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CLERK OF DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

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**UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA**

03-2659
TJH
VBKx

14 Commodity Futures Trading Commission,

15 Plaintiff,

16 v.

17 Paulino Rene Dias, Jr., Victor Smith, and Krute
18 Corporation,

19 Defendants,

20 Iceland Management Services, Inc.

21 Relief Defendant.

) Case No.:

) **COMPLAINT FOR A
) PERMANENT
) INJUNCTION,
) OTHER EQUITABLE
) RELIEF AND CIVIL
) MONETARY PENALTIES**

) **Hearing Date:**
) _____

) **Hearing Time:**
) _____

I. JURISDICTION AND VENUE

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3 1. The Commodity Exchange Act, as amended, 7 U.S.C § 1 *et. seq.*
4 (2001) (the "Act"), establishes a comprehensive system for regulating the purchase
5 and sale of commodity futures contracts and options on commodity futures
6 contracts. This Court has jurisdiction over this action pursuant to Section 6c of the
7 Act, 7 U.S.C. § 13a-1 (2001), which authorizes the Commodity Futures Trading
8 Commission ("Commission") to seek injunctive relief against any person whenever
9 it shall appear to the Commission that such person has engaged, is engaging, or is
10 about to engage in any act or practice constituting a violation of any provision of
11 the Act or any rule, regulation or order thereunder.
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16 2. Venue properly lies with the Court pursuant to Section 6c of the Act,
17 in that the Defendants are found in, inhabit, or transact business in this district, and
18 the acts and practices in violation of the Act have occurred, are occurring, or are
19 about to occur within this district.
20

II. SUMMARY

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22
23 3. Since in or about November 2001, Paulino Rene Dias, Jr. ("Dias"),
24 Victor Smith ("Smith") and Krute Corporation ("Krute") (collectively the
25 "Defendants") have solicited and accepted in excess of \$2 million from at least
26 thirteen members of the general public to participate in, among other things, an
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28

1 unnamed commodity trading pool operated by Krute ("the Pool"), to trade
2 commodity futures contracts and options on futures contracts. During the course
3 of the Pool's operations, the Defendants misappropriated at least \$530,000 of the
4 Pool's funds for their business and personal use.
5

6
7 4. Furthermore, Krute has operated as a commodity pool operator
8 ("CPO") without being registered as such, and, while operating as a CPO, failed to
9 provide Pool participants with required periodic account statements.
10

11 5. Defendants' misappropriation of Pool participants' funds violates
12 Sections 4b(a)(2)(i) and (iii), 4c(b) and 4o(1) of the Act, 7 U.S.C. §§ 6b(a)(2)(i)
13 and (iii), 6c(b) and 6o(1) (2001), and Section 33.10 of the Commission's
14 Regulations (the "Regulations"), 17 C.F.R. § 33.10 (2002).
15

16 6. Krute's failure to register as a CPO violates Section 4m(1) of the Act,
17 7 U.S.C. §6m(1) (2001).
18

19 7. Krute's failure to provide required periodic account statements
20 violates Section 4n(4) of the Act, 7 U.S.C. §6n(4) (2001), and Commission
21 Regulation 4.22, 17 C.F.R. § 4.22 (2002).
22

23 8. The actions of Dias and Smith described in this Complaint were done
24 within the scope of their employment with Krute, and therefore Krute is liable for
25 their violations pursuant to Section 2(a)(1)(B) of the Act, 7 U.S.C. § 2 (2001).
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1 the Act, 7 U.S.C. §§ 1 *et seq.* (2001), and the Regulations promulgated under it, 17
2 C.F.R. §§ 1 *et seq.* (2002).

3
4 14. Defendant Dias is an individual who resides at 6801 Retreat Lane,
5 Pollock Pines, California 95726. He has been registered as an AP with various
6 introducing brokers (“IBs”) intermittently since 1993. Until recently, Dias was
7 registered as an AP of Brewer Investment Group Inc. (“BIG”), a registered IB and
8 CPO since October 18, 2001. His AP registration was suspended by the NFA on
9 October 7, 2002 for lying, and failing to cooperate and provide information in
10 NFA’s investigation of Krute. Pursuant to a settlement accepted by the NFA on
11 February 19, 2003, and effective March 6, 2003, Dias has agreed to never apply for
12 NFA membership or Associate or principal status with any NFA member in the
13 future. Dias has never registered in any capacity in relation to his activities on
14 behalf of Krute Corporation.

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19 15. Defendant Victor Smith is an individual who resides at 6596 Bradley
20 Place, Los Angeles, California, 90056. He has been registered as an AP with
21 various IBs since 1996. Smith has been registered as an AP of BIG, a registered
22 IB and CPO, since August 28, 2002. Smith has never been registered in any
23 capacity in relation to his activities on behalf of Krute Corporation.
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1 commodities trading account (acct. no. 64204) at Man Financial, Inc. ("Man
2 Financial").

