

UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

In the Matter of

GRACE HSU and CMB CAPITAL
MANAGEMENT CORP.,

Respondents.

CFTC Docket No. 98-10

Administrative Law Judge
Bruce C. Levine

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**ORDER GRANTING THE DIVISION OF ENFORCEMENT'S MOTION FOR ENTRY
OF A DEFAULT ORDER, FINDINGS OF FACT AND CONCLUSIONS OF LAW AND
IMPOSITION OF SANCTIONS AGAINST RESPONDENTS GRACE HSU AND CMB
CAPITAL MANAGEMENT CORP.**

I. Introduction

On March 31, 1998, the Commission filed a three-count Complaint and Notice of Hearing, Pursuant to Sections 6(c) and 6(d) of the Commodity Exchange Act, as Amended, dated March 31, 1998 ("Complaint"), alleging violations of the antifraud provisions of the Commodity Exchange Act ("Act") and the regulations promulgated thereunder ("Regulations") by Grace Hsu ("Hsu"), CMB Capital Management Corp. ("CMB") and one other individual (collectively, "Respondents"). The Complaint charges that Hsu and CMB cheated or defrauded or attempted to cheat or defraud customers in violation of Section 4b(a)(i) of the Act, 7 U.S.C. § 6b(a)(i), effected unauthorized transactions in violation of Rule 166.2, 17 C.F.R. § 166.2, and failed to furnish customers with a risk disclosure statement in violation of Rule 1.55(a)(1), 17 C.F.R. § 1.55(a)(1).

The Complaint ordered that a hearing be held for the purposes of taking evidence on the allegations it set forth and determining whether an order should be entered: (1) directing the Respondents to cease and desist from further violations of the provisions of the Act and Regulations alleged in the Complaint; (2) prohibiting the Respondents from trading on or subject to the rules of any contract market and requiring all contract markets to refuse them trading privileges thereon; (3) revoking, suspending or restricting all registrations held by the Respondents; (4) assessing each of the Respondents a civil monetary penalty not to exceed \$100,000 or triple the monetary gain, whichever is greater, for each violation of the Act or Regulations committed prior to November 27, 1996, and not more than \$110,000 or triple the monetary gain, whichever is greater, for each violation of the Act or Regulations committed on or after that date, and (5) requiring the Respondents to make restitution to customers of damages proximately caused by the Respondents' violations of the Act or Regulations.¹

II. The Division's Default Motion

Rule 10.23(c) of the Commission's Rules of Practice, 17 C.F.R. § 10.23(c), provides that if a party fails to file an answer within 20 days following service of a complaint as set forth in Rule 10.22, 17 C.F.R. § 10.22, the party shall be in default and, pursuant to procedures set forth in Rule 10.93, 17 C.F.R. § 10.93, the proceeding may be determined against such party by the

¹ The Division of Enforcement ("Division") has indicted that, given the default of CMB and Hsu, the fact that the Division knows of no assets owned by CMB or Hsu, and that the Division has no information as to the whereabouts of Hsu, it is not seeking restitution in this matter. Division of Enforcement's Memorandum of Law in Support of its Motion for Entry of a Default Order, Findings of Fact and Conclusions of Law and Imposition of Sanctions Against Grace Hsu and CMB Capital Management Corp., dated February 22, 1999 ("Division's Memorandum"), at 13 n.41; see Division of Enforcement's Motion For Entry of a Default Order, Findings of Fact and Conclusions of Law, and Imposition of Sanctions Against Grace Hsu and CMB Capital Management Corp., dated February 22, 1999 ("Division's Motion"), at 1-2.

Court upon its consideration of the complaint, the allegations of which shall then be deemed to be true.

On May 1, 1998, the Court issued a Notice of Default whereby it deemed CMB and Hsu in default. On February 23, 1999, the Division filed the instant Default Motion. The Division's Default Motion asks this Court to:

a. enter a default order;

b. find that, among other things:

1. CMB, through Hsu, and Hsu defrauded customers by failing to disclose the risks of futures trading, trading customers accounts without authorization, and misrepresenting the reasons customers accounts no longer would be maintained at a futures commission merchant;
2. CMB, through Hsu, and Hsu engaged in unauthorized trading in three customer accounts;
3. CMB, through Hsu, failed to provide some customers with complete copies of the required risk disclosure statement; and
4. CMB, through Hsu, and Hsu knowingly provided some customers with the risk disclosure statement in a language they could not read, and misrepresented and downplayed the significance of the required risk disclosure statement in discussions with customers;

c. hold that:

1. CMB, through Hsu, and Hsu cheated or defrauded or attempted to cheat or defraud customers and prospective customers in connection with commodity futures transactions, in violation of Section 4(b)(a)(i) of the Act;
2. CMB, through Hsu, and Hsu engaged in unauthorized trading in three customer accounts in violation of Section 166.2 of the Regulations;
3. CMB, through Hsu, failed to provide customers with complete copies of the required risk disclosure statement in violation of Section 1.55(a)(1) of the Regulations;

4. CMB, through Hsu, knowingly provided customers with the risk disclosure statement in a language they could not read, and misrepresented and downplayed the significance of the required risk disclosure statement so as to vitiate the acknowledgment that the customers had read and understood the statements warning and to nullify the significance of the risk disclosure statement's warnings ab initio in violation of Section 1.55(a)(1) of the Regulations;² and

