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In The United States District Court
For The District Of New Jersey
Camden Vicinage

Commodity Futures Trading Commission, Plaintiff, vs. Equity Financial Group LLC, Tech Traders, Inc., Tech Traders, Ltd., Magnum Investments, Ltd., Magnum Capital Investments, Ltd., Vincent J. Firth, Robert W. Shimer, Coyt E. Murray, and J. Vernon Abernethy, Defendants.	Hon. Robert B. Kugler District Court Judge Hon. Ann Marie Donio Magistrate **Civil Action No: 04-1512 (RBK)** **MOTION DATE: August 19, 2005**

CFTC'S RESPONSE TO ROBERT. W. SHIMER AND VINCENT J. FIRTH'S MOTION FOR SUMMARY JUDGEMENT

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CFTC's RESPONSE TO ROBERT W. SHIMER AND VINCENT J. FIRTH'S MOTION FOR SUMMARY JUDGEMENT

Plaintiff Commodity Futures Trading Commission ("the Commission") responds to the motion for summary judgment filed by Robert W. Shimer ("Shimer") and Vincent J. Firth ("Firth"), which is merely a recast version of their motions to dismiss the First Amended Complaint filed this past June, repeating the same arguments. Their summary judgment motion fails to surmount their initial responsibility of informing the district court of a cognizable legal basis for their motion, and also fails to identify any portions of the record that demonstrate the absence of a genuine issue of material fact. Notably, Shimer and Firth do not support their motion with any evidence.[1]

In short, most of Shimer's brief is a rehash of his assertion that Shasta Capital Associates, LLC ("Shasta"), is not a commodity pool. Rather than waste the Court's time with a repetition of the reasons why this assertion is specious, the Commission refers the Court to its Response to Equity Defendants' Motion to Dismiss ("CFTC Response") [Docket 214]. The Commission will limit its response here to a few salient points.

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[1] The Defendants' Statement of Material Facts (Firth's is identical to Shimer's) is merely a restatement of their legal arguments. The only fact asserted is that Shasta did not have a trading account in its own name. This is also the only fact set forth in Firth's affidavit to support the Motion for Summary Judgment. The Commission does not dispute this fact. But, as stated above and in its Response to the Equity Defendants' Motion to Dismiss, this fact does not defeat the Commission's claims. Because Shimer's argument is merely a legal one, and the only fact set forth to support it is undisputed, the Commission does not submit any opposing affidavits. Moreover, every factual allegation relied on in this brief has been admitted by Equity Financial Group LLC, Shimer and Firth (collectively "the Equity Defendants").

I. Summary Judgment Standard

The standard for considering a motion for summary judgment is clear. Summary judgment is proper "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to judgment as a matter of law." Fed.R.Civ.P. 56(c); *SEC v. Hughes Capital Corp.*, 124 F.3d 449, 452 (3rd Cir. 1997). An issue is "genuine" "if the evidence is such that a reasonable jury could return a verdict for the nonmoving party." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248, 106 S.Ct. 2505 (1986). A fact is "material" if it may affect the outcome of the suit under the applicable law. *Id.* In deciding whether there is a disputed issue of material fact, a court must view the facts and all reasonable inferences in a light most favorable to the nonmoving party. *Id.* at 250.

The moving party always "bears the initial responsibility of informing the district court of the basis for its motion, and identifying those portions of the 'pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any,' which it believes demonstrate the absence of a genuine issue of material fact." *Celotex Corp. v. Catrett*, 477 U.S. 317, 323, 106 S.Ct. 2548 (1986). However, where the nonmoving party bears the burden of persuasion at trial, "the burden on the moving party may be discharged by 'showing'-that is, pointing out to the district court-that there is an absence of evidence to support the nonmoving party's case." *Id.* at 325. The non-moving party "may not rest upon the mere allegations or denials of" its pleadings and must present more than just "bare assertions, conclusory allegations or suspicions" to establish the existence of a genuine issue of material of fact. Fed.R.Civ.P. 56(e); *Jalil v. Avdel Corp.*, 873 F.2d 701, 707 (3d Cir. 1989) (citation omitted). "A party's failure to make a showing that is 'sufficient to establish the existence of an element essential to that party's case, and on which that party will bear

the burden of proof at trial' mandates the entry of summary judgment." *Watson v. Eastman Kodak Co.*, 235 F.3d 851, 857 (3d Cir. 2000) (quoting *Celotex*, 477 U.S. at 322).

