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In The United States District Court
For The District Of New Jersey
Camden Vicinage

Commodity Futures Trading Commission, Plaintiff, vs. Equity Financial Group LLC, Tech Traders, Inc., Tech Traders, Ltd., Magnum Investments, Ltd., Magnum Capital Investments, Ltd., Vincent J. Firth, Robert W. Shimer, Coyt E. Murray, and J. Vernon Abernethy, Defendants.	Hon. Robert B. Kugler District Court Judge Hon. Ann Marie Donio Magistrate **Civil Action No: 04-1512 (RBK)** **MOTION DATE: June 2, 2006**

CFTC'S REPLY MEMORANDUM IN SUPPORT OF ITS MOTION FOR PARTIAL SUMMARY JUDGEMENT AGAINST DEFENDANTS EQUITY FINANCIAL GROUP LLC, ROBERT. W. SHIMER AND VINCENT J. FIRTH

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Plaintiff Commodity Futures Trading Commission ("the Commission" or "CFTC") submits this reply to Defendant Robert W. Shimer's Response to Plaintiff's Motion for Partial Summary Judgment ("Response"). In large measure, none of the Defendants dispute any of the evidence the Commission has submitted in support of its Motion.[1] Shimer mainly just disputes the materiality of that evidence. As shown below, the evidence the Commission has presented is material as a matter of law. The fact that parties differ on the legal conclusions to be drawn from the facts is not a bar to summary judgment. *Taylor v. City of Fort Lauderdale,* 583 F. Supp. 514 (S.D. Fla. 1984), *rev'd on other grounds,* 810 F.2d 1551 (11th Cir. 1987). Therefore, the Response shows that this matter is ripe for summary disposition on the charges for which the Commission has moved for summary judgment.[2]

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[1] Defendant Equity Financial Group LLC ("Equity") has filed a Declaration in opposition to the CFTC's Motion that merely joins in Defendant Shimer's Response. *See* Docket Document 357. Defendant Vincent J. Firth ("Firth") has filed no opposition to the Motion. He has filed only a two page Affidavit with Defendant Shimer's Response (Exhibit E to that Response). Thus, Firth's only opposition to the Commission's Motion are the assertions in Exhibit E to Shimer's Response. Defendant Shimer attempts to make assertions of fact for Mr. Firth in his Response, his Statement of Facts and in affidavits he has filed in support of his opposition. *See* Shimer Exhibit I ¶¶ 16, 18, Shimer Exhibit J ¶¶ 10, 11, Shimer Exhibit L ¶¶ 2, 3, 17, Shimer Statement of Material Facts at 4 ¶ 9 ("Shimer Facts"). Shimer does not represent Firth and cannot make assertions of fact on his behalf. Any such assertions in Shimer's Affidavits filed with his Response should be disregarded by the Court in accordance with Local Rule 7.2.

[2] Those charges are that Defendants Equity, Shimer and Firth violated §§ 4k(2), 4m and 4*o*(1) of the Commodity Exchange Act ("the Act"),7 U.S.C. §§ 6k(2), 6m and 6*o*(1) (2002), and that Shimer aided and abetted Equity's 4m violation and Tech Traders' violation of Regulation 4.30, 17 C.F.R. § 4.30 (2006) As the Commission noted in its Memorandum in Support of Motion for partial Summary Judgment Against Defendants Equity Financial Group LLC, Robert W. Shimer and Vincent J. Firth ("Memorandum"), if summary judgment is granted on these charges, the only remaining charge against these Defendants will be a fraud charge under Section 4b of the Act, 7 U.S.C. § 6b.

I. DEFENDANTS HAVE FAILED TO MEET THEIR BURDEN TO SHOW THERE IS ANY GENUINE ISSUE OF MATERIAL FACT.

The Commission has met its "initial responsibility of informing the district court of the basis for its motion, and identifying those portions of the 'pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any,' which it believes demonstrate the absence of a genuine issue of material fact." *Celotex Corp. v. Catrett*, 477 U.S. 317, 323, 106 S.Ct. 2548 (1986). The motion is amply supported by the sworn deposition testimony of both Shimer and Firth, numerous documents that were drafted by Shimer, and the sworn testimony and documents of other witnesses. Thus, the burden of production shifts to the nonmoving party, who "must do more than simply show that there is some metaphysical doubt as to the material facts." *Matsushita Electronic Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 586 (1986) (citation omitted). As Federal Rule of Civil Procedure 56(e) clearly states, he must set forth "specific facts showing that there is a genuine issue for trial."

The Defendants have failed to make the necessary specific factual showing. While Shimer claims to dispute some of the facts, he sets forth no countervailing evidence to refute them. It is not sufficient for a nonmovant to claim that he is going to produce witnesses or evidence at trial to refute the opposing party's evidence.[3] If the Defendants have countervailing evidence, the time to produce it was in their Response.

