UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

CARROLL WEAVER, Complainant, v. ALARON TRADING CORPORATION, DELAWARE INVESTMENTS, INC., and MARK BALDWIN DIAZ, Respondents.	* * * * * * * * * * *	CFTC Docket No. 03-R26

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INITIAL DECISION

Introduction

As explained below, it has been concluded that the statute of limitations bars Carroll Weaver's churning claim. In addition, as a deterrent sanction for Alaron Trading Corporation's bad faith verification of the joint answer, it has been concluded that respondents are not entitled to recover any costs or attorney fees.

Carroll Weaver, a resident of Cedar Falls, Iowa, alleges that Mark Diaz churned his non-discretionary account. Diaz was the owner of Delaware Investments, Incorporated, an introducing broker located in Pasadena, California.[1] Weaver amended his complaint by adding as a respondent Alaron Trading Corporation, a futures commission merchant with its principal place of business in Chicago, Illinois. During the relevant time, Alaron guaranteed the performance of Delaware Investments' obligations under the Commodity Exchange Act.[2]

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[1] Diaz and Delaware Investments have not been registered since August 2003.
[2] Alaron produced the guarantee agreement between Alaron and Delaware Investments in response to the first *sua sponte* discovery order. CFTC rule 1.10(j), 17 C.F.R. § 1.10(j) permits an introducing broker to satisfy its capital requirements through an FCM guarantee. The

Weaver alleges that Alaron failed to detect or prevent the churning in violation of its duty to supervise Delaware Investments and Diaz.[3]

In reply, Alaron filed a joint answer on behalf of itself, Delaware Investments, and Diaz.[4] By filing the joint answer, Alaron was exercising its exclusive right under the guarantee agreement to defend any complaint against Alaron and Delaware Investments arising out of any customer account.[5] Unfortunately, as this proceeding progressed, it became clear that when it had filed the answer Alaron had been less than candid and had disregarded its affirmative duty to conduct a reasonable pre-filing inquiry into the facts. Alaron's dereliction arose from the fact that, when it filed the answer on behalf of Diaz and Delaware Investments, Alaron had not yet located Diaz, let alone interviewed Diaz or reviewed Delaware Investments records. Only well after Alaron had filed the joint answer would it discover that Diaz had been incarcerated in a California state prison.[6] Only after prompting from the CFTC would Alaron reveal that fact to Weaver and the CFTC.

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guarantee agreement provides that the guarantor FCM will be jointly and severally liable for the obligations of the introducing broker under the Commodity Exchange Act. The guarantee agreement thus protects wronged customers by providing coverage for potential liabilities of the IB and insuring that the IB is not judgment-proof. 48 Fed. Reg. 35,248, at 35,249, and 35,264 (August 3, 1983); *see First American Discount Corporation v. CFTC*, 343 U.S. App. D.C. 71; 222 F.3d 1008; 2000 U.S. App. Lexis 20939; [1999-2000 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶28,227 (DC Cir. August 18, 2000) (Holding that guarantor FCM's contractual and regulatory obligations under guarantee agreement are not waivable.).

[3] The complaint, addressed to Diaz at the last address that he had provided to the NFA for service of reparations complaints, was returned by the Post Office: "Moved, Forward Expired."

[4] Alaron designated two in-house attorneys as counsel for the respondents, and filed the answer eleven days late without explanation.

[5] *See* ¶ 8 of guarantee agreement.

[6] Diaz refused to reveal any details about his conviction and asserted that it was unrelated to his activities as a registrant.

Diaz was the only individual with first-hand knowledge of respondents' dealings with Weaver.[7] Thus, without any input from Diaz, Alaron had precious little evidentiary support to make any unqualified factual contentions. Alaron also faced the prospect of ultimate liability for a default judgment against Delaware Investments and Diaz. When it filed the answer, Alaron could have candidly acknowledged its quandary, and either asked for more time to locate Diaz before filing the answer, or filed an answer in which it revealed that Diaz's whereabouts were unknown and in which it specifically identified those factual contentions that were "made on information (or lack of information) and belief." However, Alaron chose bluff over candor, and used its status as a guarantor to conceal Diaz's and Delaware Investments' default and to make a series of unqualified factual contentions that could have been substantiated only by Diaz: that Weaver had discussed and authorized each trade in the account, that Weaver had controlled the trading activity in the account, and that Weaver had never complained about the handling of his account.[8]

A principal of Alaron signed the answer. However, Diaz did not sign the answer, on his own behalf or as a bona fide officer of Delaware Investments, as required by CFTC rule.12.18(c).[9] Alaron also was silent on when Diaz's signature would be forthcoming. Thus, the CFTC Office of Proceedings asked Alaron to provide the signature of Diaz.