As with their Motion to Dismiss, Shimer and Firth have failed to set forth a legal theory that supports dismissal of this action and have also failed to demonstrate lack of a genuine issue of material fact to warrant summary judgment in their favor.

II. Shasta is a Commodity Pool

Shimer and Firth argue that a) there are no cases in which a feeder fund such as Shasta has been found by a court to be a commodity pool; and b) the narrowing of the definition of "pool" in the 1981 amendments to Part 4 of the Commission's Regulations, 17 C.F.R. § 4.10 (2004), somehow takes Shasta out of the definition. There is a case right on point, *CFTC v. Heritage Capital Advisory Services, Ltd.*, [1980-1982 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,627, 26,377 (N.D. Ill. 1982), cited by both the Commission and Shimer in the first round of briefing on this issue, in which a fund such as Shasta was found to be a commodity pool. And, though Shimer makes much of the fact that the definition of a "pool" in 17 C.F.R. §4.10(d)(1) was narrowed in 1981, he does not explain how that narrowing takes Shasta out of the definition of a commodity pool. In fact, a complete review of §4.10 shows that the term "pool" definitely includes feeder funds, or fund of funds, such as Shasta.

A. Feeder Funds Such as Shasta Have Been Found to be Commodity Pools.

Shimer claims that "*in all instances*, any entity held by the federal courts to be a 'commodity pool' *owned in its name a commodities trading account* that was either traded 1) illegally by the pool entity itself (and not a separate operator as required by CFTC regulations) or, 2) by a separate entity held to be the 'operator' of the 'pool' or, 3) traded

[sic] by a separate entity or person (see, for example, *Heritage*) under purported authority given to that separate entity or person by either the 'pool' or the pool's operator'." *See* Shimer Summary Judgment Brief at 2-3 (emphasis in the original). But though he cites to *Heritage* as his only support for this statement, *Heritage* does not support Shimer's position.

The Commission refers the Court to its discussion of Heritage set out in the CFTC Response at 15-18. As noted there, the facts are strikingly similar to this case – a massive commodity pool fraud involving feeder pools that spawned much litigation. At the heart of the fraud was Robert Serhant, who between 1980 and 1982 offered investors a "Hedge-Spread Program" in which for every $100,000 invested, Serhant said he would invest $97,000 in Treasury Bills and just $3,000 in commodity futures, with risk to be limited to the amount used to buy futures. In fact, this was a gimmick and Serhant invested all the funds in futures through his company Financial Partners, Ltd., and, erroneously predicting trends in short-term interest rates, Serhant lost $21 million of the $51 million invested. *Bosco v. Serhant*, 836 F.2d 271, 273 (7th Cir. 1987). For this, Serhant was convicted of mail fraud and was sentenced to 15 years prison. *US v. Serhant*, 740 F.2d 548 (7th Cir. 1984). Heritage Capital Advisory Services (HCAS) was an unregistered commodity pool operator, which, along with various other operators, invested the money entrusted to it with Financial Partners and Serhant. *CFTC v. Heritage Capital Advisory Services, Ltd.*, 823 F.2d 171, 172 (7th Cir. 1987). On September 28, 1982, the CFTC obtained a temporary restraining order against HCAS and other investors, freezing their operating accounts. *Id.* HCAS, was not alleged to have known of the fraud, *id.*, and was permitted to join a class action against Serhant, Financial Partners and others. *Baranski v. Vaccariello*, 896 F.2d 1095 (7th Cir. 1990).

