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UNITED STATES OF AMERICA
BEFORE THE
COMMODITY FUTURES TRADING COMMISSION

Charles A. McDaniel, Jr. and Alison L. McDaniel (Co-Trustees for the McDaniel Family Trust) and Alison L. McDaniel (Successor Trustee for Robert B. Miner Trust), Complainants	
v.	CFTC Docket No. 97-R057 CFTC Docket No. 97-R058
Amerivest Brokerage Services a/k/a Tradeline Brokerage Services LLC, Robert Ian Gorrie, Walter Frank Price and RB&H Financial Services LP, Respondents.	

ORDER OF CORRECTION

Typographical errors in the Initial Decision issued August 13, 1998, are herewith corrected, with the corrections set out in bold face type.

Page 4, line 5:
the Family Trust account on April 23, **1996,** was touted and recommended by Price and endorsed

Page 9, line 11:
thus implying that McDaniel would be using a system employed **by** professional insiders.

Page 9, line 19:
persisted from April 1996 to the date the accounts were closed in early **1997.** I find that

Page 11, line 8:
The co-trustees for Complainant McDaniel Family Trust **have** established by the

Issued this 17th day of August, 1998

George H. Painter
Administrative Law Judge

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UNITED STATES OF AMERICA
BEFORE THE
COMMODITY FUTURES TRADING COMMISSION

Charles A. McDaniel, Jr. and Alison L. McDaniel (Co-Trustees for the McDaniel Family Trust) Complainant v. Amerivest Brokerage Services a/k/a Tradeline Brokerage Services LLC, Robert Ian Gorrie, Walter Frank Price, RB&H Financial Services LP, Respondents.	CFTC Docket No. 97-R057

Alison L. McDaniel (Successor Trustee for Robert B. Miner Trust), Complainant v. Amerivest Brokerage Services a/k/a Tradeline Brokerage Services LLC, Robert Ian Gorrie, Walter Frank Price, RB&H Financial Services LP, Respondents.	CFTC Docket No. 97-R058

INITIAL DECISION

Appearances:

For the Complainant:
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For the Respondents:
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Before: Painter, ALJ

PROCEDURAL STATEMENT

Allison McDaniel ("McDaniel") filed these two complaints with the Commission on April 7, 1997. On December 18, 1997, after retaining counsel, McDaniel filed a First Amended complaint in each case.

The complaints allege that respondents fraudulently induced McDaniel to engage in a "delta neutral strategy" in the dollar index contract by representing the strategy to be a conservative, ultra safe method of trading; that respondents made many misrepresentations and omissions of material facts to induce McDaniel to open the accounts; and that respondents employed a reporting strategy that concealed from her the true status of the accounts and enabled respondents to churn the accounts to generate commissions.

The trial of this matter took place on February 12, 1998, in Los Angeles, California. The parties have filed post-trial briefs, and these matters are ready for decision.

FINDINGS OF FACT

1. Alison McDaniel ("McDaniel") is a 48 year old artist with limited understanding of trading futures. Prior to opening the accounts in question her only experience with futures and options trading consisted of trading a small account with an entity by the name of Behrens, and information received in the mail from one Ken Roberts. Her account with Behrens was open for only a short time, and was closed after losing $2,000. I find and conclude that McDaniel knows very little about the nuances of futures and options trading. (Tr. 46-47.)

2. McDaniel is a co-trustee for the McDaniel Family Trust ("Family Trust") the complainant in Docket Number 97-R057, and successor trustee for the Robert B. Miner Trust ("Miner Trust"), the complainant in Docket Number 97-R058. McDaniel opened the accounts in issue, and she is the only representative of the complainants that dealt with respondents. She learned of the respondents through a television commercial. After telephone conversations with respondent Walter Price ("Price") she met with him at his office at Amerivest Brokerage Services a/k/a Tradeline Brokerage Services LLC. On April 16, 1996 she and her husband, Charles A. McDaniel, Jr., signed RB&H Financial Services customer application forms and related documents, including a risk disclosure statement. (Tr. 22-25, 45-48; Ex. R-1.) On April 19, 1996 McDaniel deposited $10,000 in the Family Trust account. (Tr. 28.)

