

**IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION**

UNITED STATES COMMODITY)	
FUTURES TRADING COMMISSION,)	
Plaintiff,)	
)	
v.)	07 C 3598
)	
LAKE SHORE ASSET MANAGEMENT)	
LIMITED, et al.,)	
Defendants.)	

MEMORANDUM AND ORDER

Following the status hearing on January 10, 2008, the court had an opportunity to study the recent flurry of filings in this case. This order addresses the multiple issues raised during the status hearing, as well as Lake Shore Limited’s motion to vacate the court’s orders finding it in civil contempt and indicating that the court is considering referring this matter to the United States Attorney for potential criminal contempt proceedings against Lake Shore Limited.

I. Civil and Criminal Contempt Against Lake Shore Limited

A. Lake Shore Limited’s Motion to Vacate the Order Finding it in Civil Contempt and the Order Concerning a Criminal Contempt Referral

Lake Shore Limited has filed a motion asking the court to vacate its orders finding it in civil contempt and soliciting views regarding a possible referral for criminal contempt proceedings. In support, it asserts that it would be “unfair and unjust to place [Lake Shore Limited] under potential criminal sanction for violations of an order that must be revised pursuant to the Seventh Circuit’s opinion” or to have Lake Shore Limited “incur daily monetary sanctions for violations of an order which must be revised.” *CFTC v. Lake Shore Asset Management Limited*, Docket No. 381 at ¶¶ 5 & 6. The court disagrees, as the preliminary

injunction ordered Lake Shore Limited to turn over its own books and records. Lake Shore Limited repeatedly refused to do so, and contempt proceedings followed.

Meanwhile, the Seventh Circuit recently affirmed the portions of the preliminary injunction order directed at Lake Shore Limited, stating:

Our decision of October 15 [denying Lake Shore Limited's motion seeking a stay of the receivership order pending appeal] says pretty much everything needed to explain why the injunction entered against Lake Shore must remain in effect. The company's briefs in No. 07-3070 scarcely engage the language of 7 U.S.C. §6n(3)(A) and 17 C.F.R. §§ 1.31, 4.23, and 4.33, on which the order principally rests. Instead Lake Shore devotes most of its energies to denying that the CFTC may regulate acts that occur outside the borders of the United States. That's true enough — authority for extraterritorial regulation must be express, see *EEOC v. Arabian American Oil Co.*, 499 U.S. 244 (1991), while 7 U.S.C. §6n does not mention activities that domestic firms conduct in other nations — but beside the point.

Lake Shore transacts its business in the United States. It voluntarily registered with the CFTC and joined the NFA. It assures customers that it is subject to U.S. law, doubtless thinking that submitting to regulation in this nation would make its promises credible. Some of the trades occur on exchanges in the United States; some customers' assets are held here. Federal law controls how Lake Shore must conduct itself within the United States, even though other companies in the same affiliated group do their business outside, and even though most of the group's business is with investors from other nations. Having registered with domestic agencies — and having assured the NFA as a condition of membership that no foreign secrecy law prevents compliance with this nation's disclosure requirements — Lake Shore must abide by federal law, including the record-keeping-and-disclosure rules.

Lake Shore maintains that the freeze is invalid, even if the disclosure order is proper, because the CFTC has failed to prove that any of its customers relied on a misrepresentation. But the CFTC need not show reliance by private investors in order to obtain relief. See *Slusser v. CFTC*, 210 F.3d 783 (7th Cir. 2000). Reliance is an element in a private action for damages; proof of reliance is not required in a regulatory agency's suit — or for that matter a criminal prosecution. See *United States v. Rosby*, 454 F.3d 670 (7th Cir. 2006).

CFTC v. Lake Shore Asset Management Limited, Nos. 07-3057 & 07-3070, — F.3d. —, slip op. at 7-8 (7th Cir. Dec. 28, 2007).

