UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

RECEIVED
C.F.T.C.
2003 JAN 13 A 11: 09
OFFICE OF PROCEEDINGS
PROCEEDINGS CLERK

ALEXANDER SEREDIN, Complainant, v. MADISON FINANCIAL GROUP, L.L.C., and PHIL ANTHONY OWENS, Respondents.	CFTC Docket No. 01-R052 Served via Federal Express

INITIAL DECISION

Alexander Seredin seeks to recover $4,929 in damages and alleges that Phil Owens fraudulently solicited him to open a Madison account, and lulled him to continue trading, by representing that Owens was an expert trader and by guaranteeing that Seredin would triple his investment in six months. Owens filed an answer denying any violations. Madison Financial also filed an answer denying any violations, and later settled with Seredin.

The findings and conclusions below are based on the parties' documentary submissions and oral testimony and reflect my determination that Seredin's testimony was more plausible and believable than Owens' testimony.

Factual Findings

The parties

1. Alexander Seredin was 68 years old when he opened his non-discretionary account with Madison Financial Group. After working as a general construction contractor and real estate broker, he retired and opened the Peter Pan gift store in Delray

Beach, Florida. On his account-application, Seredin indicated that he had traded stocks for 10 years, but had no previous experience with commodity futures or options.

Before he opened his Madison account – in July 2000 -- Seredin had purchased and read a book by Ken Roberts about trading commodity options. The lead for the Seredin account would be generated in connection with this purchase.

Seredin's testimony shows that he had gleaned from the Ken Roberts book that "risk was involved," and that risk could potentially be limited with diversification:

> Nobody puts his money in the same money. It is the same risk, but everyone kind of diversifies. In my own business, I don't invest all my money in t-shirts. I put it in something else. If t-shirts don't sell, I sell something else.

[Pages 23-24 of hearing transcript.] Seredin had also concluded that he had not learned enough to trade without the guidance of an experienced broker. [Page 9 of hearing transcript.]

2. Madison Financial Group was a registered introducing broker from April 1998 to November 2001, with its principal place of business in Beverly Hills, California. Madison cleared its customer trades through Mann Financial Incorporated, a futures commission merchant located in New York City.

By consent order dated August 28, 2002, the CFTC imposed sanctions including a permanent trading ban on Madison's president Richard Cohen and a registration ban on Madison and Cohen. The order found that although approximately 97% of Madison's customers had suffered losses, Madison had instructed its brokers to fraudulently solicit customers by falsely stating that Madison customers had high success rates and that its customers were making money. (*In re Richard Alan Cohen, Ronald George Scott and Madison Financial Group*, CFTC Docket no. 01-09.)

3. Phil Anthony Owens solicited and handled Seredin's account. Owens, a resident of Canoga Park, California, was a registered associated person with Madison from June 1998 through April 2001. He is currently associated with Tiger Financial Group, LLC.

Owens testified that after he passed the series 3 exam, his training by Madison was on-the-job and limited to sales techniques. [See pages 33-34 of hearing transcript.] Owens' compensation was based on a percentage of the commissions charged to client accounts.

Owens gave inconsistent testimony about the performance of his customer accounts. He initially testified that his clients "probably were not doing all that well," but later testified that he had recommended a "weather-based" sugar trade, because other customers were supposedly making "a lot of money" in sugar. [Pages 34-36, and 39-40 of hearing transcript.] In this connection, when asked if he had fairly conveyed to Seredin the reality that most of his customers had failed to realize profits, he vaguely replied:

> I don't think I ever said that most people weren't making money, no. . . . I thought he knew what was involved in it. . . . I think he knew that it was risky. And I didn't blow it up, like 'here this is the way we are going to do this; or we're going to do that.' I said 'there was,' yeah, 'I think there's an opportunity in that.' And I mentioned the risk that came with it.

[Page 45 of hearing transcript.]

Summary of trading activity

4. On July 27, 2000, Seredin would deposit $5,000. On February 22, 2001, Mann Financial would return the account balance of $122. Thus, Seredin would realize a total loss of $4,978.