² The Division posits that Rule 1.55(a) has implicit requirements. Specifically, it argues that Rule 1.55 requires brokers to provide a risk disclosure statement printed in a language that the customer can understand. Division's Memorandum at 10-11. In addition, it asserts that fraudulent, vitiating statements that undermine the gestalt of a risk disclosure statement violate Rule 1.55 as well as general, anti-fraud provisions. Id. In the case of vitiating by affirmative conduct, this is no simple question of semantics. The requirements of Section 1.55 are absolute. Batra v. E.F. Hutton & Co., Inc., [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,937 at 34,286-87 (CFTC Sept. 30, 1987); Sher v. Dean Witter Reynolds, Inc., [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,266 at 29,370 (CFTC June 13, 1984). In other words, liability is strict. Id. If the Court were to accept the Division's argument, the Division would be able to establish liability for a broad spectrum of affirmative, fraudulent statements without proof of scienter. In the context of reparations, a failure to comply with such implicit requirements would also trigger a presumption of reliance. Batra, ¶ 23,937 at 34,286-87. A rule that would produce these results is contrary to the weight of Commission case law and other rule-making.

The Division cites Knight v. First Commercial Fin. Group, Inc., [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,942 (CFTC Jan. 14, 1997), and Wang v. Trans-American Commodity Corp., [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,651 (ALJ July 1, 1985), for the notion that, even if a broker strictly complies with the express provisions of Rule 1.55, vitiating statements or conduct not only violate anti-fraud provisions but also violate Rule 1.55. Division's Memorandum at 11 n.37. These cases do not provide a basis that can support that structure. Wang held that when a commodity trading advisor, by its associated person and principal, "knew that the complainant's command of the English language was limited" and "urged and permitted the complainant to" execute English language "risk disclosure documents without explanation," it violated Sections 4b and 4c of the Act. Wang, ¶ 22,561 at 30,755. Wang made no mention of Rule 1.55 or any other Commission regulation relating to disclosure. Knight involved vitiating conduct. ¶ 26,942 at 44,554-55. However, it also involved a failure to comply with Rule 1.55's technical requirement of providing a "'separate' risk disclosure statement." Id. at 44,555. The Commission described the failure to comply with the express terms of the regulation as "fail[ure] to comply with Rule 1.55." Id. It opined that vitiating conduct "nullif[ied] the significance of the risk disclosure statement's warnings ab initio." Id. In other words, the Commission did not say that vitiating conduct amounted to the violation of Rule 1.55. Rather, it ruled that respondents could not rely on the provision of a vitiating risk disclosure statement, standing alone, to satisfy their Section 4b disclosure obligation or to render affirmative misrepresentations non-fraudulent. Id. at 44,555-

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56. Accordingly, the Commission made an express finding that the vitiating statements violated Section 4b. Id. at 44,556.

Curiously, the Division's appeal to case law avoids the two cases that have directly addressed the issues raised. Gemeinder v. Gartmann, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,068 at 45,100 (ALJ May 30, 1997), considered a claim based on a broker's failure to provide a risk disclosure statement in the German language when a broker "knew that German was" the customer's language. Judge Painter found that "[t]here are no provisions in the Act or in Commission Regulations which mandate that risk disclosure statements be written in the primary language of the investor." Id. at 45,104. Accordingly, he went on to opine that a claim, based on a broker's failure to provide risk disclosure documents in a language that the customer understood, if "cognizable, . . . would have to be under Section 4b(a)." Id. These observations find corroboration in recent regulatory history. In its explanation of amendments to Rule 1.55, the Commission apparently recognized the problem that non-English-reading customers posed. See Protection of Commodity Customers; Risk Disclosure by Futures Commission Merchants and Introducing Brokers to Customers; Bankruptcy Disclosure, 57 Fed. Reg. 46101, 46103 (1992). It addressed this problem by giving brokers the option of providing a foreign-language translation of the Rule 1.55-required disclosure document. Protection of Commodity Customers; Risk Disclosure by Futures Commission Merchants and Introducing Brokers to Customers; Bankruptcy Disclosure, 58 Fed. Reg. 17495, 17497 (1993). However, the Commission did not require the provision of such a translated, written statement. Id. ("[T]he Commission intends that the consolidated risk disclosure statement may be presented to a non-English speaking customer in the foreign language that such customer understands rather than in English, provided that the disclosure statement provided is an accurate translation of the English version and the English text is provided upon request." (emphasis added)).

In a recent reparations case, the Court considered the question of whether Rule 1.55 posed implicit requirements and provided the following explanation.

