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IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF GEORGIA
ATLANTA DIVISION

Commodity Futures Trading Commission Plaintiff v. Risk Capital Trading Group, Inc., Deron Baugh, Tyrone Edwards, Stephen Margol, Rick Siegel, Richard Tillman, and Juan Valentin Defendants	CIVIL ACTION NO. 1:03-CV-02633-ODE

ORDER

This civil enforcement action brought under the Commodity Exchange Act (the "Act"), 7 U.S.C. § 1 et seq., is currently before the Court for findings of fact and conclusions of law as to Plaintiff's claims against Defendant Rick Siegel ("Siegel") following a bench trial on June 12-15, 2006.[1]

Plaintiff Commodity Futures Trading Commission ("Plaintiff" or "CFTC") is the independent federal regulatory agency charged with the administration and enforcement of the Act and the regulations promulgated thereunder, 17 C.F.R. § 1.1 et seq. Plaintiff alleges that Siegel, in his capacity as an Associated Person ("AP")[2] of Risk Capital Trading Group, Inc. ("Risk

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[1] All claims against other Defendants have been settled. Defendants Risk Capital Trading Group, Inc., Baugh, Edwards, Margol, and Valentin settled just before trial. Defendant Tillman was in jail and was unable to attend the trial. He settled soon after the trial.

[2] In the commodity industry, "associated person" is the term commonly used for a person who is essentially a broker.

Capital"), violated the anti-fraud provisions of the Act, specifically 7 U.S.C. § 6b(a)(2)(i) and (iii), 7 U.S.C. § 6c(b), and 17 C.F.R. § 33.10, in soliciting customers to buy and sell commodity futures contracts and options on commodity futures contracts. Plaintiff claims that Siegel caused his customers to invest money under a false impression of the probability of large profits. Almost all of Siegel's customers lost all or substantial portions of their investments.

Plaintiff seeks a permanent injunction, restraining Siegel from further violating the Act and also from engaging in any commodity-related sales activity.

Plaintiff seeks restitution in the following amounts for the four former customers of Siegel who testified at trial: Etienne Brown - $2,985.12; Michael Maiorino - $ 9,432; Sandra Brothers - $8,301.92; and Dean Wiegand - $2,892.41. Plaintiff also seeks restitution for all of Siegel's other customers in the amount of $990,492.55.

Plaintiff seeks disgorgement of Siegel's compensation derived from his customers in the amount of $102,417.

Finally, Plaintiff seeks civil monetary penalties in the maximum amount allowed under the Act of $120,000 for each violation of the Act.

Having heard the evidence and arguments presented by the parties and having reviewed their briefs which have been filed, the Court makes the following findings of fact and conclusions of law:

I. Findings of Fact

Beginning in January 2001, Risk Capital operated as an "introducing broker,"[3] soliciting orders for options and futures contracts. Its primary place of business was in Atlanta, Georgia. Risk Capital sold predominantly commodity options to small retail customers whose business was sought through "cold call" telemarketing. Risk Capital closed in September 2003, following an investigation and Complaint by the National Futures Association ("NFA"), an investigation by the CFTC, and the filing of the instant lawsuit.

The trial evidence showed that Risk Capital was a scam: Its principals had been involved in other similar schemes. By using aggressive sales techniques and false and misleading representations with clients who were gullible and vulnerable, Risk Capital induced the clients to pay commissions (often on a repeat basis) for speculative investments which had no real chance of success.

From 2002 to 2003 Risk Capital took in approximately $7,300,000 in commissions in $200 and $100 increments. It had over 1,000 customers who collectively lost over $11,000,000. Approximately 97% of Risk Capital's customers lost money - exceeding the 85% loss rate which has been estimated for the small investor commodity industry as a whole.

[3] An introducing broker cannot hold clients' money. This requires an association with a Futures Commission Merchant. 7 U.S.C. § 1a(23). Risk Capital had an association which fulfilled that function.

Risk Capital's customers usually purchased "call" options.[4] The owner of a call option on a futures contract has the right to purchase the underlying futures contract at a specified price ("strike price") at any time before a specified date in the future. Risk Capital sold primarily so-called "deep out of the money" call options. These options are cheap in relation to other options because the strike price is so far above the futures market price (when the option is purchased) that it is highly unlikely that the futures market price will ever reach the strike price. In the highly unlikely event that the market rises above the strike price, the option holder can make a large leveraged profit. Otherwise a modest profit can be made by selling the option on the secondary options market if and when the market price for the option has risen above the price originally paid by the client. Of course, the client's break-even point includes not only the price of the option (called the "premium") but also commissions and NFA fees.[5]

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[4] The purchaser of a call option is betting that the price of the underlying futures market will rise. If the futures market rises above the strike price of the option, the option is said to be "in the money." This means that the holder of the option has the right to purchase the subject futures contract at a price below that for which it can be purchased in the market. If the commodity futures market price is the same as the strike price of the option, the option is said to be "at the money." If the commodity futures market price is below the strike price of the option, the option is said to be "out of the money."

[5] Where the transactional costs are equal to one-quarter of the premium - a typical scenario for Risk Capital clients - the premium must rise more than 25% in a few months to yield a profit when the option is sold.

The movement of the commodity options market is unpredictable and can be volatile. Capturing a profit (or minimizing a loss) through sale of the option requires close, continuous attention to the market and an element of luck in effecting the sale before the market worsens. Sale of an option at a loss may be the best course of action. The passage of time (moving toward the expiration date) tends to degrade the option's value. When an out-of-the-money option expires, it is worthless and the customer will have lost his total investment (the price of the option plus commissions and NFA fees).

