



**U.S. COMMODITY FUTURES TRADING COMMISSION**

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LANCE A. JOHNSON,  
Complainant,

v.

BENSON-QUINN COMMODITIES, INC.,  
INFINITY TRADING GROUP, and  
CHRISTOPHER ANTHONY SMITHERS,  
Respondents.

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CFTC Docket No. 98-R197

**INITIAL DECISION**

Lance Johnson alleges that Christopher Smithers fraudulently solicited his account by misrepresenting the likelihood of profits and the risk of loss and that Smithers fraudulently induced him to float an option purchase without sending in the required funds. Respondents deny the allegations. As explained below, it has been concluded that Johnson has established that he is entitled to an award of \$5,040 for which the three respondents are jointly and severally liable. This conclusion is based on the documentary evidence and the parties' oral testimony, and reflects the determination of the undersigned that Johnson's testimony was more reliable and credible than the testimony of respondents' witnesses.

## Factual Findings

### *The parties*

1. Benson-Quinn Commodities, Incorporated ("B-Q") is a futures commission merchant, located in Minneapolis, Minnesota.
2. Infinity Trading Group was an introducing broker located in Jupiter, Florida, and guaranteed by B-Q during the relevant time. Infinity is no longer in business.
3. Christopher Anthony Smithers is currently a registered associated person and principal with Matrix Trading Group. Smithers was a registered associated person with Infinity from February 26, 1998 to July 31, 1998. Infinity compensated Smithers with a percentage of the commissions collected by Infinity. On March 5, 1998, the NFA granted Smithers a temporary license. By this date, Smithers had already begun his solicitation of Johnson's account.<sup>1</sup> Before the end of March 1998 and before Johnson opened his account with respondents, Smithers had agreed to reimburse \$19,204 to Infinity in connection with a series of misdeeds involving customer accounts, including permitting his sister to trade while her account was under-funded. Under this arrangement, Infinity withheld Smithers' commissions until he had satisfied the debt. See finding 17 below.

Smithers previously had been a registered associated person with American Futures Group, Ceres Trading Group and LMB Trading Group. On November 25, 1997, soon after Smithers had left Ceres to join LMB as a principal, Ceres initiated a breach of contract law suit that claimed that Smithers had stolen a Ceres customer list and convinced Ceres

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<sup>1</sup> Infinity's phone bill shows several lengthy phone conversations initiated by Smithers on March 4 and 5, 1998.

customers to switch accounts to LMB.<sup>2</sup> On December 30, 1997, the Illinois Circuit Court entered an order of default, and on April 28, 1998, the court entered judgment for \$14,000.<sup>3</sup> Smithers then entered into an agreement with Ceres involving monthly payments to satisfy the judgment. Thus, by late April 1998, Smithers was obligated to make substantial monthly payments to his current and his former employers.

4. Lance Johnson is an accountant with three dependents who resides in Salem, Oregon. When Smithers first contacted Johnson, Johnson was 25 years old, with an average annual income between \$25,000 and \$50,000, and a net worth of about \$114,000. Johnson had no investment experience except for a mutual fund.

As described below in more detail, a few days before Smithers first contacted Johnson, Johnson would open an account with another commodity firm. Then after a series of numerous and lengthy conversations with Smithers over six weeks, Johnson would transfer the account to Benson-Quinn.

***The solicitation:***

5. In late February of 1998, Johnson called a toll-free telephone number in response to a radio commercial claiming huge profits to be made trading heating oil and unleaded gasoline options, such as "\$2,000 to \$10,000 overnight." After leaving his name

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<sup>2</sup> Although Smithers did not disclose the pending Ceres law suit in his application to become a registered associated person with Infinity, he did disclose the Ceres lawsuit to the Infinity principal who hired him in late February of 1998, Jay R. Stoelting.

<sup>3</sup> Coincidentally, the next day Smithers would successfully convince Johnson to authorize a trade that would generate over \$4,000 in commissions.

and telephone number, Johnson received calls from a series of commodity brokers, first Mel Kline of American Financial Trading Corporation ("AFT"),<sup>4</sup> and later Smithers.