After this prompting, Alaron finally revealed that it had not known Diaz's whereabouts when it filed the answer, and that it subsequently learned that Diaz had been "incarcerated in a

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[7] *See* Isaacson affidavit (produced in reply to first *sua sponte* discovery order).
[8] The evidentiary basis for Alaron's denials and assertions was limited to the account statements and the account-opening documents.
[9] CFTC rule 12.18(c) requires an affirmation by each respondent that "all statements in the answer are accurate and true." *See* The Advisory Committee Notes to the 1993 amendments to analogous Rule 11 of the Federal Rules of Civil Procedure (Rule 11 imposes on attorneys and *ex parte* parties a "duty of candor" to conduct a "reasonable inquiry into the facts and law" before signing a pleading.).

California penal institution" and that Diaz could not be contacted except through his California attorney. Alaron also represented that it had obtained a promise from Diaz's California lawyer to obtain Diaz's signature "when he next visited Diaz in prison."

After a few weeks without word or signature from any respondent, I issued a default notice that directed respondents to show why Delaware Investments and Diaz should not be defaulted for failure to sign and verify the answer. Finally -- two months after it had filed the joint answer -- Alaron produced the original signed verification by Diaz on behalf of himself and Delaware Investments.[10] An additional eight months later, Diaz filed an *ex parte* statement in which he produced, for the first time in this proceeding, evidentiary support for the factual contentions in the answer, in the form of a brief description of his dealings with Weaver.[11] Diaz also asserted that Alaron's counsel had not been responding to his phone calls and e-mails, and complained that Alaron had been improperly withholding Delaware Investments' funds pending the outcome of this case.[12] In the meantime, Alaron responded to a discovery order by representing that it was actively trying to obtain Delaware Investments' phone records from the phone company. It subsequently became apparent that Alaron had actually abandoned any meaningful effort to obtain the records and not bothered to notify the CFTC. Alaron also simply ignored a request to identify where Delaware Investments' records were stored.[13]

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[10] Five weeks after filing the joint answer, Alaron filed a motion to dismiss the complaint on grounds that it was barred by the statute of limitations. I denied Alaron's motion on the grounds that it was premature, but liberally construed, and granted, the motion as a request to amend the answer by adding the statute of limitations affirmative defense.

[11] The manner in which Diaz submitted this statement indicates that he had prepared and filed it on his own initiative.

[12] Diaz, nonetheless, decided not to terminate Alaron's in-house counsel as his attorney. *See* Notice dated April 20, 2004.

[13] *See* Alaron's replies to orders dated July 7, 2003, and March 26, 2004.

A guarantor futures commission merchant is ultimately responsible for the guaranteed introducing broker's liability, and thus has an obvious interest in defending and participating in the case where violations by the IB are alleged. A guarantor FCM typically has greater resources, more litigation experience, better access to certain records, and presumably has familiarity with the guaranteed IB's operations gained from its supervision of the IB's activities. Thus, normally, when a guarantor FCM takes the lead in defending a reparations case, the FCM's and the IB's interests are better defended, the issues are more clearly defined, and the evidentiary record is more completely developed. Also, both sides benefit from avoiding a protracted collection action if the complainant prevails. However, here Alaron's lackadaisical and less than candid conduct concealed the default of Diaz and Delaware Investments, thwarted development of the record, and caused unnecessary procedural delay. Such conduct frustrates the aim of CFTC rule 12.1(c) to provide a "just, speedy and inexpensive determination of the issues presented with full protection for the rights of the parties," and thus warrants a deterrent sanction, even though respondents ultimately prevailed on the statute of limitations affirmative defense. Accordingly, it is concluded that respondents are not entitled to any reimbursement of costs or attorneys fees from Weaver.

Factual Findings and Legal Conclusions

When Weaver opened his account with Alaron and Delaware Investments, he was over 65 years old and still working. Weaver is a high school graduate who attended college for two years. Weaver had previously traded futures and options for five years in an account with R.J. O'Brien.