3. RB&H Financial Services LP ("RB&H") was at all relevant times registered as a futures commission merchant, and was the guarantor for Amerivest Brokerage Service, a/k/a Tradeline. (Commission records; Guarantee agreement form Comm. Fut. L. Rep., Vol. 1 [CCH] paragraph 3503)

4. Respondent Robert Ian Gorrie ("Gorrie") was at all relevant times registered as an associated person and president of Tradeline. His experience includes 10 years as an associated person of Monex, a leverage merchant, and 4 years as an associated person with Premex, also a leverage merchant. He was the supervisor of respondent Walter Price. (Tr. 105,121-122.)

5. Respondent Walter Price ("Price") was at all relevant times registered as an associated person of Tradeline. His prior experience includes four years with Monex. Price served as the account executive for the accounts at issue. (Commission records)

6. Although McDaniel was initially interested in grain trading, Price recommended that she trade the "delta neutral strategy," which involves the writing of puts and calls. Price told

McDaniel that she could make some money if the market stayed within a defined range, and that it was a slow process. (Tr. 28-29.)

7. Trading in the Family Trust account was essentially limited to grains from the time it opened through April 22, 1996. The writing of dollar index puts and calls, which commenced in the Family Trust account on April 23, 1998, was touted and recommended by Price and endorsed by Gorrie. (Tr. 28-32, 42, 49,106.). The writing of the options generated premiums for the account, and conversely exposed the account to unlimited risk.

8. According to McDaniel, Price described her grain trading as "gunslinging," and he recommended using the "delta neutral option strategy," the "best kept secret in the industry." (Tr. 49-51.) She further testified that Price assured her that "It was very safe. He never explained the downside risk to me." (Tr. 61.) Price testified that he had "touted" the strategy and that McDaniel then wrote the options. (Tr. 42.) Price also testified that he explained to McDaniel that the strategy would produce limited gains, with unlimited risk. (Tr. 29.) I find that Price persuaded McDaniel to switch from grain trading to writing puts and calls on the dollar index by emphasizing profits and down playing the risks, and that he did so to inflate the excess equity with premiums earned, which in turn permitted the account to be churned to generate commissions.

9. Price was aware that the premiums earned from writing options were reflected in the account equity. He was incapable of explaining how the risk associated with writing the options was reflected in the account statements. (Tr. 31-34.)

10. McDaniel opened the Miner Trust account on June 14, 1997, with an initial deposit of $15,000. Trading in the Miner account was dominated by the writing of options on the dollar index. (Account statements)

11. I find and conclude that all trades made on the dollar index were based on recommendations of Price, and that Gorrie approved of Price's conduct. (Tr. 105-108.)

12. Beginning with May 1996 statement, RB & H, the carrying futures commission merchant, consistently overstated the "excess equity" for the Family Trust account. On May 31, 1996, the statement showed an account value of $11,303, a maintenance margin requirement of $25,755, and a margin deficit of only $1285. Clearly, this was a false statement. On June 7, 1996 the market value of the account was reported as $13,658, with a maintenance requirement of $19,688. Despite an obvious margin deficiency of $8,468, the statement shows excess equity of $4,265. This pattern of false reporting persisted throughout the life of the account. I find and conclude that the false excess equity reports misled the complainant as to the true status of the accounts, and enabled respondents to excessively trade the accounts to generate commissions. (Ex. C-1.)

13. McDaniel testified that based on what Price told her about the delta neutral strategy, she caused some of her friends to open accounts through Price, including her daughter-in-law Linda McDaniel, Patricia Bragg and Holly and Bob Reynolds. McDaniel further testified that the account statements were so confusing that she first learned that the trust accounts were losing when Patricia Bragg called to tell her that her account (Bragg's) was wiped out. (Tr. 48-50.)

14. RB&H statements for the Miner Trust show the same pattern of overstating excess equity. On July 10, 1996 the excess equity was reported as $12,710.86. In point of fact, the account value was $22,407.86, the initial margin requirement $21,707, and maintenance margin $19,297., leaving excess equity of less than $200. On October 21, 1996, the RB&H statement showed excess equity of $9461.76, when in fact the account value was $29,379.76, and the maintenance margin was $35,407.75. I find and conclude that this system of providing

McDaniel with false excess equity statements was used to mislead her as to the status of her account, and to enable respondents to trade the accounts excessively to generate commissions. (Ex. C-1.)

