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**UNITED STATES OF AMERICA**
**Before the**
**COMMODITY FUTURES TRADING COMMISSION**

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| In the Matter of: | ) | |
| | ) | |
| Hernando Chovil, | ) | |
| | ) | CFTC Docket No. 11 –09 |
| Respondent. | ) | |
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**ORDER INSTITUTING PROCEEDINGS PURSUANT TO SECTIONS 6(c) AND 6(d) OF THE COMMODITY EXCHANGE ACT, AS AMENDED, MAKING FINDINGS AND IMPOSING REMEDIAL SANCTIONS**

**I.**

The Commodity Futures Trading Commission ("Commission") has reason to believe that Hernando Chovil ("Chovil" or "Respondent") has violated Sections 4b(a)(1)(A) and (C), 4c(b), and 4o(1)(A) & (B) of the Commodity Exchange Act ("Act"), 7 U.S.C. §§ 6b(a)(1)(A) and (C), 6c(b), and 6o(1)(A) & (B) (2006), and Commission Regulations 4.20 and 33.10(a) and (c), 17 C.F.R §§ 4.20 and 33.10(a) and (c) (2009). Therefore, the Commission deems it appropriate and in the public interest that a public administrative proceeding be, and hereby is, instituted to determine whether Respondent has engaged in the violations as set forth herein and to determine whether an order should be issued imposing remedial sanctions.

**II.**

In anticipation of instituting an administrative proceeding, Respondent has submitted an *Offer of Settlement* ("*Offer*"), which the Commission has determined to accept. Without admitting or denying any of the findings herein, Respondent acknowledges service of this *Order Instituting Proceedings Pursuant to Sections 6(c) and 6(d) of the Commodity Exchange Act, as amended, Making Findings and Imposing Remedial Sanctions* ("*Order*").[1]

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[1] Respondent consents to the entry of this *Order* and to the use of these findings in this proceeding and in any other proceeding brought by the Commission or to which the Commission is a party; provided, however, that Respondent does not consent to the use of the *Offer*, or the findings consented to in the *Order*, as the sole basis for any other proceeding brought by the Commission, other than in a proceeding in bankruptcy or to enforce the terms of this *Order*. Nor does Respondent consent to the use of the *Offer* or this *Order*, or the findings in this *Order* consented to in the *Offer*, by any other party in any other proceeding.

## III.

The Commission finds the following:

### A. Summary

In or about August and September 2008, Chovil fraudulently solicited individuals to trade commodity futures and options on commodity futures ("options") through a commodity pool. Chovil subsequently lost the pool participants' funds trading, but concealed those losses through false statements made to the investors that they were making profits.

### B. Respondent

**Hernando Chovil** resides in McLean, Virginia. Chovil has never registered with the Commission.

### C. Facts

In or about August and September 2008, Chovil solicited at least seven individuals to trade commodity futures and options through a commodity pool. Chovil solicited individuals he knew as acquaintances and from business dealings. Of the individuals he solicited, only two individuals deposited funds into the pool.

In the course of his solicitations, Chovil held himself out to prospective pool participants as someone who knew the commodity futures business and who had been trading for a long time. He claimed that he had developed a successful trading system that would produce profits for his participants; in fact, he guaranteed that they would not lose their principal. At no time during the course of his solicitations did Chovil ever disclose to potential pool participants the risks involved in trading commodity futures or options.

At the time of their investment, pool participants each signed an agreement with Chovil in which Chovil guaranteed their principal, agreed to provide a monthly report of all trading, and agreed to make a monthly payment for each month in which a profit was earned. Under the terms of the contract, Chovil was to receive compensation equal to twenty percent (20%) of each month's profits.

Chovil deposited the pool participants' funds into his personal bank account and then transferred that money to his personal commodity trading account at a registered Futures Commission Merchant ("FCM). In that account, he also traded his personal funds.

In his trading account, Chovil traded commodity futures and options that were executed on a designated contract market. Chovil sustained consistent losses as a result of his trading, and eventually lost all of his participants' funds. Chovil never provided pool participants with any account statements or reports on the status of the trading account. In fact, in order to conceal the losses he had incurred, Chovil told one participant that the account had made a small profit. At

another point, in response to questions from a pool participant, Chovil told him that there was "no problem" with the account, that he was "doing okay," and that "we're going to make money."