To be sure, the district court's opinion in *Heritage* does not state that the Heritage pool had a commodity trading account in its own name. *Heritage*, [1980-1982 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,627. The case is silent on the ownership of the commodity trading account. However, even just looking at the district court opinion, it is clear that the entity that did the ultimate trading of commodity interests was Financial Partners, and the facts indicate that Heritage withdrew funds from its pooled accounts and sent them to FPB, which deposited them in **its** account at the Berwyn National Bank, just as Tech Traders deposited Shasta funds into its account at the Bank of America. *See Id.* at 26,381. Moreover, the Heritage principals described the investment program as one in which its customer's funds would be combined with the funds of **other investors** into an investment account, just as Shasta's funds were combined with the funds of other Tech Traders investors. *Id.* at 26,380. It is highly unlikely that the commodity trading account was in the name of Heritage when it contained the funds of other investors and investor money was deposited into FPB's bank account.

The court in *Lopez v. Dean Witter Reynolds, Inc.*, 805 F.2d 880, 884 (9th Cir. 1986) relies on *Heritage* in determining the factors that make up a commodity pool.[2] Its reliance on *Heritage* shows that the name on the commodity trading account is not a factor in determining whether a commodity pool exists. The fact that Shasta did not have a trading

[2] Shimer states that *Lopez* is controlling case law and that the Commission has somehow conceded this by citing the case in its brief in support of a statutory restraining order. *See* Shimer's Summary Judgment Brief at 5. As the Court knows, a Ninth Circuit decision is not controlling in the Third Circuit. But, as stated above, there is nothing in *Lopez* that precludes determining that Shasta is a commodity pool.

account in its own name is a distinction without a difference, no matter how many times Shimer repeats it.[3]

B. Shasta Meets the Definition of a Pool Found in Commission Regulation 4.10(d).

Shimer makes much of the fact that the Commission narrowed the definition of "pool" found in 17 C.F.R. § 4.10(d) in 1981 amendments. *See* Shimer Summary Judgment Brief at 3, 11. But he does not explain how narrowing the definition excludes Shasta from the definition of a commodity pool. There is nothing in the amendment that indicates that the definition was narrowed to exclude entities that did not have commodity accounts in their own name, but funneled most of their funds to another entity to trade commodity interests. Prior to 1981, §4.10(d) stated:

> "Pool" means any investment trust, syndicate or similar form of enterprise that trades commodity interests.

Since the 1981 amendment, §4.10(d) now states:

> *Pool* means any investment trust, syndicate, or similar form of enterprise operated for **the purpose of trading** commodity interests.

Although the Federal Register does not contain an extensive discussion of the reason for the definitional change, the commentary on the Commission's May 8, 1981 final amendments to 17 C.F.R. Part 4, its Commodity Pool Operator ("CPO") and Commodity Trading Advisor ("CPA") Regulations, indicates that the change was meant to exclude some small group of entities that did not intend to trade commodity interests, though the Commission did not necessarily exclude an entity that only occasionally acquires or trades commodity interests from the definition of a commodity pool.

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[3] Shimer also states that *Lopez* "requires that funds be pooled into that account in question and *obviously remain in that account* in order to be traded in the name of the entity sought to be characterized as a 'pool'."

At 46 FR 26004, the Commission notes that while agreeing that adding the phrase "operated for the purpose of trading commodity interests" clarified the scope of the term "pool", certain commentators believed the proposed definition was still overbroad. One person had suggested that an entity whose assets committed to trading commodity interests did not exceed a specified percentage, such as 10%, should be excluded from the definition. The Commission rejected this approach. "The Commission finds this approach deficient because it fails to take into account the fact that such an entity might, nonetheless, be marketed and sold as a commodity pool, so that the participants therein should not be denied the protection of the Part 4 Rules." *Id.* The Commission also rejected the suggestion that "pool" be defined as an entity formed for the "principal" purpose of trading commodity interests as too narrow and found that even entities formed pursuant to the securities laws that only occasionally traded commodity interests could be commodity pools and subject to the Part 4 regulations:

> ...the Commission is aware of the argument advanced by such persons as pension funds and limited partnerships registered as broker-dealers under the Securities Exchange Act of 1934 that they are not "pools." Among other reasons, these persons state that they only occasionally trade commodity interests, that they commit a limited amount of assets to such trading, that they are hedging those assets as opposed to speculating with them, and that their "participants" are knowledgeable in business matters and financially secure. Whether a particular entity is operated "for the purpose" of trading commodity interests, and thus is a pool within the scope of §4.10(d), depends on an evaluation of all the facts relevant to the entity's operation.
>
> *Id.*