Lake Shore Limited's position that the Seventh Circuit's opinion somehow vitiated the preliminary injunction's command to turn over its own books and records is thus wholly unfounded. No amount of further briefing will change the fact that the Seventh Circuit's opinion narrowed the scope of the preliminary injunction order but left the heart of that order requiring immediate production of Lake Shore Limited's own books and records intact. Any revisions to the preliminary injunction once the mandate issues, therefore, do not affect Lake Shore Limited's obligation to produce its own books and records as Lake Shore Limited was obligated to produce its own books and records both before and after the Seventh Circuit issued its opinion in the preliminary injunction appeal. Accordingly, Lake Shore Limited's request to vacate based on the need to revise the preliminary injunction order is denied.

B. Civil Contempt

To this day, Lake Shore Limited has refused to turn over its own books and records. After the Seventh Circuit issued its opinion, Lake Shore Limited asserted that it had produced all of the documents it controlled. *See CFTC v. Lake Shore Asset Management Limited*, Docket No. 377. It now appears to be arguing that the court should revisit its order imposing civil contempt sanctions based on this alleged and unsubstantiated lack of control. Upon reviewing Lake Shore Limited's first filing containing this assertion (which is dated January 8, 2008 – two months after the court's finding of civil contempt) the court stated:

In response to the Seventh Circuit's opinion, Lake Shore Limited has advised the court that it has produced everything it can, because its documents located outside the United States are beyond its control. It does not provide

specifics or point to any evidence supporting this contention. If Lake Shore Limited wishes to continue to advance this argument, it must state exactly what documents are allegedly beyond its control, identify the custodian and location of those documents, and otherwise produce admissible evidence documenting its claim that it cannot produce its own documents. Vague assertions are insufficient.

In any event, this argument is frivolous because if Lake Shore Limited gave its documents to another entity, it has the power to get them back. Merely passing Lake Shore Limited documents to a different entity (*e.g.*, another Lake Shore entity) – assuming this happened – does not magically transform those documents from Lake Shore Limited documents into a different Lake Shore entity's documents. As the court has said time and time again, and as the Seventh Circuit has affirmed, Lake Shore Limited must turn over its own documents. This includes but is not limited to the boxes of Lake Shore Limited documents that were previously held by Roth Mosey & Partners LLP, a Canadian accounting firm that acted as Fund Administrator, given that Lake Shore Limited was the trading advisor and pool operator for the Lake Shore funds.

The claim that Lake Shore Limited's own documents are outside its control is also inconsistent with the receiver and CFTC's contention that one of Lake Shore Limited's own lawyers, Alexandre Schwab, took boxes of the Roth Mosey Lake Shore Limited documents from Bermuda to Switzerland. Obviously, documents that are in the possession of a party's attorney or documents that have been secreted somewhere by a party's attorney or agent are still in that party's control, regardless of whether the documents are in the United States or not. Any other holding would make a mockery out of not only this court's orders but also the discovery rules.

CFTC v. Lake Shore Asset Management Limited, Docket No. 385.

Subsequent to this order, the CFTC filed a memorandum and supporting exhibits consisting largely of documents obtained from authorities in Bermuda. *See id.* at Docket No. 379. These documents make for compelling reading and, among other things, detail the journey of Lake Shore Limited's books, records, and computer server from Canada (where they were held by Roth Mosey) to Bermuda and then onto Switzerland in the care of Mr. Schwab. *See id.* at Ex. 4 & 6. Lake Shore Limited appears to believe that if it transfers its documents to an entity that gives the documents to another entity that then gives the documents to yet another entity that

sends the documents to Mr. Schwab, Lake Shore Limited's own attorney, the documents are somehow beyond its control.

Courtesy of the authorities in Bermuda, the court has reviewed emails from Mr. Schwab authorizing the shipment of the Lake Shore Limited server and documents to him. *See id.* at 6, page 4 & 5; *see also* Ex. 4 at pp. 12-13 ("Lake Shore Box Delivery List" including, among other things, eighteen boxes of client files). On September 11, 2007 (the day after Lake Shore Limited learned of the Seventh Circuit's order denying Lake Shore Limited's motion for a stay of the preliminary injunction order), Mr. Schwab described the server and boxes as belonging to Pinnacle Ventures (a new Belize entity formed by Mr. Baker and staffed by Lake Shore employees, *see id.* at Ex. 1, 2 & 4) and asked the custodian to send them to him. *Id.* at Ex. 6, p. 4.

