U.S. COMMODITY FUTURES TRADING COMMISSION
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PROCEEDINGS

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GREGG FAGER,
Complainant,

v.

TIJEAN CLEMENT BARRERE,
JAMES A. LANE,
ROBERT MYRON NADELL, and
THE SIEGEL TRADING COMPANY,
INCORPORATED.
Respondents.

CFTC Docket No. 95-R90

NOTICE OF CORRECTIONS

Set out below are corrections to the text of the Initial Decision. Corrected portions of the text are underlined here:

Footnote 2 should read:

> *See* Fager's discovery replies filed March 14, 1996. Respondents did not challenge Fager's list of the dates when he claims he spoke to respondents. Respondents also did not maintain a telephone log of their contacts with Fager, <u>and</u> did not produce any phone bills<u>.</u>

Footnote 11 should read:

> Fifty-percent profit calculation based on recovering $9,320 costs ($9,010 purchase costs plus $310 sale costs), plus $4,660 profit (50% of $9,320) for a total of $13,990. If sold at 7 points, <u>$14,000 in premiums</u> would have been collected.

Footnote 18 should read:

> Profit calculation based on recovering $9,260 costs ($8,795 purchase costs plus $465 sale costs), plus $1,714 profit, for a total of $10,974. If sold at 5 <u>32/64</u> points, an $11,000 premium would have been collected.

The text accompanying footnote 18 should read:

> In order to recapture the $1,714 soybean loss, these March puts would have had to appreciate by 199%, to 5 32/64 points in three months.

For the parties' convenience, corrected copies of pages 3, 12 and 20 are attached.

Dated March 25, 1997.

Philip V. McGuire,
Judgment Officer

U.S. COMMODITY FUTURES TRADING COMMISSION
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OFFICE OF
PROCEEDINGS

GREGG FAGER, Complainant, v. TIJEAN CLEMENT BARRERE, JAMES A. LANE, ROBERT MYRON NADELL, and THE SIEGEL TRADING COMPANY, INCORPORATED. Respondents.	)	CFTC Docket No. 95-R97

INITIAL DECISION

Before: McGuire, Judgment Officer

Gregg Fager claims that respondents fraudulently guaranteed profits and gave him false price information and seeks to recover $10,766. Fager's damage calculation excludes the profits from the winning trades in his account. Respondents deny any of the alleged violations.

The findings and conclusions below are based on the parties' documentary submissions and oral testimony. Unless otherwise noted, amounts are rounded to the nearest dollar, and dates are in 1994.

For the reasons set out below, it is concluded that Fager has established violations by respondents, but that he is entitled to no more than his aggregate out-of-pocket losses of $858.

Findings of Fact

The Parties

1. Gregg Fager is a lawyer residing in Centerville, Utah. According to Fager, his law practice is "transaction-oriented." [Pages 88-89 of the hearing transcript.] Fager was an unsophisticated investor with no commodities experience before opening his Siegel Trading Company account, and little experience in other sorts of investments.[1]

2. The Siegel Trading Company ("STC") is a registered futures commission merchant. Robert Nadell, Tijean Barrere and James Lane are registered associated persons with STC. Nadell solicited Fager's account and acted as Fager broker. Barrere and Lane substituted for Nadell near the end of Fager's account, when Nadell was out with a health problem. STC and Nadell were compensated solely by the commissions charged to Fager's account.

Tape-Recorded Conversations

3. STC was required to tape-record sales solicitation telephone calls from August 8, 1991 to August 8, 1996. [Order of Permanent Injunction, *CFTC v. The Siegel Trading Company, Inc.*, (U.S. District Court for the Central District of California, May 8, 1991 Civil Action no. 89-5364JMI); CFTC Opinion and Order

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[1] In reply to respondents' interrogatory 5 and in his account-application, Fager represented that his investment experience was limited to a single slightly profitable venture in penny stocks. [Exhibit I to joint Answer.] In contrast, during the recorded portion of the account solicitation, Fager told Nadell that he had been "burned" a couple of times before with investments. [Exhibit II to joint Answer.] This contradiction has not been resolved on this record.

