U.S. COMMODITY FUTURES TRADING COMMISSION
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PROCEEDINGS

BRIAN JACOBSEN, Complainant, v. COMMONWEALTH FINANCIAL GROUP, INC., GERRI STERNFELD, and MICHAEL FRIEDMAN, Respondents.	*	CFTC Docket No. 96-R67

INITIAL DECISION

Before: McGuire, Judgment Officer

Appearances: Brian Jacobsen, *pro se*

Steven Halfhill, Esq. and Christopher Holley, Esq., for respondents

Brian Jacobsen alleges that respondents deceived and defrauded him throughout the solicitation and trading of his account. Jacobsen's principal allegations are that Gerri Sternfeld exaggerated the track record of respondents' trading strategy; that Tom Clancy, Jr., perpetuated Sternfeld's track-record fraud during the account-opening compliance review; and that Sternfeld and Michael Friedman made a variety of deceptive or false statements about risk, profit potential, trade results, and account status in order to generate excessive commissions. Respondents deny any wrongdoing.

The findings and conclusions below are based on the complaint, the answer, complainant's replies to respondents' discovery requests, the parties' replies to discovery orders issued by the undersigned, and the parties' oral testimony, and reflect my determination that complainant's testimony was significantly more reliable and credible than respondents' testimony.

On the whole, after careful consideration of the parties' demeanor, the substance of their oral and written testimony, and their documentary submissions, I have found that the preponderance of the evidence establishes: (1) that Sternfeld and Commonwealth falsely represented that the consistent, predictable nature of the "seasonal" demand and price trends in the heating oil market translated into an increased likelihood of dramatic profits and a corresponding decreased risk of loss; (2) that Sternfeld's message of essentially inevitable and dramatic profits was unrealistic and deceptive because the vast majority of Sternfeld's customers had lost money; (3) that Sternfeld made grossly misleading statements about the track record of Commonwealth's trading strategy; (4) that Commonwealth employee Tom Clancy, Jr., perpetuated Sternfeld's fraudulent statements about Commonwealth's track record; (5) that Friedman misrepresented his expertise and the likelihood of making profits; and (6) that Sternfeld and Friedman engaged in a strategy to increase commissions which involved falsely representing that Jacobsen should buy more options to increase

his profits, misrepresenting trading results and the cost of recommended trades, and recommending the purchase of excessive option contracts. Unless otherwise noted, dates are in 1995, and amounts are rounded to the nearest dollar.

The Parties:

1. Brian Jacobsen, a resident of Waterloo, Iowa, is the manager of a franchise restaurant and has a high school education. At the time that he opened his Commonwealth account, he had no experience with futures or options and a limited two-year experience with the stock market. On the account application, he listed his net worth as under $50,000 and his annual income as between $25,000 and $50,000 [Respondents' May 10, 1996 discovery production, and Jacobsen's reply to respondents' interrogatory 4.]

2. Commonwealth Financial Group, Incorporated ("CFG"), located in Ft, Lauderdale, Florida, has been a registered introducing broker since 1992.

CFG principally compensated Sternfeld and Friedman with a percentage of commissions paid by their clients. [Hoffecker declaration, produced June 18, 1996.]

3. Gerri Sternfeld was an associated person with CFG since from March 1995 to July 1995. She was previously associated with Cromwell Financial Services, Global Futures Services and Universal Commodity Corporation. After working for CFG, she worked for Barley Financial Corporation, and is currently employed by FSG International.

Sternfeld's testimony about the performance of her CFG customer accounts was generally evasive and unconvincing. However, she did reluctantly testify that most of her customers had failed to close their accounts with profits. Sternfeld's testimony also indicated that at the time that Jacobsen opened his account, few if any of the approximately 20 accounts handled by her had realized any overall net profits. [Pages 105-112 of hearing transcript.]

