U.S. COMMODITY FUTURES TRADING COMMISSION
Three Lafayette Centre
1155 21st Street, NW, Washington, DC 20581
www.cftc.gov

Office of Proceedings

Received
C.F.T.C.

2009 JUL 24 AM 8: 54

Office of
Proceedings
Proceedings Clerk

ROBERT B. JOHNSON, Complainant,	*	
v.	*	CFTC Docket No. 08-R042
MICHAEL ZALMAN HURWITZ, KERRY DEAN MARSHALL, TODD OWEN MARSHALL, MATTHEW ELLIOT MEYER, STEPHEN ROBERT MILES, MILES, INCORPORATED, and STERLING INTERNATIONAL COMMODITIES, Respondents.	*	

NOTICE OF CORRECTION

Corrections to typographical and grammatical errors on pages 4, 8, 12, 17, 18 and 21, and revisions for the sake of clarification on pages 23, 31 and 32, for the Default Order dated July 16, 2009, have been made as follows:

On page 4, in the last sentence to footnote 7, insert the word "the" before "June 3rd Order".

On page 8, on the next to last line, change the word "allegation" to "allegations".

On page 12, in the second sentence of the first full paragraph, delete the word "the" before "Miles, Incorporated."

On page 17, move footnote 13 to the end of the second paragraph on the page.

On page 18, in the first sentence of finding 10, insert the word "the" before "Sterling agents".

On page 21, in the first sentence of finding 14, change the word "options" to "option".

On page 23, in the fourth line of the page, change the first part of the sentence to read:

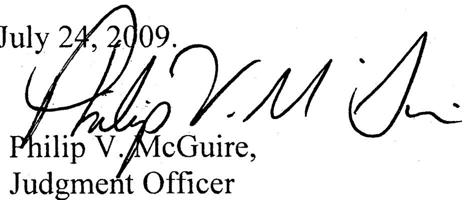
> Somehow, Marshall disregarded or deflected Johnson's complaint about Miles, and Johnson's intention to close the account,

On page 31, in the first sentence of the first full paragraph, delete "multiple and".

On page 32, in the first sentence of the first full paragraph, insert before the period at the end of the sentence: ": $20,943".

For the convenience of the parties, a corrected version of the Default Order is attached to the non-defaulting parties' copies of this Notice. Corrected copies will be provided to any defaulting party who files a motion to vacate the default.

Dated July 24, 2009.



Philip V. McGuire,
Judgment Officer

U.S. COMMODITY FUTURES TRADING COMMISSION
Three Lafayette Centre
1155 21st Street, NW, Washington, DC 20581
www.cftc.gov

Office of Proceedings

Received
C.F.T.C.

2009 JUL 24 AM 8:55

Office of
Proceedings
Proceedings Clerk

ROBERT B. JOHNSON, Complainant,	*	
v.	*	CFTC Docket No. 08-R042
MICHAEL ZALMAN HURWITZ, KERRY DEAN MARSHALL, TODD OWEN MARSHALL, MATTHEW ELLIOT MEYER, STEPHEN ROBERT MILES, MILES, INCORPORATED, and STERLING INTERNATIONAL COMMODITIES, Respondents.	*	

DEFAULT ORDER
(Stephen R. Miles; Sterling International Commodities; and Miles, Incorporated)
(corrected version)

Introduction

Stephen Robert Miles, Sterling International Commodities, and Miles, Incorporated have failed to file answers to Robert Johnson's complaint, and thus are in default. Pursuant to CFTC rule 12.22, their defaults constitute: admissions of the allegations in Robert Johnson's complaint, as supplemented; waivers of any affirmative defense; and waivers of any decisional procedure afforded by the Commission's reparations rules.[1] Johnson essentially alleges a variety of boiler room violations -- high-pressure, and false and deceptive, sales tactics, lulling, churning, fraudulent breach of fiduciary duty, aiding and abetting, and failure to supervise by

[1] Similarly, by defaulting, Stephen Miles, Sterling and Miles, Inc. may not benefit from the general denials set out in the answers and statements of the non-defaulting respondents.

various agents and principals of Sterling International Commodities; and fraudulent solicitation and unauthorized trading by an agent and principal of Miles, Incorporated.[2] Both firms were located in southern Florida.