Accepting Respondents' Offer of Settlement, *In re The Siegel Trading Company, Inc.* (May 12, 1991, CFTC Docket No. 91-6); and NFA Order of Settlement, *In re The Siegel Trading Company, Inc., et al.* (May 8, 1991, NFA Case No. 93-BCC-26).] However, in response to an order to produce recordings of the "numerous" conversations during the solicitation that stretched over March, April and May 1994,[2/] STC produced the recording of just one conversation during the second week of May 1994. [Labelled by STC "Time Period 5/7/94-5/13/94" (respondents' discovery replies filed May 10, 1996).]

STC also produced recordings and transcripts of several routine conversations between Fager and the STC compliance department. These conversations consisted of STC's initial compliance review when Fager opened his account, STC's follow-up calls to discuss the May through July monthly account statements, and Fager's oral authorizations to place buy and sell orders recommended by Nadell. STC informed Fager that it was recording these conversations. [Exhibit II of the joint Answer; *see also* pages 8-9 of respondents' discovery reply dated March 15.]

4. Fager produced recordings of conversations with Nadel on September 23 and October 26, 1994. Fager did not inform STC that he was recording these conversations. Fager produced the transcript of these conversations on April 26, 1996.

2/ *See* Fager's discovery replies filed March 14, 1996. Respondents did not challenge Fager's list of the dates when he claims he spoke to respondents. Respondents also did not maintain a telephone log of their contacts with Fager, did not produce any phone bills, and otherwise.

The Solicitation

5. Nadell's solicitation stretched out over March, April and May of 1994. According to Nadell, he cold-called Fager after the Utah State Bar had provided Fager's name and telephone number to STC. [Page 86 of hearing transcript.] Nadell and Fager spoke several times in March and April. During this series of conversations, Nadell and Fager discussed bond options. In mid-April, Fager stated that he was not immediately interested in speculating in commodity options, but might seek "partners" for a joint account. [Page 6 of respondents' transcript (filed May 10, 1996); and Fager's discovery reply (filed March 14, 1996).] Neither side produced a detailed description of these unrecorded conversations.

6. Sometime in March or April, Nadell sent an account-opening package to Fager that included an STC Customer Agreement, a separate STC Customer Agreement for Exchange-Traded Options on Futures Contracts, a standard futures risk disclosure statement, an Acknowledgement that he had received a standard options disclosure statement, and an Acknowledgment of Commissions.

The Acknowledgment of Commissions and the separate STC Options Customer Agreement both disclosed that STC charged a commission of 45% of the option premium, plus an additional $155 per-contract entry commission and another $155 per-contract exit commission.[3/] Paragraph 2 of the separate STC Options Customer

[3/] The STC commission structure is reviewed here in light of Fager's allegations that Nadell's made misrepresentations during (continued...)

Agreement included a clause that the customer understood that the cost of the commissions must be overcome before an option position could become profitable. [Exhibit I to joint Answer.]

7. Nadell and Fager spoke several times between May 1 and May 24. [*See* Fager's reply to respondents' interrogatory 11.] As noted above, STC produced the tape-recording of only one of these conversations. Neither side produced a detailed description of the unrecorded conversations.

8. During the recorded May conversation, Nadell made references to the speculative nature of trading options. However, Nadell undermined these references with numerous enthusiastic and unrestrained promises of tremendous profits:

- "In my opinion, you could easily see $20,000 on this September [coffee] contract."
- "If it continues up the way it's going now, you'll double, easily triple, your money."
- "You will not regret it my friend; in my opinion, you'll make a very handsome profit and we'll be trading for a long time."
- "I've got guys in the market -- honestly, in two weeks who have tripled their money in fourteen working days."
- "I'll send the family skiing on me this winter, believe me."
- "It's beautiful . . . It's flying . . . it's roaring right back."
- "One penny [move] produces 375 [dollars] in profit."

[Respondent's discovery replies filed May 10, 1996.] At no point

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3/ (...continued) trading recommendations that amounted to guarantees of profits. Fager has waived recovery based on an unjust enrichment theory.

during this conversation did Nadell temper his claims of large potential profits with a meaningful disclosure of the accompanying possibility of large losses or with any discussion of the detrimental effect of STC's commission load on the likelihood of making profits.

Although Fager testified that he understood that he could potentially lose his entire investment, Fager's descriptions of his subsequent decisions to accept Nadell's trading recommendations establish that Nadell's strong suggestions of huge profits during this conversation induced Fager to cling to unrealistic expectations of profits which Nadell took no meaningful steps to cure. [Pages 10-11, and 38 of hearing transcript; *see* Fager's reply to respondents' interrogatories 11 and 12, and page 4 of transcript of May 24 compliance review.]