For the most part, Shimer does not dispute the facts the Commission has set forth in its Statement of Material Facts in Support of The CFTC's Motion for Partial Summary Judgment

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[3] *See, e.g.,* Response at 8: "The above discussion clearly indicates the extent to which much of the documentation now presented to the Court by Plaintiff in it current motion will clearly be contradicted by specific documentary evidence offered by Defendants and testimony by both Shimer and Firth as well as other witnesses offered to distinguish, explain, or completely disprove may of the specific 'facts' offered by Plaintiff."

Against Equity Financial Group, LLC, Robert W. Shimer And Vincent J. Firth ("Statement of Material Facts" or "SMF"). Instead, Shimer disputes just the characterization, materiality or relevancy of those facts, many of which, in reality, are directly supported by Shimer's own sworn testimony or documents he wrote during the period relevant to this action. Indeed, some of those characterizations are the **exact words** Shimer used in documents he drafted during the time relevant to this case.[4] For this Court's purposes, a fact is "material" if it may affect the outcome of the suit under the applicable law. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 248, 106 S.Ct. 2505 (1986); *accord, U & W Indus. Supply, Inc. v. Martin Marietta Alumina, Inc.*, 34 F.3d 180, 185 (3rd Cir. 1994). The issue of materiality typically presents a mixed question of law and fact for the court to assess. *Semerenko v. Cendant Corp.*, 223 F.3d 165, 178 (3rd Cir. 2000), *cert. denied, Forbes v. Semerenko*, 531 U.S. 1149 (2001)..

II. THE UNDISPUTED FACTS ESTABLISH LIABILITY FOR THE REGISTRATION COUNTS CHARGED IN THE COMPLAINT.

Defendants do not even attempt to dispute any of the underlying facts that establish that Equity failed to register as a commodity pool operator ("CPO"), in violation of Section 4m, and that Shimer aided and abetted that violation. *See* SMF ¶¶ 104-125. Shimer knew all along that registration was an issue, was warned repeatedly by experienced commodities counsel, Arnold & Porter, that Shasta was a commodity pool and that Equity ran the risk of serious sanctions and

[4] *See, e.g.,* Shimer's Facts at 4, ¶ 7, in which Shimer disputes the characterization of there being any "conflict" as stated in Plaintiff's SMF ¶ 50. The characterization was his own. In the referenced letter from Shimer to Coyt Murray, Shimer wrote "there is an obvious and inherent **conflict** between your need to maintain your financial privacy and the often legitimate need for an investor like David to receive information that he clearly views as simple good due diligence on his part." Exhibit 405 at RSC 00353 (emphasis added.) in Appendix Volume II in Support of CFTC's Motion for Partial Summary Judgment ("Appendix II"). *See also* Attachment 1 to Second Declaration Of Investigator Joy McCormack In Support Of CFTC's Motion For Partial Summary Judgment ("McCormack Declaration II") in Reply Appendix in Support of CFTC's Motion for Partial Summary Judgment, attached to this Reply Brief ("Reply Appendix").

trading bans for running an illegal commodity pool. *See* SMF ¶¶ 104-125. Shimer's only defense is his claim, already rejected by this Court, that Shasta was not a commodity pool. *See* Response at 2, 10.

The Defendants also do not refute the Commission's well-supported facts that they solicited investors for Shasta without benefit of registration, in violation of § 4k(2) of the Act. *See* SMF ¶¶ 3, 11, 13, 33 and Response at 10. Shimer's only response to this fact is to contend that it does not support a violation of the Act because there was no trading account in Shasta's name. But if this Court affirms its finding that Shasta *was* a commodity pool, Shimer and Firth essentially concede they were its associated persons ("APs").

Shimer likewise presents no credible defense to the charge that he aided and abetted Tech Traders' violation of Regulation 4.30 – a charge that is not dependent on Shasta's status as a commodity pool. Regulation 4.30 states that no commodity trading advisor ("CTA") may accept and trade a client's funds in its name. Shimer does not dispute that he drafted the Investment Agreement between Shasta and Tech Traders that provides that Shasta's funds will be held in the name of Tech Traders, that he drafted the private placement memorandum ("PPM") that sets out the Shasta's funds will be held in the name of the trader or that he collected investor funds in his attorney escrow account and forwarded them to Tech Traders to be traded in Tech Traders' name. *See* SMF ¶¶ 9, 27, 37 and Response at 10-11.[5] Since Tech Traders was a CTA, Shimer is liable for aiding and abetting its violation.

[5] Shimer disputes that he and Firth had "direct knowledge that Murray received any significant funds for commodity trading from individuals or entities other than Shasta," but does not dispute that Murray told him Tech Traders had other investors, which is the salient fact.