"Complainants maintain that strict, 'technical compliance' with the enumerated requirements of Rules 1.55 and 33.7 is insufficient to fully comply with those regulations. They do so on grounds of the 'fundamental law that one cannot do something and not do it at the same time' and, therefore, '[r]espondents did not comply with the letter or spirit of the Rule.' Regardless of whether this statement of 'fundamental law' is tautologically correct, the underlying factual basis does not exist with regard to Webster's account and Rules 1.55 and 33.7. Rules 1.55 and 33.7 are technical in the sense that substantial, but imperfect, compliance with the three enumerated requirements has been found to constitute a violation. Accordingly, just as the Court must apply

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5. Hsu aided and abetted CMB's violations of Section 1.55(a)(1) of the Regulations, and therefore, pursuant to Section 13(a) of the Act, is liable for those violations;

d. impose sanctions on Hsu and CMB as follows:

1. civil monetary penalties of \$300,000;
2. cease and desist orders;
3. an order prohibiting Hsu and CMB from trading on or subject to the rules of any contract market, and requiring all contract markets to refuse them all trading privileges thereon; and

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those rules strictly, it has good reason to construe them strictly. McCarthy v. Northwest Airlines, Inc., 56 F.3d 313, 316 (1st Cir. 1995). Employing the long-held rule of statutory construction expressed in the maxim expressio unius est exclusio alterius, the Court will presume that the requirements listed in the rules are the only requirements of compliance. Tennessee Valley Auth. v. Hill, 437 U.S. 153, 188 (1978). . . . However, that does not preclude the possibility that respondents violated Section 4b or 4c(b) by affirmatively vitiating the risk disclosure statement. It simply means that proof of such affirmative vitiation does not shift the burden of proving reliance from complainants to respondents nor does it eliminate the complainants' need to prove scienter."

Webster v. Aiello, CFTC Docket No. 98-R005, 1999 WL 41818, at *35 n.404 (CFTC Feb. 1, 1999) (citations to the record and cross-references omitted). The Division has presented no reason to abandon Webster's reasoning.

In a sense, this particular discussion is academic. For reasons set out below, and detailed in the attached findings, the Court finds that respondents' knowing vitiation by affirmative misrepresentation and knowing failure to disclose trading risks, by providing only written risk disclosures that they were aware some of their customers could not read, amount to violations of the Act meriting sanctions. See infra note 4. Because it is the nature of this violative conduct, rather than the number of theories under which the Division may establish violations, that figures into determining what sanctions the conduct ultimately merits; having found fraud, the Court has no need to consider the alternative theories of liability. In re Interstate Securities Corp., [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,295 at 38,954-55 (CFTC June 1, 1992).

4. an order revoking Hsu's registration as an associated person and CMB's registration as an guaranteed introducing broker.

III. Procedural History

On or about April 1, 1998, the Commission's Office of Proceedings, pursuant to Section 10.22(b) of the Regulations, mailed a copy of the Complaint by certified mail to CMB at its last known address, 133-38 41st Road, 2nd Floor, Flushing New York, 11355.

On or about April 1, 1998, the Commission's Office of Proceedings, pursuant to Section 10.22(b) of the Regulations, mailed a copy of the Complaint by certified mail to Hsu at her last known address of 133-38 41st Road, Flushing New York, New York 11355.

Since the service of the Complaint by the Commission's Office of Proceedings, Hsu and CMB have not filed appearances, requested extensions of time within which to answer, filed answers or otherwise pled to the Complaint. Pursuant to Rule 10.23(c), the Court, on May 1, 1998, issued a Notice of Default deeming Hsu and CMB in default.

IV. Default Order Standards

Under Rule 10.93, when a respondent has failed to file an answer as provided in Rule 10.23, the Division may request that the Court enter a default order against a defaulting respondent and enter findings and conclusions based on the allegations of the complaint, which shall be deemed to be true for purposes of this determination.³

As the court has issued a Notice of Default as to Hsu and CMB, this matter is ripe for an entry of a default order, findings of fact and conclusions of law, and imposition of sanctions.

³ 17 C.F.R. § 10.93. In re Global Link Miami Corp., [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,391 at 46,781-88 (CFTC June 26, 1998), provides a detailed discussion of the
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V: DEFAULT ORDER

Respondents Hsu and CMB, having failed to file an answer to the Complaint as provided in Rule 10.23, the Court having issued, on May 1, 1998, a Notice of Default against Hsu and CMB, and the Division having filed the Default Motion, the Court hereby **GRANTS** the Default Motion. Accordingly it is hereby **ORDERED** that:

1. The Default of CMB and Hsu is **ENTERED**.
2. The Findings of Fact and Conclusions of Law attached hereto are **ENTERED**.
3. The Court further **FINDS** that, during the period of time covered by the Complaint:
 - a. Hsu cheated or defrauded or attempted to cheat or defraud customers and prospective customers in connection with transactions in futures contracts, in violation of Section 4b(a)(i) of the Act, and CMB is liable for Hsu's violations of Section 4b(a)(i) of the Act pursuant to Section 2(a)(i)(A)(iii) of the Act;
 - b. Hsu effected unauthorized transactions, in violation of Section 166.2 of the Regulations and CMB is liable for Hsu's violations of Section 166.2 of the Regulations pursuant to Section 2(a)(i)(A)(iii) of the Act;
 - c. CMB, through Hsu, failed to provide customers with complete copies of the required risk disclosure statement in violation of Section 1.55(a)(1) of the Regulations;
 - d. Hsu aided and abetted CMB's violations of Section 1.55(a)(1) of the Regulations and, therefore, pursuant to Section 13(a) of the Act, is liable for those violations.
 - e. CMB, through Hsu, knowingly provided customers with the risk disclosure statement in a language they could not read and misrepresented

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effect of a default under the Part 10 rules and the Court's role in determining the merits of a case in a default proceeding.

and downplayed the significance of the risk disclosure statement so as to defraud customers in violation of Section 4b(a)(i) of the Act;⁴ and

⁴ As presaged above and set out here, the Court finds that respondents violated Section 4(b)(i) when they knowingly disclosed risk by means of a writing that the customer could not read and provided no other risk disclosure. The Court is hesitant, however, to find liability under this pure omission theory, given the real possibility that such a rule amounts to a step onto a slippery slope. Harris v. Connelly, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,919 at 41,016 n. 25 (CFTC Jan. 3, 1994). Harris included the following Federal Trade Commission discussion of why this is so.