9. Near the beginning of the recorded May conversation, when Fager said that he had been too busy working to notice the run-up in the coffee market, Nadell replied: "Let me drive the bus, and you will, in my opinion, do very, very well on coffee." [Page 2 of respondents' transcript.] When asked whether he and Nadell discussed the specific duties encompassed by Nadel's promise to "drive the bus," Fager replied that he asked Nadell to keep Fager "informed," and that Fager otherwise assumed that Nadell broadly intended for Fager to "leave it to me." [Pages 29-30 of hearing transcript.] Nadell provided a less convincing interpretation of the phrase "let me drive the bus," claiming that it meant that he would be "very, very alert in handling [Fager's] account," and that

he would "keep in touch with Fager." Nadell admitted that he "regularly" used the phrase "let me drive the bus" with Fager. [Nadell's reply to Fager's request for admission 133.]

10. The next week, Nadell called Fager back to continue his solicitation. Nadell told Fager that coffee was a "good investment," and repeated his assurance that he "would drive the bus."

11. On May 19, 1994, Fager decided to open an account and to buy a coffee option. Fager filled out and signed the account-opening documents. On the account application, Fager listed his annual income as between $50,000 and $100,000, and his net worth as between $50,000 and $100,000. Fager described his trading objective as "increase personal wealth." [*See also* Fager's reply to respondents' interrogatory 12.]

12. On May 24, during the initial compliance review and before the first option purchase, an STC compliance department employee explained to Fager how STC calculated commissions and that an option had to overcome the costs of commissions merely to break even. [Pages 4-5 of transcript (Exhibit II to joint Answer).] For the other three option purchases, each time an STC compliance department employee reported the fill price, the STC employee would break out the purchase price and the commission charges. [June 30, July 7 and November 1 conversations at pages 23, 25 and 39-40, respectively, of transcript, *see also* May 31 conversation at pages 14-15 of transcript (Exhibit II to joint Answer).] Also, the trade confirmation statements (dated May 24, June 30, July 6, and

November 1) set out the commission charges. [*See* page 15 of hearing transcript.]

Trading Activity

13. Fager would deposit a total of $9,210 ($7,000 on May 24, $496 on May 26, and $1,714 on July 15), and receive a total of $8,352 in disbursements ($8,085 on July 6, and $267 on November 3), for an aggregate net loss of $858.

14. Fager would realize aggregate gross trading profits of $8,644, which was obliterated by the $9,811 in total commissions. The commission-to-investment ratio would be 106%,[4/] the commission-to-gross profit ratio would be 112%,[5/] and the commission-to-premium-paid ratio would be 55%.[6/] Given these circumstances, the fact that Fager's account failed to realize an over-all net profit was no surprise, if not virtually inevitable. At no point during any of the recorded conversations did Nadell refer to the difficulty of breaking even, let alone making the

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4/ This calculation is based on $9,210 in aggregate deposits. The commission-to-investment ratio represents the return on funds invested necessary to recover transaction costs and to break even, and thus reflects the burden of commission costs on profit potential.

5/ This calculation is based on $8,644 in gross profits or aggregate net premiums collected (the difference between the $26,313 total premiums collected and the $17,669 total premiums paid). The commission-to-gross profit ratio reflects the detrimental effect of transaction costs on gross trading profits.

6/ Based on the $17,669 total in premiums paid. The commission-to-premium-paid ratio reflects the rate at which options much appreciate merely to overcome the transaction costs and to break even.

highly touted profits, given the detrimental effect of STC's enormous commissions.[7]

15. For each option purchase, the STC confirmation statement separately reported the trade price, the premium paid, the 45% commission, and the $155 per-contract entry commission. The STC monthly account statement, but not the STC confirmation statement, reported the current market price and liquidation value for any open position. Thus, Fager had to rely on Nadell for regular updates on the value of his open positions.