15. Complainants have placed in evidence charts and summaries prepared by one Edward B. Horwitz. (Ex. C-2.) The figures reported in the charts have been verified by comparison with the actual account statements, and fully support Mr. Horwitz's conclusion that RB&H calculated the so-called "excess equity" by comparing the margin requirement with the **cash balance** instead of the **account value.** I find and conclude that respondents deliberately engaged in this scheme to conceal the status of the account from McDaniel, and to enable the introducing broker to churn the account to generate commissions for the benefit of RB&H, Tradeline, Gorrie and Price.

16. Respondent Gorrie, president of Tradeline and supervisor of Price, expressed the opinion that the account statements generated by RB&H correctly showed "excess equity" and that the calculations by Horowitz were "ludicrous." (Tr. 107.) However, Gorrie made no attempt to explain how the excess equity figure was computed, and merely testified that "Margin requirements are set by the exchange, not the clearing firm." (Tr. 107.) He also testified without equivocation that when the accounts at issue were closed out, checks for $37,000 and $50,000 were sent to the successor broker. (Tr. 114-115.). When confronted with account statements showing a close-out check for less than $800

, Gorrie finally conceded that the accounts were worth less than $800 when the accounts were closed. (Tr. 126.) It is appalling that the president of Tradeline and the supervisor of Price would testify under oath that some $87,000 was paid out to the accounts, when in fact that pay out was under $800. Gorrie was named as a respondent in this case in 1997, and his testimony

suggests that he was either careless or indifferent in preparing for trial, or that he is not concerned with determining the truth.

17. The account statements in evidence show that complainants deposited $57,000 in the Family Trust account, and that commissions over the ten months of its existence totaled $32,403. The Miner Trust was funded with $31,215 and commissions totaled $17,366 for the eight months the account was open. (Account statements)

18. The average commission-to-equity ratio for the McDaniel Family Trust account equalled 15.44% per month, with a high of 24.87%. The monthly average commission-to-equity ratio for the Miner Trust 11.43%, with a high of 21%. (Account statements; confirmed Horowitz calculations)

19. Gorrie testified that after the accounts were closed, McDaniel agreed to drop any complaint against the respondents provided Gorrie would "Restore the equity in Linda McDaniel's account." (Tr. 117.) This conversation, according to Gorrie's testimony, was secretly taped without McDaniel's knowledge.(Tr. 128.) This is not disputed by McDaniel. I find, however, that at the time of this oral agreement, McDaniel was totally unaware of the practices respondents employed in the trading of the accounts at issue. The purported agreement does not bar the filing of these complaints. A transcript of the telephone call is appended to complainants' post-trial brief.

20. Respondents were invited to file, post-hearing, their own charts, graphs, and/or calculations to rebut those figures prepared by Horwitz at the direction of counsel for complainant. (Ex. C-2.) On June 1, 1998, counsel for respondents submitted a two page document, admitted in evidence as Exhibit R-6. The first page of R-6 is a Chicago Mercantile Exchange document entitled Standard Portfolio Analysis of Risk * (Span*) Overview. The

second page is a letter from Daniel F. Lazarus, attorney, on exchange stationary. This is simply a statement that the Miner Trust account was properly margined from January 1, 1997 to February 19, 1997, and that the Family Trust account was properly margined from January 1, 1997 to February 9, 1997, and under margined from February 10, 1997, through February 19, 1997. This exhibit does not rebut the charts and summaries set out in complainants' exhibit C-2, and is of little or no value in deciding the issues in this case.

DISCUSSION

Alison McDaniel, the person who opened the accounts at issue, and caused the filing of the complaints, is an intelligent, educated individual who has no understanding of how the futures and options market works. She is not, however, unsuitable to trade in this area. This Commission has not adopted a suitability standard, and relies essentially on the National Futures Association Compliance Rule 2-30 which requires members to "know your customer." McDaniel is neither dumb-as-a-post nor mentally impaired and she is free to open and trade commodity accounts. Suitability is not an issue in these cases.

The issue in these cases is whether respondents engaged in a scheme to cheat and defraud complainants by 1) fraudulently inducing McDaniel to write put and call options; 2) concealing the true status of the accounts by providing false information on the excess equity; and 3) using the false excess equity to over-trade the accounts and generate commissions.