5. Four trades would be made in Seredin's account: first, the purchase on July 28, 2000, of three January sugar calls, which would expire on December 11, for a total loss of $1,984; second, the purchase on July 28, of one March coffee call, which would expire on February 12, 2001, for a total loss of $485; third, the purchase on August 10, of two March soybean calls, which would be sold on September 1, for a net profit of $178; and fourth, the purchase on September 6 and 15, of nine March corn puts, which would expire on February 19, 2001, for a total loss of $2,631.

6. Owens would recommend all of the trades, except for the coffee trade that Seredin would pick "on a hunch" in order to diversify. [See pages 22-23, and 39-42 of hearing transcript.] Thus, the trades recommended by Owens would realize a total net loss of $4,493, and generate about $1,460 in commissions and fees. The commission-to-premium-paid ratios for the trades recommended by Owens ranged from 20% for the sugar trade, to 35% for the soybean trade, to 55% for the corn trade.

Owen's solicitation and recommendations

7. On or about Tuesday July 26, 2000, Owens convinced Seredin to open an account with Madison.[1] According to Seredin, Owens convinced him to open the account after several conversations by emphasizing the message that he was an expert trader, that Seredin had missed out on several opportunities for profits in several markets -- including heating oil, sugar and corn -- and that he would triple Seredin's investment in six months, with little mention of the associated risks:

[1] A summary of phone records produced by Madison shows seven phone calls (over one minute duration) from July 19 to July 27, and four such calls on July 28. This summary is insufficient to prove the existence or nonexistence of phone calls before July 19, and thus cannot be used to resolve the dispute between Seredin and Owens about the number of conversations they had before Seredin opened the account.

> [On July 16] was almost an iron-clad guarantee that he's going to triple my money. The way he was speaking, he was an expert; he knows exactly what to do. Just send me the money and I'm going to triple it. No problem at all. And for this reason he was very convincing.

[Page 16 of hearing transcript; *see* pages 11-19, 33-39, and 44-45 of hearing transcript.]

Owens faxed to Seredin the account-opening documents, which Seredin then signed and faxed back to Owens. These documents included an acknowledgement that he had read the standard risk disclosure statement and a "supplemental risk disclosure statement." Owens also deposited $5,000. [*See* pages 17-19, and 39 of hearing transcript.]

8. On July 28, Owens advised Seredin to purchase sugar options. However, Seredin did not want to trade in just one market, because Owens had discussed several markets during the solicitation, which was consistent with Seredin's belief in diversification: "[Owens] wanted to put all of it in sugar, which immediately rang a bell in my head, because nobody ever invests everything in one thing." [Page 14 of hearing transcript.] After some discussion, Seredin approved the purchase of three January sugar calls, which would expire on December 11, for a total loss of $1,984, and also, on his own hunch, instructed Owens to purchase one March coffee call, which would expire on February 12, for a total loss of $485.

9. On July 30, Seredin e-mailed Owens:

> Thanks for guiding me through my initiation steps, Phil, and please bear with my inexperience.
>
> I am waiting for the confirmation for the four options, and the entry numbers. I read quite a bit about sugar, and we are located in the sugar country of south Florida. Seems the feds are taking steps to keep the price jacked up. They burnt tons of sugar last week, to cease overproduction. The sky is polluted form the fires.

[Attachment to Owens' answer.]

10. On August 10, Seredin accepted Owens' recommendation to buy two March soybean calls. On September 1, Seredin accepted Owens' recommendation to sell the soybean calls, for a small net profit of $178. On September 6 and 15, Seredin accepted Owens' recommendation to buy a total of nine March corn puts, which would expire on February 19, 2002, for a total loss of $2,631. Neither Seredin nor Owens could remember much about the conversations concerning these trades. However, Seredin testified that Owens repeated his assurances that Seredin would eventually triple his money.