For each option sale, the STC confirmation statement separately reported the trade price, the premium collected, and the $155 commission paid. However, the STC confirmation statement and the STC monthly account statement did <u>not</u> report the net premium on the trade and did <u>not</u> report the net profit or loss. Thus, Fager either had to calculate the net results of any trade, by comparing two confirmation statements, or had to rely on an STC agent to provide the net results. Fager's testimony about the trades, and the several recorded conversations between Fager and STC agents establish that he knew the net results of his trades. On this record it cannot be established whether Fager's information was based on reports from Nadell or based on Fager's own calculations.

16. The first trade in Fager's account was the purchase on May 24 and the sale on June 29 of one December coffee call option.

According to Fager, he told Nadell that he hoped to double his

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[7] Respondents have produced no evidence that Nadell varied his pitch during any of the <u>un</u>recorded conversations with Fager.

investment, which Nadell had previously predicted as quite reasonable. [Pages 9-10 of hearing transcript.] Given the total cost of $9,641,[8] Fager would have to collect a $19,282 premium to achieve this goal. Put differently, the burden of the commissions was so great that for Fager to double his investment, the coffee option $5,063 premium essentially had to quadruple. Nadell never cautioned Fager how unrealistic such a hoped-for return would be.

17. On about June 7, an STC compliance department employee named "Dee" called Fager to review the May monthly account statement. Fager told Dee that he had "a lot of questions" about the monthly account statement. Dee replied that she might be able to answer his questions by reviewing the statement in detail. Since the only trading activity had been the coffee purchase, the statement essentially recapped the May 24 transaction. Dee explained that the monthly account statement broke the trade costs into two debit entries; and clearly explained that the first entry (a $155 debit) titled "Commission Charge/Cash" related to the $155 entry commission, and that the second entry ($7,340.75 debit), titled "Net Prem" was the sum of the premium paid and the 45% commission.[9] Dee also clearly explained that the $3,375 liquidation value corresponded to the amount Fager would collect if

[8] Based on the sum of the $5,063 premium paid, the $2,278 45%-commission, plus the $155 entry commission, and the $155 exit commission.

[9] By only explicitly identifying the much smaller $155 commission, the format of the STC monthly account statement materially obscured the onerous 45% commissions, and thus was inherently misleading.

he had sold the option on May 31. After Dee's explanation, Fager stated that he had no questions.

At the end of this conversation, Fager told Dee that -- "based on what [he was] hearing [from Nadell] -- he expected to recoup $7,340.75 by the end of June." Dee merely replied "Well, we hope so," and made no effort to ensure that Fager knew that breaking even or making profits could not be "expected." [Pages 16-17 of transcription, Exhibit II of Answer, emphasis supplied.]

18. On June 29, Fager accepted Nadell's recommendation to sell the coffee option. [*See* pages 98-100 of hearing transcript.] On the coffee trade, Fager collected a net premium of $12,187, and paid a total of $2,588 in commissions, thus realizing a net profit of $9,599.

19. Fager then accepted Nadell's recommendation to use the coffee proceeds to purchase two December Treasury Bond puts based on Nadell's strong belief that a widely anticipated interest rate hikes by the Federal Reserve would trigger a strong reaction in the bond market. Fager told Nadell that he expected to make at least a 50% profit on this trade. [¶ III.A.33 of Fager's Final Verified Statement; and pages 11-12 of hearing transcript.] Before obtaining Fager's authorization to buy the two December T-Bond puts, Dee of the STC compliance department estimated that the T-Bond options would cost $5,000 each.

The order was filled at 3 points.

20. On June 30, Dee called Fager to report the fill on the T-Bond order. Dee reported that Fager had paid a total cost per

contract of $4,505, and broke down the per-contract cost into the $3,000 premium, the 45% commission of $1,350, plus the $155 entry commission. [Pages 20-23 of transcript (Exhibit II of Answer).] Thus, the total cost for the two December T-Bond puts was $9,010.

In order to break-even, the two December T-Bond would have to appreciate by 64% to 4 33/44 points.[10] In order for Fager to realize a 50% profit, the two T-Bond puts would have had to appreciate by 234% to 7 points.[11] Respondents have produced no evidence that Nadell tempered Fager's expectations of large profits with any meaningful reference to the difficulty of making any profits, let alone a 50% profit, in these circumstances.

21. On July 6, Fager accepted Nadell's recommendation to buy one November soybean call option. According to Fager, Nadell did not explain in detail the basis for this recommendation, and merely asked Fager to "trust" him to make a profit. [Page 82 of hearing transcript; and ¶ III.A.34 of Fager's Final Verified Statement.]