"The Commission does not treat pure omissions as deceptive, however. There are two reasons for this. First, we could not declare pure omissions to be deceptive without expanding the concept virtually beyond limits. . . . Second, pure omissions do not presumptively or generally reflect a deliberate act on the part of the seller, and so we have no basis for concluding, without further analysis, that an order requiring corrective disclosure would necessarily engender positive net benefits for consumers or be in the public interest.

"If we were to ignore this last consideration, and were to proceed under a deception theory without a cost-benefit analysis, it would surely lead to perverse outcomes. The number of facts that may be material to consumers . . . is literally infinite. . . . Since the seller will have no way of knowing in advance which disclosure is important to any particular consumer, he will have to make complete disclosures to all. A television ad would be completely buried under such disclaimers, and even a full-page newspaper ad would hardly be sufficient for the purpose. . . . The resulting costs and burden on . . . communication would very possibly represent a net harm to consumers."

Id. (quoting In re International Harvester Co., 104 F.T.C. 949, 1059-60 (1984)). Accordingly, the Court limits this holding to the precise facts of this case and may very well revisit the issue. The Court finds that providing the required risk disclosure in a language that the customer cannot read amounts to a Section 4b(i) fraud only when: (1) the Act or a Commission regulation expressly requires disclosure of the information, (2) the information is "technically" disclosed but done so in a manner that amounts to no actual communication of any of the bare information that the Act or regulation specifically requires and (3) the brokers knows (or with regard to this fact has a reckless state of mind) that the technical disclosure amounts to no (as opposed to imperfect or unattended to) communication of the information. This ruling does not extend to those situations when: (1) disclosure of the information is not expressly and precisely required under the Act or Commission regulation, (2) disclosure is made but imperfectly attended to, (3)

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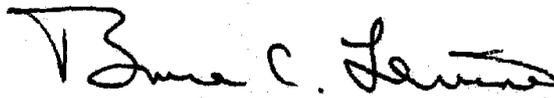
- f. Hsu aided and abetted CMB's violations of Section 4b(a)(i) of the Act and, therefore, pursuant to Section 13(a) of the Act, is liable for those violations.

4. It is hereby further **ORDERED** that:

- a. Hsu and CMB are hereby each assessed a civil monetary penalty of \$300,000;
- b. Hsu and CMB shall cease and desist from further violations of the provisions of the Act and Regulations which they have been found to have violated;
- c. Hsu and CMB are prohibited from trading on or subject to the rules of any contract market, and all contract markets are directed to refuse Hsu and CMB all trading privileges thereon; and
- d. Hsu's registration as an associated person and CMB's registration as an guaranteed introducing broker are revoked.

IT IS SO ORDERED.

On this 6th day of April, 1999



Bruce C. Levine
Administrative Law Judge

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disclosure is made but not in the optimal manner and (4) the information is disclosed but in terms that are arcane or general, but no less so than the express language required under the Act or Commission regulations. See Clayton Brokerage Co. v. CFTC, 794 F.2d 573, 581 (11th Cir. 1986) ("the [Commission-mandated risk disclosure] uses terms of art that require explanation").

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Administrative Law Judge
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FINDINGS OF FACT AND CONCLUSIONS OF LAW

I. Findings of Fact

A. Respondents

1. CMB Capital Management Corp. ("CMB") is a New York corporation. Its last known address is 133-38 41st Road 2nd Floor, Flushing, New York 11355. CMB has been registered with the Commission as a guaranteed introducing broker since August 23, 1996. Complaint and Notice of Hearing, Pursuant to Sections 6(c) and 6(d) of the Commodity Exchange Act, as Amended, dated March 31, 1998 ("Complaint"), ¶ 4.

2. Grace Hsu ("Hsu") is an individual whose last known address is 133-38 41st Road, Flushing, New York 11355. Hsu has been registered with the Commission as an associated person ("AP") of CMB since August 23, 1996 and listed as a principal of CMB, where she was employed from approximately August 23, 1996 until mid-July 1997. Hsu was also the sole stockholder and president of CMB. Complaint, ¶¶ 3,10.