Occasionally Risk Capital's clients would purchase commodity futures contracts. A commodity futures contract is a contract to buy (or sell) a standard quantity of a particular commodity at a specified price and time in the future. The owner of a futures contract is exposed to risk far beyond the purchase price of the futures contract. If he still owns the contract at maturity, he would be forced to purchase (or sell) the specific commodity at the price set in the contract or to meet his obligation through alternative means.[6]

Risk Capital purchased names and telephone numbers of potential customers. Its representatives would make cold calls

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[6] Two types of investors purchase commodity futures contracts: hedgers and speculators. Hedgers buy futures contracts to minimize (or transfer) risk and to lock in a price certain for the underlying commodity; speculators buy futures contracts to take on risk in the hopes of realizing capital gains on their investment. Risk Capital's clients were all speculators. For obvious reasons, speculators (especially retail investors such as Risk Capital's customers) typically do not hold commodity futures contracts to maturity; speculators purchase futures contracts to make a profit, not to take actual delivery of a large quantity of commodities.

to these prospects, often using misleading sales scripts. The cold caller would fill out a prospect information sheet which would describe the call. If the prospect showed some interest, the cold caller would send Risk Capital's "Risk Disclosure Packet" and the prospect information sheet would be turned over to an account executive (such as Siegel) who would make a follow-up sales call. If an account was opened, the account executive would make the first options purchase. The account would then be turned over to a "trading advisor" who determined when the option should be sold and who would pitch another investment. Risk Capital had four trading advisors. Because 97% of Risk Capital's clients lost money, the Court infers that either the trading advisors did not adequately follow the movement of the options market or that the market rarely moved above the clients' break-even point within the option period, or both.

While Risk Capital utilized written risk disclosures signed by clients,[7] as well as recorded client interviews to document clients' appreciation of the high risk in commodities trading, it also undertook to offset the cautionary effect of these warnings. One such measure was the aggressive, overly optimistic verbal sales pitch of the account executive seeking to open the account. Another was the routine coaching of prospective customers that the risk disclosure form and recorded interview had to be done a certain way - otherwise, they would not be allowed to open an account. Clients were told that they should state a certain

[7] The disclosures were in a packet of materials sent after a "cold call" in which the customer indicated possible interest. These materials are reproduced as an Appendix to this Order.

level of income and level of assets (whether true or not) and that when asked if anyone had coached them on what to say in the recorded interview they should say "no."

Prior to joining Risk Capital, Siegel was a "market maker" on the floor of the Chicago Board of Trade for twenty years. He owned a seat on the Board of Trade. Siegel mainly traded in the bond futures market but also traded in a wide variety of commodity futures. He traded for his own account and made significant profits in all years except the last one. Prior to the initiation of this lawsuit, Siegel never was the subject of an enforcement action.

After leaving the Chicago Board of Trade, Siegel took some time off before joining Risk Capital on February 19, 2002. He was employed in the Atlanta office as an AP. Siegel's title was Account Executive. He rarely made cold calls. His primary function was to persuade customers to open accounts and to send in the initial deposit for trading. He was a persuasive salesman. Once the account was opened, Siegel would make the first options purchase for a new customer. When a customer was considering purchasing a commodity futures contract (as opposed to an option), Siegel would handle that transaction. He was Risk Capital's only AP who was allowed to handle futures contracts.

Siegel shared an office with Mark Chambers, who was his assistant. Chambers did Siegel's paperwork. This included checking to make sure that new clients had filled out the risk disclosure forms in the "right" way - that is, to meet minimum financial requirements and to verify an understanding of the risks of trading, and to verify that no one had coached them.

When the forms were not filled out in the manner which permitted the account to be opened, Chambers would call and give instructions to the client. The Court infers that Siegel overheard these telephone calls.

Risk Capital's account executives and trading advisors were commission-paid. Each options purchase involved a $200 commission. Each futures contract purchase called for a $100 commission. The commission was split among Risk Capital (60%) and also among all persons who had advised the client, including the account executive who had opened the account and the trading advisor. Siegel was entitled to consideration for bonuses, and Risk Capital paid his apartment rent. Siegel's income from Risk Capital was primarily tied to his success in getting clients to open accounts and send in their money.

Siegel spent his first three days at Risk Capital observing and listening to other APs converse with prospective and current clients. He was troubled by some of the leveraging examples he heard other APs providing to customers. He observed some of the APs using sales scripts. After that he began to open accounts. Siegel did not use sales scripts to solicit customers or to discuss trades with them. Siegel did tell potential customers that options and futures trading was risky, but he also emphasized his considerable past experience plus the fact that he personally had been successful financially in the commodities field. He encouraged his customers to trust in his judgment and rely on his expertise, downplaying the need to be concerned with the extensive warnings in the written materials they had received from Risk Capital.

While Siegel's representation that he had considerable experience trading futures contracts and options was literally true, trading on the floor of the Chicago Board of Trade was far different from working in Risk Capital's retail sales office. Most importantly, at Risk Capital he did not have access to up-to-the-minute new information as he had had on the floor of the Chicago Board of Trade. Also, neither Siegel nor the trading advisors could effect trades as quickly as at the Board of Trade. According to testimony at trial, which the Court credits, the commodity futures market very quickly factors new information into prices. Thereafter, the information has no relevance to later movement of the market. The Court is doubtful that Risk Capital's APs had any special information or insights which were helpful in trading options on futures contracts.

