

SEP 30 2003



Michael N. Milby, Clerk of Court

IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

COMMODITY FUTURES TRADING
COMMISSION,
Plaintiff,
v.

ALLEGHENY GULF
INVESTMENTS, INC., and
RICHARD A. HALE

Defendants.

Civil Action No. **H-03-3526**

**COMPLAINT FOR A
PERMANENT INJUNCTION,
OTHER EQUITABLE RELIEF
AND CIVIL MONETARY
PENALTIES**

I.

SUMMARY

1. From at least November 1998 through December 1999 (the "relevant period"), Richard A. Hale ("Hale") and Allegheny Gulf Investments, Inc. ("Allegheny") (collectively "Defendants") accepted \$1.8 million from three clients for the purpose of trading commodity futures and/or options on futures contracts. Allegheny entered into separate "joint venture" agreements ("Joint Venture Agreement") with the three clients for the purpose of trading natural gas futures and options on futures contracts.

2. Allegheny, through Hale, managed and controlled the trading for each of the three joint trading accounts ("Joint Trading Accounts") established pursuant to the Joint Venture Agreements. In addition to the three Joint Trading Accounts, Hale managed and controlled the trading of a fourth account, which was Allegheny's master trading account ("Master Account"). Each of the Joint Trading Accounts was set-up as a sub-account of Allegheny's Master Account at Refco. Furthermore, each of the Joint Trading Accounts was cross-margined with the Master

Account. Hale failed to disclose to each of the clients that their accounts would be cross-margined with the Master Account.

3. Each of the Joint Venture Agreements provided that: (1) Allegheny and the client would each deposit matching funds into the Joint Trading Account to trade futures and options; (2) Allegheny would have the authority to make all trading decisions; and (3) Allegheny would receive a fee for managing the Joint Trading Accounts.

4. Allegheny received the clients' funds in its own name, deposited the funds into its bank account, and then transferred the funds to trading accounts in its own name at Refco, Inc. ("Refco"), a registered futures commission merchant ("FCM").

5. During the relevant period, the Master Account, which was managed and controlled by Hale, sustained substantial trading losses through trading futures and options on futures contracts. Since the Joint Trading Accounts were cross-margined with the Master Account, the losses in the Master Account were covered by funds from the Joint Trading Accounts causing two of the clients to lose a substantial portion of their investment.

6. By providing advice to the three clients as to the value of trading futures and options on futures contracts for compensation, Allegheny acted as a Commodity Trading Advisor ("CTA") pursuant to Section 1a(6) of the Commodity Exchange Act, as amended ("Act").

7. By misappropriating client funds to cover losses in the Master Account and failing to disclose to the three clients that their investments would be cross-margined with the Master Account, Hale engaged in practices that constitute violations of Sections 4b(a)(2)(i) and (iii), 4c(b), and 4o(1) of the Act, 7 U.S.C. §§ 6b(a)(2)(i) and (iii), 6c(b), and 6o(1) (2001), and Section 33.10 of the Commission's Regulations promulgated thereunder ("Regulations"), 17

C.F.R. § 33.10 (2003). In addition, by acting as a CTA and accepting funds its own name, Allegheny violated Section 4.30 of the Regulations, 17 C.F.R. § 4.30 (2003).

8. Accordingly, pursuant to Section 6c of the Act, 7 U.S.C. § 13a-1, the plaintiff Commodity Futures Trading Commission (“Commission”) brings this action to enjoin such acts and practices, and to compel compliance with the provisions of the Act and Regulations. In addition, the Commission seeks an accounting, disgorgement, restitution, civil monetary penalties and such other equitable relief as the Court may deem necessary or appropriate under the circumstances.

9. Unless restrained and enjoined by this Court, the Defendants are likely to continue to engage in the acts and practices alleged in this Complaint and in similar acts and practices, as more fully described below.

II.

JURISDICTION AND VENUE

10. This Court has jurisdiction over this action pursuant to Section 6c of the Act, 7 U.S.C. § 13a-1, which authorizes the Commission to seek injunctive relief against any person whenever it shall appear to the Commission that such person has engaged, is engaging, or is about to engage in any act or practice constituting a violation of any provision of the Act or any rule, regulation or order thereunder.