As alleged in the First Amended Complaint and admitted by the Defendants, Shasta was an entity created solely to pool investor assets, 99% of which were transferred to Defendant Tech Traders for trading in the commodity markets. *See* First Amended Complaint at ¶29; Shimer and Firth Statements of Uncontested Facts at ¶ 10 [Docket No. 64,

159 and 160]. *See also* CFTC Response at 12. If the Commission considers an entity that only occasionally trades commodity interests to be a commodity pool and finds that requiring an entity to have as its "principal" purpose the trading of commodity interests narrows the definition of commodity pool too much, it must consider an entity who markets an investment vehicle through the internet and third parties by touting **solely** the fictitious returns of a commodity trading system to be an entity "whose participants should not be denied the protections of the Part 4 Rules" and therefore is a commodity pool. *See* First Amended Complaint at ¶¶ 40-46 and Equity Defendants' Answer at 40-46.

Amendments to Part 4 made in 1995 also show that feeder funds, or fund of funds, like Shasta are pools within the meaning of Commission Regulations. In 1995, the term "investee pool" was added to §4.10(d). An "investee pool" is "any pool in which **another pool** or account invests, *e.g.* as a limited partner thereof." 17 C.F.R. § 4.10(d)(4). In discussing revisions to §4.24 in the commentary to the 1995 revisions, which deals with disclosures CPOs must give in disclosure documents, the Commission noted that "commenters were invited to address any special public policy or disclosure considerations presented by tiered investment structures by means of which a **commodity pool** can, in effect, appropriate the value of a second fund's management by **investing all** or a portion **of its funds in the second fund**."(emphasis added). The Commission also requested comment concerning whether any additional protections, other than disclosure of applicable fees, are appropriate in light of the "'layering' of fees that typically occurs at each level of a fund of funds structure." 60 FR 38146 at 69. No comments were received. Thus, it is apparent that both the Commission and the industry considered entities formed for the purpose of investing all of their funds in other commodity pools to be commodity pools as a matter of course.

Despite Shimer's lengthy and repetitive arguments to the contrary, the Commission is not redefining the term "pool" in this case.

Shimer also engages in a curious and superfluous discussion about deference to agency interpretations of statutory language, citing cases where it was found that agency regulations or positions in cases conflicted with statutory language or Congressional intent, yet does not argue that the regulatory definition of "pool" conflicts with the Commodity Exchange Act. 7 U.S.C. § 1 *et seq.*(2002) ("the Act."). *See* Shimer's Summary Judgment Brief at 9-11. The Commission agrees that it does not. Moreover, the statutory definition of "commodity pool operator", selectively defined by Shimer (*See Id at* 11, n.15) supports a finding that Defendant Equity Financial Group LLC ("Equity") was a CPO. The statutory definition of a CPO is

> any person engaged in a business that is of the nature of an investment trust, syndicate, or similar form of enterprise, and who, in connection therewith, solicits, accepts, or receives from others, funds, securities, or property, **either directly or through capital contributions, the sale of stock or other forms of securities**, or otherwise, for the purpose of trading in any commodity for future delivery on or subject to the rules of any contract market or derivatives transaction execution facility...

7 U.S.C. § 1(a)(5)(emphasis added).

The key phrase in the pool definition is "investment trust, syndicate or similar enterprise", which generally means any arrangement in which investors' funds are commingled for the purpose of investing or trading and the profits and losses therefrom are allocated pro rata to the investors. Commodity futures need not have been the main instrument traded by the entity.