In explaining commodity trading to prospective clients, Siegel used the "delta" concept[8] to explain that the upward movement of futures contract prices can result in large leveraged increases in the value of an option to purchase the contract. It is correct that such increases can occur. However, because most of Risk Capital's customers purchased deep out-of-the-money options (the cheapest options and the least likely to result in a large profit), the "delta" formula had little practical

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[8] Delta expresses a theoretical relationship between a futures contract price and the value of an option to purchase the futures contract. Siegel's clients probably thought, incorrectly, that whenever the commodity price went up (e.g., heating oil in the winter), the value of their option would increase by a multiple of the commodity's increase. Siegel did understand the distinction between the commodity price and the commodity futures contract price and undoubtedly knew that his clients were confused.

application;[9] it served only to add a formulaic patina to what was really more like buying a lottery ticket.

After Siegel had made the first options purchase for a client, he would tell the client that the account had been turned over to one of four "trading advisors" who would advise the client as to when to sell the option. These sales normally caused losses, triggering complaints from clients who had been expecting profits based on Siegel's projections. The clients would often contact Siegel again for an explanation or to seek advice.

The Court also infers and finds that after Siegel had worked at Risk Capital for a period of time, he gained an actual awareness that almost all of the customers were losing their investments, including those whose accounts he had opened. Certainly, that must have been true by the fall of 2002. Siegel knew because clients called him with complaints about the trading advisors. The trading advisors' track records, which were disastrous, are set forth in Plaintiff's Exhibits 97 and 101. Nonetheless, he continued with prospective clients to emphasize his own expertise and the fact that he had had financial success with commodity trading despite its risky nature. This was deceptive because the trading advisors, who he knew would be making the decision as to when to sell the option, regularly sold at a loss.

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[9] In the case of a deep out-of-the-money-option, delta approaches zero.

At trial, Plaintiff called four previous customers of Risk Capital to testify about their dealings with Risk Capital and Siegel.

1. Etienne Brown

Etienne Brown ("Brown") had limited investment experience in stocks and mutual funds. He had no experience in commodities markets and no understanding of how those markets worked.

Brown testified that he was cold called by Siegel in May or June 2002. According to the prospect information sheet memorializing this phone call, however, Jason McGill was the cold caller. The Court finds that Brown was mistaken about the identity of his cold caller. The prospect information sheet is dated May 14, 2002 and has McGill's name on it. The Court accepts Siegel's testimony that the handwriting on the sheet was not his. Def.'s Ex. 39 (RS-00173). McGill and Brown discussed the unleaded gasoline market but Brown did not agree to invest at this time. He requested additional information.

After Brown received a packet of materials Siegel called Brown. They developed a good rapport. Brown was impressed by Siegel's experience in and knowledge of the commodities market.

Brown opened an account at Risk Capital, depositing a total of $5,450. Siegel was the account executive. Siegel said that there were opportunities in the soybean market. Brown could not recall the exact reasons Siegel gave for why the soybean market was attractive, but he said that the reasons had something to do with drought, harvest shortages, and pestilence in certain areas that would cause supply to be depressed. Brown purchased 5

soybean call options on or around May 13, 2002 for $5,450, of which the premium was $4,250, the commissions were $1,000, and the NFA fees were $200. The trade ticket for this investment is dated May 31, 2002 and bears the initials "RS/JMC," meaning that Siegel earned the primary commission on the trade and McGill earned a residual commission for making the cold call.

After this first purchase, Brown's account was transferred to Deron Baugh, a trading advisor at Risk Capital. Baugh recommended that Brown sell his soybean call options, which were showing a profit, and invest in 8 call options on Euro futures. Brown agreed to the proposed investment and the trade was placed on or around June 28, 2002. The premium for the 8 Euro options was $4,800, and Brown paid $1,600 in commissions and $320 in fees. Brown was notified that he owed an additional $470 to cover the cost of the trade, which he refused to pay. Brown did not like Baugh and the trade which Baugh recommended lost money. Ultimately, the 50% stop loss placed on the Euro investment was triggered and Brown's account value was $1,690, reflecting a decline of $3,110 or 64.8%.

Brown submitted a complaint to the NFA on July 22, 2002 concerning his dealings with Baugh. Ultimately, Risk Capital agreed to refund the amount lost in Brown's account on the condition that he continue to invest with Risk Capital. Brown agreed and signed a release form. He requested that his account be transferred back to Siegel because he was comfortable with him and they had a good rapport.

Siegel did not charge Brown commissions on further trades. He recommended that Brown purchase call options on wheat futures,

citing reasons similar to the ones he gave for investing in soybeans. Per Siegel's advice, Brown purchased three call options on wheat futures on or around September 10, 2002. Siegel placed a 50% stop-loss order on this trade. Brown testified that he was under the impression that this meant that he could lose no more than half of his investment. The Court finds that while Brown may have been under this impression during the trade with Baugh, by the time of his final trade with Siegel, he knew that the 50% stop-loss did not guarantee that losses would be limited to 50% of the investment. The details of this final investment are unclear, but apparently it fared poorly.

Brown closed his account and received a check for approximately $836. He did not file a complaint with the NFA against Siegel.

2. Michael Maiorino

Michael Maiorino testified that Siegel cold-called him and discussed trading options on commodity futures. Maiorino testified that Siegel stated that he was a successful AP; that the heating oil futures market was promising because the winter months were approaching and the demand for heating oil would increase; that small moves in the price of the heating oil futures market would yield large profits for investors; and that Maiorino could make 4 or 5 times his investment if he invested soon.

Siegel testified that he did not place the cold call to Maiorino and that he had not been the Account Executive. Mikeal Masterson cold called Maiorino and another Account Executive,

Jack Sini ("Sini"), was the account executive. Siegel stated that Maiorino and Sini were arguing over whether Maiorino could buy an option with a different strike price than the one Sini was attempting to sell him. Sini asked Siegel to discuss this matter with Maiorino. Siegel testified that he had a two-minute conversation with Maiorino, after which Sini placed the order that Maiorino desired.