11. Venue properly lies with the Court pursuant to Section 6c of the Act, 7 U.S.C. § 13a-1(e), in that the Defendants are found in, inhabit, or transact business in this district, and the acts and practices in violation of the Act have occurred, are occurring, or are about to occur within this district.

III.

THE PARTIES

12. Plaintiff **Commodity Futures Trading Commission** is an independent federal regulatory agency charged with the responsibility for administering and enforcing the provisions of the Act, 7 U.S.C. §§ 1 et seq., and the Regulations promulgated thereunder, 17 C.F.R. §§ 1 et seq.

13. Defendant **Richard A. Hale** resides at 1 Deer Ridge Estate, Humble, TX 77339. During the relevant period, Hale was a 50% shareholder and Vice President of Allegheny. Hale has never been registered in any capacity with the Commission.

14. Defendant **Allegheny Gulf Investments, Inc.** is a Texas corporation with last known business address at 1010 Frost Bank Plaza, Corpus Christi, Texas 78470. During the relevant period, Hale was the Vice President and 50% shareholder of Allegheny.

IV.

FACTS

Background

15. On July 11, 1996, Hale and Charlie Steen ("Steen") formed Allegheny for the purported purpose of trading physical natural gas. During the relevant period, Hale was the Vice President and 50% shareholder of Allegheny and Steen was the President and 50% shareholder of Allegheny.

16. On or about April 8, 1998, Allegheny opened the Master Account at Refco. According to the account opening documents, Allegheny opened the account for the purpose of hedging and speculating in natural gas futures and options on futures contracts. Hale signed the account opening documents as Vice President and Secretary of Allegheny. Hale made all of the

trading decisions for the Master Account, while Steen was responsible for the administrative duties of the company.

Allegheny's CTA Conduct

17. During the relevant period, Allegheny accepted \$1.8 million from three clients to trade futures and options on futures contracts. Allegheny, through Hale and Steen, instructed the clients to wire their funds to a bank account in the name of Allegheny. Allegheny then transferred the funds to the Master Account before finally transferring the funds to each of the Joint Trading Accounts. Furthermore, Allegheny, through Hale, managed and controlled the trading in each of the Joint Trading Accounts. In exchange for managing each of the Joint Trading Accounts, Allegheny was authorized to receive a percentage of each of the clients' profits. Allegheny, through Hale, traded both futures and options on futures contracts in the Master Account and in the sub-accounts.

Joint Venture Agreements

18. Between November 1998 and February 1999, Allegheny entered into three Joint Venture Agreements with three individuals for the purpose of trading natural gas futures and options on futures contracts. Each of the Joint Venture Agreements contained similar standard provisions, which provided in part that:

- (a) By operation of the Joint Venture Agreement, Allegheny would create a sub-account at Refco to trade the client's funds;
- (b) Allegheny and each joint venturer would deposit an equal amount into the joint account. Each party would receive one half of all profits or losses and neither party would be required to make further deposits;

(c) Allegheny would trade the funds using natural gas options and/or futures. Allegheny would routinely provide the joint venturer with information reflecting the sub-account's position;

(d) Each quarter, Allegheny would be entitled to 15% of all profits (but not losses) of the joint venturer's gains, if any, marked to market for the quarter;

(e) After twelve months, either party could cancel the agreement or request partial or total liquidation at the end of any quarter with 15 days written notice to the other party; and

(f) If the agreement extended beyond the first twelve months, the fees payable to Allegheny would increase from 15% to 20%.

Client Losses

19. Each of the Joint Trading Accounts was opened in the name of Allegheny.

20. In or about January 1999, Refco issued a memo indicating that Allegheny requested that each of the Joint Trading Accounts be cross-margined with the Master Account. The clients were not aware that their accounts were cross-margined with the Master Account. Prior to and during the trading of the Joint Trading Accounts, Hale failed to disclose to the clients that their accounts would be cross-margined with the Master Account.