Eventually, Chovil's participants asked for their principal back and Chovil was forced to admit that he had lost their money. Chovil paid back some but not all of the funds of the pool participants.

## IV. LEGAL DISCUSSION

### A. Section 4b(a)(1)(A) and (C) and 4c(b) of the Act and Commission Regulations 33.10(a) and (c) : Fraud by Misrepresentations and Omissions

Section 4b(a)(1)(A) and (C) of the Act makes it unlawful to cheat, defraud, or deceive, or to attempt to cheat, defraud, or deceive, any person in or in connection with any order to make, or the making of any contract or sale of any commodity for future delivery. Similarly, Section 4c(b) of the Act and Section 33.10(a) and (c) of the Regulations make it unlawful to cheat, defraud, or deceive, or attempt to cheat, defraud, or deceive, any person in or in connection with an offer to enter into, the entry into, the confirmation of the execution of, or the maintenance of, any commodity options transaction.

To prove that a respondent has violated these provisions by misrepresentations or omissions, the Commission need only show that: 1) the respondent made a misrepresentation, misleading statement, or omitted a fact; 2) that the misrepresentation or omission was material; and 3) the respondent knew the information was false and calculated to cause harm or recklessly disregarded the truth or falsity of the information (in other words, that he acted with "scienter"). *Hammond v. Smith Barney Harris Upham & Co.*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,617 at 36,659 (CFTC Mar. 1, 1990); *In re JCC*, [1992-1994 Transfer Binder] Comm. Fut. L Rep. (CCH) ¶ 26,080 at 41,568 (CFTC May 12, 1994), *aff'd sub nom. JCC, Inc. v. CFTC*, 63 F.3d 1557 (11th Cir. 1995); *CFTC v. R.J. Fitzgerald & Co., Inc.*, 310 F.3d 1321, 1328 (11th Cir. 2002), *cert. denied*, 543 U.S. 1034 (2004).

A statement is material if "it is substantially likely that a reasonable investor would consider the matter important in making an investment decision." *Sudol v. Shearson Loeb Rhoades, Inc.*, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,748 at 31,119 (CFTC Sept. 30, 1985) (*citing TSC Indus. Inc. v. Northway, Inc.*, 426 U.S. 438, 449 (1976)); *R.J. Fitzgerald*, 310 F.3d at 1328 (same); *CFTC v. Rosenberg*, 85 F. Supp. 2d 424, 447 (D. N.J. 2000) (same). Any fact that enables customers to assess independently the risk inherent in their investment and the likelihood of profit is a material fact. *In re Commodities International Corp.*, [1996-1998 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,943 at 44,463-64 (CFTC Jan. 14, 1997) (finding that misrepresentations and omissions to customers were material and fraudulent because customers could not properly evaluate their circumstances with regard to risk of loss and opportunity for profit).

The scienter requirement is met when "highly unreasonable omissions or misrepresentations [are made]...that present a danger of misleading [customers] which is either

known to the Defendant[s] or so obvious that Defendant[s] must have been aware of it." *R.J. Fitzgerald*, 310 F.3d at 1328.

Chovil fraudulently solicited prospective pool participants by guaranteeing to them that their principal deposit would be safe from losses and by failing to disclose to them the risks inherent in trading commodity futures and options. Chovil also made false statements to one pool participant by falsely claiming to have made a profit and that the account was doing "okay" when in reality Chovil was sustaining trading losses and eventually lost all of the participants' funds. Such misrepresentations and omissions are material in that a reasonable investor would want to know that trading of commodity futures and options is risky and that his principal is at risk; moreover, he would want to know his actual trading results. As Chovil claimed to have experience trading commodity futures and options, and, at the same time, knew that he was not a successful trader, Chovil thus knew, or recklessly disregarded, that his guarantees, omissions, and misrepresentations were misleading.

Accordingly, Chovil violated Section 4b(a)(1)(A) and (C) and Section 4c(b) of the Act, 7 U.S.C. § 6b(a)(1)(A) and (C) and Section 6c(b) (2006), and Commission Regulations 33.10(a) and (c), 17 C.F.R §§ 33.10(a) and (c) (2009).

