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DAVID L. PITMAN, Complainant, v. IOWA GRAIN COMPANY, CERES TRADING GROUP, INCORPORATED, and JAMES PETER DOENGES, Respondents.	*	CFTC Docket No. 99-R75

INITIAL DECISION

David Pitman seeks $9,175 in damages based on the claim that James P. Doenges, an associated person with Ceres Trading Group, made material misrepresentations and omissions during the solicitation and trading of his non-discretionary options account. Pitman asserts that Ceres Trading Group is liable for the fraud of its agent and that Iowa Grain is liable as the guarantor of Ceres. Respondents filed a joint answer, denying the allegations, and asserting that Pitman had received adequate written oral risk disclosures in the customer contract and risk disclosure statement and had received adequate oral risk disclosures by Doenges and the Ceres compliance department. Respondents also asserted that notwithstanding Iowa Grain's guarantee of Ceres, Iowa Grain was not liable because Pitman had failed to allege any specific violations by Iowa Grain.

The findings and conclusions below are based on the parties' documentary submissions and oral testimony, and reflect the determination of the undersigned that the testimony of Pitman was generally more credible and plausible than the testimony of Doenges. For the reasons set out below it has been concluded that Pitman is entitled to an award of $8,543, plus prejudgment interest and costs.

Factual Findings

The parties

1. David Pitman was an undergraduate psychology instructor at St. Mary of the Woods college in Indiana when he opened his account with respondents in October 1997. Pitman has bachelors, masters and doctoral degrees in psychology. Pitman had no previous investment experience. [Pages 13-15 of hearing transcript.]

2. Iowa Grain Company is a registered futures commission merchant with its principal place of business in Chicago. Ceres Trading Group ("Ceres") was a registered introducing broker, with its corporate office located in Atlanta, Georgia, and sales offices located in Singer Island and Del Ray Beach, Florida, and Annapolis, Maryland. Pursuant to a guarantee agreement between Iowa Grain and Ceres, Iowa Grain agreed that it would be jointly and severally liable for all obligations of Ceres under the Commodity Exchange Act with respect to the solicitation and trading of customer accounts introduced by Ceres. [Guarantee agreement produced by respondents May 20, 1999.] By a Decision issued by the National Futures Association on November 16, 1999, Ceres and its owners agreed to pay a $75,000 fine and agreed that Ceres would withdraw from NFA

membership, in connection with charges that Ceres had "used television and radio ads that were deceptive, misleading and unbalanced in the possibility of profit and loss." *In re Ceres Trading Group, Inc., Warren Scott Parker and Robert E. Parker, Jr.*, NFA Case No. 99-BCC-5.

James Peter Doenges was a registered associated person with Ceres from January 31, 1997 to May 10, 1999.[1] [NFA records.] Doenges was principally compensated with a percentage of commissions charged to his clients accounts. As of September 1, 1997, at least 33 of the 35 accounts handled by Doenges had realized aggregate net losses.[2] These losses ranged from $52 to $27,598, with 9 accounts experiencing losses over $10,000, 10 accounts experiencing losses between $5,000 and $10,000, and 14 accounts experiencing losses less than $5,000. Since Doenges typically relayed Ceres' trade recommendations to his clients, rather than performing independent market analyses, it is reasonable to conclude that the dismal performance of his clients' accounts was representative of the overall performance of Ceres clients' accounts during the same period.

The account solicitation

3. In September of 1997, Pitman mailed a business reply post-card to *The First Wall Streeter*. At about the same time Pitman heard a radio commercial discussing 75% to 100% returns on energy options, and called the toll-free telephone number provided in the commercial. Neither the print advertisement

[1] Doenges currently is a registered associated person with Winner Group, Inc.
[2] Account statements produced for the other two accounts show small account balances and no trading activity, but are insufficient to establish any trading losses or profits.

nor the radio ad mentioned Ceres Trading by name. [*See* pages 15-19 of hearing transcript.]