6. On February 27, 1998, Johnson opened an account with AFT. Johnson would invest \$11,919 with AFT. AFT charged a \$230 commission per option contract.<sup>5</sup> The trades recommended by Kline generated more than \$11,500 in commissions, and consumed almost all of Johnson's initial investment. The resulting commission-to-premium-paid ratio was about 30%.<sup>6</sup> The two trades completed before Johnson transferred the account to Benson-Quinn realized an aggregate trading loss of only \$440. However, the \$8,800 in commissions and fees swelled the loss to \$9,240.

On April 16, 1998, Johnson would instruct Kline to close the AFT account and to transfer an open unleaded gasoline option position to B-Q.<sup>7</sup> However, the position was not transferred until April 22, 1998, because Kline tried to convince Johnson to change his mind about transferring the account.

7. Between March 4 and April 16, 1998, Smithers and Johnson spoke 28 times on 17 different days.<sup>8</sup> Johnson told Smithers that he was disappointed with his AFT account because he was not making the profits promised by Kline. Smithers told Johnson that he would double Johnson's investment and recounted stories where he had made clients

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<sup>4</sup> Mel Kline has worked for a string of firms disciplined for fraudulent sales and trading practices, including Bachus and Stratton, Commonwealth Financial Group, and Multivest Options.

<sup>5</sup> AFT's commission charges included a \$200 "commission" and a \$30 "transaction fee." AFT also charged a small NFA fee and exchange fee, which was passed on to those organizations.

<sup>6</sup> The commission-to-premium-paid ratio represents the rate at which a long option must appreciate to overcome costs and merely break-even. Thus, a higher ratio indicates a greater cost burden and corresponding lesser likelihood of profit.

<sup>7</sup> Johnson had bought the ten unleaded gasoline calls at 1.80, paying \$7,560 in premiums and \$2,300 in commissions and fees. The break-even price was 1.92. The gas calls would trade at or above the 1.92 break-even price on April 16, 17 and 21. On April 22, the gas calls hit a high of 1.44 points.

<sup>8</sup> These numbers are based on calls lasting one minute or more that were reported in an itemized phone bill.

\$100,000 profits on \$2,000 investments in thirty days. Smithers did not mention any clients who failed to realize any profit. Smithers also told Johnson that AFT's commissions were excessive and astronomical, and promised that Infinity's commissions would be appreciably less. When Johnson told Smithers that he had no additional funds to invest, Smithers told him that he could use a current open gasoline option position to "cover" the cost of any new option purchases. Smithers also underplayed the importance of the account-opening documents. For example, when Smithers told Johnson where to sign the risk disclosure statement, he told Johnson not to worry about the risk of loss because that had never happened with his clients. At the hearing, Smithers conceded that most of his clients had failed to realize overall net profits.

8. On April 16, 1998, respondents received the account-opening package signed by Johnson. On April 16, the gas calls traded at a high of 1.85, with a liquidating value of \$7,728.

On April 22, 1998, the ten unleaded gasoline options were transferred from AFT to B-Q. Between April 16 and 22, Johnson told Smithers that he wanted to sell the gas options if they became profitable. However, when they would become profitable on May 1 and 4, Smithers would disregard Johnson's wishes.

9. On Wednesday, April 29, 1998, Johnson accepted Smithers' recommendation to buy ten July 1998 soybean calls, at 10 ½ cents or better. Smithers told Johnson not to worry about sending in money because he would be "in-and-out" with huge profits before he had to wire funds. Smithers also promised that, in the unlikely event that the soybean market did not perform as expected, he would closely monitor the trade and get Johnson out before the trade lost money. Smithers also instructed Johnson to tell the Infinity

compliance representative that he would be wiring money. Smithers convinced Johnson that such a lie would be harmless by repeating his promise that Smithers would get Johnson in and out with profits before he had to wire funds.

During the taped compliance review for this trade, the Infinity representative stated the estimated premium cost and commission cost per contract, estimated that the total cost would be \$6,930,<sup>9</sup> and calculated that the breakeven price would be 13 ½ cents based on a fill at 10 ½ cents.