**B. <u>Section 4o(1) of the Act: Fraud by CPO's</u>**

Section 4o(1) of the Act, in relevant part, makes it unlawful for a CPO, by using the mails or any means or instrumentality of interstate commerce, directly or indirectly (a) to employ a device, scheme or artifice to defraud pool participants, or (b) to engage in a transaction or course of business that operated as a fraud or deceit upon pool participants. 7 U.S.C. § 6o(1)(A) & (B) (2008). This section of the Act applies to all CPOs, whether registered, required to be registered, or exempt from registration. *Skorupskas*, 605 F. Supp. at 932. Although scienter must be proven to establish violations of Sections 4b and 4o(1)(A) of the Act, it is not necessary to prove scienter to establish a violation of Section 4o(1)(B) of the Act. *See Messer v. E.F. Hutton & Co.*, 847 F.2d 673, 678-79 (11th Cir. 1988). *Accord In re Kolter*, [1994-1996 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,262 (CFTC Nov. 8, 1994) (Commission cited *Messer* for this proposition with approval).

By operating a business in the nature of an investment pool, syndicate or similar form of enterprise and by soliciting, accepting or receiving funds for the purpose of trading commodity futures or options, Chovil was acting as a CPO. Section 1a(5) of the Act, 7 U.S.C. § 1a(5) (2006) (defining CPO). *See, e.g., In re Slusser*, [1998-1999 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,701 at 48,310 (CFTC July 19, 1999), *aff'd in relevant part sub nom. Slusser v. CFTC*, 210 F.3d 783 (7th Cir. 2000) (respondent acted as a CPO when it accepted investment funds from individual investors who deposited funds in respondent's bank account for the purpose of trading in a commodity pool); *SEC v. Princeton Econ. Int'l*, 73 F. Supp. 2d 420, 424 (S.D.N.Y. 1999) (defendant acted as a CPO by commingling proceeds derived from sale of notes to customers in a commodity pool).

The same fraudulent conduct that violates Section 4b(a) and 4c(b), as set forth above, also violates Section 4o(1)(A) & (B). *Skorupskas*, 605 F. Supp. at 932-33. Accordingly, Chovil violated Section 4o(1)(A) & (B) of the Act.

### C. Commission Regulation 4.20(a): Failure to Operate a Pool as a Separate Legal Entity

Commission Regulation 4.20(a)(1) provides that a "commodity pool operator must operate its pool as an entity cognizable as a legal entity separate from that of the pool operator." 17 C.F.R. § 4.20(a)(1) (2009). Chovil accepted and traded pool participant funds in his own name and failed to operate the pool as a separate legal entity. Chovil thus violated Commission Regulation 4.20(a)(1).

### D. Commission Regulation 4.20(c): Commingling Pool Funds

Commission Regulation 4.20(c) states that "[n]o commodity pool operator may commingle the property of any pool that it operates or that it intends to operate with the property of any other person." 17 C.F.R. § 4.20(c) (2009). Chovil deposited pool participants' funds into bank accounts in his own name and then transferred them into a commodity trading account in his own name. Chovil thus violated Commission Regulation 4.20(c).

## IV. FINDINGS OF VIOLATIONS

Based upon the foregoing, the Commission finds that Respondent violated Sections 4b(a)(1)(A) and (C), 4c(b), and 4o(1)(A) & (B) of the Act, 7 U.S.C. §§ 6b(a)(1)(A) and (C), 6c(b), and 6o(1)(A) & (B) (2006), and Commission Regulations 4.20 and 33.10(a) and (c), 17 C.F.R. §§ 4.20 and 33.10(a) and (c) (2009).

## V. OFFER OF SETTLEMENT

Respondent has submitted his *Offer* in which he, without admitting or denying the findings herein:

A. Acknowledges receipt of service of this *Order*;

B. Admits the jurisdiction of the Commission with respect to all matters set forth in this *Order*;

C. Waives: the filing and service of a complaint and notice of hearing; a hearing; all post-hearing procedures; judicial review by any court; any and all objections to the participation by any member of the Commission's staff in consideration of the *Offer*; any and all claims that he may possess under the Equal Access to Justice Act (EAJA), 5 U.S.C. § 504 (2006) and 28 U.S.C. § 2412 (2006), and/or Part 148 of the Commission's Regulations, 17 C.F.R. §§ 148.1, *et seq.* (2009), relating to, or arising from, this proceeding; any and all claims that he may possess under the Small Business Regulatory Enforcement Fairness Act of 1996, Pub. L. No. 104-121, §§ 201-253, 110 Stat. 847, 857-