The Court finds Siegel's version of the story more credible because it is supported by objective evidence, and because it was clear that Maiorino's memory of the events in question was lacking. First, the prospect information sheet confirms that Masterson did call Maiorino on December 3, 2002. Additionally, Maiorino's trade tickets are not in Siegel's handwriting. Siegel's initials do not appear in the box in which the initials of Maiorino's primary APs appear. Siegel's initials do appear outside of the box because of Risk Capital's policy that any AP who talked to a client (even if only for a short period of time) would receive a portion of the commissions generated on the account. The objective evidence shows that after the initial trade was placed the account was transferred to David Mittler, a trading advisor.

Thus, the Court finds that with respect to Maiorino, Siegel had only a brief conversation that did not involve any misrepresentations.

3. <u>Dean Wiegand</u>

Prior to investing with Risk Capital, Dean Wiegand, a farmer in Canada, had no investment experience. It was clear at trial that he had no understanding of the commodities market.

In March 2002, Wiegand was called by Desmond Muthemba, an AP at Risk Capital. Muthemba told Wiegand that peak driving season was approaching and that crude oil was a good investment. Muthemba stated that other investors had doubled and tripled their money in that market and the faster Wiegand invested the better. Wiegand agreed to invest money with Muthemba. Muthemba faxed the account opening documents to Wiegand. Wiegand did not read the documents; he just signed them, faxed them back to Muthemba, and wired approximately $3,000 on March 22, 2002. That same day, Muthemba placed an order to purchase three option contracts on unleaded gasoline futures.

Some time later, Wiegand received a phone call from Siegel, who told Wiegand that he had lost $2,000 and that only $1,000 remained. Siegel stated he was optimistic about making the money back with the remaining $1,000. He told Wiegand that he would call back when an investment opportunity arose.

Approximately one week later, Siegel called Wiegand and told him that the gasoline futures market was an attractive investment. Wiegand testified that Siegel told him that there was an announcement coming out and that if the announcement was favorable, Wiegand could make money. Wiegand said that he "had to go with [Siegel's] knowledge instead of his." The trade was placed on April 17, 2002. Shortly thereafter, Siegel called Wiegand and informed him that the investment had been sold at a loss.

Wiegand closed his account and received a check from Risk Capital in the amount of $107.59.

4. Sandra Brothers

Sandra Brothers' memory of the events in question was lacking, and the Court questions the credibility of some of her testimony. However, Plaintiff presented notes of conversations with Siegel that Brothers had made contemporaneously with the conversations, as well as other objective evidence that corroborated some parts of her testimony.

From 2002 to 2003, Brothers was a sales representative at a department store in Georgia. According to her testimony, she had between $100,000 to $150,000 invested in mutual funds for retirement. She read money and investment magazines on occasion. Her only experience with investing was with mutual funds.

On September 24, 2002, she received an unsolicited phone call from Muthemba at Risk Capital. Brothers' testimony concerning the call contradicts the prospect information sheet that Muthemba completed during their conversation. According to the prospect information sheet (which the Court finds to be more credible), Brothers indicated some interest in investing in commodity futures and options. Muthemba wrote:

> Went through a 9¢ [heating oil] move, loves it, has [illegible] interested & looking for this opportunity, wants to feel [illegible] informed on the in/outs. Close, Close, Close. - (Very open [illegible] Gone through calls & puts.

Siegel called Brothers that evening. She jotted down notes of this and subsequent conversations between them, which were admitted at trial. Siegel told Brothers about his credentials

and that he had been among the best at the Chicago Board of Trade. He did acknowledge that there was risk, but he also implied that he could navigate around the risk using his knowledge of the commodity futures and options markets. Brothers' notes state "Rick said to 'Risk a little to make a lot.'" Pl.'s Tr. Ex. 629.

Brothers received the packet from Risk Capital which was sent via Federal Express. She attempted to read the documents but did not understand them. Siegel told her not to worry because he had the knowledge. He discussed heating oil futures, which he said was a promising market because of the possibility of a war with Iraq which would cause the supply of heating oil to decrease. He further indicated that as winter approached, demand for heating oil would increase. He stated that in previous wars, investors had been successful in investing in heating oil futures and options. Brothers' notes state, "I'll Double your (or better) money in a [month]. Or: at least a 20% profit." Pl.'s Tr. Ex. 629.

On one occasion, when Siegel and Brothers met in person at a restaurant, Siegel wrote down an example of how an out-of-the-money call option would work. This example was admitted at trial. To summarize, it shows how Brothers would make money if she purchased an out-of-the-money call option for heating oil and the price of the heating oil futures market subsequently increased. Siegel assumed a delta of 40%, and calculated that for every upward penny move in the price of the heating oil

futures market, Brothers would make $168 per option.[10] Siegel did not present a written example of what would happen if the price of the heating oil futures market decreased or if delta was a smaller number, although he did mention that she could lose part or all of her investment. At the same meeting, Siegel also told Brothers not to invest all of her retirement funds in commodity options trading.