III. THE DEFENDANTS HAVE SET FORTH NO EVIDENCE THAT WOULD PRECLUDE A FINDING OF SECTION 4*O* LIABILITY HERE.

A. Key Facts are Undisputed.

The Defendants do not dispute key facts that prove elements of the Commission's § 4*o* claim. They do not dispute that performance results that were produced by Coyt Murray and "verified" by Vernon Abernethy were false. *See* Response at 3. They also do not dispute that these identical false numbers were provided to potential and actual Shasta investors on the Shasta website and that Shimer wrote the content of what appeared on Shasta's website. SMF ¶¶ 34, 35, Response at 10, Shimer Facts at 6, ¶ 11. They do not dispute that between at least June 2001 and April 1, 2004, they solicited and received over $14 million from 65 investors for participation interests in Shasta and transmitted most or all of those funds to Tech Traders. SMF ¶ 33, Response at 10. Thus, the Equity Defendants engaged in "transactions[s], practice[s] or course[s] of business that operate[d] as a fraud or deceit upon [Shasta] participants" under § 4*o*(1)(B). As explained in the Commission's initial Memorandum, it is not necessary to show that Shimer and Firth intended to defraud Shasta participants to hold them liable under §4*o*(1)(B), but only that they acted intentionally. Memorandum at 23-24. The Defendants have not disputed that they intentionally transmitted these false performance numbers to Shasta participants. SMF ¶¶ 10, 35, Response at 10, Shimer Facts at 6 ¶ 11. Shimer also admits that the Defendants had a fiduciary duty to the Shasta investors.[6] The only issue, then, with regard to the Defendants' § 4*o*(1)(B) liability is whether Shimer and Firth did adequate due diligence of the

[6] *See* March 3, 2001 letter to Coyt Murray from Robert Shimer, attached to Exhibit K to the Response at 3, ¶ 3 ("Knowing what I know about Tom and Jerry, **it would be a breach of my fiduciary duty to any of my investors, Vince's investors** and Ursula or Fertina's investors to place funds with you knowing that you have accepted funds from Tom and Jerry or may possibly accept funds from them in the near future after receiving funds from us." emphasis added.)

Tech Traders' investment before soliciting millions of dollars from 65 clients, particularly in light of the numerous red flags they had about Tech Traders. The Commission has set forth ample evidence of Shimer's and Firth's failures to assure their investors' money was properly invested and their total disregard of red flags about Tech Traders. What the Defendants have provided this Court in response does not refute the Commission's well-documented facts.

B. Defendants' Claimed Total Reliance on Elaine Teague to Assure Tech Traders' Trading Results Were Accurate is Unsupported by the Record and Would be Unreasonable Even If True.

It is clear from the record that Shimer orchestrated a flawed independent verification process. Shimer chose an inexperienced friend to handle part of the job and acquiesced in Murray's choice of an inappropriate accountant to perform the other part of the job. Shimer also interposed himself in the design and implementation of the procedures used and then ignored signs that the process was not working. Shimer's submitted evidence either fails to refute the Commission's proof or supports the Commission's case.

1. Neither Teague Nor Abernethy Was Independent.

Shimer has admitted that it was his idea to obtain "independent" verification of Tech Traders' trading results. *See* Shimer Exhibit A to the Response. He attaches three pages of a nine page fax that he sent to Coyt Murray [7] as evidence that he proposed "independent" verification of Tech Traders' returns. The omitted pages from that fax show that, even at its inception, Shimer's "independent" verification process was fatally flawed. On page 8 of the

[7] A slightly different version of this letter, Exhibit 405, is in the summary judgment record. Exhibit 405 was obtained by the Commission from Shimer's computer records. *See* Appendix II; McCormack Declaration II at ¶ 3. Exhibit 405 was marked in Shimer's deposition as it was the only version the Commission had at the time. McCormack Declaration II at ¶ 4 in Reply Appendix. The Commission submits the entire document to the Court with this Reply in the interest of full disclosure. *See* Attachment 1 to McCormack Declaration II.

letter, Shimer proposes that his choice for the "independent" CPA, "dear friend" Elaine Teague, be secretly given a share of the "profits" for verifying those same profits:

> Elaine's real incentive for doing this (apart from the fact that she is a dear friend) is the fact that Vince and I would provide her with compensation that would include a bonus profit sharing plan from our share of company profits. Such an opportunity in profit sharing through the establishment of an account **earmarked for her but not in her name** would provide her with a very tidy retirement sum in addition to what she is earning with her firm.

March 1, 2001 Letter to Murray from Shimer, at 8, ¶ 6 (emphasis added). This statement is compelling evidence that though Shimer touted the "independence" of the CPA verification process in the PPM,[8] in reality, he had no compunction with compromising that independence as to either CPA.[9]

As to Vernon Abernethy's independence, Shimer admits that Abernethy solicited investors for Shasta in 2002 – the first year in which Shasta had any investors. *See* Shimer Exhibit J, ¶¶ 6-8. Although only one prospect invested, Jerry Pettus, the record shows that Firth and Shimer worked with Abernethy in 2002 to attract several other investors, including one "Ron" with whom they discussed forming an LLC to bring in a whole group of Ron's clients as investors. *See* Exhibit 43 (also attached to Shimer Exhibit F) and Exhibit 435 in Appendix II. Firth talked to Abernethy as early as October 2001 about referring investors to Equity and paying him fees. *See* Exhibit 18 and Firth Deposition at 172-73 in Reply Appendix. Shimer also was aware that Abernethy may have solicited investments on behalf of the Sterling entities into Tech Traders, but did not care to investigate whether Abernethy's relationship with Sterling compromised his independence in any way. *See* Shimer Deposition at 853-57 in Reply

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[8] *See* Exhibit 49 at p.17 in Appendix II.