Thirty-four minutes later, he emailed the custodian again and clarified that the documents and server in fact belonged to Lake Shore Limited, stating, "I am acting on behalf of Lake Shore Asset Management Ltd. and therefore confirm the request of Pinnacles [sic] Ventures to have you send to my address below the server and all books and records of 'Lakeshore.'" *Id.* at p. 5. The documents and server were then mailed to Mr. Schwab via UPS. *See id.* at Ex. 8. No evidence suggests that the documents and server failed to reach their destination.

A lawyer is an agent of his client, so when an attorney possesses his client's business records, the client constructively possesses those records and must produce them. *See Fisher v. U.S.*, 425 U.S. 391, 403-04 (1976) ("pre-existing documents which could have been obtained by court process from the client when he was in possession may also be obtained from the attorney by similar process following transfer by the client" even if the client transfers its pre-existing

documents to seek legal advice); *see also Avery Dennison Corp. v. UCB Films PLC*, No. 95 C 6351, 1998 WL 293002, at *2 (N.D. Ill. May 28, 1998) (client documents held by an attorney are not shielded from production).

Lake Shore Limited has never suggested that it would have produced its documents (both paper and electronic) but was thwarted from doing so because Mr. Schwab or the custodian of the moment refused to comply with its directions to turn over its documents. To the contrary, nothing in the record even remotely supports such a theory, and all of the evidence flatly contradicts it. For example, Lake Shore Limited's brief opposing the imposition of civil contempt sanctions, its status reports post-dating the imposition of civil contempt sanctions, and its brief opposing a criminal contempt referral would have been excellent times to raise a defense of impossibility. Lake Shore Limited, however, simply reiterated its refusal to comply with the court's orders.

Moreover, even assuming hypothetically that Lake Shore Limited lacks control over its own documents now and thus cannot produce them, an alleged lack of control today does not translate into past lack of control. Anyone even remotely familiar with this case will recall that prior to the December 28, 2007, genesis of Lake Shore Limited's current and unsupported "lack of control" argument, Lake Shore Limited flatly refused to produce its documents based on arguments that had been previously rejected by this court and were recently rejected by the Seventh Circuit. It cannot go back in time and rewrite history to change its past claims that this court lacked authority to order it to produce its documents into an argument that it was always ready, willing, and able to produce its documents but was prevented from doing so by forces beyond its control.

In addition, again assuming for the moment that evidence showing that the documents and server are currently beyond Lake Shore Limited's control exists, in light of the preliminary injunction order's language, Lake Shore Limited was required to maintain control over its own documents. *See Goluba v. School Dist. of Ripon*, 45 F.3d 1035, 1037 (7th Cir. 1995) (the district court "may find a party in civil contempt if that party has not been reasonably diligent and energetic in attempting to accomplish what was ordered") (internal quotations omitted). Thus, even if Lake Shore Limited can produce evidence substantiating its alleged lack of control today, it cannot absolve itself from responsibility for its past actions by simply pointing a finger at someone else now.

Lake Shore Limited's recent, conclusory, and unsupported arguments about lack of control, therefore, do not advance its cause. The court has provided Lake Shore Limited with numerous chances to produce its books and records as it has repeatedly ordered Lake Shore Limited to file written submissions advising the court if its position regarding production had changed. Nothing – except a complete lack of desire to produce its books and records – has ever stopped Lake Shore Limited over the past months from raising the defense of lack of control and submitting supporting evidence.

In short, Lake Shore Limited's present, unsubstantiated claim of lack of control appears to be yet another delay tactic. Lake Shore Limited's past refusal to comply with the portion of the preliminary injunction order requiring production of its own documents in and of itself provides ample support for the court's imposition of civil contempt sanctions. This is not a case where a party has made a colorable claim of lack of control, shown that there are no documents to produce, or pointed to evidence indicating that it is acting in good faith. Instead, it is a case

where a party has deliberately flouted the court's order to produce its books and records at every turn. The Seventh Circuit affirmed the portion of the injunction requiring Lake Shore Limited to produce its own books and records and Lake Shore Limited must do so.