Brothers still was hesitant to invest. Siegel called her numerous additional times urging her to go ahead. Brothers signed the account opening documents on October 10, 2002. Although Siegel testified that he never assisted clients with filling out these forms, the Court finds that Siegel instructed Brothers on how to answer certain questions in order for her to meet the minimum financial requirements to open an account. The Court also finds credible Brothers' testimony that Siegel told her that these documents and disclosures were mere formalities. Siegel told Brothers to represent her annual gross income as $38,000 (this was more than her actual salary) and her net worth as $100,000 (it is unclear whether this exceeded her net worth). The notes that Brothers took during her conversations with Siegel state:

> Remember these #s per Rick
> 38/100
> they don't
> follow up
> they don't [check]
> those [numbers]

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[10] The assumption of a delta of .40 in the case of a deep out-of-the-money option is inappropriate. For such an option, delta would be close to zero. The Court finds that use of the .40 example was misleading and deceptive.

just do it!

Pl.'s Ex. 629. Brothers' account opening documents indicate that she did in fact use these numbers as Siegel instructed. Also, Brothers used those amounts when questioned about gross income and net worth in the compliance interview conducted by Risk Capital's trading desk just before placing her first order to purchase call options.

In filling out the New Account Checklist form, Brothers originally answered "yes" to question 12, which asks "Have you been instructed or prompted by any person to knowingly provide false, inaccurate or untruthful information on your account opening documents?" Siegel's assistant, Chambers, personally picked up the completed account opening documents from Brothers at her place of employment. Chambers reviewed the documents before leaving and noticed that Brothers had answered "yes" to question 12. Chambers told Brothers to change her answer to this question or the account would not be approved. Brothers checked "no," circled the new answer, and initialed it. Def.'s Tr. Ex. 17 (RS-00029).

The account was approved by a Risk Capital branch manager on October 11, 2002. On October 14, 2002, Brothers, acting on Siegel's advice, purchased five call options for heating oil futures for $4,900. $1,000 went to Risk Capital in the form of commissions ($200 per option) and $225 went to the NFA in the form of fees ($45 per option). Thus, the value of Brothers' options was $3,675. Per Brothers' instructions, Siegel put a 50% stop-loss on the trade.

Approximately one week later, the market turned downward. Siegel tried unsuccessfully to reach Brothers to get her approval to sell the heating oil call options. The market fell until the stop loss was activated. The call options were liquidated for $1,679.80.

Siegel turned Brothers' account over to Chris Harris, a trading advisor at Risk Capital. Siegel expressed to Brothers that Chris Harris was an expert, and that he could make her money back. Brothers' notes state the following:

> Do as he
> says
> I trust him
> In re: Chris Harris
> We'll make back the
> monies and use
> that for our
> futures.

Pl.'s Tr. Ex. 629. Brothers put more money into the account. On October 22, 2002, Harris purchased seventeen put options [11] on wheat futures for $16,490.68 on Brothers's behalf. Of that, $3,400 went to commissions and $765 went to NFA fees. The premium for the put options, therefore, was approximately $12,325. Brothers lost money on this investment as well.

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[11] A put option is the opposite of a call option. Whereas a call option is the right to purchase the underlying commodity futures contract at the strike price before the expiration date, a put option is the right to *sell* the underlying commodity futures contract at the strike price before the expiration date. Whereas the purchaser of a call option is betting that the price of the underlying commodity futures contract will increase, the purchaser of a put option is betting that the price of underlying commodity futures contract will decrease.

Brothers did one final investment with Siegel, purchasing two wheat futures contracts on November 7, 2002. The details of this investment were not explained at trial.

Brothers told Siegel that her home was "in distress" and that she wanted to close her account. He told her that she should not be trading if her home was in distress. A couple of days later, Brothers received a check in the amount of $11,412. Her total investment with Risk Capital was $19,714 (including commissions and fees), of which she lost $8,301.92 (42.1%).

II. Conclusions of Law

A. Liability

"[T]he [Commodity Exchange Act] is a remedial statute that serves the crucial purpose of protecting the innocent individual investor - who may know little about the intricacies and complexities of the commodities market - from being misled or deceived." CFTC v. R.J. Fitzgerald & Co., Inc., 310 F.3d 1321, 1329 (11th Cir. 2002).

Regarding the sale of commodity futures, the Act provides that:

> It shall be unlawful . . . for any member of a registered entity, or for any correspondent, agent, or employee of any member, in or in connection with any order to make, or the making of, any contract of sale of any commodity in interstate commerce, made, or to be made, on or subject to the rules of any registered entity, for or on behalf of any other person . . . -
>
> (i) to cheat or defraud or attempt to cheat or defraud such other person;
>
> * * *
>
> (iii) willfully to deceive or attempt to deceive such other person by any means

> whatsoever in regard to any such order or 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.

7 U.S.C. § 6b(a)(i), (iii).

> Regarding the sale of commodity options, it is unlawful:
>
> for any person directly or indirectly
>
> > (a) To cheat or defraud or attempt to cheat or defraud any other person; . . . [and]
> >
> > (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.

The NFA "is a congressionally authorized futures industry self regulatory organization . . . [the purpose of which is] to assure high standards of business conduct by its Members and to protect the public interest." R.J. Fitzgerald, 310 F.3d at 1326 n.3. APs such as Siegel are required to be members of the NFA and are governed by its rules.

Of particular relevance to the instant case is NFA Rule 29-2, which prohibits certain deceptive sales practices. Rule 29-2 generally prohibits "any communication with the public which: (1) operates as a fraud or deceit; (2) employs or is part of a high-pressure approach; or (3) makes any statement that futures trading is appropriate for all persons."

The NFA also publishes interpretive notices further explaining the reach of Rule 29-2 with respect to specific conduct and sales pitches. Interpretive notices have the force and effect of NFA Rules. The thrust of these rules and

interpretive notices is that an AP cannot make customers think that they are more likely to make money than lose money. One such interpretive notice issued May 23, 1996 discusses, among other things, a specific example of a deceptive sales pitch called "seasonal trades." A misleading claim about a seasonal trade occurs when, for example, an AP convinces a customer to purchase call options on heating oil futures, stating that winter is nearing and the demand for heating oil will increase as people try to heat their homes and businesses. Another example involves soliciting a customer to purchase options on crude oil futures, stating that the summer "driving season" is nearing and the demand for gasoline will drive gas prices upward.