21. In or about July 1999, the Master Account had a negative balance of \$1,667,809.57. Hale continued to trade the Master Account until at least October 1999, when the account reached a negative balance of \$1,899,804.97. On May 17, 2000, a total of \$1,999,403.37 was transferred from two of the Joint Trading Accounts to the Master Account to cover the losses in the Master Account. As a result, clients sustained a loss of approximately

\$1,000,000. In addition, Hale and Allegheny received the benefit of the approximately \$1,000,000 in client funds.

Pasmas/Allegheny Sub-Account

22. On or about November 15, 1998, Allegheny and Arthur Pasma ("Pasma") entered into a joint venture agreement to trade natural gas futures and options on futures contracts. On or about November 16, 1998, Pasma wired \$1,000,000 to a bank account in the name of Allegheny.

23. On or about November 19, 1998, Allegheny wired the \$1,000,000 to the Allegheny Master Account at Refco and then on November 24, 1998, transferred that amount and another \$1,000,000 to the account designated for Pasma and Allegheny ("Pasma/Allegheny sub-account"), funding the account with a total of \$2,000,000.

24. At the time that Pasma made his initial investment, Hale did not inform Pasma that his account with Allegheny would be cross-margined with the Master Account. After Allegheny instructed Refco to cross-margin the accounts, Hale also failed to disclose to Pasma the fact that his account would be cross-margined with the Master Account.

25. Hale began trading the Pasma/Allegheny sub-account on or about December 1998. The Joint Trading Agreement provided that Allegheny would receive 15% of Pasma's profits per quarter as a management fee. Hale made all of the trading decisions for the Pasma/Allegheny sub-account. Hale traded futures and options on futures through this sub-account. During the time period this sub-account was traded, funds were withdrawn from it to pay margin deficits in the Master Account. Pasma did not receive any account statements from Refco. Steen periodically provided Pasma with account statements Allegheny generated based

on Refco statements, but Pamas never received any statements reflecting the withdrawal used to pay the margin deficit in the Master Account.

26. In or about July 1999, Pamas requested that Hale stop trading the Pamas/Allegheny account. There was no additional trading activity in the Pamas/Allegheny sub-account after July 1999. The Refco month-end statement for July 1999 indicated a balance of \$1,732,513.30 in the Pamas/Allegheny sub-account.

27. On November 12, 1999, Pamas sent a letter to Hale requesting that his portion of the Pamas/Allegheny account be returned. On that same day, Steen informed Pamas that there was no money in the account. Pamas then contacted Hale, who confirmed that all of Pamas' investment had been lost. Hale did not tell Pamas that the loss was due to the cross-margining of Pamas' Joint Trading Account and the Master Account.

28. Despite Hale and Steen's representations, from November 1999 to April 2000, the Refco monthly account statements reported approximately \$1,732,513.30 in the Pamas/Allegheny sub-account. In reality, these funds were frozen because they were being used to satisfy the margin requirements for the Master Account. On May 17, 2000, Refco formally transferred the frozen \$1,727,258.89 from the Pamas/Allegheny sub-account to the Master Account.

29. Prior to this transfer, on January 21, 2000, Hale executed a promissory note, promising to pay Pamas \$1,080,000. On January 25, 2000, Hale issued a check to Pamas in the amount of \$25,000. At no time prior to January 25, 2000, did Hale inform Pamas that his Joint Trading Account was cross-margined with the Master Account. To date, Hale claims to have paid Pamas all but \$200,000 of the promissory note.

30. Pamas did not know Hale or Allegheny used funds from the Pamas/Allegheny sub-account to cover the losses in the Master Account, and never authorized them to do so.

Avare/Allegheny Sub-Account

31. On or about January 6, 1999, Allegheny and Rick Avare ("Avare") entered into a joint venture agreement to trade natural gas futures and options on futures contracts. On or about January 7, 1999, Avare wired \$200,000 to a bank account in the name of Allegheny.

32. On or about January 12, 1999, Allegheny wired \$200,000 to the Master Account at Refco and then transferred that amount as well as another \$282,256 to the account designated for Avare and Allegheny ("Avare/Allegheny sub-account") for a total deposit of \$482,256.