Before obtaining Fager's authorization to buy the soybean call, Dee estimated that the option premium would be $1,080, and that the with the commissions the total cost would be "a little under $1,800." The soybean order was filled at 21 1/2 points. Later that day an unidentified STC compliance employee confirmed that Fager had paid a $1,075 premium and $484 in commissions for a

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10/ Break-even calculation based on recovering the $9,010 purchase cost plus the $310 exit commission, for a total of $9,320.

11/ Fifty-percent profit calculation based on recovering $9,320 costs ($9,010 purchase costs plus $310 sale costs), plus $4,660 profit (50% of $9,320) for a total of $13,990. If sold at 7 points, a $7,000 premium would have been collected.

total of $1,714, [Pages 23-25 of transcript (Exhibit II of Answer).] Afterwards, the soybean call steadily declined and eventually expired worthless.

22. On July 14, Dee called Fager to review the June monthly account statement. Dee confirmed that the December T-Bond puts had a liquidation value of $7,406, still below the break-even price. Dee did not discuss the soybean call, which settled that day with a liquidation value of $688.[12/] [Pages 27-28 of transcript (Exhibit II of Answer).]

23. According to Fager, he spoke to Nadell one more time in July, on July 22. On that date, the T-Bond puts had a liquidation value of $5,250, and the soybean call had a liquidation value of $331, both well below their purchase prices. When Fager expressed concern about both losing positions, Nadell reassured him that as to the December T-Bond puts "everything is fine -- we have time -- this <u>will</u> work out in time." [Pages 15-16, 18-19, and 24-25 of hearing transcript.]

24. The July monthly account statement reported that as of July 29, the soybean call had a $406 liquidation value, and that the December T-Bond puts had a $3,219 liquidation value.

25. On August 10, Dee reviewed the July monthly account statement with Fager. Dee merely mentioned that the soybean option and T-Bond puts had a $3,625 aggregate liquidation value. Fager

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12/ Unless otherwise noted, liquidation values are based on settlement prices. By Order dated February 20, 1996, official notice was taken of a price history of the options in Fager's account provided by the CFTC Division of Economic Analysis.

replied that he understood that both positions had significantly declined, but did not express any concern. [Pages 28-31 of transcript (Exhibit II of Answer).]

26. Throughout August, the December T-Bond puts traded well below the purchase price, with a $3,094 liquidation value on August 31. By August 31, the soybean call had declined to a $219 liquidation value.

27. Fager and Nadell next spoke on September 7, 12 and 13. By September 13, the December T-Bond options had slightly rebounded to a $5,844 liquidation value, settling at 2 60/64 points. During one of these conversations, Fager told Nadell that he had given up on his initial objective of realizing a 50% profit on the December T-Bond puts, in favor of recovering his expected loss on the soybean option. In order for Fager to realize this somewhat more modest objective, the two T-Bond puts would have had to appreciate by 188%, from 2 60/64 to 5 34/64 points, in just two months.[13]

28. On September 21, Dee called Fager to review the August monthly account statement. Dee did not state the value of the soybean call or December T-Bond puts. However, Fager indicated that he was aware that the soybean call and T-Bond puts were not profitable, stating that he was "chagrined" at the performance of the soybean option, and that he was "still wondering" about

13/ Profit calculation based on recovering $9,320 costs ($9,010 purchase costs plus $310 sale costs), plus $1,714 profit (assuming a total loss on the soybean call) for a total of $11,034. If sold at 5 34/64 points, a $11,061 premium would have been collected.

Nadell's advice on the T-bond option.[14/] Fager stated that had been "assured [by Nadel] that things are going to look up," and that he "hop[ed] that [Nadell's] assurances pan-out." Dee replied that "you know of course [that] your broker [has just] given you his best opinion; but he's not a fore-teller of events." Dee did not explain why she had waited almost a month to call about the August monthly, and Fager asked that the monthly reviews be discontinued because he did not find them particularly helpful. [Pages 31-34 of transcript (Exhibit II of joint Answer); *see* page 66 of hearing transcript.]