In November of 2002, the CFTC issued a commission advisory regarding misleading claims about investment opportunities resulting from the possibility of war with Iraq.

The foregoing sales pitches are misleading because such known, available information about supply and demand is already factored into the futures price of the commodity.

In order to establish fraud under the Act, Plaintiff must prove "(1) the making of a misrepresentation, misleading statement, or a deceptive omission; (2) scienter; and (3) materiality." R.J. Fitzgerald, 310 F.3d at 1328. Although not entirely clear from the Act or case law, the parties agree that Plaintiff must prove the foregoing elements by a preponderance of the evidence. Cf. Herman & MacLean v. Huddlestone, 459 U.S. 375, 390 (1983) (holding preponderance of the evidence to be the appropriate standard in cases brought under § 10(b) of the

Security Exchange Act of 1934 (15 U.S.C. § 78j(b)) and Rule 10b-5, 17 C.F.R. § 240.10b-5).

"Whether a misrepresentation has been made depends on the 'overall message' and the 'common understanding of the information conveyed.'" R.J. Fitzgerald, 310 F.3d at 1328. Scienter exists when "Defendant's conduct involves highly unreasonable omissions or misrepresentations . . . that present a danger of misleading which is either known to the Defendant or so obvious that Defendant must have been aware of it." Id. (internal quotations omitted). Finally, the materiality requirement is met when "it is substantially likely that a reasonable investor would consider the matter important in making an investment decision." Id. (internal quotations omitted).

The "overall message" in the instant case comprises (1) the risk disclosures in the account opening documents and compliance interviews; and (2) the representations made by Siegel to customers.

The risk disclosures in the Risk Capital Packet were replete with disclosures and disclaimers concerning the high degree of risk inherent in investing in commodity futures and options. The New Account Checklist contained in the Risk Capital Packet required prospective customers to affirmatively answer 12 questions about whether they read the risk disclosure documents and understood the risk of loss, and whether anyone had coached them on how to answer these questions. The oral disclosures and questions provided in the Compliance Interview covered similar topics.

Notwithstanding the abundance of these risk disclosures, Siegel is not insulated from liability. "[T]he fact that [there is] a general risk disclosure statement does not automatically preclude liability under the [Commodity Exchange Act] where the overall message is clearly and objectively misleading or deceptive." R.J. Fitzgerald, 310 F.3d at 1330; see also CFTC v. Sidoti, 178 F.3d 1132, 1136 (11th Cir. 1999) ("We seriously doubt whether boilerplate risk disclosure language could ever render an earlier material misrepresentation immaterial."); Clayton Brokerage Co. of St. Louis, Inc. v. CFTC, 794 F.2d 573, 580 (11th Cir. 1986) ("[P]resentation of the risk disclosure statement does not relieve a broker of any obligation under the [Commodity Exchange Act] to disclose all material information about risk to customers.").

Plaintiff did not prove by a preponderance of the evidence that Siegel made misrepresentations or material omissions of fact with respect to Brown, Maiorino, and Wiegand. With respect to Maiorino, Siegel had only a brief conversation concerning whether Maiorino could purchase a call option with a different strike price. This in no way amounts to a misrepresentation. With respect to Brown and Wiegand, their testimony was insufficient to establish that Siegel made misrepresentations. Brown vaguely testified that the reasons Siegel gave for investing in soybeans and wheat had something to do with drought, harvest shortages, and pestilence in various areas of the world that would depress the supply of those commodities. As for Wiegand, he testified that Siegel merely expressed hope that he could make back

Wiegand's money lost on a previous trade with another account executive. This does not constitute a violation of the Act.

Plaintiff also did not prove that, as to Brown and Wiegand, Siegel should have disclosed his or Risk Capital's track record. In R.J. Fitzgerald, 310 F.3d at 1332-33, the Court held that where the defendant knew that 95% of its customers lost money and painted an otherwise "extremely rosy picture for profit potential," it was misleading not to disclose its track record. Brown's first trade and Wiegand's only trade with Siegel took place in May and April 2002, respectively, which was before this Court found that Siegel had knowledge of his or Risk Capital's track record. While Siegel may have had knowledge of their track records by the second trade with Brown in September 2002, Plaintiff did not establish that Siegel painted such a rosy picture to Brown as to require disclosing them. See id.

In sum, the evidence with respect to Brown, Maiorino, and Wiegand is insufficient to establish that Siegel violated the Act.

In contrast, the overall message presented by Siegel to Brothers amounted to misrepresentation and material omission of facts. Although Risk Capital provided general risk disclosures and Siegel intermittently made statements that Brothers could conceivably lose part or all of her investment, Siegel's other statements (for example "I'll double your money in a month") undercut these warnings and made Brothers believe that she was more likely to make money than to lose money. This is the hallmark of misleading sales practices under the Act.

Additionally, Siegel coached Brothers on how to answer the questions in the Risk Capital Packet and the Compliance Interview, stating that they were just "formalities." Brothers' notes from their conversations reflect this, as do her answers to the questions in the account opening documents, and her affirmative answer to question 12 of the New Account Checklist asking whether she had been instructed or prompted by any person to provide untruthful information on these documents. Such coaching amounts to a misrepresentation under the Act. See CFTC v. Trinity Fin. Group, Inc., 1997 WL 820970, at *9-10 (S.D. Fla. Sept. 29, 1997), aff'd in relevant part sub nom. CFTC v. Sidoti, 178 F.3d 1132 (11th Cir. 1999) (finding similar statements to be misleading and fraudulent); Clayton Brokerage Co., 794 F.2d at 580 ("Oral representations may effectively nullify the warnings in the statement by discounting its general significance and its relevance to the customers' particular situation.").

