting Professor Thomas Hieronymus) ("If the cash price were above the futures price, users would buy futures and stand for delivery as the cheapest source of supply."), *available at* http://www.hsgac.senate.gov/download/psi-report-excessive-speculation-in-the-wheat-market-june-24-2009. In *Soybeans*, 892 F. Supp. at 1056 n.33, the court noted that cash and futures prices "generally should move in the same direction because they respond to the same market forces." This phenomenon is what is known as convergence. *Sullivan & Long*, 47 F.3d at 862.

would extend its holding from *Sullivan & Long* from the stock market to the futures markets; that is, the court would hold that conduct that causes convergence cannot create an artificial price.

IV. The Resolution of Defendants' Questions of Law Will Expedite the Litigation.

The resolution of these questions will expedite the litigation and "materially advance the ultimate termination of the case." 28 U.S.C. § 1292(b). If Counts I and II of Plaintiff's Complaint are removed, major aspects of discovery in this matter will disappear. While Counts III and IV addressing unrelated conduct would survive, the burden and scope of this matter would be materially reduced without Plaintiff's manipulation claims. In *Sterk v. Redbox Automated Retail, LLC*, 672 F.3d 535, 536 (7th Cir. 2012), Judge Posner writing for the Seventh Circuit found that where a grant of interlocutory appeal would destroy one of the plaintiff's main claims, that would be sufficient to satisfy the "may materially advance" clause of § 1292(b). As such, Defendants' questions of law are particularly ripe for review at this stage.

V. The Questions Presented Are of Great Importance.

While not a factor under § 1292(b), this Court's Opinion may have significant implications given that this Circuit is home to the largest commodity trading market in the country. From the outset of this case, Plaintiff's aggressive interpretation of § 6(c)(1) and Rule 180.1 has drawn critical attention from the legal and trading communities. *See, e.g.*, Michael Spafford & J. Bub Windle, *CFTC Action Against Kraft May Be an Important Early Test of New Anti-Fraud Authority, Part 2*, December 10, 2015 (*available at* http://www.paulhastings.com/publications-items/details/?id=98c9e769-2334-6428-811c-ff00004cbded). Among the concerns raised by the community is that the CFTC's position leaves market participants unable to "tailor [their] behavior . . . [to] an amorphous regulatory regime, particularly in markets, such as commodities markets, that are based on asymmetrical information and where . . . participants have no duty to disclose material non-public information before trading." *Id.*

Furthermore, the Court's presumption that "legitimate demand" must relate to an immediate need for wheat overlooks (and may constrain) the fundamental purpose of hedging, as well as the fact that most market participants are speculators with no actual demand for wheat. CFTC rules (and Defendants' hedge exemption) authorize wheat users like Defendants to take futures positions equal to twelve months' supply, including purchases *anticipated* over that period, and Plaintiff admits that wheat users rarely intend to take delivery and use wheat from the futures market. By holding that Plaintiff adequately alleged that Defendants' futures position did not reflect a "legitimate demand" because Defendants purportedly did not intend to take delivery on its position or immediately acquire cash wheat in an equivalent amount, the Court's decision, without guiding precedent, effectively rewrites CFTC regulations and constrains commercial users' ability to hedge *future* demand, which is the purpose of the futures market. Immediate review will forestall that result.

CONCLUSION

For all of the foregoing reasons, and the reasons contained in the Defendants' prior briefing, Defendants respectfully submit that this Court should certify the legal questions identified herein for immediate interlocutory appeal under 28 U.S.C. § 1292(b) and stay the proceedings until the United States Court of Appeals for the Seventh Circuit decides Defendants' petition for permission to appeal and all appeals resulting therefrom are finally resolved.

Dated: January 19, 2016

Respectfully submitted,

/s/ Gregory S. Kaufman

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CERTIFICATE OF SERVICE

I certify that on January 19, 2016, I served the foregoing **Defendants Kraft Foods Group, Inc. and Mondelēz Global LLC's Memorandum of Law in Support of Their Motion To Certify Issues for Interlocutory Appeal Pursuant to 28 U.S.C. § 1292(b) and Stay Proceedings** on counsel of record via the Court's CM/ECF system.

Dated: January 19, 2016 /s/ Stephen T. Tsai