B. Proceedings to Date

3. On March 31, 1998, the Commission filed the Complaint. The Complaint alleges violations of Section 4b(a)(i) of the Commodity Exchange Act (the "Act") and Sections 1.55 and 166.2 of the regulations promulgated thereunder ("Regulations") on the part of Hsu, CMB, and another individual (collectively, the "Respondents"). The Complaint ordered that a hearing be held for the purposes of taking evidence on the allegations set forth in therein and determining whether an order should be entered: (1) directing the Respondents to cease and desist from further violations of certain provisions of the Act and Regulations; (2) prohibiting the Respondents from trading on or subject to the rules of any contract market and requiring all contract markets to refuse them trading privileges thereon; (3) revoking, suspending or restricting all registrations held by the Respondents; (4) assessing each Respondent a civil monetary penalty of not more than \$100,000 or triple the monetary gain, whichever is greater, for each violation of the Act or Regulations committed prior to November 27, 1996, and not more than \$110,000 or triple the monetary gain, whichever is greater, for each violation of the Act or Regulations committed on or after that date; and (5) requiring the Respondents to make restitution to customers of damages proximately caused by their violations of the Act or Regulations.

4. On or about April 1, 1998, the Commission's Office of Proceedings ("Proceedings"), pursuant to 17 C.F.R. § 10.22(b), mailed a copy of the Complaint by certified mail to CMB at its last known address of 133-38 41st Road, 2nd Floor, Flushing, New York 11355. Affidavit of Glenn M. Jones, Esq., dated February 15, 1999 ("Jones Aff."), ¶ 3.

5. On or about April 1, 1998, Proceedings, pursuant to Rule 10.22(b), mailed a copy of the Complaint, by certified mail, to Hsu at her last known address of 133-38 41st Road, Flushing, New York 11355. Jones Aff., ¶ 3.

6. In the time since Proceedings served the Complaint, neither CMB nor Hsu has filed an appearance, requested any extension of time within which to answer, filed an answer or otherwise pled to the Complaint. Jones Aff., ¶ 4.

7. On May 1, 1998, the Court, pursuant to 17 C.F.R. § 10.23, issued a Notice of Default, deeming CMB and Hsu in default. Notice of Default, dated May 1, 1998, at 5; Jones Aff., ¶ 5.

C. Fraud and Non-Disclosure

8. Unless stated otherwise, the period relevant to the allegations in the Complaint is from at least August 23, 1996 to July 1997. Complaint, ¶ 9.

9. From on or about August 29, 1996 to on or about June 12, 1997, CMB introduced over 50 accounts to three futures commission merchants ("FCM"). Complaint, ¶ 11.

10. CMB and Hsu solicited customers by advertising free futures trading seminars in Chinese-language newspapers and by asking for and receiving referrals from CMB customers and seminar participants. Complaint, ¶ 11.

11. Hsu conducted the seminars and encouraged prospective customers to open futures trading accounts. Hsu recommend to prospective customers that their friends open accounts at CMB as well. Complaint, ¶11.

12. When CMB customers opened accounts:

- a. Hsu knew that some customers only spoke Chinese and those customers could not read English well enough to understand the risk disclosure statement and other account-opening documents. Complaint, ¶¶ 15, 16.
- b. Hsu often rushed customers to fill out the documentation, including the acknowledgement for the risk disclosure statement which some customers could not read. Complaint, ¶¶ 12-13, 15-16.

- c. Hsu filled out much of the account documentation, often reporting to the carrying FCM fictitious income and net worth information for the customers. Complaint, ¶ 13.
- d. Hsu told customers that their signatures on the risk disclosure statements were merely formalities to be completed before one could begin trading. Complaint, ¶ 12.
- e. Hsu never told customers the full extent or nature of the risks inherent in futures trading. Complaint, ¶ 17.

13. Some CMB customers were not provided with a complete, written risk disclosure statement to read and Respondents did not provide those customers with an explanation as to the contents of the risk disclosure statement. Complaint, ¶ 14.

14. On April 23, 1997, CMB was informed, in writing, by one of its FCMs, Swiss Financial Services ("SFS"), that over 20 of CMB customers' accounts were undermargined and that margin calls were being made on those accounts. Complaint, ¶ 22.

15. SFS informed CMB that, in order to satisfy these margin calls, CMB customers had to wire funds to SFS no later than April 24, 1997, and that, if the funds were not received by wire transfer before the close of business on April 24, 1997, SFS would liquidate the open futures positions on April 25, 1997. Complaint, ¶ 22.

16. Hsu did not tell CMB customers that money had to be wired to SFS before the close of business on April 24, 1997, to meet the margin calls and she accepted checks from CMB customers who were trying to meet the margin calls. Complaint, ¶ 22.

17. On April 25, 1997, SFS liquidated the CMB customers' accounts for which margin calls had been made but not satisfied. Complaint, ¶ 22.

18. After SFS liquidated CMB's customers' accounts for failure to meet the margin calls, SFS informed CMB, in writing, that CMB customers would no longer be allowed to trade at SFS. Complaint, ¶ 23.

19. After receiving this information, Hsu falsely told CMB's customers that CMB had decided, because of SFS's poor service, that CMB would no longer do business with SFS. In addition, Hsu told CMB customers that the liquidation of CMB customer accounts on April 25, 1997, pursuant to the margin call, had been caused by SFS's wrongdoing. Hsu then recommended that CMB customers transfer their accounts to another FCM. After this recommendation, many CMB customers transferred their accounts to the FCM recommended by CMB. Complaint, ¶ 24.