After September 15, Owens stopped calling Seredin. On December 5, Seredin called Owens because he was concerned by the declining option values reported in the monthly account statements. Owens assured Seredin that the options were certain to rebound and realize the promised triple-profits. However, the options continued to decline, and Seredin became "disgusted" and decided not to initiate any more trades, and thus Seredin declined subsequent suggestions by Owens that he invest additional funds. [*See* pages 25-31, and 41-44 of hearing transcript.]

11. On January 6, 2001, Seredin sent a letter to Madison and Owens demanding that they close his account:

> When you suggested that [I] hire you six months ago to invest my $5,000 . . . . , I thought that you had my own interest in mind, first and foremost!
>
> You first insisted that I invest ALL of the money in sugar, which would have been a predetermined disaster, because even the stupidest of us investors knows that you never put ALL the eggs in one basket. And you know what happened to sugar, one of the most volatile commodities.

> I asked you to invest into calls in soya and coffee, and you did that, but shortly afterwards you insisted that I sell soya at a minute profit and invest into the puts in corn. It was obvious then as it was obvious now, that this was a simple manipulation leading to disaster.

[Attachment to addendum to complaint, all caps in original.]

Discussion

Seredin complains that Owens fraudulently solicited him to open an account and lulled him to continue trading. The applicable antifraud provision, Section 4c(b) of the Commodity Exchange Act, provides, in relevant part, that:

> No person shall offer to enter into or confirm the execution of, any transaction involving any commodity regulated under this Act which is of the character of, or is commonly known to the trade as an "option, . . . contrary to any rule or order of the Commission . . . allowing any such transaction under the terms and conditions as the commission shall prescribe."

7 U.S.C. § 4c(b). In turn, CFTC rule 33.10 provides:

> It shall be unlawful for any person directly or indirectly --
>
> (a) To cheat or defraud or attempt to cheat or defraud any other person;
>
> (b) To make or cause to be made to any other person any false report or statement thereof or cause to be entered for any person any false report thereof;
>
> (c) To deceive or attempt to deceive any other person by any means whatsoever
>
> in or in connection with an offer to enter into, the entry into, the confirmation of the execution of, or the maintenance of, any commodity option transaction.

17 C.F.R § 33.10 (2002). For Seredin to prevail on his claims, he must prove by a preponderance of the evidence that Owens (i) made the misrepresentation(s) or omission(s); (ii) of material fact; (iii) intentionally or recklessly; and (iv) on which Seredin justifiably relied and which proximately caused Seredin's damages. *Bishop v.*

First Investors Group [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,004 at 44,840-42 (CFTC 1997).

Seredin's testimony did not describe Owens' solicitation and trading advice word-for-word. However, his recollection was sufficiently specific and plausible to establish that the main message of Owens' solicitation was that he was an expert who would certainly triple Seredin's money in six months with minimal risk. Because few, if any, of Owens' customers had closed an account with any profit, let alone a triple profit, this message was patently false and misleading. The fact that some of Owens' customers may have enjoyed profits on recent, isolated trades, did not cure the patently deceptive nature of his message. *See Hammond v. Smith Barney*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,080 at 41,576 n.23 (CFTC 1994), *aff'd* 63 F.3d 1557 (11th Cir. 1995).

It is rudimentary that such misrepresentations concerning profit potential and risks are material. *In re JCC*, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,617 at 36,657 and n.12 (CFTC 1990). Similarly, a reasonable novice investor who hires a broker to select trades and provide advice would clearly find it material that the broker and his firm seldom, if ever, closed an account with a profit. *Jakobsen v. Merrill Lynch, Pierce, Fenner & Smith*, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,812 at 31,392 (CFTC 1985). Although Seredin had independently gained a general understanding that trading options involved risk, and had read and signed the risk disclosure documents, respondents' written disclosures of general risks, by themselves, were insufficient to cure Owens deceptive message that he possessed the expertise to make triple profits. *See Ferriola v. Kearse-McNeill*, [1999-2000 Transfer Binder]

Comm. Fut. L. Rep. (CCH) ¶ 28,172 at 50,153 (CFTC 2000); *Bishop*, at 44,841; and *Levine v. Refco,* [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶24,488, at 36,115-36,116 (CFTC 1989).