According to Johnson, a resident of Bend, Oregon:

> I'm writing this letter to you, as I feel I have been manipulated, wrongly steered and fraudulently cheated out of thousands of dollars. . . .
>
> Living alone, with no wife, kids or roommate, I fell prey to a lesson I was about to learn. I'm a high school graduate. I became a carpenter out of school. I've never taken any kind of risk in business. I don't subscribe to any financial information. Four years ago, I stopped using credit cards, because of the [identity theft] that I went through.
>
> Now I always ask myself, why me, why not my neighbors or my friends? Why me, why would Sterling International Commodities call me 3500 miles away? Telling me "we're going to make you wealthy on unleaded gasoline." I must have been the lucky one. I learned a lesson in the power of persuasion, greed, and how ignorant I have been all my life. I'm just a very hard-working honest person. It took me to the age of 50 to start understanding the word trust. . . .
>
> Because I am a victim of fraud, cheat[ing] and crude sales tactics, I learned my lesson. Trust for me, that's always going to be a hard commodity to buy in to.[3]

As explained in more detail below, based on various deemed admissions of Stephen R. Miles, Sterling International Commodities, and Miles, Incorporated, it has been concluded:

- That Stephen R. Miles and other agents of Sterling International Commodities, working separately and together, used a combination of high-pressure tactics, deceptions, misrepresentations and omissions to perpetuate a load and churn scheme, and convert $20,943 of Johnson's funds for their enrichment, in violation of Section 4c(b) of the Commodity Exchange Act and CFTC rule 33.10.[4]

---

[2] *Pro se* complainants are not required to cite the specific provisions in the Commodity Exchange Act or the specific Commission regulation that they assert have been violated, as long as they provide sufficient notice to respondents by offering an "intelligible description" of the allegedly wrongful conduct. *See Hall v. Diversified Trading Systems, Inc.*, Comm. Fut. L. Rep. (CCH) ¶26,131 (CFTC 1994).

[3] In order to simplify matters for the reader, I have slightly revised, without notation, several unconventional spellings and punctuations in Johnson's written narratives in his complaint and his statement. No offense, and no change in meaning, has been intended.

[4] Section 4c(b) of the Act provides in pertinent part: "No person shall offer to enter into or confirm the execution of, any transaction involving any commodity regulated under this Act which is of the character of, or is commonly known to the trade as "option," . . . "put," "call," . . . contrary to any rule, regulation, or order of the Commission

- That Stephen R. Miles fraudulently breached his fiduciary duty to Johnson first by churning Johnson's account, and second by abandoning his account, in violation of Section 4c(b) of the Commodity Exchange Act and CFTC rule 33.10. Miles churned Johnson's Sterling account: by steering him into substantially high-risk, multi-contract, out-of-the-money options and option spreads which generated burdensome commissions since Sterling charged commissions on a per-contract basis; by urging Johnson to approve multiple option trades before Johnson had sent additional funds; and by accelerating the depletion of Johnson's account with a series of short-term options trades. Miles abandoned Johnson's account in mid April 2007, when, without warning to Johnson, he stopped monitoring Johnson's account, stopped returning Johnson's calls, and eventually left Sterling.

- That Stephen R. Miles perpetuated his fraud by falsely guaranteeing that Sterling would promptly pay Johnson a promised $1,500 commission rebate, in violation of Section 4c(b) of the Commodity Exchange Act and CFTC rule 33.10.

- That various Sterling agents aided and abetted the fraud of Stephen R. Miles and other Sterling agents, in violation of Section 13(a) of the Act,[5] by encouraging and facilitating the patently fraudulent trading activity in Johnson's account, and by deliberately deflecting and discouraging Johnson's complaints about excessive commissions, about high pressure tactics, and about his thwarted efforts to limit his losses and close his account.

- That Sterling and Sterling agents failed to adequately supervise Stephen R. Miles and other Sterling agents, in violation of CFTC rule 166.3,[6] by recklessly disregarding the patently fraudulent trading activity in Johnson's account, by recklessly permitting Johnson's account to go unmonitored for over a month, and by deliberately disregarding

---

prohibiting any such transaction or allowing such transaction under such terms and conditions as the Commission shall prescribe." In turn, CFTC rule 33.10 provides: "It shall be unlawful for any person directly or indirectly – (a) To cheat or defraud or attempt to cheat or defraud any other person; (b) To make or cause to be made to any other person any false report or statement thereof or cause to be entered for any person any false record thereof; (c) To deceive or attempt to deceive any other person by any means whatsoever – in or in connection with an offer to enter into, the entry into, the confirmation of the execution of, or the maintenance of, any commodity option transaction."