Next, the agent and Johnson discussed funding the trade. The following portion of that conversation supports Johnson's contention that Smithers had advised him not to wire any funds and directed him to deceive the Infinity compliance representative about funding the trade:

*Infinity:* Now we are purchasing these options prior to your funds being received, and it is my understanding that you are going to be sending the funds to us via FedEx. Is that correct?

*Johnson:* He has money for me. Yeah.

*Infinity:* He has money?

*Johnson:* Well no. He's got my accounts, yes. So he [inaudible] money comes.

*Infinity:* Okay. So how much are you sending?

*Johnson:* Approximately \$7,000 to cover that.

*Infinity:* Okay. So you're going to be sending about \$7,000 FedEx. Is that correct?

*Johnson:* Yes.

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<sup>9</sup> However, the Infinity agent did not state the total commissions.

The order was filled at 10 cents for a total cost of \$6,682. At this fill price, the break-even price was 13 cents.

10. On Thursday, April 30, Johnson accepted Smithers' advice to buy fifteen more soybean options without sending in any funds. Smithers told Johnson to repeat his deception about wiring funds, and not to worry because the order would be taken by a different compliance representative. Infinity did not produce tape-recordings of these conversations with the compliance representative. Johnson first placed an order to buy five more soybean calls at 11 ½ cents or better, and later placed an order to buy an additional ten soybean calls, at 9 ½ cents or better. The first order was filled at 9 ¾ cents, and the second order was filled at 8 cents. The two orders were filled at a total cost of \$8,565.50.

11. For the 25 total soybean calls, Johnson was charged \$11,437.50 in premiums and \$4,205 in commissions and fees, for a total of \$15,642.50. Infinity charged a smaller commission per contract than AFT: \$168 compared to \$230. However, despite the fact that Smithers' had criticized AFT's commissions as excessive and astronomical, the trades recommended by Smithers actually resulted in a higher commission-to-premium-paid ratio than did the trades recommended by Kline: 35% compared to 30%.

12. Also on April 30, Johnson again reminded Smithers to sell the gasoline options if they were in profit. On May 1, the gas options would hit a high of 2.20, for a liquidating value of \$9,240. If sold at this price, the gasoline options would have realized a net profit \$1,680. However, Smithers never advised Johnson to place a sell order, and otherwise ignored his instructions.

13. The first entry in the telephone log produced by Infinity was dated May 4, and signed by Infinity's compliance director, Colin Flood:<sup>10</sup>

Reviewed cash, positions, gave margin calls and market quotes. Told him to talk to broker about strategy.

According to Johnson, Flood asked Johnson about the account deficit and accepted Johnson's explanation that Smithers "had everything handled."

14. On May 7, Smithers disregarded Johnson's request to sell the bean options, which were trading above the break-even price. On May 11, Johnson complained to Smithers, after he realized that Smithers had not sold the gasoline options or the bean options.

15. On May 14, Stoelting called Johnson and demanded that Johnson send in funds or Stoelting would have the federal marshals throw Johnson in jail. When Johnson informed Stoelting that Smithers had disregarded his sell instructions and had told him to lie about wiring funds, Stoelting reacted by supporting Smithers and questioning Johnson's integrity: "So, what you are telling me is, because you lied, that makes it okay."

After Johnson refused to wire funds, Infinity sold the 25 bean options and collected a \$8,437.50 premium, which resulted in a net loss and account deficit of \$7,206.00. Infinity then liquidated the gasoline calls, and collected a premium of \$4,200, which reduced the account deficit to \$3,006.

Benson-Quinn charged Infinity for the \$3,006 debit, and Infinity charged Smithers for half that amount.

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<sup>10</sup> The log also contains an entry by Flood on May 13 and entries by Stoelting on May 14 and 15. The log contains no entries by Smithers. Respondents did not produce Flood as a witness.

16. The gasoline options had declined \$5,040 between May 1, when Johnson had instructed Smithers to sell the gasoline options which then had a \$9,240 liquidation value, and May 14, when Infinity collected a \$4,200 premium.

