

UNITED STATES OF AMERICA
Before the
COMMODITY FUTURES TRADING COMMISSION

In the Matter of:)
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Roy E. Scarboro, Jr.,)

Respondent.)
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CFTC Docket No. 11 - 222

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Proceedings
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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 Roy E. Scarboro, Jr. ("Scarboro" or "Respondent") has violated Section 4b(a)(2)(A)-(C) of the Commodity Exchange Act ("Act"), as amended by the Food, Conservation, and Energy Act of 2008, Pub. L. No. 110-246, Title XIII (the CFTC Reauthorization Act of 2008 ("CRA")), §§ 13101 - 13204, 122 Stat. 1651 (enacted June 18, 2008), to be codified at 7 U.S.C. § 6b(a)(2)(A)-(C). 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

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

Beginning in or about June 2009, Scarboro fraudulently solicited and accepted approximately \$713,000 from six individuals for the purpose of trading off-exchange foreign currency (“forex”) contracts on a leveraged or margined basis through a pooled investment. Scarboro lost most of the funds trading; however, he concealed those losses through the issuance of false monthly statements to the participants that showed at various times that they were either making modest profits or incurring only modest losses. In addition, Scarboro misappropriated at least \$59,000 of pool participants’ funds for his personal use.

B. Respondent

Roy E. Scarboro, Jr. resides in Archdale, North Carolina. Scarboro has never registered with the Commission. On December 3, 2010, Scarboro pleaded guilty to a federal criminal Bill of Information charging him with various counts of fraud and money laundering based on the conduct found herein. *United States v. Roy E. Scarboro*, Case Number 3:10-cr-254 (W.D.N.C.). On May 4, 2011, Scarboro was sentenced to a term of twenty-six months in federal prison and ordered to pay restitution in the amount of \$682,663.62.²

C. Facts

Beginning in or about June 2009, Scarboro solicited and accepted approximately \$713,000 from at least six individuals in order to trade forex contracts on their behalf through a pool called Capital Asset Management Fund, L.P. (“CAMF”). Scarboro was the General Partner and Manager of CAMF.

In the course of his solicitations, Scarboro represented to at least one participant that only 20% of CAMF’s funds would be used to trade forex, with the remainder being invested in “U.S. Treasuries.” In fact, Scarboro used participants’ funds to trade forex only and never invested in any type of U.S. Treasury instrument.

² The Court’s judgment orders Scarboro to make restitution pursuant to a schedule detailing the name of the payees and the corresponding amount of restitution. The total restitution amount pursuant to the payee schedule correctly totals \$682,663.62; however, due to a clerical error, the Criminal Monetary Penalties section of the judgment provides restitution of \$322,663.62. The United States Attorney for the Western District of North Carolina has filed a motion to correct the clerical error in the judgment; Scarboro has raised no objection to this motion and does not contest that the restitution amount should be \$682,663.62. Because the criminal court awarded restitution to Scarboro’s defrauded participants for the misconduct at issue in this matter, the Commission does not require additional restitution in this Order.

Of the approximately \$713,000 Scarboro received from participants for investment through CAMF, he deposited approximately \$612,000 in forex trading accounts at registered Futures Commission Merchants. Scarboro sustained consistent losses as a result of his trading, with no profitable months, and lost approximately \$597,000 of his participants' funds. In order to conceal his trading losses, Scarboro issued false monthly account statements to CAMF's participants that showed at various times that the participants were either making modest profits or incurring only modest losses. In addition, Scarboro reported to participants on these account statements that he was taking no allocation of the profits for himself as CAMF's General Partner.

Scarboro also misappropriated participants' funds. From about July 2009 through November 2009, Scarboro misappropriated at least \$59,000 of participants' funds by transferring such funds to bank accounts he controlled either in his own name or in the name of Interactive Marketing Services, an entity he owned and controlled. Scarboro then used the funds transferred to these accounts to pay for personal expenses, including meals, gas, and home improvements. At no time did Scarboro ever inform pool participants of these transfers and expenditures.

In or about October and November 2009, Scarboro made partial payments to two pool participants; however, he has not fully repaid these participants, nor has he repaid any of the remaining participants.

IV. LEGAL DISCUSSION

A. Violations of Section 4b(a)(2)(A)-(C) of the Act, as Amended by the CRA: Fraud by Misrepresentations, Omissions, Misappropriation and False Statements

Section 4b(a)(2)(A)-(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, or to willfully make or cause to be made to any person any false report or statement. Section 4b(a)(2)(A)-(C) of the Act, as amended by the CRA, applies to Respondent's forex transactions "as if" they were a contract of sale of a commodity for future delivery. See Section 2(c)(2)(C)(iv) of the Act, as amended by the CRA, to be codified at 7 U.S.C. § 2(c)(2)(C)(iv).

1. Fraud by Misrepresentations and Omissions

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.

Scarboro fraudulently solicited at least one pool participant by misrepresenting the nature of the investment and using all of the pool participants’ funds to trade forex. Scarboro also did not disclose that he would use their funds for personal expenses. Such misrepresentations and omissions are material in that a reasonable investor would want to know the risk involved in his investment, how his money was being used, and what his actual trading results were. As Scarboro was the General Partner and Manager of CAMF and controlled CAMF’s trading accounts, he knew that all of the money invested by CAMF was being invested in forex. He also knew that CAMF was incurring consistent losses and that he had misappropriated a significant portion of CAMF’s funds. Scarboro thus knew, or recklessly disregarded, that his statements, omissions, and misrepresentations were misleading.