Nevertheless, Lake Shore Limited is entitled to try to purge its contempt via the submission of admissible evidence. Lake Shore Limited's requested two-week date to respond to the CFTC's January 9th filing is unacceptable. Lake Shore Limited could have submitted evidence about its purported lack of control over its own records at any point after the Seventh Circuit denied its motion for a stay of the preliminary injunction order on September 7, 2007. It also could have submitted evidence regarding its new lack of control argument at any point after December 28, 2007, when the Seventh Circuit's opinion caused it to conceive this defense. Yet, it is asking to push this issue into February of 2008. Its suggested briefing schedule is thus rejected. Lake Shore Limited may file a response to the CFTC's filing placing Lake Shore Limited's records and server with Mr. Schwab in Switzerland (Docket No. 379) by no later than January 17, 2008. In the meantime, the remedial and coercive civil contempt sanctions imposed by the court will continue to accrue.

C. Criminal Contempt

18 U.S.C. § 401(3) gives a federal court power to punish "[d]isobedience or resistance to its lawful writ, process, order, rule, decree, or command" as contempt. Civil contempt is meant to coerce, while criminal contempt is meant to "punish the contemnor, vindicate the court's authority, or deter future misconduct." *In re Grand Jury Proceedings*, 280 F.3d 1103, 1107 (7th Cir. 2002). As noted above, even if Lake Shore Limited is able to produce evidence that

convinces the court that it cannot control its own documents today, it still has a serious problem on its hands because a purported lack of control today does not equate to past lack of control.

In the interests of judicial efficiency, however, the court will decide whether to refer this matter to the United States Attorney for consideration of criminal contempt charges against Lake Shore Limited after Lake Shore Limited responds to the CFTC's January 9th filing.

II. Civil and Criminal Contempt Against Mr. Baker

In its January 9, 2007, order, the court stated:

The court previously found that Mr. Baker was in civil contempt based on his willful refusal to comply with the preliminary injunction and receivership orders. In general, Rule 65(d) is considered to be a codification of “the long settled principle that personal service of an injunction is not required so long as those whom the plaintiff seeks to hold in contempt had actual notice of the decree.” *Vuitton et Fils S.A. v. Carousel Handbags*, 592 F.2d 126, 129 (2d Cir. 1979); *see also U.S. v. Baker*, 641 F.2d 1311, 1316 (9th Cir. 1981) (“In civil contempt proceedings, formal or personal service is not required” – instead, “[k]nowledge of the order suffices”); *U.S. v. Phillips*, 525 F.Supp. 1, 7 (N.D. Ill. 1981) (“personal service of a court order is not generally required in order to support a finding of civil contempt for disobeying the order”).

However, Local Rule 37.1 has come to the court's attention. This rule provides that “a proceeding to adjudicate a person in civil contempt of court . . . shall be commenced by the service of a notice of motion or order to show cause Where the alleged contemnor has appeared in the action by an attorney, the notice of motion or order to show cause and the papers upon which it is based may be served upon that attorney; otherwise service shall be made personally, in the manner provided for by Fed.R.Civ.P. 4 for the service of a summons.” This rule would appear to support the conclusion that Mr. Baker must be personally served with the rule to show cause prior to holding him in civil contempt. Based on Local Rule 37.1, the court is considering revisiting its civil contempt order directed at Mr. Baker due to the lack of personal service of the underlying rule to show cause. *See Drywall Tapers and Pointers of Greater New York, Local 1974 of I.B.P.A.T. AFL-CIO v. Local 530 of Operative Plasterers and Cement Masons Intern. Ass'n*, 889 F.2d 389, 397-98 (2d Cir. 1989). The court notes that any such ruling would not preclude it from referring Mr. Baker's knowing refusal to comply with court orders for possible criminal contempt proceedings. *See In re Teknek*, No. 07-1498, — F.3d —, slip op. at 6 (7th Cir. Dec. 28, 2007).