29. Set out below are pertinent portions of the next conversation, on September 23, recorded by Fager:

> *Fager:* . . . What's going on?
>
> *Nadell:* . . . T-Bond is down seven more. I hate to talk about soybeans because they're not doing a thing. So forget your soybean contract. That's a loser, unless a miracle happens . . . . We got till November, but it just keeps goin' down.
>
> *Fager:* We have 'til October on the soy.
>
> *Nadell:* Yeah. But the bond looks stronger and stronger and stronger, . . . so <u>we'll make it back on the bond. Please God.</u>
>
> *Fager:* Where's the bond at right now?
>
> *Nadell:* Three-thirty. That's three thousand and five eleven. Thirty-five-eleven apiece. Seven something. So we have a little ways to go.
>
> *Fager:* That's . . . seven-thousand twenty-two total?

14/ On September 21, the soybean option had dropped to 1 point, but the December T-Bond puts had continued their gradual rebound, settling at 3 28/64 -- barely above the purchase price and well below the break-even price.

Nadell: But I feel really, really . . . , I feel very good about it.

Fager: Yeah.

Nadell: The bond just keeps going down. . . . The talk is that . . . Greenspan sees inflation and he's going to raise the rates. Not only will that help your . . . bond, but it's causing the metals to run.

Fager: Yeah, well, I put in about ten-thousand-eight-hundred . . . with soy.

Nadell: You'll get it out. You'll get it out. I can't say enough about soybeans, but you'll get it out of the bond. I wish you had another one.

Fager: Another bond?

Nadell: Sure looks good.

[Emphasis added; pages 1-2 of Exhibit B to Complaint; *see also* pages 24-25 of hearing transcript, and Fager's final verified statement ¶ III.C.10.]

30. Fager and Nadell spoke on September 28 and 29, and October 7 and 25. Respondents have not contradicted Fager's assertion that during this time Nadell kept reassuring him that the December T-Bond puts had adequate time to recoup the soybean loss. On this record, it is not clear whether Nadell was referring to the time before the November 15 Fed meeting or the November 18 expiration date.

On September 28, the December T-bond puts had a $6,695 liquidation value; and on October 7 an $8,063 liquidation value. The December T-bond puts continued to climb, and on October 25 hit a new high of 4 54/64 ($9,688 liquidation value), closed at 4 48/64 ($9,500 liquidation value), and settled at 4 49/64 ($9,594 liquidation value).

31. Fager and Nadell next spoke on October 26, when the December T-Bond puts opened at 4 32/64 ($9,000 liquidation value). As can be seen from the transcript below, Nadell recommended that Fager hold the puts based on his extremely high level of confidence that the market's mere expectations of a Fed rate would drive up Fager's T-Bond puts another $1,000 each, which would have been more than enough to recover the soybean loss:

> *Nadell:* Yesterday [the December T-Bonds] were a little bit higher than today. But today they're still worth [$9,145]. So, we're getting there guy.
>
> *Fager:* Yeah. That's what I put into them.15/
>
> *Nadell:* Yeah. Yesterday it was at ninety-six-hundred. The two of them.
>
> *Fager:* Uh-huh.
>
> *Nadell:* And it took a little profits today. Just wanted to give you some assurance that all is not lost.
>
> *Fager:* So. What should I do with them?
>
> *Nadell:* My opinion. Stay with them for a while. You didn't give me nine-thousand to break-even. You follow?
>
> *Fager:* Yeah.
>
> *Nadell:* Stay with them a little while. Here's my reasoning. . . . [According to the Commodity Research Bureau], all the options, especially agriculturals, coppers, metals, they're going up. Whenever that happens, it's a small sign of inflation generally followed by a raise in interest rates. And of course, that's what we'll . . . you know . . . we're praying for. You follow? A raise in the interest rate will knock that bond down more. Are you following me?
>
> *Fager:* Yeah, sort of, yeah.
>
> *Nadell:* Well, in other words, if the new issues [sic] -

15/ Fager was very close: he had actually put in $9,165 on June 30.

- and there's one at auction right now -- should produce well over eight percent, . . . the bond holders are gonna start redeeming their old bonds, Gregg.

Fager: Uh huh.

Nadell: And when they do that, they're gonna take a loss, because they don't bear eight percent interest. Follow?

Fager: Uh huh.

Nadell: And <u>if the interest rates go along as Greenspan said he's gonna do in November</u>, uh . . . <u>just as the rumor heats it up, as the CRB heats up, [sic] should produce another thousand dollars apiece on those bonds</u>.