68 (1996), as amended by Pub. L. No. 110-28, § 8302, 121 Stat. 112, 204-205 (2007), relating to or arising from this proceeding; and any claim of Double Jeopardy based upon the institution of this proceeding or the entry in this proceeding of any order imposing a civil monetary penalty or any other relief;

D. Stipulates that the record upon which this *Order* is entered shall consist solely of the findings contained in this *Order* to which the Respondent has consented in his *Offer*; and

E. Consents, solely on the basis of the *Offer*, to entry of this *Order* that:

1. makes findings by the Commission that Respondent violated Sections 4b(a)(1)(A) and (C), 4c(b), and 4o(1) (A) & (B) of the Act, 7 U.S.C. §§ 6b(a)(1)(A) and (C), 6c(b), and 6o(1)(A) & (B) (2006), and Commission Regulations 4.20 and 33.10(a) and (c), 17 C.F.R. §§ 4.20 and 33.10(a) and (c) (2009);

2. orders Respondent to cease and desist from violating Sections 4b(a)(1)(A) and (C), 4c(b), and 4o(1) (A) & (B) of the Act, 7 U.S.C. §§ 6b(a)(1)(A) and (C), 6c(b), and 6o(1) (A) & (B) (2006), and Commission Regulations 4.20 and 33.10(a) and (c), 17 C.F.R. §§ 4.20 and 33.10(a) and (c) (2009);

3. permanently prohibits Respondent from trading on or subject to the rules of any registered entity, as that term is defined in Section 1a(29) of the Act, 7 U.S.C. § 1a(29) (2008), for his own account, for any account in which he has a direct interest or indirect interest, or for any other account for or on behalf of any other person or entity, whether by power of attorney or otherwise, and all registered entities shall refuse him all privileges thereon;

4. orders Respondent to pay restitution to pool participants, in accordance with Schedule A attached to the Offer, in the amount of seven thousand three hundred forty-five dollars ($7,345) within ten (10) days of the date of entry of this Order;

5. orders Respondent to pay a civil monetary penalty in the amount of ten thousand dollars ($10,000) within ten (10) days of the date of entry of this *Order*;

6. appoints the NFA as Monitor in this matter; and

7. orders Respondent to comply with his undertakings consented to in the *Offer* and set forth below in Section VII of this *Order*.

Upon consideration, the Commission has determined to accept the Respondent's *Offer*.

## VI. ORDER

**Accordingly, IT IS HEREBY ORDERED THAT:**

A. Respondent shall cease and desist from violating Sections 4b(a)(2)(A) and (C), 4c(b), and 4o(1) of the Act, 7 U.S.C. §§ 6b(a)(2)(A) and (C), 6c(b), and 6o(1) (2008), and Commission Regulations 4.20 and 33.10(a) and (c), 17 C.F.R. §§ 4.20 and 33.10(a) and (c) (2009).

B. Respondent is permanently prohibited from trading on or subject to the rules of any registered entity, as that term is defined in Section 1a(29) of the Act, 7 U.S.C. § 1a(29) (2008), for his own account, for any account in which he has a direct interest or indirect interest, or for any other account for or on behalf of any other person or entity, whether by power of attorney or otherwise, and all registered entities shall refuse him all privileges thereon.

C. Respondent is liable for and shall pay restitution in the amount of seven thousand three hundred forty-five dollars ($7,345) (the "Restitution Obligation") within ten (10) days of the date of entry of this Order. Respondent shall direct his restitution payments to the NFA, which has been appointed to act as Monitor in this matter. Should Respondent submit proof to the Monitor of previous repayments made to pool participants beyond the two thousand six hundred fifty-five dollars ($2,655) for which he has already been credited in Schedule A, the Monitor shall credit those repayments against Respondent's Restitution Obligation. All restitution payments shall be made payable to the Hernando Chovil Restitution Fund, c/o Suzanne Cech, National Futures Association, 300 South Riverside Plaza, Suite 1800, Chicago, Illinois 60606 by electronic funds transfer, U.S. postal money order, certified check, bank cashier's check, or bank money order. Along with any restitution payment, Respondent shall provide to the Monitor a cover letter that identifies Respondent and the name and number of this proceeding. Respondent shall simultaneously transmit copies of the cover letter and the form of payment to: (a) Director, Division of Enforcement, Commodity Futures Trading Commission, Three Lafayette Centre, 1155 21st Street, NW, Washington, D.C. 20581; and (b) Chief, Office of Cooperative Enforcement, Division of Enforcement, at the same address. Restitution shall be distributed by the Monitor to the pool participants in accordance with Schedule A attached to Respondent's Offer.