More to the point, the statutory definition of a CPO contemplates indirect investments in commodity interests through vehicles such as the shares in a limited liability corporation that Shasta investors purchased. The fact that Shasta investors invested in commodities

through this intermediary, as noted by Shimer in his original brief in support of his motion to dismiss, also does not take Equity out of the definition of a CPO found in the Act. *See* Shimer Motion to Dismiss For Failure to State a Claim Upon Which Relief Can Be Granted, Firth Motion to Dismiss For Failure to State a Claim Upon Which Relief Can Be Granted, Brief of Defendant Robert W. Shimer in Support of Motions Filed Pro Se on Behalf of Himself and Motions Filed Separately by Vincent J. Firth Pro Se Pursuant to Federal Rules 56(b), 12(b)1 and 12(b)(6) for Summary Judgment and Dismissal ("Shimer's First Brief" at 52)[Docket 159].

III. The Equity Defendants' Fraudulent Conduct was "In Connection With" Commodity Futures Trading and Violated Section 4b(a)(2)(i)-(iii) of the Act.

Shimer repeats the argument he made in his Motion to Dismiss that Shasta must be found to be a commodity pool for liability to be found against the Equity Defendants on Count I of the First Amended Complaint, which alleges that each of the Equity Defendants violated Section 4b(a)(2)(i)-(iii) of the Act, 7 U.S.C. § 6b. The reason why this is dead wrong is set out in the CFTC Response at 9 and will not be repeated here. Shimer also argues in this round that because none of the Equity Defendants engaged in commodity futures trading themselves, their fraudulent conduct was not "in connection with commodity futures trading" under Section 4b[4] of the Act. As support for this argument, Shimer quotes extensively from the case *CFTC v. Mass Media Marketing, Inc.*, 156 F. Supp. 2d 1323 (S.D.Fla. 2001). *See* Shimer Summary Judgment Brief at 16-19. His reliance on this case is misplaced because the facts are much different than this case and it did not involve the same

[4] Section 4b of the Act, 7 U.S.C. § 6b(a)(2)(i) (2002), provides in pertinent part that "[i]t shall be unlawful...for any person, in or in connection with any order to make, or the making of, any contract of sale of any commodity for future delivery, made or to be made, for or on behalf of any other person ... (i) to cheat or defraud such other person..."

statutory provision at issue here.

In *Mass Media*, the Commission sued mass marketing companies that marketed a wide range of products that included Ginsu knives and exercise equipment. Media, 156 F.Supp.2d at 1324. In 1995, those companies began creating commercials and infomercials involving options on commodity futures. When interested viewers called a toll free number, the defendants obtained their names and telephone numbers and sold them to registered introducing brokers, who would then solicit the interested person to invest in commodity futures options. *Id.* at 1325. The Commission argued that these marketing companies were acting as introducing brokers under the Act. *Id.* at 1328. The District Court for the Southern District of Florida found that Congress did not contemplate that companies who collect leads for registered introducing brokers were "engaged in soliciting or in accepting orders" and thus did not fit the definition of "introducing broker" found in the Act. *Id.* at 1332.

In contrast here, the Equity Defendants aggressively solicited investors, through their web site, third party web sites and their private placement memorandum, to invest in Shasta, which would place their funds with a trading company that showed "astonishing performance" of approximately 100% per annum trading commodity futures contracts. *See* First Amended Complaint at ¶¶ 4, 42, and 44 Equity Defendants' Answer at ¶¶4, 42, 44. Unlike the *Mass Media* defendants, the Equity Defendants did not just pass the names of Shasta investors along to Tech Traders, who then solicited the investors to trade commodity futures contracts. Tech Traders did not directly solicit most of the Shasta investors. In fact, the Equity Defendants did not even tell most investors the name of the trader. *See* First Amended Complaint at ¶32, Equity Defendants' Answer at ¶32. The Equity Defendants directly solicited the investors and accepted their money to invest with Tech Traders. Thus,

Mass Media is inapposite here.

Shimer's extensive discussion of *Mass Media's* analysis of 17 C.F.R. § 33.10 (2004) is also off the mark. The *Mass Media* court engaged in an extensive analysis of § 33.10 because it is a regulation adopted by the Commission that the Commission asserted was authorized by Section 4c(b) of the Act, 7 U.S.C. § 6c(b), the statutory provision that deals with commodity futures **options.** The *Mass Media* court found that Section 4c(b) did not give the Commission the authority to impose anti-fraud regulations on entities, such as the defendants in that case, that did not participate in commodity trading transactions. *Id.* at 1334.