D. Unauthorized Trades

20. The known customer accounts introduced by CMB were non-discretionary accounts, that is, accounts for which trades could be made only after a customer, or the customer's designee, provided specific authorization to place the trade. Complaint, ¶ 18.

21. Typically, CMB customers holding non-discretionary accounts traded pork belly futures, many times at the recommendation of Hsu. Complaint, ¶ 18.

22. Beginning in May of 1997, Hsu engaged in the unauthorized trading of at least three customer accounts. First, Hsu placed 10 unauthorized pork belly trades in one customer's account while the customer was away in Hong Kong. These unauthorized trades, established and liquidated between May 30 and June 12, 1997, resulted in a loss of \$102,698. Complaint, ¶ 19.

23. On June 12, 1997, Hsu engaged in unauthorized trading for two other accounts. She placed three trades in pork belly futures in one, and four such trades in the other. Complaint, ¶ 20.

24. Hsu placed the June 12, 1997 pork belly trades in the customers' accounts without authority. Hsu's unauthorized trading on June 12, 1997 resulted in losses of \$6,630 for one customer and \$36,160 for the other. Complaint, ¶ 21.

II. Conclusions of Law

A. Default

1. Pursuant to 17 C.F.R. § 10.23(c), a party that fails to file an answer within 20 days following service of a complaint, as set forth in 17 C.F.R. § 10.22, shall be in default. Pursuant to procedures set forth in 17 C.F.R. § 10.93, the proceeding may be determined against such party by the Court upon consideration of the complaint, the allegations of which shall be deemed to be true. Hsu and CMB have failed to file an answer, as required, and the Court, on May 1, 1998, issued a Notice of Default, finding that Hsu and CMB were in default. Therefore, this matter is ripe for an entry of a default order, findings of fact and conclusions of law, and the imposition of sanctions against CMB and Hsu.

B. Violations of the Act and Regulations

2. Section 4b(a)(i) of the Act makes it 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 . . . for or on behalf of any other person . . . to cheat or defraud or attempt to cheat or defraud such other person." 7 U.S.C. § 6b(a)(i).

3. To prove a violation of Section 4b(a)(i), it must be established that a respondent knowingly or recklessly defrauded or attempted to defraud customers. Hammond v. Smith Barney, Harris Upham & Co., [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,617 at 36,658-59 (CFTC Mar. 1, 1990); Knight v. First Commodity Fin. Group, Inc., [Current

Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,942 at 44,556 (CFTC Jan. 14, 1997); see also First Commodity Corp. v. CFTC, 676 F.2d 1, 6-7 (1st Cir. 1982).

4. A misrepresented or omitted fact is material if it is substantially likely that a reasonable investor would consider it important in making an investment decision. Sudol v. Shearson Loeb Rhoades Inc., [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,748 at 31,119 (CFTC Sept. 30, 1985).

5. By engaging in intentional conduct that included a failure to disclose the risks of futures trading, discounting the significance of risk disclosure statements, trading customer accounts without authorization, and misrepresenting the reasons customer accounts no longer would be maintained at SFS, Hsu cheated or defrauded or attempted to cheat or defraud customers. Therefore, Hsu violated Section 4b(a)(i) of the Act. Herman v. T&S Commodities, Inc., 578 F. Supp. 601, 603 (S.D.N.Y. 1983).

6. CMB is liable for Hsu's violations of Section 4b(a)(i) of the Act, pursuant to Section 2(a)(1)(A)(iii) of the Act, because Hsu--AP, sole shareholder and president of CMB--was acting within the scope of her office or employment with CMB. Under the strict liability provisions of Section 2(a)(1)(A)(iii) of the Act and Rule 1.2, "[t]he act, omission, or failure of any official, agent, or other person acting for any individual, association, partnership, corporation, or trust within the scope of his employment or office shall be deemed the act, omission, or failure of such individual, association, partnership, corporation, or trust, as well as such official, agent, or other person." 7 U.S.C. § 4; 17 C.F.R. § 1.2. See Stotler and Co. v. CFTC, 855 F.2d 1288, 1292 (7th Cir. 1988); Rosenthal & Co. v. CFTC, 802 F.2d 963, 967 (7th Cir. 1986) ("[T]he only question is whether the [misconduct] was within the scope of his agency.").

7. Pursuant to 17 C.F.R. § 166.2, no IB nor any of its APs may directly or indirectly effect a trade for the account of any customer unless the customer or person designated by the customer to control the account specifically authorizes the IB or AP to effect the transaction. See Peltz v. SHB Commodities, Inc., 115 F.3d 1082, 1087-88 (2d Cir. 1997).

8. Hsu knowingly placed 17 trades for three non-discretionary customer accounts without being authorized to trade for those accounts by the customers holding the accounts or by persons designated by those customers to control the accounts, or without being authorized in writing to effect transactions in commodity interests for the accounts without the customers' (or the customers' designees') specific authorization. Therefore, Hsu violated Rule 166.2. See Peltz, 115 F.3d at 1087-88 (holding that Rule 166.2 imposes a standard of "reasonable" care).

9. CMB is liable for Hsu's violations of 17 C.F.R. § 166.2, pursuant Section 2(a)(i)(A)(iii) of the Act, because Hsu--AP, the sole shareholder and president of CMB--was acting within the scope of her office or employment with CMB. See Rosenthal & Co., 802 F.2d at 967.