D. Respondent shall pay a civil monetary penalty in the amount of ten thousand dollars ($10,000) ("CMP Obligation") within ten (10) days of the date of entry of this *Order*. Respondent shall pay his civil monetary penalty by electronic funds transfer, U.S. postal money order, certified check, bank cashier's check, or bank money order. If payment is to be made by other than electronic funds transfer, the payments shall be made payable to the Commodity Futures Trading Commission, and sent to the address below:

Commodity Futures Trading Commission
Division of Enforcement
ATTN: Marie Bateman – AMZ-300

DOT/FAA/MMAC
6500 S. MacArthur Blvd.
Oklahoma City, OK 73169
Telephone: 405-954-6569

If payment by electronic transfer is chosen, Respondent shall contact Marie Batemen or her successor at the above address to receive payment instruction and shall fully comply with those instructions. Respondent shall accompany payment of his penalty with a cover letter that identifies Respondent and the name and docket number of this proceeding. Respondent shall simultaneously transmit copies of the cover letter and the form of payment to (1) the Director, Division of Enforcement, Commodity Futures Trading Commission, 1155 21st Street, N.W., Washington, D.C. 20581 and (2) the Chief, Office of Cooperative Enforcement, Division of Enforcement, Commodity Futures Trading Commission, at the same address. In accordance with Section 6(e)(2) of the Act, 7 U.S.C. § 9a(2) (2006), if the CMP Obligation is not paid in full within fifteen (15) days of the due date, Respondent shall be prohibited automatically from the privileges of all registered entities, and, if registered with the Commission, such registration(s) shall be suspended automatically until the Respondent has shown to the satisfaction of the Commission that payments of the full amount of the CMP Obligation with interest thereon to the date the payment has been made;

E. All payments by Respondent pursuant to this Order shall first be applied to satisfy the Restitution Obligation. After satisfaction of the Restitution Obligation, payments by Respondent pursuant to this Order shall be applied to satisfy the CMP Obligation.

F. Any acceptance by the Commission or the NFA of partial payment of Respondent's Restitution Obligation and/or CMP Obligation shall not be deemed a waiver of the Respondent's requirement to make further payments pursuant to this Order, or a waiver of the Commission's right to seek to compel payment of any remaining balance; and

G. Respondent shall comply with the following undertakings:

1. Public Statements: Respondent agrees that neither he, nor any of his employees or agents under any of their authority or control, shall take any action or make any public statement denying, directly or indirectly, any findings or conclusions in this *Order*, or creating, or tending to create, the impression that this *Order* is without a factual basis; provided, however, that nothing in this provision affects Respondent's: (i) testimonial obligations; or (ii) rights to take legal positions in other proceedings to which the Commission is not a party. Respondent shall undertake all steps necessary to ensure that all of his employees and agents under his authority or control understand and comply with this undertaking;

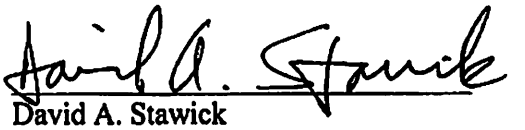
2. Respondent shall never apply for registration or claim exemption from registration with the Commission in any capacity, and shall never engage in any activity requiring such registration or exemption from registration

with the Commission, except as provided for in Commission Regulation 4.14(a)(9), 17 C.F.R. § 4.14(a)(9) (2009); and

3. Respondent shall not act as a principal (as that term is defined in Commission Regulation 3.1(a), 17 C.F.R. § 3.1(a) (2009)), agent or any other officer or employee of any person registered, exempted from registration or required to be registered with the Commission except as provided for in Commission Regulation 4.14(a)(9), 17 C.F.R. § 4.14(a)(9) (2009).

The provisions of this Order shall be effective as of this date.

By the Commission.



David A. Stawick
Secretary of the Commission
Commodity Futures Trading Commission

Dated: March 22, 2011