[9] Although Shimer proposed to share profits with Teague, there is no evidence in the record that she ever participated in a profit sharing plan with Equity, Shimer or Firth.

Appendix. Abernethy's cessation of solicitation efforts with Shimer and Firth had nothing to do with any sudden concern on Shimer's or Firth's part that Abernethy was not sufficiently independent, but instead reflects a falling out between them. Id. Abernethy testified that he expected to get paid for his referrals from Shasta, but felt that Shimer and Firth cheated him out of such fees. *See* Abernethy Deposition at 341-42 in Reply Appendix.

2. Shimer and Firth Did Not Rely on Teague to Assure a Reliable Performance Verification Process.

Neither Firth nor Shimer relied on Teague to assure that the performance verification process that Shimer instituted was reliable. Firth had few dealings with Teague and relied on Shimer to handle the performance verification process. SMF ¶¶ 63, 67, 72. Shimer had extensive contact with Abernethy, whom Teague never even met. *See* SMF ¶ 74, Shimer Facts at 7, ¶ 20. Shimer interposed himself into every part of Equity's relationship with Abernethy. SMF ¶¶ 59-60, 62-63, 67, 74, 76-77, and 79-81. Thus, it defies credibility for him to claim that he sat back and let Teague and Abernethy work out the performance verification process.

3. Shimer Was Heavily Involved in the Performance Verification Process and Encountered Red Flags that the Process was not Reliably Verifying Returns.

In submitting Exhibit H, Shimer apparently suggests that he did not see Abernethy's Agreed Upon Procedures ("AUP") letter and that he was not involved in the process by which returns would be verified, reported to Equity and in turn, reported to Shasta investors. However, Shimer received a copy of Abernethy's AUP letter from Teague. *See* Shimer Deposition at 780-81 in Appendix Volume I in Support of CFTC's Motion for Summary Judgment ("Appendix I") and Exhibit S-2 in Reply Appendix. The fact that he claims to not understand these procedures, (SMF ¶ 69) combined with the fact that the language in Abernethy's letter was dramatically different than language that Shimer proposed to Teague, should have caused him to inquire

further about what Abernethy was really doing. (Compare S-2 to draft Collis Wilson & Associates letter attached to June 24, 2001 Shimer letter to Teague, attached to Shimer Exhibit G).

This duty of inquiry was heightened when Shimer interposed himself in the drafting of a letter Teague sent to Equity, which recited the procedures Abernethy was supposed to be performing. SMF ¶ 81. Because Teague did no independent work to verify the returns (SMF ¶ 67), but just passed them along to Equity, which, in turn, passed the performance numbers along to Shasta investors, it was vitally important that the Defendants knew what procedures Abernethy was performing to verify returns. Shimer was confronted with clear evidence early on in the relevant time period that Abernethy was not provided full access to original, unaltered, brokerage statements. There is no basis for Shimer to contend otherwise.

In that same letter, Shimer does not dispute knowing that Abernethy crossed out language reciting that Abernethy had full access to the in-house trading records of Tech Traders and was given the opportunity to review original brokerage statements. Shimer does not dispute that he did not point out to Teague that Abernethy had removed this language. Unlike Teague, Shimer **knew** that Abernethy crossed out this crucial language. Thus, it is of no moment that Teague never advised him that she doubted Abernethy was reviewing original brokerage statements (Shimer Exhibit D, ¶ 5). **Shimer** is the one with an admitted fiduciary duty to Shasta investors – who he told in the PPM would receive returns verified by a CPA who was reviewing original brokerage statements. SMF ¶ 81.

Shimer's reference to a March 15, 2002 email he sent to Abernethy in which he refers to brokerage statements does not refute this clear evidence Shimer had that Abernethy's review of original brokerage statements was suspect. *See* Exhibit 43 at Appendix II (also attached to

Shimer's Exhibit F). In this email, Shimer discusses the minimum account verification he wants Abernethy to perform. He states that he would like to have Teague send Abernethy a fax to which Abernethy would respond that "based upon the original brokerage statements that [Abernethy] reviewed, that the balance reflected on those statements exceeded the amount stated by Elaine to be her estimate of Shasta's investment balance with Tech as of the end of the reporting month." Shimer proceeded to draft letters to and from Abernethy and Teague that stated that Abernethy's confirmation of a minimum account balance was based on the "observation of brokerage account statements for Tech Traders, Inc." *See* Exhibit 465 in Appendix II. Just as he crossed out the wording that he had reviewed original brokerage statements in the draft Teague letter to Equity on the verified rate of return number, Abernethy refused to use Shimer's draft letters that stated he had observed brokerage account statements to determine the minimum account verification. *See* SMF ¶ 89, 92. Ultimately, Abernethy added only a sentence to his AUP letters quarterly that said nothing about "observing" original brokerage statements. Id.