Accordingly, by such acts of fraudulent solicitation, Scarboro violated Section 4b(a)(2)(A)-(C) of the Act, as amended by the CRA, to be codified at 7 U.S.C. §§ 6b(a)(2)(A)-(C).

2. Fraud by Misappropriation

Scarboro used CAMF participants’ funds to pay for personal expenses. Accordingly, Scarboro misappropriated pool participant funds in violation of Section 4b(a)(2)(A) and (C) of the Act, as amended by the CRA, to be codified at 7 U.S.C. § 6b(a)(2)(A) and (C). *CFTC v. Noble Wealth Data Info. Serv., Inc.*, 90 F. Supp. 2d 676, 683-87 (D. Md. 2000) (defendants defrauded investors by diverting investor funds for operating expenses and personal use), *aff’d in part, vacated in part, sub nom. CFTC v. Baragosh*, 278 F.3d 319 (4th Cir. 2002); *In re Slusser*, [1998-1999 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 27,701 at 48,315 (CFTC July 19, 1999), *aff’d in relevant part sub nom. Slusser v. CFTC*, 210 F.3d 783, 784-85 (7th Cir. 2000) (respondents violated Section 4b by surreptitiously retaining money in their own bank accounts that should have been traded on behalf of participants); *CFTC v. Skorupskas*, 605 F. Supp. 923, 932 (E.D. Mich. 1985) (defendant violated Section 4b(a) of the Act by misappropriating customer funds entrusted to her for trading commodity futures contracts).

3. Fraud by Issuance of False Statements

Issuing or causing to be issued false statements to participants concerning the profitability of commodity futures trading conducted on their behalf violates Section 4b(a)(2)(B) of the Act, as amended by the CRA, to be codified at 7 U.S.C. § 6b(a)(2)(B). *Rosenberg*, 85 F. Supp. 2d at 447-48 (defendant violated Section 4b(a) of the Act by falsely stating that he would set up account in customer's name, among other misrepresentations); *Skorupskas*, 605 F. Supp. at 932-33 (defendant violated Section 4b(a) of the Act by issuing false monthly statements to customers); *CFTC v. Sorkin*, [1982-1984 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 21,855 at 27,585 (S.D.N.Y. Aug. 25, 1983) (distribution of account statements that falsely report trading activity or equity is a violation of Section 4b of the Act).

The monthly account statements that Scarboro intentionally issued to CAMF participants misrepresented the performance of CAMF by claiming profits and minimizing losses as he was sustaining overall losses in his trading. By knowingly issuing such false statements, Scarboro violated Section 4b(a)(2)(B) of the Act, as amended by the CRA, to be codified at 7 U.S.C. § 6b(a)(2)(B).

IV. FINDINGS OF VIOLATIONS

Based upon the foregoing, the Commission finds that Respondent violated Section 4b(a)(2)(A)-(C) of the Act, as amended by the CRA, to be codified at 7 U.S.C. § 6b(a)(2)(A)-(C).

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, 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.* (2010), 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 Section 4b(a)(2)(A)-(C) of the Act, as amended by the CRA and the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (“Dodd-Frank Act”), Pub. L. No. 111-203, Title VII (the Wall Street Transparency and Accountability Act of 2010), §§ 701-774, 124 Stat. 1376 (enacted July 21, 2010), to be codified at 7 U.S.C. § 6b(a)(2)(A)-(C);
 - 2. orders Respondent to cease and desist from violating Section 4b(a)(2)(A)-(C) of the Act, as amended by the CRA and the Dodd-Frank Act, to be codified at 7 U.S.C. § 6b(a)(2)(A)-(C);
 - 3. permanently prohibits Respondent from trading on or subject to the rules of any registered entity, as that term is defined in Section 1a of the Act, as amended by the CRA and the Dodd-Frank Act, to be codified at 7 U.S.C. § 1a, 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 a civil monetary penalty in the amount of three hundred fifty thousand dollars (\$350,000) within ten (10) days of the date of entry of this *Order*; and
 - 5. 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 Section 4b(a)(2)(A)-(C) of the Act, as amended by the CRA and the Dodd-Frank Act, to be codified at 7 U.S.C. § 6b(a)(2)(A)-(C).

- 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 of the Act, as amended by the CRA and the Dodd-Frank Act, to be codified at 7 U.S.C. § 1a, 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 shall pay a civil monetary penalty in the amount of three hundred fifty thousand dollars (\$350,000) ("CMP Obligation") within ten (10) days of the date of entry of this *Order*. Should Respondent not satisfy the CMP Obligation within ten (10) days of the date of entry of this *Order*, post judgment interest shall accrue on the CMP Obligation beginning on the date of entry of this *Order* and shall be determined by using the Treasury Bill rate prevailing on the date of entry of this *Order* pursuant to 28 U.S.C. § 1961. Respondent shall pay his CMP Obligation 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: Linda Zurhorst – AMZ-341
DOT/FAA/MMAC
6500 S. MacArthur Blvd.
Oklahoma City, OK 73169
Telephone: 405-954-5644

If payment by electronic transfer is chosen, Respondent shall contact Linda Zurhorst 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, as amended by the CRA and the Dodd-Frank Act, to be codified at 7 U.S.C. § 9a(2), 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;

- D. Any acceptance by the Commission of partial payment of Respondent's 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

E. Respondent shall comply with the following undertakings:

1. Public Statements: Respondent agrees that neither he nor any of his employees or agents under his 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/or 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) (2010); 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) (2010)), 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) (2010).

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: September 1, 2011