10. Rule 1.55(a)(1) provides that "no [FCM], or in the case of an introduced account no [IB,] may open a commodity futures account for a customer unless the [FCM] or [IB] first . . . furnishes the customer with a separate written disclosure statement." 17 C.F.R. § 1.55(a)(1).

11. CMB is liable for violating Rule 1.55(a)(1). This liability is based upon CMB's, through Hsu, failure to provide a number of customers with complete copies of the mandatory risk disclosure statement.

12. To be liable as an aider and abettor under Section 13(a) of the Act, 7 U.S.C. § 13c(a), a respondent "must knowingly associate himself with an unlawful venture, participate in it as something that he wishes to bring about and seek by his actions to make it succeed." In re

Commodities Int'l Corp., [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,943 at 44,564 (CFTC Jan. 14, 1997).

13. Hsu aided and abetted CMB's violations of Section 1.55 of the Regulations by failing to provide customers with complete copies of the risk disclosure statement.

C. Sanctions

14. Sections 6(c) and 6(d) of the Act, 7 U.S.C. §§ 9 and 13b, authorize, as sanctions against a respondent upon a determination that such respondent has violated the Act or Regulations, the entering of an order that: (1) directs a respondent to cease and desist from further violations of the provisions of the Act and Regulations that are found to have been violated; (2) prohibits a respondent from trading on or subject to the rules of any contract market and requiring all contract markets to refuse such respondent trading privileges thereon; (3) revokes, suspends or restricts all registrations held by a respondent; (4) assesses, upon a respondent, a civil monetary penalty not to exceed \$100,000 or triple the monetary gain, whichever is greater, for each violation of the Act or Regulations committed prior to November 27, 1996, and not more than \$110,000 or triple the monetary gain, whichever is greater, for each violation of the Act or Regulations committed on or after that date, and (5) requires a respondent to make restitution to customers of damages proximately caused by that respondent's violations of the Act or Regulations.¹

¹ The Division of Enforcement ("Division") has indicted that, given the default of CMB and Hsu, the fact that the Division knows of no assets owned by CMB or Hsu, and that the Division has no information as to the whereabouts of Hsu, it is not seeking restitution in this matter. Division of Enforcement's Memorandum of Law in Support of its Motion for Entry of a Default Order, Findings of Fact and Conclusions of Law and Imposition of Sanctions Against Grace Hsu and CMB Capital Management Corp., dated February 22, 1999 ("Division's Memorandum"), at 13 n.41; see Division's Motion For Entry of a Default Order, Findings of

15. A cease and desist order is appropriate where there is a reasonable likelihood of future violations by a respondent. In re Dillon-Gage, Inc., [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,574 at 30,482-83 (CFTC June 20, 1984). One indicator of the likelihood of future violations is the existence of a pattern of misconduct. Id.

16. Upon consideration of the record, the Complaint and the materials filed in support of the Division's Motion, the Court finds that there is a reasonable likelihood that CMB and Hsu would commit future violations of the Act and Regulations. The violations in this case occurred repeatedly and over a period of more than 10 months. Accordingly, they amount to the kind of pattern of misconduct that warrants the imposition of an order that directs CMB and Hsu to cease and desist their violative acts and practices.

17. A revocation of Hsu's and CMB's registrations is appropriate, as they have engaged in intentional conduct that included, among other things, material misrepresentations regarding customers' relationships with SFS, fraud regarding the risks of futures trading and unauthorized trading in violation of the Act and Commission regulations. Section 8a(3)(A) of the Act provides that the Commission "may . . . refuse to register . . . [any] person, if it is found, after opportunity for a hearing, that . . . such person has been found by the Commission or by any court of competent jurisdiction to have violated . . . any provision of this [Act], or any rule, regulation, or order thereunder." 7 U.S.C. § 12a(3)(A); see also In re Sanchez, CFTC Docket No. 82-5,1984 WL 48105, at *8 (CFTC Jan. 31, 1984). Additionally, Section 8a(3)(M) provides that the Commission may refuse to register, condition, suspend, revoke or place restrictions upon the registration of any person if it is found, after opportunity for a hearing, that "there is other

Fact and Conclusions of Law and Imposition of Sanctions Against Grace Hsu and CMB Capital Management Corp., dated February 22, 1999 ("Division's Motion"), at 1-2.

good cause.” 7 U.S.C. § 12a(3)(M). An intentional violation of the Act or Commission regulations generally amounts to “other good cause” within the meaning of Section 8a(3)(M) and 8a(4) of the Act. In re Kelly, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,289 at 46,305-06 (ALJ Feb. 24, 1998), aff’d in part, modified in part, 1998 WL 802091 (CFTC Nov. 19, 1998). Section 8a(4) provides the authority “to suspend, revoke, or place restrictions upon the registration of any person registered under this [Act] if cause exists under [Section 8a(3)] which would warrant a refusal of registration of such person.” 7 U.S.C. § 12a(4). It has been established that violations similar to those committed by Hsu and CMB, as well as violations that are less serious, constitute grounds for revocation of registration under the Act. See, e.g., In re Saryk, CFTC Docket No. 95-5, 1998 WL 834656, at *11 (CFTC Dec. 4, 1998) (“Saryk Order On Remand”); In re Clark, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,032 at 44,927 (CFTC Apr. 22, 1997); Kelly, ¶ 27,289 at 46,305-06 (finding “other good cause” based on a willful failure to respond to a Division request for documents pursuant to 17 C.F.R. § 1.31(a)); In re Saryk, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,701 at 43,938 (ALJ June 5, 1996) (“Saryk ID”) (revoking, with reference to Section 8a(2)(E) of the Act, 7 U.S.C. § 12a(2)(E), the registration of an AP who engaged in options fraud by misrepresenting, among other things, the nature of trading risks in customer solicitations), aff’d in part, vacated in part, remanded in part [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,207 (CFTC Dec. 18, 1997).