33. At the time that Avare executed the Joint Venture Agreement, Hale did not inform Avare that his sub-account with Allegheny would be cross-margined with Allegheny's Master Account. After Allegheny instructed Refco to cross-margin the accounts, Hale also failed to disclose to Avare the fact that his account would be cross-margined with the Master Account.

34. Hale began trading the Avare/Allegheny sub-account on January 15, 1999. Hale made all of the trading decisions for the Avare/Allegheny sub-account. Hale traded futures and options on futures through this sub-account. During the time period this sub-account was traded, funds were withdrawn from it to pay margin deficits in the Master Account. Avare did not receive any account statements from Refco. Instead, Steen provided Avare with monthly account statements Allegheny generated based on the Refco statements.

35. After November 1999, the trading activity in the Avare/Allegheny sub-account ceased. The month-end statement for December 1999 showed a balance of \$272,144.48. Allegheny did not return Avare's portion of the remaining funds in the Avare/Allegheny sub-

account. On May 17, 2000, the remaining \$272,144.48 in the Avare/Allegheny sub-account was formally transferred to the Master Account to cover the losses in the Master Account. Prior to that transfer, on or about January 26, 2000, Hale and Avare executed a promissory note which provided that Avare would loan Hale approximately \$236,000 in exchange for Hales promise to pay Avare \$250,000 within ninety days form the date of the agreement. At no time prior to January 26, 2000, did Hale inform Avare that his Joint Trading Account was cross-margined with the Master Account. To date, Avare has received approximately \$100,000 of the \$250,000 loan.

36. Avare did not know that Hale or Allegheny used funds from the Avare/Allegheny sub-account to cover the losses in the Master Account, and never authorized them to do so .

Laufer/Allegheny Sub-Account

37. On or about January 6, 1999, Allegheny and Wayne Laufer ("Laufer") entered into a joint venture agreement to trade natural gas futures and options on futures contracts. Hale told Laufer that investing in Allegheny would be a good idea. On or about January 7, 1999, Laufer wired \$600,000 to a bank account in the name of Allegheny.

38. On or about January 8, 1999, Allegheny wired \$600,000 to the Master Account at Refco and then transferred that amount as well as another \$600,000 to the account designated for Laufer and Allegheny ("Laufer/Allegheny sub-account") for a total of \$1,200,000.

39. At the time that Laufer entered into the agreement with Allegheny, Hale did not inform Laufer that his account with Allegheny would be cross-margined with the Master Account. After Allegheny instructed Refco to cross-margin the accounts, Hale also failed to disclose to Laufer the fact that his account would be cross-margined with the Master Account.

40. Hale began trading the Laufer/Allegheny sub-account on January 11, 1999. Hale made all of the trading decisions for the Laufer /Allegheny sub-account. Hale traded futures and options on futures through this sub-account. Laufer did not receive any account statements from Refco. Steen periodically provided Laufer with account statements Allegheny generated based on Refco statements.

41. In or about May 1999, Laufer requested that Hale cease trading activity on the Laufer/Allegheny account. Hale stopped trading the Laufer/Allegheny account on July 2, 2003. At that time, the Laufer/Allegheny had a balance of \$1,067,128.50. On July 22, 1999, \$533,564.25 was withdrawn from the Laufer/Allegheny account. On or about July 22, 1999, Allegheny issued a check to Laufer in the amount of \$533,564.25. On July 23, 1999, the remaining \$533,564.25 was transferred to the Master Account. At no time prior to July 23, 1999, did Hale inform Laufer that his Joint Trading Account was cross-margined with the Master Account.

Hale's Control of Allegheny

42. During the relevant period, Hale was 50% shareholder and Vice President of Allegheny. Hale and Steen were the only employees of Allegheny. Although Steen was the co-owner and President of Allegheny, Hale made all of the trades and decisions concerning trading in the Master Account and the Joint Trading Accounts. Hale made the substantive business decisions for Allegheny, while Steen was only responsible for the bookkeeping and administrative duties for Allegheny.

V.