On about September 25, 1997, Doenges called Pitman. Neither Doenges nor Pitman can recall whether they discussed the print or radio advertisement. Pitman credibly testified that Doenges' core message was that Ceres' clients had consistently enjoyed profits and that Pitman would realize much greater profits than he could with a mutual fund by following Ceres' trade recommendations. Doenges told Pitman that Ceres' trading strategies were based on seasonal price movements of various petroleum and grain products. When Pitman told Doenges that he had no meaningful investment experience and had no idea how to pick and handle options trades, Doenges reassured Pitman that he would provide the necessary advice about selecting specific strategies, markets and contracts, and about when to buy and sell. Pitman credibly testified that Doenges emphasized the great profits to be made trading with Ceres, without mentioning risk and without accurately conveying the reality that all, or almost all, of his clients had failed to realize the sort of profits that he was emphasizing. When Pitman told Doenges that he was ready to open an account, Doenges said that he would be sending the necessary account-opening documents. [*See* pages 19-25 of hearing transcript.] As discussed below, Doenges and Ceres processed Pitman's account application in a haphazard and confusing manner which contributed in large part to Pitman's confused recollection of the exact sequence of events during the account-opening.

The account-opening:

4. According to respondents, in September 1997, the account-opening package to be provided by Ceres to prospective clients included: (1) a "Special Report on Heating Oil"; (2) a Ceres promotional brochure; (3) a Ceres "Additional Risk/Fee Disclosure;" and (4) a two-booklet Iowa Grain account-opening document. [Produced by respondents May 20, 1999.] However, Pitman testified that he could not remember receiving or reading the heating oil special report, the Ceres brochure, or the Ceres additional fee/risk disclosure. In this connection, respondents have not shown that Pitman actually received and signed the Ceres additional fee/risk disclosure form, and respondent have failed to make a sufficiently reliable showing that they actually provided a complete Iowa Grain account-opening application to Pitman.

5. The heating oil special report is virtually identical to the special report distributed by various firms during the past decade. *See, e.g., Ricci v. Commonwealth Financial Group,* [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,545 (Initial Decision 1995), *affirmed* ¶ 26,917 (CFTC 1996); and *Kelley v. First Investors Group of the Palm Beaches* [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,940 (Initial Decision 1996), *summarily affirmed* unpublished slip op. CFTC Docket No. 95-R131 (CFTC August 1, 1997).

Notwithstanding the fact that special Heating Oil report, and the Ceres brochure, were not factors in Pitman's decision to open the Ceres account, these two documents tend to corroborate his description of Doenges' misrepresentations and omissions because both documents conveyed the same message with similar

misrepresentations and omissions. For example, neither document contained a meaningful explanation of the risk of trading with Ceres that would have accurately reflected the dismal performance of Ceres' customers, that would have [illegible] the claim in the Ceres brochure that Ceres specialized in "discovering trades with large profit potential and limited risk," or that would have cured the strong, false inference in the special report that Ceres' seasonal trading strategy had actually been successful.

6. As noted above, respondents have not established that they actually sent the Ceres additional risk and fee disclosure statement to Pitman. However, even if they had provided this disclosure, it would not have cured respondents' oral and written misrepresentations about the supposedly successful seasonal trading strategies, because the disclosure statement merely represented that novice customers should "carefully consider the risks associated with [options]," and did not actually describe or explain those risks.

7. The July 1997 version of the Iowa Grain account-opening package consisted of two separate booklets. Booklet No. 1 was to be filled out and signed by the customer, and consisted, in pertinent part, of the New Account Fact Sheet, which requested personal information from the customer (pages 1 through 3); the Customer Agreement (pages 4 through 11); an acknowledgment that the customer had received and read the risk disclosure statement contained in Booklet Number 2 (page 11), the Arbitration Agreement (pages 23-24); and a Notice principally reminding the customer to monitor account statements (last page). The second

booklet consisted of the risk disclosure statement, and was to be retained by the customer.

During their initial conversations, Doenges asked Pitman personal information such as his age, address, and current job, which Doenges entered into the "New Account Fact Sheet" which was part of the first booklet. [*See* pages 187-188 of hearing transcript.] Doenges then mailed the first booklet of the Iowa Grain account-opening document to Pitman, who promptly signed the customer contract and returned the booklet without carefully reading it. When Ceres discovered that Pitman had not signed the risk disclosure acknowledgment, Doenges faxed a single page to Pitman with blanks for signatures for the customer contract and for the risk disclosure acknowledgment. However, this page was not from the application returned and partially singed by Pitman, but from an older version of the Iowa Grain account-opening form. Pitman did not notice the discrepancy and signed this page in both blanks and returned it to Doenges.

On January 22, 1998, after Pitman had lost most of his investment, Dana Jackson, a compliance representative for Ceres, would call Pitman and ask him to sign the risk disclosure acknowledgment in the original account-opening documents. Jackson then would send the separated page for Pitman's signature. However, Pitman would return the acknowledgment without signing it, because by then he could not remember exactly what he had received from Doenges and Ceres. [Pages 76-77 of hearing transcript.]