4. Michael Friedman has been an associated person with CFG since December 1993.

Respondents' Records of Conversations with Jacobsen:

5. Sternfeld and Friedman did not maintain telephone logs of their conversations with Jacobsen, and CFG did not require them to do so. [*See* respondents' reply to ¶ 2 of May 7, 1996 Order; and Sternfeld's and Friedman's testimony at pages 99-100 and 142-143, respectively, of hearing transcript.] Therefore, Commonwealth's tape recordings of these conversations are the only routine records of communications with Jacobsen.[1/]

6. In response to an order compelling production of all tape-recordings of all conversations with Jacobsen, respondents produced recordings for 14 conversations on the following dates:

1/ During the relevant time, the National Futures Association ("NFA") required Commonwealth to tape-record all telephone conversations between its brokers and their customers as a sanction in a membership responsibility action ("MRA"). *In re Commonwealth Financial Group, Incorporated,* NFA Case No. 94-MRA-001 (Decision dated February 27, 1995), *affirmed* Comm. Fut. L. Rep. [Current Transfer Binder] (CCH) ¶ 26,993 (CFTC March 18, 1997), *appeal filed* April 4, 1997 (11th Cir.).

August 18 (2 conversations); September 1 (3); September 5 (2); September 12; September 13 (3); September 27 (2); and October 2. However, respondents did not produce recordings for significant conversations during Sternfeld's solicitation on the following dates: August 23, 24, 28, 29, 30 and 31 (2:27 p.m.).[2/] Also, respondents did not produce recordings for significant conversations on September 5 (fill report); September 8 (regarding payment for second option purchase); September 12 (recommendation to roll-over option position to fund a second option purchase); September 20 and 21 (sell recommendation); September 22 (fill report); between September 22 and 27 (regarding heating oil losses); September 29 (Jacobsen's attempt to sell profitable position); and all of Friedman's conversations after October 2. Pursuant to CFTC rule 12.35, respondents' failure to produce the recordings for these dates is grounds for making adverse inferences that the recordings not produced would have tended to support Jacobsen's assertions, and would have tended to contradict Sternfeld's and Friedman's assertions, concerning these conversations.

Sternfeld's Solicitation:

7. Jacobsen called a toll-free telephone number after viewing a television infomercial promoting the profits to be made in options on corn futures. [*See* Jacobsen's reply to

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[2/] The existence of these calls was established by an itemized phone bill for this time period that was produced by Commonwealth's phone company in reply to a subpoena. *See* Notice dated October 29, 1996.

respondents' interrogatory 25; ¶ 5 of respondents' discovery production filed May 10, 1996; and Sternfeld's testimony at pages 102-103 of hearing transcript.]

8. On August 18, 1995, Sternfeld called Jacobsen. Sternfeld represented that options were less risky than futures because any loss would be limited to the purchase amount, but also said that "the profit potential was limitless." Sternfeld first discussed supply and demand factors, such as bad weather and disease, that she said would drive up the price of corn, and used two hypothetical examples where a $5,000 investment yielded 300% and 150% profits. Sternfeld then said that the "worst case scenario" would involve the loss of Jacobsen's entire investment, but strongly implied that this would be unlikely by giving a hypothetical example where the U.S. Department of Agriculture predicted the largest bumper crop in 20 years, despite all of the factors mentioned by Sternfeld that strongly supported projections of lower production.

When Jacobsen expressed concern about the risk, Sternfeld represented that the risk could be managed with stop-loss orders, and gave an example where stops would be adjusted upward to lock-in ever-increasing profits as the option increased in value. Sternfeld also alleviated Jacobsen's concern by promising that she and CFG's research department would act as his "navigators" and maintain daily "constant contact."[3/]

[3/] Sternfeld regularly repeated these types of assurances. For example, on September 1 when she reported the fill price, she promised "keep you posted."

Sternfeld then shifted the discussion to heating oil options, which she described as her "top recommendation." Sternfeld's message was that a dramatic increase in the price of heating oil was imminent based on seasonal price patterns repeated for sixteen straight years, and that an options customer could exploit this knowledge to realize extraordinary profits by buying before demand peaks, with only the price of the option premium at risk. Sternfeld represented that the heating oil market had "gone up every year that it [had] traded, which is 16 years going from the end of the summer to the end of the year," and that the heating oil market had a "nice track record of working every year." Sternfeld never clearly and fairly explained that she was discussing price patterns in the cash and futures markets rather than the options markets, and never disclosed that heating options had not begun trading until 1987. [*See* page 26 of hearing transcript.]