Complainants have failed to prove by a preponderance of the evidence that McDaniel was fraudulently induced to open the Family Trust account in April 1996. McDaniel knew something about trading commodities as she had lost some $2,000 with another firm. She knew that there was risk in commodity trading, and she had traded and lost. Once the Family Trust account was opened, Price began to tout the "delta neutral strategy" of writing put and call

options on the dollar index. This strategy was a far cry from the grain trading McDaniel employed in the early days of the Family Trust account. Price touted the delta neutral strategy as the "best kept secret" in the industry, a conservative strategy and, according to McDaniel, a safe strategy. Gorrie, Price's supervisor, condoned and endorsed the strategy touted by Price.

McDaniel was led to believe that the delta neutral strategy of writing put and call options was a proven strategy for making profits. McDaniel not only believed Price's representations that the strategy was conservative and successful, but she also persuaded her friends and daughter-in-law to open accounts with Price as the account executive. The testimony of record establishes that Price did not explain to McDaniel the huge risk involved in writing options. Instead, he emphasized that the strategy was "safe" and the "best kept secret in the industry," thus implying that McDaniel would be using a system employed professional insiders.

To compound the wrongdoing in the inducement, respondents engaged in a nefarious reporting scheme that prevented McDaniel from knowing the true status of her account at any time. For instance, the July 31, 1996 RB&H Miner Trust statement sent to McDaniel reported the market value of the account as $17,287 and the excess equity as $3,247, even though the initial margin requirement for positions on the account exceeded $40,000. The September 17, 1996 Family Trust statement shows a market value of $24,497, an initial margin requirement of $51,309 for established positions, and an excess equity of $4,689. This pattern of false reporting persisted from April 1996 to the date the accounts were closed in early 1996. I find that McDaniel testified honestly when she said that she first learned of the status of the trust accounts when Patricia Bragg called to tell her that her account had been wiped out.

There is a wealth of evidence in this case to show that the accounts were churned to generate commissions. Respondents converted $32,316 of the $57,000 deposited in the Family

Trust account into commissions in less than 10 months, with an average commission-to-equity ratio of more than 15%. More than half of the $31,215 deposited in the Miner Trust was converted to commissions in only eight months time. It is unnecessary to do a churning analysis in these cases as the complainants prevail on the fraud associated with the so-called delta neutral strategy and the false equity reports which commenced on April 23, 1996. On April 22, 1996, the Family Trust account had a market value of $9,428. I find that Price had effective control over all trading in the Family Trust thereafter, and full control over the Miner Trust from the time it was opened on June 14, 1996 to the date it was closed. Complainant Family Trust is liable for the $522 in losses incurred in the Family Trust account up through April 22, 1996. I further find and conclude that all losses incurred in both accounts on and after April 23, 1996 are directly related to the fraudulent conduct of the respondents. By inflating the excess equity in the accounts, respondents were able to conceal the status of the account from McDaniel, and convert substantial portions of the true equity to commissions for the benefit of respondents. It was not until Bragg informed McDaniel that her account had been wiped out that McDaniel became aware of the status of the trust accounts.

ORDER

The trustee for Complainant Robert B. Miner Trust has established by the preponderance of the evidence that respondents violated Section 4b of the Commodity Exchange Act, 7 U.S.C. 6b, in connection with the handling of its account, and that the wrongful conduct resulted in direct monetary damages amounting to $31,215. Respondents are **ORDERED** to pay this sum, plus the filing fee of $250, plus interest at the rate of 5.375% from January 1997 to the date of payment, within 30 days after this award becomes final. Respondents are jointly and severally liable for payment of this award.

The co-trustees for Complainant McDaniel Family Trust has established by the preponderance of the evidence that respondents violated Section 4b of the Commodity Exchange Act, 7 U.S.C. 6b, and that the wrongful conduct of respondents resulted in losses of $56,478 ($57,000 less $522 lost prior to April 23, 1996) from April 23, 1996 to the date the account was closed in January 1997. Respondents are **ORDERED** to pay this sum, plus the $250 filing fee, plus interest at the rate of 5.375% from January 1997 to the date of payment. Respondents are jointly and severally liable for payment of this judgment.

Issued this 13th day of August, 1998

George H. Painter
Administrative Law Judge