After Pitman had closed the account in June 1998, he would ask Jackson for a complete set of the account-opening documents. Jackson sent him a cobbled-

together set of documents which was made up of portions of the July 1997 account application form (pages 1-2) and portions of the older customer contract (pages 3-

On July 29, 1998, Iowa Grain would provide the CFTC Division of Enforcement with the original account-opening documents, which was yet another agglomeration of pages from two account-opening packages: pages 1-28 of the July 1997 account application form, and the signature page from the superceded form that Pitman had signed.

8. On September 29, 1997, Doenges told Pitman that Ceres had approved the account. Doenges then told Pitman that he had to go through an account-opening routine, and instructed him how to answer the questions. Dana Jackson conducted a brief and rushed compliance review. Jackson underscored the *pro forma* nature of the review by reading a script so quickly that she was barely comprehensible. The effectiveness of Jackson's review was further undermined by the fact that Jackson's questions appeared designed not to discover or cure Doenges' deceptive pitch about the trading strategy based on seasonal price trends. [See pages 38-44, and 207-210 of hearing transcript.]

Trading the account

9. Pitman deposited a total of $9,175 – $5,000 on September 29, $1,175 on October 2, and $3,000 on October 14, 1997 – and received back on July 2, 1998 $432. Thus, Pitman's out-of-pocket losses totaled $8,543.

10. Pitman made five option trades following Doenges' advice: a heating oil spread, a soybean spread, a corn spread, a short soybean trade, and a long corn trade. All of these trades lost money. All of the trades had been initiated by December 23, 1997. The last options expired worthless on June 22, 1998.

Pitman credibly testified that Doenges, during the initial trade recommendations, falsely represented that his other clients had been enjoying profits on similar trades and effectively guaranteed profits. [Pages 44-76 of hearing transcript.]

11. Respondents charged Pitman's account a total of $7,802 in commissions and fees. These costs consumed approximately 83.5% of Piton's investment, and represented 93% of his out-of-pocket losses.

Conclusions

Pitman has established by a preponderance of the evidence that James Peter Doenges violated Section 4c(b) of the Commodity Exchange Act and CFTC rule 33.10, proximately causing $8,543 in damages; that Ceres Trading Group is liable for Doenges' violations pursuant to Section 2(a)(1)(A) of the Act; and that Iowa Grain Company is liable as guarantor of Ceres Trading Group.

Deonges fraudulently induced Pitman to open an account with Ceres and to approve various trades by misleading Pitman about the relative risks and rewards of trading with Ceres. Most significantly, Deonges falsely claimed that his other customers were making profits and falsely asserted that the predictable nature of the seasonal demand and price trends in certain commodities essentially guaranteed

profits. Doenges omitted various material facts that would have at least partially cured his deceptive and misleading message of certain profits and reduced risk. For example, he did not provide any disclosure that a seasonal increase in demand for a commodity would not necessarily result in the increased value of a corresponding option, because the market had already factored seasonal demand into the option price. He also did not remotely allude to the patently material fact that most, if not all, of his customers had failed to realize net profits. The intentional nature of Doenges' misrepresentations and omissions is underscored by the blatant nature of the misrepresentations and omissions, and his knowledge of Pitman's investment inexperience.

Ceres' scripted and *pro forma* compliance review cannot be used as "advance exoneration" of respondents' fraud, especially where Doenges down-played the importance of the review by instructing Pitman how to answer the questions, and where the review itself was rushed, obviously *pro forma*, and not designed to cure misrepresentations about the seasonality trading strategy promoted by Ceres and Doenges. *See JCC, Incorporated v. CFTC*, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,492 (11th Cir. September 15, 1995).

The proper measure of damages is Pitman's out-of-pocket losses: $8,543.

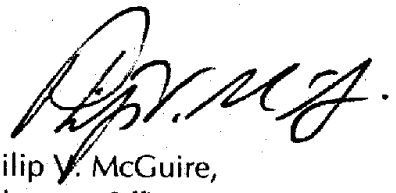
ORDER

Respondents Iowa Grain Company, Ceres Trading Group, Incorporated, and James Peter Doenges are ORDERED to pay to David L. Pitman reparations of

$8,543, plus interest on that amount at 5.997% compounded annually from September 29, 1997, to the date of payment, plus $50 in costs for the filing fee.

Liability is joint and several.

Dated January 19, 2000.



Philip V. McGuire,
Judgment Officer