This case does not involve commodity options and the Commission is not relying on a Commission regulation in Count I of its First Amended Complaint. Count I alleges a violation of Section 4b of the Act itself. As to this provision of the Act, the *Mass Media* court noted that the provision is narrower than §33.10 and distinguished the Commission's cited cases because they involved violations of Section 4(b) rather than §33.10. *Id* at 1334.

Shimer's arguments to the contrary notwithstanding, the case law interpreting Section 4b of the Act shows that it is "not restricted …to instances of fraud or deceit 'in' orders to make or the making of contracts. Rather, [Section 4b] encompasses conduct 'in or in connection with' futures transactions. The plain meaning of such broad language cannot be ignored. And liability under [Section 4b] explicitly extends beyond 'member[s] of the contract market' to 'any person' engaging in conduct 'in connection with' futures transactions." *CFTC v. Vartuli,* 228 F.3d 94, 101 (2d^{d} Cir. 2000), citing *Saxe v. E.F. Hutton & Co.,* 789 F.2d 105, 110-11 (2d Cir.1986) (quoting *Hirk v. Agri-Research Council, Inc.,* 561 F.2d 96, 103-04 (7th Cir. 1977)). Thus, the *Vartuli* court found that misleading advertising by

the sellers of a computer trading program for trading futures contracts was "in connection" with futures trading within the meaning of Section 4b. *Id* at 101. In *Saxe*, the plaintiff had opened a commodity trading account in reliance upon the defendant's statements that a particular commodities trader was "an experienced commodities trading advisor, which [sic] would use a sophisticated computerized trading program custom-tailored to [the plaintiff's] investment objectives." *Saxe,* 789 F.2d at 110. The misrepresentations in *Saxe* were found to be "in connection with" futures trading under Section 4b even though the misrepresentations concerned a separate broker who in turn made independent recommendations about commodity transactions.

Similarly here, the Equity Defendants made representations about the trading prowess and results of Tech Traders, the entity that made all the trading decisions. *See* First Amended Complaint at ¶¶ 42, 44. Equity Defendants' Answer at 42, 44. These representations were "in connection" with futures trading within the meaning of Section 4b and are actionable.

IV. The Commission's Count V Allegations Against Shimer for Aiding and Abetting A Violation of Regulation 4.30 Do Not Require A Finding that Shasta was a Commodity Pool.

In his current motion, Shimer repeats his argument made at 81 – 91 of his First Brief, that he cannot be liable for aiding and abetting Tech Traders' violation of Regulation 4.30, 17 C.F.R. § 4.30 because of his assertion that Shasta is not a commodity pool. *See* Shimer Summary Judgment Brief at 21-23. As set out in the CFTC Response at 10, no element of this violation requires a finding that Shasta was a commodity pool. Although styled as a summary judgment motion this time around, Shimer does not support his argument with any evidence to show that he did **not** aid and abet Tech Trader's §4.30 violation. In fact, the undisputed facts support a finding that Shimer did violate this provision. Regulation 4.30

prohibits any CTA from soliciting, accepting or receiving from an existing or prospective client funds, securities or other property in the trading advisor's name to purchase, margin, guarantee or secure any commodity interest of the client. 17 C.F.R. § 4.30 (2004) Shimer admits that he drafted the private placement memorandum that sets out that Shasta's funds will be held in the name of the trading company.[5] Shimer's arguments to defeat Count V are factually and legally incorrect and should be rejected.

V. CONCLUSION

Shimer and Firth's Motion for Summary Judgment is a thinly disguised attempt to reargue a motion that is already pending with the Court. They do not support it with any evidence; they just reargue the same points they made in their motion to dismiss. For the reasons set forth above and in the CFTC Response to that motion, Shimer and Firth's motion for summary judgment should be denied.

[5] *See* Equity Defendants' Answer at ¶29.

Date: August 5, 2005

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The undersigned, a non-attorney, does hereby certify that on August 5, 2005, she caused true and correct copies of the foregoing ***CFTC'S Response to Robert W. Shimer and Vincent J. Firth's Motion for Summary Judgment*** to be served via U.S. mail:

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