In connection with the purported heating oil "track record," Sternfeld mentioned that this consistent historical performance did not necessarily mean that "past performance is indicative of future results," but immediately undercut this cursory proviso by emphasizing that the market had always gone up even in the "worst years ever" when the fundamentals were weak, that some of the greatest price run-ups had occurred in years with "nothing too unusual" happening, and that various fundamental factors, such as tensions in the Persian Gulf, pointed to a "very good year" with a greater than average price jump. Sternfeld then concluded by

representing that heating oil had a "bit of better track record" than corn, that CFG had a "very sophisticated research department" that "really makes a difference," and that she would be sending Jacobsen materials on the corn and heating oil markets.[4/] Jacobsen reasonably concluded from Sternfeld's statements that "this year would be no different then, if the past 16 years . . . went up an average of . . . eight cents, or whatever she told me -- that this year would be no different." [Page 21 of hearing transcript.] At the end of this conversation, Jacobsen said that he would need about a week to evaluate the information provided by Sternfeld.[5/] [*See* Jacobsen testimony at pages 8-22 of hearing transcript.]

9. Sternfeld sent to Jacobsen a CFG account-opening package which included "Special Reports" on heating oil and on grains. [Respondents' May 10, 1996 production.] Commonwealth's heating oil special report comported with Sternfeld's solicitation and featured the following description of Commonwealth's heating oil strategy:

TAKING ADVANTAGE ...HEATING OIL OPTIONS

The key to successful investing is maximizing your

[4/] Sternfeld's testimony about the basis for her various representations about "worst case scenarios," "track records," and CFG's supposedly "sophisticated" research department, was especially evasive and unconvincing, and showed that she had no reasonable basis for making these statements. [*See* pages 112-118 of hearing transcript.]

[5/] During this week, Jacobson contacted the Miami Better Business Bureau which told him that CFG was a firm in good standing, and that the CFTC's civil lawsuit against CFG was "closed." Jacobson's reply to respondents' interrogatory 23.

> profit potential while controlling your risk. That's why we believe that purchasing options on futures could be the ideal way to speculate in these enormously promising markets. . . .
>
> To the speculator, this remarkable mix of unlimited potential and limited risk means "staying power" -- the ability to remain in the market for a specified time, even in the face of possible short term price swings.
>
> While the potential for substantial upward price moves seems enormous, the gains we anticipate may take some time. The market could suffer short term dips. That's why we believe that by purchasing call options, you can remain in the market right up to the expiration date of your options . . . or exit the market earlier any time before expiration.
>
> In our opinion, the time to participate in the exciting heating oil market is now. Call your Commonwealth Financial Group Broker to get our strategies on heating oil options **NOW!**

[Emphasis and ellipsis in original, page 10 of heating oil special report; *see* Jacobsen's testimony at page 25 of hearing transcript.]

The heating oil special report stated that for sixteen straight years cold weather patterns had caused the price of heating oil to increase between June and December, and predicted increased demand in 1995 the use of heating oil based on increased inclement weather caused by El Nino and the Mount Pinatubo eruption, the embargo on Iraqi oil and an expected U.S. energy tax. The Heating Oil Special Report also contained a table titled "Heating Oil Futures June to December" that asserted that, since 1979, from June to December the price of heating oil futures had increased an average of $21. [Jacobsen's discovery replies filed June 26, 1996.]

Sternfeld did not adequately explain that the information in the special report reflected futures prices and not options prices, and did not explain that the price movements of heating oil futures and of heating oil options often differed dramatically. She also did not explain how radically futures and options price movements could differ, and otherwise pointedly avoided a meaningful explanation of the futures/options distinction in the context of the seasonality trading strategy promoted by her and CFG. For example, she never alluded to the fact that a seasonal increase in the demand for unleaded gasoline would not necessarily result in the increased value of a gasoline option, because the market had already factored seasonal demand into the price of the option. Also, she never mentioned that the past trends in gasoline futures prices had proven dismally ineffective at forecasting the current profitability of options on gasoline futures contracts.