Fager: Okay.

Nadell: So we have the time. You follow? And it's not going against you.

Fager: When does it expire?

Nadell: . . . [Hey Vinny, do the . . . December bonds expire in the first week in December? Third. Thankyou.] It's the third week in November. So we have time.

Fager: So we're fine?

Nadell: Yeah.

[Emphasis added; pages 3-6 of Exhibit B to Complaint.]

Fager interpreted Nadell's statement that "we're getting there" to mean that the December T-Bond puts were "continually on the rise." [Pages 77-78 of hearing transcript.]

On October 26, the December T-Bond puts closed at 4 52/64 ($9,625 liquidation value).

32. By October 31, the December T-Bond puts had lost ground, opening at 3 60/64 ($7,875 liquidation value) and closing at 3 45/64 ($7,406 liquidation value).

33. On November 1, the soybean option expired worthless for

a total loss of $1,714.

34. Also on November 1, the December T-Bond puts opened significantly higher, at 4 34/64 points ($8,938 liquidation value). The December T-Bond puts would trade between a low of 4 26/64 points ($8,781 liquidation value) and a high of 4 46/64 points ($9,438 liquidation value).

35. After the November 1 market open, Nadell called Fager to report the soybean option expiration and to recommend that Fager roll over his December T-Bond puts to March T-Bond puts. Nadell told Fager that the December T-Bond puts were "down" to $8,752.74. [¶ III.B.12.c of Fager's Final Verified Statement]. Fager's assertion is supported by the recorded conversation with the STC compliance department later that day when Fager stated that he expected to collect a premium of at least $8,700. Thus, it appears that Nadell and Fager spoke when the market was trading at what would turn out to be the low that day.[16/]

Nadell continued to reassure Fager that he would eventually recoup the soybean loss, and advised Fager to roll-over to March T-Bond options, because Nadell believed that the price decline signalled the end of any rally before the Fed's November 15 meeting and because the three days between the scheduled Fed meeting on November 15 and the puts expiration date on November 18 would be inadequate time for the bond market to react to any Fed action. [*See* Nadell's reply to Fager's requests for admission 27 and 28.]

16/ The unusually precise $8,752.74 quote most closely corresponds to a 4 25/64 price, which is one tick below the daily low. Thus it appears that Nadell made a one-tick, or $29, reporting error.

Based on this advice, Fager authorized the sale of the two December T-Bond puts and the purchase of three March T-Bond puts. The sell order was filled at 4 34/64 points. On the sale of the two December puts, Fager collected a $9,063 premium, and realized a net profit of $53.17/

For the purchase of the three March Treasury bond put options (filled at 1 54/64 points), Fager paid $5,531 in premiums and $3,264 in commissions, for a total of $8,795. In order to recapture the $1,714 soybean loss, these March puts would have had to appreciate by 199%, to 5 33/64 points in three months.18/ Respondents have not contradicted Fager's assertion that Nadell continued to represent that a Fed hike "will" result in profits on the T-Bond puts at least sufficient to recover the $1,714 loss.

35. Ironically, in the days leading up to the Fed's November 15 meeting, the December T-Bond puts continued to rally, trading over the 5 33/64 price necessary to recover the soybean loss on November 4, 7 and 8, and hitting highs on November 7 (5 58/64 points, $11,814 liquidation value) and November 11 (5 60/64 points, $11,875 liquidation value).

36. On November 15, the Fed raised interest rates as long-anticipated. However, the bond market did not react as expected,

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17/ STC did not charge the $310 exit commission on the sale of the two December puts, apparently because the sale was made in connection with a roll-over.

18/ Profit calculation based on recovering $9,260 costs ($8,795 purchase costs plus $465 sale costs), plus $1,714 profit, for a total of $10,974. If sold at 5 33/64 points, an $11,000 premium would have been collected.

and the March T-Bond puts steadily declined, losing half of their value by November 25, 1994, and losing three-quarters of their value by December 14, 1994.

On November 21, Nadell reassured Fager that a second expected Fed interest rate hike "will" trigger a favorable price move by the March T-Bond put. In December 1994 and January 1995, Barrere and Lane, acting for Nadell while he was out with health problems, repeated this advice. However, the March T-Bond puts continued to drop after the Fed raised interest rates on February 1, and expired worthless on February 17, 1995. Throughout this time, neither respondents nor Fager discussed selling the puts to limit his losses. [Page 73 of hearing transcript.]