During the life of the Alaron account, Weaver received statements that reported the commissions charged, the trading results and the account balance. The trading activity in Weaver's account can be divided into two distinct periods. The first period was the seven and a half months

before August 14, 2000, and the second period was the three months after August 14, 2000. Before August 14, Weaver had deposited $4,000, and had lost about $2,722. Fourteen trades were winners and eighteen trades were losers. After August 14, Weaver deposited an additional $8,000, and lost an additional $8,886. Thirteen trades were winners and nine trades were losers. On September 30, 2001, the account balance was $774. On November 6, 2000, Weaver closed out the last trade in the account, leaving an account balance of $392. On December 5, 2000, Weaver instructed Alaron to return the $392 account balance. Weaver admits that by this date he knew that he had lost almost all of his $12,000 investment and had paid more than $3,155 in commissions.[14]

Weaver did not file his complaint until December 23, 2002, and did not complete filing supplements to the complaint until April 16, 2003. When asked why he had waited so long before filing the complaint, Weaver explained that he had been "working a lot of overtime." Weaver also stated that he consulted a firm called Aster Communications, which proved to be uncooperative and useless. Weaver otherwise did not consult a lawyer, any investor or consumer protection group, or any local, state or federal agency.

The statute of limitations set out in Section 14(a) of the Commodity Exchange Act requires a reparations complaint to be filed within two years after the cause of action "accrues." A cause of action accrues when a complainant knows, or should have known in the exercise of due diligence, that wrongful conduct likely has occurred resulting in monetary damages. The determination of when the cause of action accrues turns on when a customer discovers those *facts* enabling him to detect the general outlines of any violations, rather than when the customer grasps the full details of the violations or determines the available legal remedies.[15/] The record establishes that well before

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[14] *See* Weaver's reply to second *sua sponte* discovery order.

[15/] *See, e.g., Cook v. Money International, LTD.*, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. ¶22,532 (CFTC 1985), *reconsideration denied* [1986-1987 Transfer Binder] Comm. Fut. L. Rep.

December 5, 2000, when Weaver closed the account, Weaver knew that he had lost almost all of his investment, and that Weaver knew he had paid about $3,155 in commissions. Thus, Weaver knew that commissions and trading losses had combined to consume almost all of his net investment. From this negative performance, Weaver possessed sufficient knowledge to detect any inconsistencies between the results and respondents' representations about the relative risks and rewards of the recommended trading strategies, and Weaver possessed sufficient knowledge to suspect whether respondents may have recommended high-risk trading strategies designed to generate excessive commissions. Therefore, by December 5, 2000, Weaver had enough information to form reasonable suspicions about Diaz's trade recommendations.

The date that Weaver filed his complaint, December 23, 2002, is clearly past the two-year statute of limitations deadline, and Weaver's claim will be time-barred unless he can successfully invoke equitable estoppel or equitable tolling.

Equitable estoppel focuses on any misleading actions by respondents. To show that respondents should be estopped from raising the statue of limitations, Weaver must prove that he reasonably relied on an action or representation by respondents that forestalled him from filing a claim. Here, Weaver has produced no evidence that respondents made any false promises or withheld any material information that would have precluded or obscured the obvious conclusions to be drawn from the losing performance of his account. Weaver has also produced no evidence that respondents otherwise dissuaded or delayed him from initiating legal action, and thus has failed to show that respondents are estopped from asserting the statute of limitations defense.

(CCH) ¶23,078 (CFTC 1986); *Martin v. Shearson Lehman Brothers/American Express*, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶23,354 (CFTC 1986); and *Marraccini v. Conti-Commodity Services, Inc.*, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶23,793 (CFTC 1986).

Equitable tolling focuses on the reasonableness of the complainant's action or inaction. The factors considered in determining whether a late filing is excused by principles of equitable tolling include the reasonableness of a complainant's continuing ignorance of the filing requirement and his diligence in pursuing his rights. The fact that Weaver deferred seeking legal redress because he was busy at work, and the fact that he neglected to consult an attorney, any investor or consumer protection group, or any local, state or federal agency, do not support a conclusion that Weaver acted diligently, or otherwise excuse his late filing. Therefore, Weaver's claim against respondents is barred by the statute of limitations.

ORDER

Carroll Weaver's claim against Mark Baldwin Diaz, Delaware Investments, Incorporated, and Alaron Trading Corporation is barred by the statute of limitations. Accordingly, Carroll Weaver's complaint against Mark Baldwin Diaz, Delaware Investments, Incorporated, and Alaron Trading Corporation is DISMISSED.

Dated July 23, 2004.

Philip V. McGuire,
Judgment Officer