18. Trading prohibitions are appropriate when a respondent’s conduct adversely affects the integrity of the futures market. In re Citadel Trading Co., [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,082 at 32,191 (CFTC May 23, 1986). “Trading prohibitions are appropriate where there is a nexus between [a] respondent’s violations and the

integrity of the futures market." Staryk ID, ¶ 26,701 at 43,938. "A nexus exists when a respondent's misconduct represents an inherent threat to the market." Id. This threat "is sufficiently present where the conduct erodes '[p]ublic perception, protection, and confidence in [the] markets.'" Id. (citing In re Miller, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,440 at 42,914 (CFTC June 16, 1995)). A trading prohibition is appropriate in this case because CMB's and Hsu's actions directly undermined the integrity of the futures markets, by lowering their esteem in the public eye, since CMB and Hsu engaged in fraud and unauthorized trading. See Miller, ¶ 26,440 at 42,913-14 (quoting, with approval, In re Paragon Futures Assoc., [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 25,266 at 38,852 (CFTC Apr. 1, 1992) (Dial, Commissioner, concurring in part and dissenting in part)); see also Staryk Order On Remand, 1998 WL 834656, at *11 (imposing a permanent trading ban of an AP who engaged in options fraud by misrepresenting, among other things, the nature of trading risks in customer solicitations).

19. The Division seeks the imposition of a \$300,000 fine upon Hsu and CMB each. Division's Memorandum at 15.

20. Commission policy embraces imposing penalties that have both a specific and general deterrent effect and, when possible, rest on a respondent's gains or customer losses. Kelly, ¶27,289 at 46,307-08, and Staryk ID, ¶26,701 at 43,939-42. The Court prefers a gains-based standard as a regulatory approach. In cases where the customer losses outweigh the respondent's gain, the Court consider that as an aggravating factor. In addition, "deterrence theory dictates that [a gains-based] penalty include a premium to offset the benefit of engaging in undetected illegal conduct. Penalties are set such that the amount of the penalty multiplied by the perceived probability of detection exceeds the expected gain of the violative act." In re Fritts, [1994-1996

Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶26,255 at 42,133 (CFTC Nov. 2, 1994) (citation omitted). Congress has endorsed a multiplier of three or more. See 7 U.S.C. § 9.

21. In this case, the Court is unable to impose a gains-based or customer-loss-based penalty with the usual, necessarily rough precision. The record does not indicate the gains that Hsu and CMB derived from their violative conduct nor, with the exception of the \$145,488 in losses attributed to unauthorized trading, does it detail or approximate customer losses resulting from all of the violations that have been found to have occurred.

22. The Commission has imposed substantial civil monetary penalties based on the social costs that certain violations impose without regard to customer losses or a respondent's gains. See, e.g., In re New York Currency Research Corp., [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,223 at 45,915 (CFTC Feb. 6, 1998) (imposing a \$110,000 civil monetary penalty, for one failure to provide records upon request, solely on grounds of the "serious nature of the violation"); In re Rousso, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,133 at 45,311 & n.22 (CFTC Aug. 20, 1997). See In re R&W Technical Servs., Ltd., [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,193 at 45,734 n.119 (ALJ Dec. 1, 1997), aff'd in part, modified in part, vacated in part, CFTC Docket No. 96-3, 1999 WL 152619 (CFTC Mar. 16, 1999). In such cases, the Commission has sought to impose fines that are "commensurate with the gravity of the violation[s]." Rousso, ¶ 27,133 at 45,311. The activity in this case not only involved grave violations of the Act, it involved violations that occurred repeatedly over a substantial period of time. Accordingly, the Court finds that substantial civil monetary penalties are warranted with respect to Hsu and CMB. At this point and eschewing any "simple formulaic solutions," the Court could enter into an interminable exploration of factors including, but not limited to: (1) "the relationship of the violation[s] at

issue and the . . . purposes of the Act," (2) "respondent[s] state of mind," (3) "the [private and social] consequences flowing from the violative conduct," (4) "respondent[s] post-violation conduct," (5) "Commission-approved penalties in analogous cases," and (6) "particular mitigating or aggravating circumstances." In re Grossfeld, [Current Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,921 at 44,467-68 (CFTC Dec. 10, 1996). At the end of such a process, the Court would arrive at a specific level of penalties that would undoubtedly differ from the Division's proposed fines. However, there is no reason to believe that such a specific figure would be any more precise. Accordingly, the Court finds that Hsu should be assessed a civil monetary penalty of \$300,000 and that CMB should be fined \$300,000.