17. On July 24, 1998, A. Colin Flood, the compliance director for Infinity, sent to the National Futures Association a letter which supplemented the Form 8T that Infinity had filed with NFA to terminate Smithers' registration with Infinity. Flood's letter stated in pertinent part:

Specifically, Smithers engaged in a pattern of conduct, which was inconsistent with the just and equitable principles of trade for several client accounts. He was not trustworthy or free of deceit. He did not exercise due care with his client funds as if they were his own.

He traded while under-capitalized: advising clients that they would not have to send in additional funds. He made trades without following internal office procedures and without client permission. He exercised high-pressure sales techniques and did not consistently follow up with clients after opening accounts.

Flood then separately described Smithers' misdeeds, including floating trades in the accounts of Johnson and Smithers' sister. Flood attached a debt repayment schedule which documented payments made by Smithers to compensate Infinity for its losses in connection with the listed misdeeds. This payment schedule shows that: (1) Before the end of March Infinity had already discovered the bulk of Smithers' misdeeds – including floating trades in his sister's account– and had obtained his agreement to begin payments; (2) Infinity had collected payments from Smithers by deducting his commissions (\$7,624 in April, \$6,504 in May, and \$7,149 in June); and (3) Smithers had agreed to pay half of the debit balance in the Johnson account, which contradicts Smithers' assertion in his reparations answer that he paid the full amount of the debit balance. [See pages 108-116 of hearing transcript.]

## Conclusions

Johnson has established by a preponderance of the evidence that Smithers defrauded him when soliciting the account, when recommending the purchase of the soybean options and when disregarding Johnson's instructions to sell the gasoline options. When Smithers convinced Johnson to switch his account from AFT to Infinity, he deceptively downplayed the risk of trading options with him and Infinity by essentially guaranteeing that Johnson would easily double his investment in a few days, by falsely stating that none of customers had ever lost money and that they typically had made astronomical profits, by falsely stating that Johnson could purchase options without adequate funding, and by falsely stating that Infinity's commission structure would be materially less burdensome than that of AFT. Smithers fraudulently obtained Johnson's authorization to buy the soybean options by falsely promising huge short-term profits, by falsely promising that Johnson would not lose on the trade, by falsely assuring Johnson that he could trade without adequate funding, and by recommending a trade that generated an effectively heavier commission burden than the trades in the AFT account – after Smithers had represented that Infinity's commissions would not be excessive. Smithers also disregarded Johnson's instructions to sell the gasoline and soybean options when they became profitable. Smithers' conduct constituted repeated violations of CFTC rule 33.10 and Section 4c(b) of the Commodity Exchange Act. The pervasive and blatant nature of his deceptive conduct underscores the intentional nature of these violations.

Although Johnson has shown that respondents are responsible for the losses on the fraudulently procured soybean trade, he has not shown that he suffered any financial loss on that trade because he never wired any funds to pay for that trade. However, he has

shown that he suffered a financial loss in connection with Smithers' fraudulent solicitation and refusal to follow Johnson's instructions to sell the gasoline options at a profit. Here, the proper measure of damages for the fraudulent solicitation is based on the 36-point (\$1,512) decline in value of the gasoline options from April 22, 1998, when the gasoline options were transferred to Benson-Quinn, to May 14, 1998 when the options were sold. The proper measure of damages for Smithers refusal to follow Johnson's sell-at-a-profit instruction is the 120-point (\$5,040) difference between the liquidation on May 14, 1998, and the high price on May 1, 1998. Since cumulative awards are not permitted in reparations, the larger amount will be awarded: \$5,040.

Infinity Trading Group is liable for Smithers' violations pursuant to Section 2(a)(1)(A) of the Commodity Exchange Act.<sup>11</sup> Benson-Quinn Commodities, Incorporated is liable as guarantor of Infinity Trading Group's obligations under the Act.

### ORDER

Benson-Quinn Commodities, Incorporated; Infinity Trading Group; and Christopher Anthony Smithers are ORDERED to pay to Lance A. Johnson reparations of \$5,040, plus interest on that amount at 5.471% compounded annually from May 1, 1998, to the date of payment, plus \$125 in costs for the filing fee. Liability is joint and several.

Dated November 30, 1999.

  
Philip V. McGuire,  
Judgment Officer

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<sup>11</sup> Johnson did not raise failure to supervise as a theory for recovery.