10. Both sides' versions of events differ most dramatically on the existence or non-existence of a second conversation after August 18 and before August 31. Sternfeld and Commonwealth claim she spoke to Jacobsen just once before he sent in account-opening documents, and that Sternfeld was "surprised" when on August 31 she received the account-opening package signed by Jacobsen. [*See* ¶ 3 of answer and ¶ 2 of respondents' discovery production dated June 14, 1996.] Also, Jacobsen credibly testified that he asked Sternfeld how many of CFG's customers had made money, and she replied that "for every winner, there is a loser," and

replied affirmatively when Jacobsen asked her if this statement meant that she and CFG had a "50/50" success ratio with customer trades. [Pages 29-31 of hearing transcript.] Significantly, reliable phone records establish a 24-minute call from CFG to Jacobsen on August 23, which supports Jacobsen's assertion that this conversation took place, and contradicts respondents' assertion that this conversation did not take place.[6/]

Sternfeld's implicit claim of a fifty percent success rate distorted respondents' actual success rate by 333% to 1,000%, assuming a 5% to 15% success rate.

11. Jacobsen then decided to open the account and signed the account-opening documents. On August 31, he mailed a check for $4,300.

12. On September 1, Sternfeld called Jacobsen and recommended that he buy four January heating oil calls. Sternfeld also advised Jacobsen that when he placed his order, the CFG compliance department would conduct a compliance review which she characterized as a "little formality." [*See* Sternfeld's testimony at pages 118-119 of hearing transcript.]

13. During the compliance review, Jacobsen confirmed that his investment decision was based on the mistaken assumption that he was entering an investment with a "50/50" chance of making

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[6/] The telephone bill also established outgoing calls from CFG to Jacobson during the solicitation on the following dates: August 24 at 3:49 p.m. (7.2 minutes); August 28 at 10:39 a.m. (1.8 minutes); August 29 at 1:46 p.m. (5.9 minutes); August 30 at 1:53 p.m. (16.4 minutes) and at 7:38 p.m. (1.0 minute); and August 31 at 2:27 p.m. (11.6 minutes). (Other calls under one minute have not been included here.)

money. As can be seen, the CFG compliance reviewer, Tom Clancy, Jr., made no meaningful attempt to cure Jacobsen's obvious misunderstanding that he had an even chance of making or losing money:

> *Clancy:* Can you explain to me what you feel the risk is with this type of investment?
>
> *Jacobsen:* Oh, right around probably 50/50.
>
> *Clancy:* 50/50. can you be a bit more descriptive there? I mean -- I don't understand -- 50/50 is what? I mean --
>
> *Jacobsen:* Oh, either make it or lose it.
>
> *Clancy:* Well, you've sent us $4,300. Is it my understanding that your risk is only half of that?
>
> *Jacobsen:* Yeah. Ok.
>
> *Clancy:* Is that what you are saying?
>
> *Jacobsen:* No. it's a matter of make it or lose it, it could go 50/50 to lose it all, or it could make money off of it.
>
> *Clancy:* Ok. That's what I'm trying to find out and I didn't know what you were trying to say. That is correct. You are at risk for the full amount of the money, the $4,300 that you sent in.
>
> *Jacobsen:* Yeah.

Trading Activity:

14. Sternfeld would recommend three heating oil trades, for which Jacobsen would pay $1,350 in commissions and fees. The first trade initiated on September 1, and stopped out on September 22, realized a $1,935 net loss (four January calls with

a 54 strike price);[7] the second trade initiated on September 5, and stopped out on September 20th, realized a $615 net loss (one December call with a 54 strike price); and the third trade initiated on September 13, and stopped out on September 21, realized a $250 net loss (one January call with a 56 strike price).

15. On September 5, Jacobsen's account had $124 in available cash. That day, Sternfeld called Jacobsen and told him that the four January options were "ahead" by 35 cents over the 195-cent purchase price -- *i.e.*, at 230 cents -- which she represented as a $147 per-contract profit. However, at 230 cents, the options were actually trading below the 245-cent break-even point.[8] [*See* page 119 of hearing transcript.] Sternfeld then told Jacobsen that he was likely to make $4,200, if he sent in another $850 to buy another heating oil option, and "you're really going to see a lot more money if you have more leverage." Jacobsen then agreed to purchase another heating oil option (one December call with a 54 strike price). [*See* pages 35-36 and 119-121 of hearing transcript.]