CONCLUSIONS

The evidence establishes that Nadell knew that Fager was an unsophisticated investor, with no experience in risky derivatives, and that Nadell knew that Fager had little time to track the market. The record establishes further that Nadell convinced Fager to let him select and time trades, by making representations of tremendous profits for his other customers, and that Nadell strongly implied he would likely do the same for Fager, if Fager "trusted" him to "drive the bus." The fortuitous profit on the first trade reinforced Fager's belief that Nadell in fact knew how to select profitable trades. The recordings of the conversations in early May and on September 23 and October 26, 1994, establish that Nadell routinely overemphasized profits by making highly confident forecasts of price movements, such as "you'll double, easily triple your money;" and "you'll get it [*i.e.*, recover the soybean loss] out of the bond." These bold profit predictions did not remotely reflect the detrimental effect on profit potential by STC's heavy commissions.[19] Nadell's unrestrained profit predictions also induced unreasonable expectations of profits, which Nadell failed to temper. The fact that STC accurately disclosed the size of the commissions, and the fact that the first trade was profitable, still did not free Nadell to make unrestrained claims regarding profitability. *See Johnson v. Fleck*, [1990-1992 Transfer Binder] Comm. Fut. L Rep. ¶ 24,957 at pages 37,501-37,502 (CFTC November 20, 1990, Gramm concurrence) ("All else being equal, customers of a firm with a high commission or fee structure will have a more difficult time making a profit than those that employ a less expensive firm. As a result, the firm charging higher commissions and fees is more limited in what it can claim regrading profit potential.") Nadell's unrestrained claims of profits constituted at best reckless misrepresentations and deceptions in violation of CFTC rule 33.10 and Section 4c(b) of the Commodity Exchange Act. The proper measure of damages is Fager's $858 out-of-pocket losses.[20]

19/ Based on the experience of the undersigned, STC's commissions continue to be "one of the highest and most burdensome commission structures in the business." *Woyce v. STC, et al.*, [87-90 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,535 at page 36,316 (Initial Decision October 17, 1989).

20/ Fager's waiver of recovery based on an unjust enrichment theory has precluded an award based on the amount of the commissions, and has resulted in the near absurdity of awarding Fager $858, while respondents reaped over $9,000 in commissions while Fager's money was at risk.

Nadell's recommendation on November 1 to roll over the T-Bond position -- based on a belief that the price drop on November 1 signalled an end to the rally based on market expectations of an increase in the Fed prime rate and a belief that the December T-Bond puts would lack time to react to the Fed hike -- proved to be disastrous for Fager. However, the Commission has consistently held that it will not award reparations merely because the trading strategy chosen by a broker turns out unsuccessful, or because other available strategies would have been profitable, absent evidence of bad faith. *Vetrano v. Manglepus*, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶22,702 (CFTC 1985). This is based on a policy not to second-guess trading decisions so long as they are made with a reasonable basis. The mere fact that Fager would have met his investment objective of recouping his soybean losses had he just held the December T-Bond puts another week does not establish that Nadell's advice was made in bad faith or lacked a reasonable basis. Similarly, Nadell's one-tick reporting error is insufficient to establish a violation, because it appeared to be negligent at worst, and did not materially distort the fact that the market was down from its open.

Finally, Fager has failed to show any violations by Barrere or Lane proximately causing any damages.

ORDER

Robert Myron Nadell violated of CFTC rule 33.10 and Section 4c(b) of the Commodity Exchange Act by misrepresenting the potential profitability of trading with Siegel Trading Company, proximately causing $858 in damages. Siegel Trading Company, Incorporated, is liable for Nadell's violations under Section 2(a)(1)(A) of the Act. Accordingly, Siegel Trading Company, Incorporated, and Robert Myron Nadell are ORDERED to pay to Gregg Fager reparations of $858, plus interest on that amount at 5.67% compounded annually from November 1, 1994 to the date of payment, plus $125 for the cost of the filing fee. Liability is joint and several.

The complaint against Tijean Clement Barrere and James A. Lane is DISMISSED.

Dated March 20, 1997.

Philip V. McGuire,
Judgment Officer