VIOLATIONS OF THE COMMODITY EXCHANGE ACT AND REGULATIONS THEREUNDER

COUNT ONE

VIOLATIONS OF SECTION 4b(a)(2)(i) and (iii) OF
THE ACT: FUTURES FRAUD & MISAPPROPRIATION

43. Paragraphs 1 through 42 are re-alleged and incorporated herein.

44. During the relevant time, Hale violated Section 4b(a)(2)(i) and (iii) of the Act, 7 U.S.C. §§ 6b(a)(2)(i) and (iii), in that he: (i) cheated or defrauded or attempted to cheat or defraud other persons; and (iii) willfully deceived or attempted to deceive other persons by making misrepresentations and omissions of material facts, including, but not limited to, the misappropriation, misrepresentations and omissions set forth at paragraphs 20, 21, 22, 24, 27, 29, 30, 31, 33, 35, 36, 37, 39, 41 and 42.

45. Hale engaged in this conduct in or in connection with orders to make, or the making of, contracts of sale of commodities for future delivery, made, or to be made, for or on behalf of other persons where such contracts for future delivery were or may have been used for (a) hedging any transaction in interstate commerce in such commodity, or the products or byproducts thereof, or (b) determining the price basis of any transaction in interstate commerce in such commodity, or (c) delivering any such commodity sold, shipped, or received in interstate commerce for the fulfillment thereof.

46. The misappropriation, misrepresentations and omissions of Hale described in this count were while Hale was an officer and an agent of Allegheny and, therefore, Allegheny is also liable for his violations of Section 4b(a)(2)(i) and (iii) of the Act, 7 U.S.C. §§ 6b(a)(2)(i) and (iii), pursuant to Section 2(a)(1)(B) of the Act, 7 U.S.C. § 2(a)(1)(B).

47. Each material misrepresentation and omission, including but not limited to those specifically alleged herein, is alleged as a separate and distinct violation of Section 4b(a)(2)(i) and (iii) of the Act, 7 U.S.C. §§ 6b(a)(i) and (iii).

COUNT TWO

**VIOLATIONS OF SECTION 4c(b) OF THE ACT AND
REGULATION 33.10: OPTIONS FRAUD & MISAPPROPRIATION**

48. Paragraphs 1 through paragraph 42 are re-alleged and incorporated herein.

49. During the relevant time, Hale violated Section 4c(b) of the Act, 7 U.S.C. § 6c(b) and Regulation 33.10, 17 C.F.R. §33.10 in that he: (i) cheated or defrauded or attempted to cheat or defraud other persons; and (iii) deceived or attempted to deceive other persons by: misappropriating client funds, making material misrepresentations and omissions of material facts to clients and prospective clients including, but not limited to, the misrepresentations or omissions set forth at paragraphs 20, 21, 22, 24, 27, 29, 30, 31, 33, 35, 36, 37, 39, 41 and 42.

Hale's misappropriation, misrepresentations and omissions described in this count were made in connection with an offer to enter into, the entry into, the confirmation of the execution of, or the maintenance of, commodity options transactions.

50. The misappropriation, misrepresentations and omissions of Hale described in this Count were done while Hale was an officer and an agent of Allegheny and, therefore, Allegheny is also liable for his violations of Section 4c(b) of the Act, 7 U.S.C. § 6c(b) and Regulation 33.10, 17 C.F.R. §33.10, pursuant to Section 2(a)(1)(B) of the Act, 7 U.S.C. § 2(a)(1)(B).

51. Each misappropriation, material misrepresentation and omission, including but not limited to those specifically alleged herein, is alleged as a separate and distinct violation of Section 4c(b) of the Act, 7 U.S.C. § 6c(b) and Regulation 33.10, 17 C.F.R. §33.10.

COUNT THREE

**VIOLATIONS OF SECTION 4o(1) OF THE ACT:
FRAUD BY A CTA**

52. Paragraphs 1 through 42 are re-alleged and incorporated herein.

53. During the relevant time, Allegheny, acting as a CTA pursuant to Section 1a(6) of the Act. Hale, acting as an AP of Allegheny, violated Section 4o(1), 7 U.S.C. § 6o(1) by directly or indirectly employing one or more devices, schemes, or artifices to defraud clients or prospective clients and by engaging in transactions, practices or courses of business which operated as a fraud or deceit upon clients or prospective clients in that they misappropriated client funds, and made misrepresentations and omissions of material facts including, but not limited to, the misrepresentations or omissions set forth at paragraphs 20, 21, 22, 24, 27, 29, 30, 31, 33, 35, 36, 37, 39, 41 and 42.