The option actually cost $960. Respondents did not produce the recording of the conversation when Sternfeld reported the fill price and instructed Jacobsen how to cover the deficit

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[7] On Sternfeld's recommendation, on September 12, Jacobson had to sell one of the January 54-strike price options to cover the purchase cost of a December option. The $141 net loss on this sale is included in the total $1,935 net loss mentioned in the text.

[8] The options would eventually settle that day above the break-even point.

resulting from this purchase. According to Jacobsen, Sternfeld indicated that he had until Monday, September 11, to pay for this purchase. Jacobsen expected that the clearing broker would receive the check by Saturday, September 9, or Monday, September 11, since he had sent the check by an express service on Thursday, September 7. Sternfeld and Jacobsen did not speak on Monday, September 11.

16. On Tuesday, September 12, the clearing broker issued a margin call and also issued a confirmation statement that reported that Jacobsen's check had been received that day. Because discovery was not taken of the clearing broker, on this record it cannot be established precisely when the check was received, or whether the margin call was issued in error, or whether the margin call was issued earlier that day before the check had been received.

In any event, that same day, Sternfeld called Jacobsen and told him about the margin call. Sternfeld advised Jacobsen either to wire immediately additional funds, or to sell one of the January options in which case he could repurchase a January option once his check was received. Jacobsen authorized the sale of one January option and realized a $121 net loss. Jacobsen credibly testified that Sternfeld did not report to him that he had lost money in this sale.[9/] [Pages 36-38 of hearing

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[9/] The account statements reported gross profits, but not net profits. For example, for this trade, the account statement reported an $84 gross profit -- the "premium collected" -- for this trade, but did not report the $121 net loss (the difference between (continued...)

transcript.]

17. On September 13, the January options traded between 200 and 220 cents and settled at 201 cents -- above the 195-cent purchase price, but well below the break-even price; and the December option traded between 135 and 180 cents -- barely above the 175-cent purchase price and well below the break-even price. That day, Sternfeld called Jacobsen to represent that his options were profitable and to urge him to buy one more option:

> So we need to buy that one position now. I'm looking at the screen. Heating oil, by the way, is up again. So, so you know, <u>everything's going very well for our heating oil positions</u> on -- we need to buy that one position now. . . . Obviously they're a little more expensive than when we initially started, which means <u>you're making money with these</u>.

Later that day Sternfeld called Jacobsen to report the fill price:

> The heating oil . . . it's doing good. So, <u>we're doing good in the oil</u>. We actually should have a good year, as far as the oil. I'm very excited about that -- you know the strength of the movement so early in the season. Actually I wish you had more contracts. But, you know, you can only do what you do.

[Emphasis added.] Sternfeld then agreed with Jacobsen when he replied that "hopefully when they pay off . . . I'll do it again." Jacobsen reasonably interpreted Sternfeld's statements as representations that his options were in actual net profits. [*See* pages 38-39 and 124-125 of hearing transcript.]

9/ (...continued)
the gross $84 profit and the $125 in commission and fees). Thus, Jacobson relied on respondents to provide accurate oral reports of trade results.

18. On September 20, the December option was stopped out; on September 21, the January 56-strike option was stopped out; and on September 22, the three January 54-strike options were stopped out. These three trades realized an aggregate net loss of $2,800. Jacobsen credibly testified that Sternfeld never called him to report that all of his positions had been stopped out. [Page 40-41 of hearing transcript.]

19. On September 27, Michael Friedman called Jacobsen. Respondents produced inconsistent explanations for why Friedman called Jacobsen. On one hand, respondents jointly asserted in their answer, and Sternfeld testified, that CFG had "moved" some of Sternfeld's accounts, including Jacobsen's account, to Michael Friedman, because she was unable to "service" all of them adequately. [¶4 of answer; and pages 101-102 of hearing transcript.] On the other hand, Friedman testified that he considered Jacobsen to be Sternfeld's client, and that he was merely "assisting" Sternfeld. [Pages 128-134 of hearing transcript.]