4. Shimer's Formula For Calculating the Rate of Return was Flawed.

Shimer did not rely on either Teague or Abernethy to propose the method that would be used to calculate the rate of return. He concedes that he came up with the simplistic method that essentially measured just cash flow, not actual trading profits in the account. *See* Shimer Exhibit D.[10] The Commission's expert, Susan Koprowski, a Manager in the Compliance Department of the National Futures Association, the self-regulatory arm of the futures industry, has stated in her Report, tendered to the Defendants on March 15 and to the Court in the Commission's summary

[10] He disputes only that he "created" the method. *See* Shimer Facts at 4, ¶ 10. But his sworn testimony shows that the method for calculating returns was "purely" his approach. *See* Shimer Deposition at 531-32 in Reply Appendix.

judgment submission, that one needs, at a minimum, a commodity pool's cash receipts and disbursements journal, general ledger, participants' subsidiary ledger, and bank and trading statements to properly perform a rate of return calculation. See Expert Report at 7.[11]

Ignoring this evidence, Shimer persists in attempting to show how simple it should have been to calculate Tech Trader's rate of return. In support of this proposition, he submits Exhibits C and D, his analysis of a rate of return for his wife's trading accounts and for a single month of one account Tech Traders held. These submissions only illustrate Shimer's lack of experience and show he had no business dictating a method for calculating a rate of return for a commodity pool.

Shimer's review of two months of two individual account of his wife's (Shimer Exhibit C) is not comparable to a proper analysis of Tech Traders' multiple accounts. The LFG account statement has no withdrawals or deposits to factor into the rate of return. The Refco account has only one deposit and no withdrawals. McCormack Declaration II at ¶¶ 6, 7. These are accounts of an individual – not a commodity pool, which had multiple trading accounts at two different future commission merchants ("FCMs") and pool money in a bank account.

Shimer also submits a single Tech Traders GNI account statement for October 2001 (*see* attachment to Shimer Exhibit D) and claims that this "statement of monthly activity does not appear to present any significant obstacle to the computation of an accurate rate of return for that account … after appropriately adjusting for the wire of additional funds ….", without stating what he thinks the rate of return is or indicating how the account should be adjusted for deposits made to it during the month. *See* Shimer Exhibit D ¶ 4. He does not take into account interest

[11] Shimer has not tendered any expert or otherwise disputed Ms. Koprowski's Report. The time for him to tender an expert's report has past – it was due by April 17th under the Scheduling Order. *See* Docket Document 308.

earned or the open trade equity, which would have to be evaluated to determine the profitability of the account. *See* McCormack Declaration II at ¶ 7. His tendering of this Affidavit actually proves his ignorance and inexperience in calculating a rate of return. He was reckless to dictate his simplistic method when he had no training or experience in accounting for pools. SMF ¶ 61.

Shimer and Firth also state that Abernethy and Teague never advised them that his simple method for determining a rate of return would not result in a reliable verification. *See* Shimer Exhibit D and Shimer Exhibit E at ¶ 1. However, Teague did advise both Shimer and Firth that registered CPOs used more complicated methods to calculate a rate of return. She also told Shimer that she did not know what method of calculation was being used by Tech Traders. Teague Deposition at 55-56, 272 in Reply Appendix and Exhibit 426 at ¶ 5 in Appendix II. *See* also SMF ¶¶ 70, 76, 77.[12] Moreover, Teague did not have the expertise to determine a proper method for calculating a rate of return and told Shimer she did not. *See* SMF ¶ 61. Nevertheless, she specifically advised Shimer of the risk that the reported rate of return could be "skewed" if additions and withdrawals were not properly accounted for. *See* Shimer Deposition at 790-91, Exhibit 38 in Reply Appendix. It was not reasonable in light of these facts for Firth and Shimer to rely on Teague's claimed failure to tell them Shimer's method was defective.

C. The Red Flags Surrounding Shimer's Attempts to Get Abernethy to Provide a Minimum Account Verification Are Unrefuted and Material.

Neither Shimer nor Firth dispute any of the facts concerning Shimer's attempts to obtain a minimum account verification that covered Shasta's and New Century's deposits to Tech Traders. *See* SMF ¶ 88-96 and Shimer Facts at 7 ¶ 24. Shimer claims only that these facts are

[12] Shimer states in his Statement of Facts that he disputes many of the individual facts in SMF 76. *See* Shimer Facts at 4, ¶ 14. But he does not state which of the facts he disputes. Indeed, it would be difficult for him to refute any of the facts in SMF ¶ 76, since they come from documents he authored or received and his own sworn testimony.

not material. Here, this Court can determine that it would be important to the reasonable investor to know that Murray and Abernethy would not verify that Tech Traders had enough funds on deposit to cover all its investors' deposits to it.

Shimer personally believed that some kind of minimum account verification was important to investors. He recognized a reasonable person reviewing Murray's refusal to verify investor funds would suspect a Ponzi scheme. *See* SMF ¶ 94. Thus, Shimer persisted for over two years in trying to put some kind of verification in place. On February 22, 2002 when the first investor funds were coming, in Shimer sent Teague the following email:

> I have already spoken to Vernon about this and he is aware of the importance of this general balance verification-especially in light of the Enron nonsense. This will become even more important as the amounts on deposit with Tech by both companies grow into millions and that may start to happen sooner than either one of us expected.