3
4 21. From November 2001 to August 2002, Dias used the Pool funds in the
5 Krute accounts at Man Financial to trade commodity futures and options on
6 commodity futures in the S&P 500 and NASDAQ stock indices, as well as cotton
7 and other commodities on behalf of the Pool.
8

9 22. Over the lifetime of the four Krute accounts at Man Financial, they
10 have collectively received approximately \$405,000 in deposits, experienced
11 approximately \$185,000 in net trading losses, and had total withdrawals totaling
12 \$175,000.
13
14

15 23. Krute also invested Pool funds in a commodity pool named
16 Morganheimer Fund, LLC, which is operated by BIG and trades through an
17 account at Man Financial. At the time Pool funds were placed in the
18 Morganheimer Fund, both Dias and Smith were APs of BIG, and their sole duty
19 was to solicit investors for the Morganheimer Fund. In total, Krute deposited
20 approximately \$475,000 of the Pool's money in the Morganheimer Fund.
21
22

23 24. Pursuant to Krute's account agreement with the Pool participants,
24 Krute was only entitled to one-quarter of one percent (.25%) per quarter year for
25 management and accounting fees.
26
27
28

1 25. Pool participants also agreed to pay Krute 25% of any profits
2 generated from their investments.
3

4 26. There is no evidence that Krute has ever realized any overall profits
5 on any of its various investments.
6

7 27. The account agreement between Krute and the Pool participants did
8 not allow Krute to remove pool funds for business expenses.
9

10 28. During the course of the Pool's operation from approximately
11 November 2001 to August 2002, the Defendants directed a substantial portion of
12 the Pool's funds to pay business expenses, such as employee salaries and rent, as
13 well as personal expenses, including seven months of rent on Defendant Dias's
14 apartment totaling \$10,391.17.
15

16 29. Since January of 2002, Defendants have withdrawn approximately
17 \$70,000 in cash, transferred over \$150,000 to Relief Defendant IMS, paid
18 themselves approximately \$180,000, transferred approximately \$66,000 to former
19 non-Krute employees, and paid business and personal rents totaling approximately
20 \$65,000.
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1 **V. VIOLATIONS OF THE COMMODITY EXCHANGE ACT**

2 **COUNT ONE**

3 **VIOLATIONS OF SECTIONS 4b(a)(2) OF THE ACT :**
4 **FRAUD BY MISAPPROPRIATION**

5
6 30. The allegations set forth in paragraphs 1 through 29 are realleged and
7 incorporated herein by reference.

8
9 31. Since approximately November, 2001, the Defendants have: (1)
10 cheated or defrauded or attempted to cheat or defraud other persons; and/or (2)
11 willfully deceived or attempted to deceive other persons, in or in connection with
12 orders to make, or the making of, contracts of sale of commodities for future
13 delivery, made, or to be made, for or on behalf of any other persons, where such
14 contracts for future delivery were or could be used for the purposes set forth in
15 Section 4b(a) of the Act, 7 U.S.C. § 6b(a), all in violation of Section 4b(a)(2)(i)
16 and (iii) of the Act, 7 U.S.C. § 6b(a)(2)(i) and (iii).

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20 32. By using, for their own personal expenses and for business expenses,
21 funds solicited to trade commodity futures for Pool participants, as set forth in
22 paragraphs 23-28, the Defendants knowingly misappropriated funds in violation of
23 Section 4b(a)(2)(i) and (iii) of the Act.

24
25
26 33. The actions of Dias and Smith described in this count were done
27 within the scope of their employment with Krute, and therefore Krute is liable for
28

1 their violation of Section 4b(a)(2)(i) and (iii) of the Act, pursuant to Section
2 2(a)(1)(B) of the Act, 7 U.S.C. § 2 (2001).

3
4 34. Defendant Dias, directly or indirectly, controlled Krute and did not act
5 in good faith or knowingly induced, directly or indirectly, the acts constituting
6 Krute's violations alleged in this count, and thereby Defendant Dias is liable for
7 Krute's violations of Section 4b(a)(2)(i) and (iii) of the Act, pursuant to Section
8 13(b) of the Act, 7 U.S.C. § 13c(b) (2001).

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10
11 35. Each act of misappropriation made during the relevant time period,
12 including but not limited to those specifically alleged herein, is alleged as a
13 separate and distinct violation of Section 4b(a)(2)(i) and (iii) of the Act.

14
15 COUNT TWO

16 VIOLATIONS OF SECTION 4c(b) OF THE ACT
17 AND REGULATION 33.10:
18 OPTIONS FRAUD AND MISAPPROPRIATION

19
20 36. The allegations set forth in paragraphs 1 through 35 are realleged and
21 incorporated herein by reference.