The Court also concludes that Siegel's nondisclosure of his and Risk Capital's track record - which the Court found he knew by the fall of 2002 - was a material omission of fact. Plaintiff established that approximately 97% of Risk Capital's customers lost money. The Court found that Siegel's customers did lose money the vast majority of the time. As was the case in R.J. Fitzgerald, 310 F.3d at 1332, disclosing these track records "would have gone a long way in balancing out" "the extremely rosy picture for profit potential" painted by Siegel.

Siegel attempts to distinguish R.J. Fitzgerald on the ground that in this case there was no evidence that Siegel or Risk Capital calculated their track records. This argument is not

persuasive. While Siegel may not have known his or Risk Capital's exact track records while at Risk Capital, the percentages as shown by Plaintiff's Exhibit 97 are so overwhelming that he must have had some awareness of them, at least by the fall of 2002. This Court found that Siegel had general knowledge of the fact that the vast majority of his and Risk Capital's customers lost money. In light of Siegel's positive statements concerning his experience, his ability to handle the risk, that he could double her money, and his downplaying the importance of the account opening documents and its risk provisions, it was a material omission not to disclose the fact that the vast majority of his customers and Risk Capital's customers had lost their investments.

The Court now turns to the element of scienter, which is "established if Defendant intended to defraud, manipulate, or deceive, or if Defendant's conduct represents an extreme departure from the standards of ordinary care. . . . Scienter is met when Defendant's conduct involves highly unreasonable omissions or misrepresentations . . . that present a danger of misleading which is either known to the Defendant or so obvious that Defendant must have been aware of it." R.J. Fitzgerald, 310 F.3d at 1328 (internal quotations omitted).

The Court finds no difficulty in concluding that Siegel acted with scienter. Siegel was highly knowledgeable about commodity investments. His previous experience on the floor of the Chicago Board of Trade make it undeniable that he had a deep understanding of the commodities markets and the great risk of failure associated with the low-grade investments that he was

selling at Risk Capital. He therefore was acutely aware of the fact that deep out-of-the-money options have very little chance of becoming profitable, especially accounting for the transaction costs (commissions and fees) associated with these investments. Risk Capital's 97% loss rate bears this out.

Having worked at Risk Capital for 8 to 9 months prior to soliciting Brothers, Siegel had to have been aware of both his and Risk Capital's general track record. Although Siegel strenuously argues that neither he nor Risk Capital calculated their loss rate, the loss rate is so high in this case that Siegel had to have appreciated the fact that virtually all of Risk Capital's customers lost money. Despite this knowledge, he referred to the compliance questionnaires as "formalities;" downplayed the risk associated with the investments; passed Brothers off to trading advisors (sometimes calling them "experts") who he knew were not successful; and otherwise took advantage of Brothers' lack of understanding. The Court concludes that Siegel's actions were an extreme departure from the standards of ordinary care and that Siegel thus acted with scienter.

Finally, the materiality of these misrepresentations and omissions of fact is not in serious dispute and an in-depth discussion of this element is unnecessary. Even considering the misrepresentations in light of the abundance of pro forma risk disclosures provided in Risk Capital's packet and compliance interviews, materiality is not in issue. See Sidoti, 178 F.3d at 1136 (rejecting the argument that such pro forma risk disclosures rendered previous misrepresentations immaterial).

However, one item warranting brief discussion is the materiality of Risk Capital's track record. Omission of Risk Capital's general track record is material in this case because of Risk Capital's practice of transferring clients to trading advisors after account executives, such as Siegel, opened an account and made the first trade. It therefore was a material omission on Siegel's part not to disclose Risk Capital's general track record when he knew that the trading advisors to whom customers would be transferred lost money the vast majority of the time. The Court does not hesitate to conclude that "it is substantially likely that a reasonable investor would consider [this] matter important in making an investment decision." R.J. Fitzgerald, 310 F.3d at 1328 (internal quotations omitted).

The Court therefore concludes that Plaintiff established by a preponderance of the evidence that Siegel's dealings with Brothers directly violated the anti-fraud provisions of the Act, specifically, 17 C.F.R. § 33.10 dealing with the sale of commodity options.

On a final note, the Court adds that Brothers most likely was not Siegel's only victim. Risk Capital's business model was designed to convince unsophisticated and financially insecure people to invest money (thereby generating commission income for the firm) through engaging in deceptive and high-pressure sales practices, many of which specifically were prohibited by the NFA. Siegel knew this and actively furthered the scam. He played a crucial, enabling role by persuading prospective clients to open accounts and, at least in one case, encouraging them to misrepresent their income and net worth so that the account could

be opened; placing the first trade; transferring the clients to trading advisors, referring to them as commodity investments experts thereby giving the impression that the client's money was in good hands; and convincing disgruntled customers who had lost money on previous trades to stay on board for additional trades.