See Exhibit 434 in Appendix II. On April 3, 2004, two days after this case was filed, Shimer was still trying to get Abernethy to provide a minimum account verification, albeit covering Shasta only, on a monthly, rather than a quarterly basis. *See* SMF ¶ 96.

Investors also found this minimum account verification material and those who were sophisticated enough, or who had lost money before, were concerned when they asked and found out that it did not cover all deposits to the fund. *See* SMF ¶ 93. Teague warned Shimer repeatedly that this minimum verification number was meaningless. See SMF ¶¶ 90, 93. Critically, for three months, Abernethy verified a number that was actually **lower** than the amount Shasta alone showed it had on deposit with Tech Traders! *See* McCormack Declaration to initial Memorandum at ¶ 5. Thus, Shimer was reckless to continue to solicit funds and put forth a "verified" minimum balance number that was so misleading.

D. The Defendants' Failure to Disclose the Secret Shadetree Profit Sharing Agreement Was a Material Omission.

The Defendants do not dispute that they never disclosed the secret "profit" sharing arrangement Shimer and Firth had with Murray by which they took 35% of the Tech Trader "profits" when the PPM given to investors stated that Equity was entitled to only a one-time 1% legal and administrative fee and a 5% management fee.[13] Shimer claims only that a) the existence of Shadetree was disclosed to investors who received the first two versions of the PPM, b) neither Firth nor Shimer were "authorized or empowered by any document to make any decisions for Shadetree", and c) that the secret profit split would not have been material to Shasta investors had they known about it. *See* Shimer Exhibit I ¶ 16, 24, 28 and Response at 9. None of Shimer's claims are persuasive.

While the entity Shadetree was briefly identified in the first two versions of the PPM, *see* Exhibit 49 at p. 10 (CFTC 202 01 0197) in Appendix II, nowhere in the PPM does it disclose that Shadetree would receive half of Tech Traders' 50% of profits or 5% of the 15% that the PPM states went to Tech Traders to cover "trading and operational expenses." *See* Exhibit 49 at p. 15 (CFTC 202 01 0202). It was not disclosed that Shimer controlled Shadetree, that all payments Tech Traders made to Shadetree were actually wired to an account in the name of Kaivalya that was under the control of Shimer or that Shimer received $1,314,930 from this arrangement. *See* SMF ¶¶ 24-25, 29-30.[14] Shimer's own sworn testimony shows that he directed that Shadetree be formed, but did not take an ownership interest because he did not want

[13] Defendants violated even the provisions of the PPM. The bank records show that Equity took $612,500 of investor funds when it was entitled to only $277,000 in management fees. *See* McCormack Declaration to initial Memorandum at ¶ 10.

[14] Shimer disputes the "factual accuracy" of these facts though he admits they may be "partially true." *See* Shimer Facts at 6, ¶ 8. He does not offer any contrary evidence, however, to show that the facts are at all inaccurate.

to own a foreign entity. Shimer Deposition at 385-389 in Reply Appendix. He also created Longview, Shadetree's trustee and was the only one authorized to withdraw funds from its "account" at Tech Traders. Shimer Deposition at 375, 414-415 in Reply Appendix. Shimer had Firth set up accounts on the books of Shadetree to pay people portions of the secret profit sharing. Shimer Deposition at 907, 920, 1016-19 in Reply Appendix.

Shimer is wrong as a matter of law in arguing that this secret profit sharing arrangement would not have been material to investors had it been disclosed. Any kind of fees, including any agreements or understandings to receive distributions of profits greater than a person's pro rata share based on his/her contributions to a commodity pool have to be disclosed to investors under Regulation 4.24(i). 17 C.F.R. § 4.24(i) (2006). Information required to be disclosed pursuant to Commission regulations is *per se* material and the Commission has often held that the failure to disclose a fee arrangement is a fraudulent omission. *In re Slusser*, [1998-1999 Transfer Binder] Comm. Fut. L. Rep (CCH) ¶ 27,701 at 48,305, 48,312 (CFTC July 19, 1999), *aff'd, Slusser v. CFTC*, 210 F.3d. 783, 786 (7th Cir. 2000). In *Slusser,* the Commission held that an introducing broker's failure to disclose that it had received commissions is a fraudulent material omission, where its prospectus said that its compensation would be limited to receiving a percent of profits. In the context of commodity options fraud, the Commission stated in *In re Rosenthal & Co.*, [1984-1986 Transfer Binder] Comm. Fut. L. Rep (CCH) ¶ 22,221 at 29,163, 29,177 (CFTC June 6 1984): "[W]e now hold that the omission to disclose fees and commissions is material, that the firm's sales agents violated Regulation 32.9 each time they failed to disclose commissions and fees in their telephone sales presentations to customers, and that the firm is liable as a principal for these violations by its agents." In *In re Citadel Trading Co. of Chicago, Ltd.*, [1986-1987 Transfer Binder] Comm. Fut. L. Rep (CCH) ¶ 23,082 at 32,182, 32,185 (CFTC May 12, 1986),

the Commission held that a registered CTA and AP of an FCM had violated Sections 4b and 4o by soliciting accounts through deceptive means, including "failing to disclose material facts such as his commission-sharing arrangements" with the FCM, where "especially his failure to disclose his commission arrangement … w[as] material." Id. at 32,187-88. In *In re JCC, Inc.*, [1992-1994 Transfer Binder] Comm. Fut. L. Rep (CCH) ¶ 26,080 at 41,568, 41,576 and n.23 (CFTC May 12, 1994), *aff'd*, 63 F.3d 1557 (11th Cir. 1995), the Commission held that the solicitation activities of an FCM misled customers about material elements of the investment program, such as the size of the management fee. Thus, as a matter of law, the Defendants' failure to disclose the secret Shadetree profit sharing arrangement was material.