The preponderance of the evidence also establishes that Owens lulled Seredin to continue trading by reinforcing his initial misrepresentations with confident, but baseless, assurances that Seredin's losses were temporary and that the promised triple profits remained inevitable. Although the options had declined in value, less than six months had passed and the options were not near expiration. As a result, Owens' assurances seemed plausible to Seredin in light of Owens' promise of triple profits in six months, and thus hindered Seredin from understanding that the possibility of any profits was minimal. *See O'Hey v. Drexel Burnham Lambert, Inc.*, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,754 at 31,142 (CFTC 1985).

The intentional nature of Owens' fraud is underscored by the blatantly false nature of his misrepresentations and omissions, as well as his knowledge of Seredin's inexperience and Seredin's reliance on him to provide trading advice. The fact that Owens himself was relatively inexperienced did not excuse him from making a claim that had no reasonable basis in fact.

Seredin's decision to invest $5,000 was consistent with his testimony that he relied on Owens' message that he was an expert who was certain to triple Seredin's investment in six months with minimal accompanying risk. Seredin's education and work experience do not bar finding that he reasonably relied on Owens' misrepresentations and omissions to his detriment, especially where Seredin was not particularly sophisticated, had no previous experience in the futures and options markets

and had a limited understanding of options, and where Owens overwhelmed Seredin's knowledge of the general risks by deceiving Seredin about his expertise. *Ricci v. Commonwealth Financial Group, Inc.*, [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶26,917 (CFTC 1996).

These factors also support finding that Owens' misrepresentations were a substantial factor in Seredin's losses. *See Jakobsen*, at 31,393 n.1; and *Steen v. Monex International Ltd.*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶25,245 (CFTC 1992), *aff'd* 986 F.2d 1422 (6th Cir. 1993) (conduct is the proximate cause of a loss if the conduct was a substantial factor in bringing about the loss and if the loss was a reasonably probable consequence of the conduct.). Here, Owens knew that Seredin had no options experience and limited understanding of options trading. Therefore, it was reasonably foreseeable that Seredin would rely on Owens' misrepresentations and deceptions to open an account and continue trading, and it was reasonably foreseeable that Seredin would suffer the resulting losses, because Owens knew that options trading is inherently risky and that few if any of his customers had closed an account with any profits. The fact that Seredin had exhibited an interest in trading options before Owens' first call is irrelevant in the absence of any evidence that he would have opened an account with Madison if he had known the sorry fate of most Madison customers. *See Modlin v. Cane*, [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶28,059 at 49,551 (CFTC 2000).

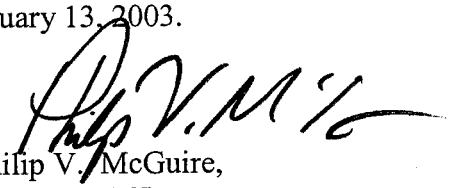
The proper measure of damages for Owens' fraudulent solicitation and lulling, is Seredin's out of pocket losses: $4,978.

Order

Seredin has established by a preponderance of the evidence that Owens fraudulently solicited Seredin to open a Madison account, and then lulled Seredin to continue trading in violation of Section of 4c(b) of the Commodity Exchange Act and CFTC rule 33.10, and that these violations proximately caused $4,978 in damages. Accordingly, Phil Anthony Owens is ORDERED to pay to Alexander Seredin reparations of $4,978, plus prejudgment interest on that amount at 1.41 % compounded annually from July 27, 2000, to the date of payment; plus $50 for the cost of the filing fee. The total amount of this judgment shall be reduced by the amount that Seredin received from Madison.

Seredin has received full payment under the terms of his settlement agreement with Madison. According the complaint against Madison Financial Group, L.L.C. is DISMISSED.

Dated January 13, 2003.



Philip V. McGuire,
Judgment Officer