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The court asked the parties to comment during the status hearing on the need for personal service in connection with civil contempt proceedings or to request a briefing schedule. As counsel did not submit argument on this issue during the status hearing, the court hereby directs the CFTC and the receiver to file memoranda addressing the necessity for personal service by January 21, 2008. It further directs Lake Shore Limited's counsel to forward these filings to Mr. Baker. In this regard, the court appreciates that Lake Shore Limited's counsel does not represent the elusive Mr. Baker, but counsel can necessarily get in touch with Mr. Baker given that he is Lake Shore Limited's Managing Director, Principal and President. Mr. Baker may respond by January 25, 2008, but if he fails to do so, the court will rule without the benefit of his views. With respect to a possible referral for criminal contempt proceeding against Mr. Baker, the court will rule on this when it rules on the propriety of civil contempt sanctions directed at an individual who has actual notice but has not been served with process under Fed. R. Civ. P. 4.

III. The Receivership Order

Lake Shore Limited has filed a motion [#383] asking this court to certify whether it would be inclined to grant a Rule 60(b) motion seeking a modification of the October 4, 2007, receivership order that is currently on appeal as Seventh Circuit Case No. 07-3408. The receivership order was immediately appealable under 28 U.S.C. § 1292(a)(2), but is not a final order. For "an appeal from an interlocutory order, Circuit Rule 57 is inapplicable." *Adams v. City of Chicago*, 135 F.3d 1150, 1153 (7th Cir. 1998).

Even if Circuit Rule 57 was applicable, Lake Shore Limited has not filed a motion under an appropriate rule requesting specific relief directed at the interlocutory receivership order. *See*

Cir. R. 57 (“A party who during the pendency of an appeal has filed a motion under Fed. R. Civ. P. 60(a) or 60(b), Fed. R. Crim. P. 35(b), or any other rule that permits the modification of a final judgment, should request the district court to indicate whether it is inclined to grant the motion”). The parties thus have not had an opportunity to address the precise nature of the changes that need to be made to the receivership order.

Nevertheless, it is clear that some changes must be made in light of the Seventh Circuit’s comments about personal service. The Seventh Circuit has noted that “the spirit of Circuit Rule 57” can provide helpful guidance if intervening events occur while an interlocutory appeal is pending. *See id.* at 1154. The court believes that the interests of judicial efficiency strongly support revisiting its receivership order in light of the Seventh Circuit’s recent opinion addressing Lake Shore Limited’s appeal of the preliminary injunction. Any party dissatisfied with the revised order can file a fresh appeal, and the Seventh Circuit thus will face only a single potential appeal based on an order that takes its pronouncements in the preliminary injunction appeal into account. Therefore, the court certifies that if the Seventh Circuit were to remand the receivership appeal, it would be inclined to solicit the parties’ views and revisit the receivership order as appropriate once the mandate issues in the preliminary injunction appeal.

In the interests of completeness, the court also notes that Lake Shore Limited did not challenge the court’s finding in the preliminary injunction order that Lake Shore Limited was the trading advisor and pool operator for the Lake Shore Funds. Indeed, the Seventh Circuit’s opinion opens by describing Lake Shore Limited as “a commodity-pool operator and adviser in the derivatives business.” *Id.* at 2. The record also shows that Lake Shore Limited had “sole authority and responsibility for the investment” of the Lake Shore Alternative Financial Asset

Fund's assets. *See, e.g.*, CFTC Preliminary Injunction Ex. 6 at p.5 (Investment, Redemption and Transfer Procedures for Lake Shore Alternative Financial Asset Fund IV).

Based on the current record, Lake Shore Limited's portrayal of itself as completely distanced from customer funds is, therefore, factually inaccurate. To the extent that Lake Shore Limited had the ability to cause the assets of the Lake Shore Alternative Financial Asset Funds to be moved, it also appears that the receiver can also do so in its capacity as a receiver for Lake Shore Limited. There are, however, issues to be resolved with respect to the entities directly bound by the receivership order that the court would like to address at whatever point the receivership order is back before it.

IV. Mr. Schwab

The court is profoundly disturbed by the emails attached to the CFTC's January 9th filing regarding Mr. Schwab's involvement with the peripatetic Lake Shore Limited documents and server. Of course, however, it reserves judgment until Mr. Schwab has had an opportunity to respond. The CFTC represented that it intends to serve Mr. Schwab with process, so the court will hold this matter in abeyance pending further developments.