Evidence also shows that this was information that investors would have found important to know and that Shimer knew that. Shimer claims that investor Stevenson testified in his deposition that he would not have cared if Murray decided to divide his "profits" with another entity. The Commission has attached to its Reply Appendix the testimony Shimer refers to as well as the follow-up testimony. *See* Stevenson Deposition at 154-55, 163-64 in Reply Appendix. This testimony shows that, although Stevenson may not have cared if Tech Traders was giving some of its "profits" to charity, it was very important to him to know Shimer and Firth were receiving these secret profits. Moreover, Shimer knew investors would find this information important and sought to conceal it from investors who might find it a deterrent to investment. In providing background information about prospective investor David Kaplan, Shimer told Murray that "he [Kaplan] does not know anything about your further profit splitting arrangement with Vince and I." Exhibit 404 at p. RSC 00351 in Appendix II. If Shimer thought this information was immaterial to investors, why did he make a point of telling Murray that Kaplan did not know anything about it?

Thus, the law and the evidence show that failure to disclose the secret profit sharing arrangement was a material fraudulent omission that is actionable under §4*o*(1)(B).

E. Shimer's Reliance on The Returns of Other Funds and Murray's Three Ring Binder is Misplaced.

Shimer asserts in Exhibit I that "the returns being verified by Abernethy and conveyed to Shasta's CPA while extraordinary were not at all impossible or unlikely in light of the demonstrated audited performance of other registered CPOs or CTA's [sic] that engaged in the trading of commodity futures." Shimer Exhibit I at ¶ 32. Shimer then claims he had such information at his disposal, but submits only a table of performance information on Hanseatic Discretionary Pool, LLC in support. Id. at ¶ 42[15]. Apparently, this is offered to support his position that it was reasonable for him to believe the Tech Traders' returns were real, despite the evidence he fails to refute that shows Shimer and Firth encountered many red flags that those results were not.

Even ignoring all those red flags, Shimer's submission of this table on Hanseatic Discretionary Pool does not support a finding that his reliance was reasonable. First, Shimer knows, because Teague told him many times, that one cannot compare the rates of return of two commodity pools unless one knows the method of calculating the rate of return for the two funds. *See* Shimer Deposition at 811-14; Teague Deposition at 500-04, 539-41; and Exhibit 423 in Reply Appendix; Exhibit 430 in Appendix II. Second, the funds' performance was not comparable. Tech Traders reported gains for every month or quarter from June 2001 through February 2004, and double digit gains for at least 23 of the 33 months during that period. *See*

[15] Shimer claims that Hanseatic Discretionary Pool, LLC, was referenced in Shasta's first PPM. *See* Shimer Exhibit I at ¶ 36. Shimer is mistaken. This fund has no relation to the pool affiliated with registered CPO Hanseatic Corporation, which was referenced in Shasta's PPM and on its website. *See* McCormack Declaration II at ¶ 8.

SMF ¶ 71. Unlike Tech Traders, Hanseatic Discretionary Pool showed both gains and losses during the 26 months reflected. For the 28 periods reported, 11 of the periods reflect losses; and for the 17 periods reported as purportedly profitable, 10 of them show single digit gains, or less. *See* McCormack Declaration II at ¶ 9 .[16]

Shimer's reliance on Murray's description of his trading system in the three ring binder is also unreasonable. *See* Shimer Exhibit L and attachment thereto. He does not provide any evidence that the trading results set out in Murray's materials were actual trading results based on trading with actual dollars, rather than hypothetical results. *See* SMF ¶¶ 22-23. And Shimer had no reason to believe that Murray's trading system was unique, given that Dennis Mayer contacted Firth and Shimer to tell them that the system they touted was based on math formulations stolen from him. SMF ¶ 36.

F. Shimer's and Firth's Past Business Failures and Murray's Continued Association with Leonard and LaTulippe are Relevant and Material to Their Section 4*o* Liability.

Shimer does not dispute any of the facts surrounding his failed relationship with Kaivalya, through which he solicited and lost approximately $2 million of investor money. He states that the facts are misleading and incomplete, but does not tell the Court how they are misleading and incomplete. *See* Shimer Facts at 6, ¶ 7, Response at 9. He also claims that his and Firth's past business failures, which involved losing client money, are irrelevant and immaterial. *See* Shimer Facts at 5, ¶¶ 1-3 and at 6, ¶¶ 6, 7.