These acts were effected by use of the mails or other means or instrumentalities of interstate commerce.

54. The misappropriation, misrepresentations and omissions of Hale described in this Count were done while Hale was an officer and an agent of Allegheny and, therefore, Allegheny is also liable for his violations of Section 4o(1), 7 U.S.C. § 6o(1), pursuant to Section 2(a)(1)(B) of the Act, 7 U.S.C. § 2(a)(1)(B).

55. Hale, directly or indirectly, controlled Allegheny and did not act in good faith or knowingly induced, directly or indirectly, the acts constituting Allegheny's violations alleged in this count, and thereby Hale is also liable for Allegheny's' violations of Section 4o(1) of the Act, 7 U.S.C. § 6o(1), pursuant to Section 13(b) of the Act, 7 U.S.C. § 13c(b).

56. Each misappropriation, material misrepresentation and omission, including but not limited to those specifically alleged herein, is alleged as a separate and distinct violation of Sections 4o(1) and of the Act, 7 U.S.C. § 6o(1).

COUNT FOUR

VIOLATIONS OF COMMISSION REGULATION 4.30,
17 C.F.P. § 4.30:
PROHIBITED ACTIVITIES BY CTAs

57. Paragraphs 1 through 42 are re-alleged and incorporated herein.

58. During the relevant time, Allegheny, while acting as a CTA, solicited, accepted or received from existing or prospective clients funds, securities or other property in its own name to purchase, margin, guarantee or secure commodity interests of clients by causing the funds of three clients to be deposited into a bank account controlled by, and in the name of, Allegheny. Therefore, Allegheny violated Commission Regulation 4.30.

59. Hale, directly or indirectly, controlled Allegheny and did not act in good faith or knowingly induced, directly or indirectly, the acts constituting the Allegheny's violations alleged in this count, and thereby Hale is also liable for Allegheny's violations of Regulation 4.30 pursuant to Section 13(b) of the Act.

60. Each act of solicitation, acceptance or receipt of funds, securities or other property in Allegheny's name to purchase, margin, guarantee or secure any commodity interest of a Client is alleged as a separate and distinct violation of Regulation 4.30.

VI.

RELIEF REQUESTED

WHEREFORE, the Commission respectfully requests that this Court, as authorized by Section 6c of the Act, 7 U.S.C. § 13a-1, and pursuant to its own equitable powers enter:

- a) a permanent injunction prohibiting the Defendants from engaging in conduct violative of Sections 4b(a)(2)(i) and (iii), 4c(b), and 6c(1) of the Act, 7 U.S.C. §§ 6b(a)(2)(i) and (iii), 6c(b), and 6c(1), and Regulations 4.30 and 33.10, 17 C.F.R. §§ 4.30 and 33.10;
- b) an order directing the Defendants to disgorge, pursuant to such procedure as the Court may order, all benefits received from the acts or practices which constitute violations of the Act or

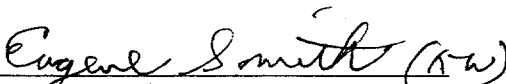
Regulations, as described herein, and interest thereon from the date of such violations;

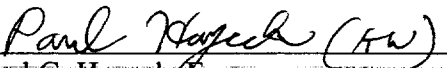
- c) an order directing the Defendants to make full restitution to every client who sustained losses proximately caused by the acts and practices which constituted violations of the Act and Regulations, described herein, and interest thereon from the date of such violations;
- d) an order directing the Defendants to pay a civil monetary penalty in the amount of not more than the higher of \$110,000 or \$120,000 for violations committed on or after October 23, 2000 or triple the monetary gain to each Defendant for each violation of the Act or Regulations;
- e) such other and further remedial ancillary relief as the Court may deem appropriate.

Date: 9-30, 2003

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