Friedman told Jacobsen that Sternfeld had asked him to call Jacobsen and "help" Jacobsen, and effectively represented that he had been making money for CFG clients by trading the S & P 500 Index options. Friedman claimed that: "one of my jobs is to try to get sometimes clients back in to the market and make money. And what I trade a lot is the S & P 500 Index. . . . <u>we have been trading this market since December, and it's been a great market for us</u>." [Emphasis added.] Friedman told Jacobsen that he had

$1,850 in the account and that with that amount he could pay for the purchase of two S & P 500 Index options. Friedman then strongly implied that Jacobsen could realize a quick $1,000 profit on an $1,850 investment:

> Now, what you need to see -- this is a very fast moving market, and what you need to see to break even, instead of 54 points in the heating oil, you need to see 45 points in this option. So if you pick up, let's say, at 140 points, you need to see it go to 185 points to break even.
>
> Now, let me give you some examples here.[10/] Let's just say we get to 185 points, we get our break-even point. If the market goes -- if the option goes to, say, 285 points -- now 285 times 5, that's going to be $1,425 minus the $925 you spend. You'll make a $500 profit. But with two positions you will make about a $1,000 profit. Okay? And this market, it's very easy to go up to 100 points in the option, okay, in a very short period of time. . . . The trend of the market is going higher. . . . And I think this is a very good trade for you.

Jacobsen's testimony established that he had reasonably concluded from Friedman's statements that CFG clients had been profitably trading S & P Index options. Furthermore, Friedman's own testimony established that he had no reasonable basis to be strongly implying or representing that CFG clients had been generally realizing profits trading S & P 500 Index options. [*See* pages 41-45 and 133-136 of hearing transcript.]

The order would be filled at 150 points, rather than the 140 points portrayed by Friedman, resulting in a $110 deficit.

20. On Friday, September 29, Friedman told Jacobsen that the options were up $500, and recommended that Jacobsen adjust

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10/ Friedman would only give the one example quoted here.

the stop-loss order to 185 points.[11/] Later that day, Jacobsen decided to that $500 was a good enough profit and called CFG. When Jacobsen told Sternfeld that he wanted to sell the options, she told him to speak to Friedman. However, Friedman was unavailable and did not return Jacobsen's call. [Pages 45-46 of hearing transcript.]

21. On Monday, October 2, the market opened at 170 points, activating the stop-loss order. The options were sold at 170 points, resulting in a $250 net loss and $1,600 in available equity. Friedman then urged Jacobsen to jump right back into the market by buying October options, and he also represented that the funds from the sale of the December options would cover the cost of the October options. As can be seen, Friedman did not know the fill price on the option sale:

> *Friedman:* Our stop worked for us here, the market came down a little bit. . . . The market looks strong today. I want to get right back in and pick up two October contracts at a better price. . . .
>
> Okay, so looks like we got it stopped out at about 185 where we raised the stop to. It's trading right now -- it did trade as low as 170 here. It's coming back a little bit. The market looks strong today.
>
> I want to go right back in and pick up two October contracts at a better strike price, which would be a 600 strike price. The market's trading right now at 587. So in my opinion it's close to the money. And these expire on 10/20.
>
> Now on this rate initially I won't place a stop in the market, and <u>I'm not going to even utilize all of the funds, I don't believe</u>. So what I want to do if you can write this down. I want to pick up two

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11/ On September 29, the option opened at 250 points (also the daily high) and closed at 225 points (also the daily low).

October S&Ps at a 600 strike price, calls at the market, and they expire on 10/20. It's a short-term trade to see if we can catch some action in the market going higher for us here. And we will go from there. All right?

Jacobsen: Hang on just a second. Well, I don't have much money left in the account then?

Friedman: Well, if we got stopped out at 185, times 5, that's $1,850, and we are looking to spend here $825 times two, about $1,650. Or, we might even spend less than that. I don't know yet.

Jacobsen: No, I think I'm done. Just go ahead and pull me out.