In short, Siegel aided and abetted Risk Capital's scheme to defraud customers. Although Plaintiff did not make such an allegation, this Court finds it too obvious to ignore. The Act imposes aider and abettor liability on "any person who commits, or who willfully aids, abets, counsels, commands, induces, or procures the commission of, a violation of the provisions of this chapter." 7 U.S.C. § 13c(a). Imposition of such liability is appropriate when a defendant "knowingly associates himself with an unlawful venture, participates in it to bring it about, and seeks by his actions to make it succeed." CFTC v. Trinity Fin. Group, Inc., 1997 WL 820970 (S.D. Fla. Sept. 29, 1997) (internal quotations omitted), rev'd on other grounds sub nom. CFTC v. Sidoti, 178 F.3d 1132 (11th Cir. 1999). The findings of fact clearly establish that all of the elements for aider and abettor liability are met in this case. Accordingly, the Court considered Siegel's role as an aider and abettor in granting injunctive relief and assessing civil monetary penalties against Siegel.

B. Relief

1. Injunctive Relief

In order to be entitled to injunctive relief, Plaintiff had to show a reasonable likelihood that Siegel would violate the Act

in the future. See SEC v. Ginsburg, 362 F.3d 1292, 1304 (11th Cir. 2004); Sidoti, 178 F.3d at 1137. The factors to be considered are "the egregiousness of the defendant's actions, the isolated or recurrent nature of the infraction, the degree of scienter involved, the sincerity of the defendant's assurances against future violations, the defendant's recognition of the wrongful nature of his conduct, and the likelihood that the defendant's occupation will present opportunities for future violations." Ginsburg, 362 F.3d at 1304 (quoting SEC v. Carriba Air, Inc., 681 F.2d 1318, 1322 (11th Cir. 1982)).

These factors support the imposition of limited injunctive relief. Plaintiff did not show that Defendant's actions in this case were extremely egregious or that his misrepresentations were recurrent or widespread. That notwithstanding, the Court believes that Brothers was not the only customer of Siegel who unwittingly invested with him in reliance on his self-proclaimed expertise and knowledge of the commodities markets and ability to make large profits. Siegel provided the Court with no assurances against future violations; he totally denied wrongdoing. Furthermore, he testified that he currently writes (or "grants") options, so the Court believes that his current occupation presents the opportunity for future violations. The Court thus finds that Plaintiff proved by a preponderance of the evidence that there is a probability of future violations.

Accordingly, the Court permanently enjoins Siegel from committing any further violations of the Act, either directly or indirectly. This includes, but is not limited to, making misrepresentations of material facts to clients in connection

with the purchase or sale of commodity futures contracts and options. The Court declines to permanently or temporarily enjoin Siegel from trading on the behalf of others in the commodity futures and options market. Plaintiff simply did not meet its burden to justify an injunction of such breadth.

2. Restitution and Disgorgement of Profits

As the Act expressly authorizes the Court to provide the equitable remedy of an injunction in 7 U.S.C. § 13a-1, the Court has the authority to award "ancillary equitable relief," including restitution. See Porter v. Warner Holding Co., 328 U.S. 395, 398 (1946) (upholding restitution awarded incident to an injunction and stating that "[u]nless a statute in so many words, or by a necessary and inescapable inference, restricts the court's jurisdiction in equity, the full scope of that jurisdiction is to be recognized and applied"); Mitchell v. Robert DeMario Jewelry, 361 U.S. 288, 291-92 (1960) ("When Congress entrusts to an equity court the enforcement of prohibitions contained in a regulatory enactment, it must be taken to have acted cognizant of the historic power of equity to provide complete relief in light of the statutory purposes."); Federal Trade Comm'n v. United States Oil & Gas Corp., 748 F.2d 1431 (11th Cir. 1984) (same); AT&T Broadband v. Tech. Communs., Inc., 381 F.3d 1309 (11th Cir. 2004) (same).

Plaintiff seeks restitution to compensate all of Siegel's customers who lost money. However, Plaintiff's evidence was insufficient to warrant such an extensive remedy. Plaintiff's evidence only specifically showed that one customer witness –

Sandra Brothers - was defrauded by Siegel. Thus, the Court will award restitution only to Brothers in the amount of $8,301.92, plus pre-judgment interest from November 12, 2002 (the date Brothers' account with Risk Capital was closed) to the date of judgment at the prevailing rate established by the Internal Revenue Service pursuant to 26 U.S.C. § 6621.

Disgorgement is not warranted in this case as an award of both restitution and disgorgement of profits would be improperly punitive in nature. See Sidoti, 178 F.3d at 1138.

3. Civil Monetary Penalties

7 U.S.C. § 9 and 17 C.F.R. § 143.8 authorize the Court to impose civil monetary penalties of up to the greater of $120,000 per violation or triple the monetary gain experienced by the defrauding party. Siegel committed numerous violations of the Act in his dealings with Brothers and also by aiding and abetting Risk Capital's general scheme to defraud customers.

In selecting the monetary penalty in this case, the Court is guided by the evidence which showed that Siegel committed numerous violations, though on occasion he appeared to try to do right by his clients. The Court assesses civil monetary penalties against Siegel in the amount of $150,000.

III. Conclusion

In summary, the Clerk is directed to enter judgment in favor of Plaintiff and against Defendant as follows:

- Restitution for the benefit of Sandra Brothers in the amount of $8,301.92, plus pre-judgment interest from

November 12, 2002 to the date of judgment at the prevailing rate established by the Internal Revenue Service pursuant to 26 U.S.C. § 6621.

- Civil monetary penalties in the amount of $150,000.

The judgment shall further reflect that Defendant is permanently enjoined from committing any further violations of the Commodity Exchange Act, either directly or indirectly, including, but not limited to, making misrepresentations of material facts to clients in connection with the purchase or sale of commodity futures contracts and options.

Plaintiff is awarded costs.

SO ORDERED this 14 day of August, 2006.

ORINDA D. EVANS
UNITED STATES DISTRICT JUDGE