Like their failure to disclose the secret profit sharing arrangement, their failure to disclose these past business failures is material as a matter of law. The Regulations with respect to CPOs

[16] A comparison of the fund that was actually listed on Shasta's website and in its first two PPMs also shows that this pool experienced losses, unlike Tech Traders' reported consistent profits. McCormack Declaration II at ¶¶ 12-15.

provide that the business background for the five years proceeding the date of a Disclosure Document has to be disclosed by CPOs, operators of major investee pools and their principals who participate in making trading or operational decisions for the pool. 17 C.F.R. § 4.24(f) (2006). As stated above, information required to be disclosed pursuant to Commission regulations is *per se* material. *In re Slusser*, [1998-1999 Transfer Binder] Comm. Fut. L. Rep (CCH) CFTC ¶ 27,701 at 48,312.

Even if the regulations did not require disclosure, Shimer's and Firth' past business failures were material to Shasta investors. They both lost other people's money. Firth's clients sued him and obtained judgments against him for his actions in introducing them to the Badische Trust. SMF ¶ 15. Shimer received a great deal of pressure from Kaivalya investors who wanted their money back. *See* SMF ¶ 21. This pressure caused him to be careless and ignore all the red flags about Murray that should have made him suspect. *See e.g.* SMF ¶¶ 22, 23.

Investors would have also found their past business failures to be material. Stevenson not only testified that Shimer and Firth's business backgrounds were important to his investment decision, but actually conducted a records search on Shimer. Stevenson Deposition at 40-41 Appendix II and 94-95, 160-61, Exhibit 654 in Reply Appendix. Moreover, Shimer himself thought this information, and his resulting strained financial circumstances, was material and knew its disclosure might squelch a deal with potential investor David Kaplan. In a letter concerning an upcoming introduction of Kaplan to Murray, Shimer wrote:

> Also please don't let on that you are aware of any of the details surrounding the postponement of our condo closing. Nor does David know anything about the Tom and Jerry fiasco. I would rather that not come up at all. David is a very good person. He is very sincere but he is also a very shrew [sic] and capable business man. No one builds a company and then sells it to Reader's Digest for that much money with out either having or developing very good business instincts.

Exhibit 404 at RSC 00350in Appendix II. Thus, this information was material as both a matter of fact and of law and should have been disclosed to Shasta investors.

The Commission submitted the fact of Murray's propensity to continue to associate with known con artists to show that it should have been a red flag to Shimer. Shimer submits Exhibit K as to counter that "impression." Response at 10. However, what Shimer has submitted goes even further and shows what he now denies – that he would be willing to solicit funds for Murray regardless, so long as Leonard and LaTulippe ("Tom and Jerry") paid off his Kaivalya investors! In the 5 page fax Shimer sent to Murray on March 3, 2001,[17] attached to Shimer Exhibit K, he wrote:

> If Tom and Jerry are *actually ready* to send you funds and you are willing to accept them I will just have to hope that you make Tom and Jerry repay me *as a condition of investing with you.*

March 3, 2001 letter at 4 (emphasis in the original).

IV. DEFENDANTS DO NOT DISPUTE CONTROLLING PERSON OR SECTION 2(a)(1)(B) LIABILITY OR THE APPROPRIATENESS OF THE RELIEF SOUGHT.

Neither Firth nor Shimer have disputed that they were controlling persons of Equity and the evidence is overwhelming that they were. *See* SMF ¶¶ 7, 10, 13, 14, 24, 27, 29- 30, 33-37, 42-44, 47–55, 59-63, 67, 70, 74, 76-94, 96-102, 104-129. Therefore, Shimer and Firth are liable for Equity's violations of the Act, pursuant to Section 13(b) of the Act, because, as set forth above and in the initial Memorandum, they both knowingly induced and failed to act in good faith with respect to Equity's violations. Likewise, Equity has not disputed that it is liable for Firth's and Shimer's actions under Section 2(a)(1)(B) of the Act, 7 U.S.C. § 2(a)(1)(B) (2002).

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[17] This is the first time the Commission has seen this letter. It has never been produced to the Commission. *See* McCormack Declaration II at ¶ 17.

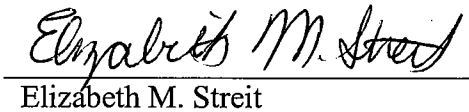
None of the Defendants have disputed the appropriateness of a permanent injunction if they are found liable of violating the charges on which the Commission has moved for summary judgment. They also do not dispute that awards of restitution and disgorgement are appropriate if they are found liable or dispute the amount of the awards that the Commission requests. Likewise, they do not dispute that civil monetary awards are appropriate or the amounts that Commission requests. The relief the Commission has requested should therefore be granted.

V. CONCLUSION

Equity, Firth and Shimer have not met their burden to set forth specific facts establishing a genuine issue of material fact. The Commission has presented overwhelming evidence that these Defendants have violated Sections 4k, 4m and 4*o* of the Act and that Shimer has violated Regulation 4.30. This evidence has gone unanswered. Under Rule 56, the Commission's motion for partial summary judgment should be granted.

Date: May 25, 2005

Respectfully submitted,



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