Friedman: You're sure?

Jacobsen: Yeah

Friedman: The market looks strong. Market was going for us before.

Jacobsen: We should have sold at that $500 when I made it.

Friedman: Well, that's what we wanted to see if we could get a little bit more money here. Now the market looks very strong, and you know we had a good trade there, we just got stopped there out with a little profit-taking and that's why I wanted to raise the stop. Because if the market went against us it would go even -- it was -- obviously it did go even a little lower. Okay, so the stop worked for us so we could get back in to the market at even a better strike price. The 600's, instead of the 620's. You follow me?

Jacobsen: Yeah.

Friedman: Go with me on this one trade. I'll put a 50 percent stop behind this ticket, and if it works for us fantastic we'll make some money. If it doesn't, then I'll send you that balance home.

Is that fair enough? Because I think the market's good. That's why Gerri asked me to give you a call, because I play this stock market here, the S&Ps, and it's been doing very well for us here.

> And just you up two positions here. And I'll place the 50 percent stop behind this buy ticket, so we are only risking just a portion of it. And it's just going to be a short-term trade. We're only looking to stay in this a matter of some time this week. We'll be in and out probably some time this week.
>
> *Jacobsen:* Okay, I can do it. All right?

Friedman's testimony that his statement that the S&P 500 index option had "been doing very well for us" related to market volatility, rather than to customer performance, was particularly specious. This unconvincing testimony supports the conclusion that Friedman had no basis to represent, or strongly imply, that his customers had been realizing profits trading the S&P 500 index option. [Pages 131-134 of hearing transcript]

The total purchase cost for the two October options was $1,850, resulting in a $250 deficit.

22. The next day, October 3, Friedman called Jacobsen and informed him that he had to either wire additional funds or liquidate one contract. Jacobsen reminded Friedman that he had already told Friedman that he had intended <u>not</u> to invest any additional funds, and authorized the sale of one October option. This forced liquidation resulted in a $375 net loss. On October 6, the second October option was stopped out. [See pages 48-49, 81-82 and 138-142 of hearing transcript.]

23. The trades recommended by Friedman generated $900 in commissions and fees, and realized aggregate net losses of $1,250.

Commonwealth's Notice about the U.S. District Court Contempt Order:

24. At about the same time that Sternfeld and Jacobsen first spoke, CFG was obligated by a United States District Court to inform current and prospective customers of the court's findings of numerous antifraud violations by CFG, its owner and its account executives by providing copies of the contempt order provide notification to CFG's current and prospective customers of the Court's contempt order.[12/]

CFG could not substantiate its initial assertion that it had delivered the court-ordered notice to Jacobsen in September 1995. [13/]

12/ *CFTC v. Commonwealth Financial Group, Inc., and Charles Paul Hoffecker*, No. 92-6692-CIV-RYSKAMP (S.D. Fla.). On October 19, 1992, the district court granted the preliminary injunction enjoining CFG and its owner, Charles P. Hoffecker, from violating the antifraud provisions of the Act. On December 28, 1994, the district court issued an order ("contempt order") holding that CFG and Hoffecker had violated the antifraud provisions of the Act during the period of the preliminary injunction, from October 1992 to August 1994, by misrepresenting risk, exaggerating profit potential,and misrepresenting their experience and training. By Order dated August 16, 1995, the district court imposed various civil sanctions, including the requirement that CFG and Hoffecker, from August 16, 1995 to August 15, 1997, inform current and prospective customers of the court's findings of antifraud violations by providing copies of the contempt order. The August 10 order also directed CFG and Hoffecker not to "disavow, downplay or otherwise attempt to minimize the serious nature of the Court's finding of contempt." In another portion of the injunctive proceeding, on August 31, 1994, the district court denied the CFTC's request for a permanent injunction. On appeal, the U.S. Court of Appeals for the Eleventh Circuit vacated the district court's order and remanded the case for further proceedings. *CFTC v. Commonwealth Financial Group, Inc., and Charles Paul Hoffecker*, 79 F.3D 1159 (February 21, 1996). This matter is currently pending.