V. Mr. Nissen

The documents obtained via the Bermuda authorities included a June 29, 2007, email from Mr. Baker to Lake Shore Limited's then-attorney, William Nissen. June 29th was two days after the issuance of the original statutory restraining order. The June 29th email sent to Mr. Nissen attached an undated letter on the letterhead of Lake Shore Alternative Financial Asset Account I Ltd. changing the asset manager for all of Lake Shore Limited's accounts at Man Financial. Specifically, the letter "authorize[d] the appointment of Geneva Asset Management,

S.A.” and “replace[d] Lake Shore Asset Management Limited and Lake Shore Asset Management, Inc. . . . effective immediately.” *CFTC v. Lake Shore Asset Management Limited*, Docket No. 379, Ex. 5. The reader may recall that Mr. Schwab’s law firm is the administrator for Geneva Asset Management. According to the CFTC, Geneva Asset Management is the successor to one or more Lake Shore entities.

On July 19, 2007, Mr. Nissen submitted a declaration in support of Lake Shore Limited’s motion to modify or dissolve the statutory restraining order and on July 23, 2007, he submitted a declaration from Mr. Baker. *See id.* at Docket Nos. 30 & 37. These filings did not reflect the change at the Man accounts, which would have been a violation of the statutory restraining order. At the status hearing on January 10, 2008, Mr. Nissen’s counsel (who has appeared due to the pending rule to show cause issued against Mr. Nissen) stated that Mr. Nissen had asked Mr. Baker about the change and Mr. Baker advised him that the letter had never been sent.

Mr. Nissen accepted this representation because documents produced by Man did not include a letter seeking to change the asset manager for the Lake Shore accounts at Man. Mr. Nissen turned over all of the documents produced by Man, but the record does not show what Man was asked to produce.

Based on the present record, therefore, the court accepts counsel’s representations regarding the basis for withholding the letter. The court trusts that the CFTC will file an appropriate motion if it believes that: (1) it would have been unreasonable to conclude that if the letter changing the asset manager for Lake Shore Limited’s Man accounts had been sent, it would have been included in the documents produced by Man; or (2) the letter should have been produced even if counsel believed it had not been sent.

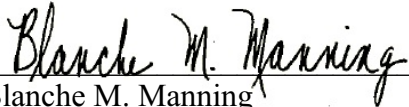
VI. Conclusion

For the above reasons:

- (1) Lake Shore Limited's motion to vacate the court's orders finding Lake Shore Limited in civil contempt and concerning a criminal contempt referral [#381] is denied;
- (2) Lake Shore Limited may respond to the CFTC's January 9, 2008, filing (Docket No. 379) by no later than January 17, 2008. In the meantime, the remedial and coercive civil contempt sanctions imposed by the court will continue to accrue;
- (3) The court will decide whether to refer this matter to the United States Attorney for consideration of criminal contempt charges after Lake Shore Limited files its response to the CFTC's filing;
- (4) The court finds that the interests of judicial efficiency strongly support revisiting its receivership order in light of the Seventh Circuit's recent opinion addressing Lake Shore Limited's appeal of the preliminary injunction. It thus certifies that if the Seventh Circuit were to remand the receivership appeal, it would be inclined to solicit the parties' views and revisit the receivership order as appropriate once the mandate issues in the preliminary injunction appeal;
- (5) The CFTC and the receiver shall file memoranda by January 21, 2008, regarding the need to personally serve Mr. Baker in connection with the civil contempt proceedings. Lake Shore Limited's counsel shall use his best efforts to forward these filings to Mr. Baker. Mr. Baker may respond by January 25, 2008, but if he fails to do so, the court will rule without the benefit of his views;
- (6) The court will hold further proceedings regarding Mr. Schwab's involvement with the hidden Lake Shore Limited documents and server in abeyance so that the CFTC can serve him with process; and
- (7) Based on the present record, the court accepts the representations regarding Mr. Nissen's reasons for withholding a letter post-dating the statutory injunction that purported to change the asset manager for all of Lake Shore Limited's accounts at

Man Financial from Lake Shore Asset Management Limited and Lake Shore Asset Management, Inc. to Geneva Asset Management.

DATE: January 14, 2008


Blanche M. Manning
United States District Judge