22
23 37. Beginning in or about November 2001, the Defendants: (1) cheated or
24 defrauded or attempted to cheat or defraud other persons; and/or (2) willfully
25 deceived or attempted to deceive other persons, in or in connection with an offer to
26 enter into, the entry into, the confirmation of the execution of, or the maintenance
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1 of, commodity option transactions, all in violation of Section 4c(b) of the Act, 7
2 U.S.C. § 6c(b), and Regulation 33.10, 17 C.F.R. § 33.10.
3

4 38. By using, for their own personal expenses and for business expenses,
5 funds solicited to trade options on commodity futures contracts for Pool
6 participants, as set forth in paragraphs 23-28, the Defendants knowingly
7 misappropriated funds in violation of Section 4c(b) of the Act and Regulation
8 33.10.
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11 39. The actions of Dias and Smith described in this count were done
12 within the scope of their employment with Krute, and therefore Krute is liable for
13 their violation of Section 4c(b) of the Act and Regulation 33.10, pursuant to
14 Section 2(a)(1)(B) of the Act, 7 U.S.C. § 2 (2001).
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17 40. Defendant Dias, directly or indirectly, controlled Krute and did not act
18 in good faith or knowingly induced, directly or indirectly, the acts constituting the
19 violations of Krute alleged in this count, and thereby Dias is liable for Krute's
20 violations of Section 4c(b) of the Act and Regulation 33.10, pursuant to Section
21 13(b) of the Act.
22

23
24 41. Each act of misappropriation made during the relevant time period,
25 including but not limited to those specifically alleged herein, is alleged as a
26 separate and distinct violation of Section 4c(b) of the Act and Regulation 33.10.
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1 46. By using, for their own personal expenses and for business expenses,
2 funds solicited to trade commodity futures and options on commodity futures
3 contracts for Pool participants, as set forth in paragraphs 23-28, the Defendants
4 have knowingly misappropriated funds in violation of Sections 4o(1)(A) and (B) of
5 the Act.
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8 47. The actions of Dias and Smith described in this count were done
9 within the scope of their employment with Krute, and therefore Krute is liable for
10 their violations of Sections 4o(1)(A) and (B) of the Act, pursuant to Section
11 2(a)(1)(B) of the Act, 7 U.S.C. § 2 (2001).
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14 48. Defendant Dias, directly or indirectly, controlled Krute and did not act
15 in good faith or knowingly induced, directly or indirectly, the acts constituting
16 Krute's violations alleged in this count, and thereby Defendant Dias is liable for
17 Krute's violations of Sections 4o(1)(A) and (B) of the Act, pursuant to Section
18 13(b) of the Act.
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21 49. Each act of misappropriation, each material misrepresentation or
22 omission, including but not limited to those specifically alleged herein, is alleged
23 as a separate and distinct violation of Sections 4o(1)(A) and (B) of the Act.
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1 monthly account statements prepared by Krute and provided to Pool participants
2 failed to provide the required information accurately. Accordingly, Krute failed to
3
4 provide the required account statements to Pool participants, in violation of Section
5 4n(4) of the Act, 7 U.S.C. § 6n(4), and Regulation 4.22, 17 C.F.R. § 4.22.

6
7 55. Dias, directly or indirectly, controlled Krute and did not act in good
8 faith or knowingly induced, directly or indirectly, the acts constituting Krute's
9
10 violations alleged in this count, and thereby Dias is liable for Krute's violation of
11 Section 4n(4) of the Act and Regulation 4.22, pursuant to Section 13(b) of the Act.

12 **VI. RELIEF REQUESTED**

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14 WHEREFORE, the Commission, respectfully requests that this Court, as
15 authorized by Section 6c of the Act, 7 U.S.C. § 13a-1, and pursuant to its own
16 equitable powers, enter:
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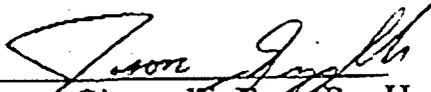
- 18 a) a permanent injunction prohibiting the Defendants and
19 any other person or entity associated with them,
20 including any successor thereof, from engaging in
21 conduct violative of Sections 4b(a)(2)(i) and (iii), 4c(b),
22 4m(1), 4n(4) and 4o(1) of the Act and Sections 4.22 and
23 33.10 of the Commission's Regulations, and from
24 engaging in any commodity-related activity, including
soliciting new customers or customer funds or pool
participants or pool funds;
- 25 b) an order directing the Defendants to disgorge, pursuant to
26 such procedure as the Court may order, all benefits
27 received from the acts or practices which constitute
28 violations of the Act or Regulations, as described herein,
and interest thereon from the date of such violations;

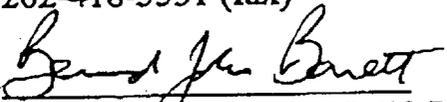
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- c) an order directing the Defendants to make full restitution to every customer whose funds were received by him as a result of acts and practices which constituted violations of the Act and Regulations, as described herein, and interest thereon from the date of such violations;
- d) a civil penalty against each Defendant in the amount of not more than the higher of \$120,000 or triple the monetary gain to the Defendant for each violation by the Defendant of the Act; and
- e) such other and further remedial ancillary relief as the Court may deem appropriate.

Date: April 16, 2003

Respectfully submitted by,


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