13/ The notice consisted of a one-page form letter signed by Charles P. Hoffecker, the owner of CFG, with a copy of the district court's order denying the permanent injunction and the contempt (continued...)

[*See* ¶ 3 of Respondents' Response to Request for Supplemental Information (filed October 10, 1996); pages 6-8 of hearing transcript; and ¶ 4 of respondents' Answer.] In contrast, Jacobsen credibly testified that he did not receive the notice until after he had closed his account -- sometime in October, 1995. Jacobsen also credibly testified that he would not have opened the account if he had known of the contempt order. [Pages 49-50 of hearing transcript.]

Conclusions

The record supports numerous direct violations of Section 4c(b) of the Commodity Exchange Act and CFTC rule 33.10 by Gerri Sternfeld, Tom Clancy, Jr., Michael Friedman, and Commonwealth Financial Group, as well as Commonwealth's liability for Sternfeld's, Clancy's and Friedman's violations under Section 2(a)(1)(A) of the Act.

Sternfeld fraudulently induced Jacobsen to open an account with Commonwealth Financial Group by claiming that the predictable nature of the seasonal demand and price trends in heating oil essentially assured that the likelihood of dramatic

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13/ (...continued)
order attached. In substance and organization, the Hoffecker letter obscured the purpose of the notification and downplayed the seriousness of the contempt order. The first paragraph of the letter described the court's denial of the permanent injunction, and incorrectly stated that this ruling "closed the case." The second paragraph referred to the contempt order, claimed that CFG was no longer in contempt, and failed to mention that the contempt order had compelled CFG's notification. The last paragraph stated that CFG tape-recorded all conversations to "protect [Jacobson] from any misrepresentation or misunderstanding," but did not mention that the tape-recording was compelled by the NFA.

profits far outweighed the risk of loss generally associated with trading commodity options; by strongly implying a fifty percent success rate which distorted respondents' actual success rate by an extraordinary 333% to 1,000%; by using hypothetical examples that exclusively featured tremendous returns without any balancing reference to risk; by describing the total loss of funds as a "worst case scenario" that was unlikely to happen; and by falsely promising to be in daily contact.

Sternfeld failed to balance her explicit and implicit claims of profits that her customers were taking with the disclosure that the vast majority of her customers had failed to realize any profits. Sternfeld omitted several other material facts that would have at least partially cured her deceptive and false message of certain profits and reduced risk. For example, she failed to disclose that the past trends in heating oil futures prices had proved dismally ineffective at forecasting the current profitability of options on heating oil futures contracts, and that a seasonal increase in the demand for unleaded heating oil would not necessarily result in the increased value of a heating oil option, because the market had already factored seasonal demand into the price of the option. Finally, Sternfeld perpetuated her initial fraud and convinced Jacobsen to buy additional options by misrepresenting the value of open positions.

Clancy perpetuated Sternfeld's fraud by disregarding Jacobsen's obvious confusion about risk and profit potential.

Also, Clancy's compliance did not remotely convey the primary material fact of interest to any reasonable investor: that knowledge of the historical price movements discussed and portrayed in CFG's special report had absolutely failed to realize the sort of dramatic profits touted by Sternfeld. *See In re First National Trading Corporation*, [1992-1994 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,142, at p.41,788, n.20 (CFTC 1994); and *Swickard v. A.G. Edwards & Sons*, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,522, at p.30,275 (CFTC 1985).

Friedman perpetuated Sternfeld's fraud and convinced Jacobsen to buy additional options by implicitly claiming that he had made money for his clients when he had no reasonable basis to make such a claim. Friedman's misrepresentations about purchase cost and account equity were reckless at best where he knew that Jacobsen was reluctant to continue trading, had stated that he did not want to invest any additional funds, and had limited account equity.

Order

Violations having been established, Geri Sternfeld, Michael Friedman, and Commonwealth Financial Group, Incorporated, are ORDERED to pay to Brian Jacobsen reparations of $4,533.40, plus interest on that amount at 5.88% compounded annually from September 5, 1995 to the date of payment, plus $50 in costs. Liability is joint and several.

Dated June 19, 1997.

Philip V. McGuire,
Judgment Officer