[5] Section 13(a) of the Act provides that: "Any person who commits, or willfully aids and abets, counsels, commands, induces or procures the commission of a violation of any provisions of this Act, or any [CFTC] rule, or who acts in combination or concert with any other person in any such violation, or who willfully causes such an act to be done or omitted which if directly performed or omitted by him or another would be a violation of [the Act or CFTC rule], may be held responsible for such violation as a principal." *See* generally *In re Richardson Securities, Inc.*, Comm. Fut. L. Rep. (CCH) ¶ 21,145 (CFTC 1981), and *McGaughey v. Hogan-Orr, Inc.*, Comm. Fut. L. Rep. (CCH) ¶22,479 (CFTC 1985). To establish aiding and abetting liability, knowing assistance may be inferred from the surrounding facts and circumstances. *See e.g., CFTC v. Premex*, 785 F.2d 1403 (9th Cir. 1986).

[6] CFTC rule 166.3 provides that: "Each Commission registrant . . . must diligently supervise the handling of its partners, officers, employees, and agents . . . of all commodity interest accounts carried, operated, advised, or introduced by the registrant and all other activities of its partners, officers, employees, and agents . . . relating to its business as a Commission registrant."

Johnson's complaints about excessive commissions, about high pressure sales tactics, and about his thwarted efforts to limit his losses and close his account.

- That the various violations by Stephen R. Miles and other Sterling agents, and by Sterling, separately and together, proximately caused $20,943 in damages.

- That Sterling International Commodities is liable for the violations of Stephen R. Miles and other Sterling agents, pursuant to Section 2(a)(1)(B) of the Act.

- That Stephen R. Miles used similarly deceptive and fraudulent tactics to convince Johnson to open a second account -- with his new firm, Miles, Incorporated -- and that Miles placed multiple trades for Johnson's account without authorization, in violation of Section 4c(b) of the Commodity Exchange Act and CFTC rule 33.10, and that these violations proximately caused damages totaling $6,243.

- That Miles, Incorporated is liable for the fraud of Stephen R. Miles, pursuant to Section 2(a)(1)(B) of the Act.

These default conclusions are not binding on the non-defaulting respondents, and the default awards do not establish, and do not diminish, the liability of the non-defaulting respondents: Michael Hurwitz, Kerry Marshall, Todd Marshall, and Matthew Meyer.[7]

For administrative convenience, two separate and distinct default awards are being issued. The first award, arising from the violations in connection with Johnson's account introduced by Sterling, and carried by Comtrust, Incorporated, is for $20,943, for which Miles and Sterling are jointly liable. This award is based on Johnson's aggregate net losses, *i.e.*, the difference between all deposits and all refunds for the Sterling/Comtrust account.

[7] Notwithstanding the defaults by Miles and Sterling, Johnson still has the burden to show, by a preponderance of the evidence, violations by the four non-defaulting respondents. However, the parties should note that the evidentiary record already shows that commissions and fees quickly depleted the Johnson account and that the trades recommended by respondents for the account – multi-contract, deep or substantially out-of-the-money options and option spreads which generated patently burdensome commissions, reflected in commission-to-premium-paid ratios as great as 83% – are the sort of trades that the Commission has found to be presumptively contrary to a customer's best interest. *See Ferriola v. Kearse-McNeill*, Comm. Fut. L. Rep. (CCH) ¶ 28,172, at 50,154-50,155 (CFTC 2000). As a result, the burden has been shifted to the non-defaulting respondents to show that the trades recommended by Sterling agents had a reasonable basis and were consistent with Johnson's trading objectives and his best interests. Respondents will have ample opportunity to present supporting evidence and arguments on this issue in their final verified statements, the deadline for which will be set in a separate order. In this connection, a summary of the trading activity in Johnson's Sterling/Comtrust was attached to the June 3rd Order.

The second award, arising from allegations concerning Johnson's account introduced by Miles, Incorporated, and carried by Alaron Trading Corporation, is for $6,243, for which Miles and Miles, Inc. are jointly liable. The $2,000 paid by Alaron, the guarantor of Miles, Inc., to settle its portion of the dispute with Johnson reduces the total amount of the second award (*i.e.*, principal, interest, and cost of filing fee), but does not reduce the total amount of the first award.

Factual background:[8]

The parties

1. Robert Johnson is an unsophisticated, novice speculator. Johnson, a resident of Bend, Oregon, is in his fifties, lives alone with no dependents, has a high-school degree, and has been employed all of his adult life as a carpenter. In November 2006, when he was cold-called by an agent of Sterling, Johnson had partially paid off his mortgage, had paid off and cut up all his credit cards, and had been maintaining a modest IRA for a few years. Johnson had conservative investment objectives geared toward his retirement, had no investment experience beyond his IRA, and knew nothing about commodity markets or commodity options.

2. Sterling International Commodities, located in Pompano Beach, Florida, with a branch office in Deerfield Beach, Florida, was registered with the National Futures Association as an

---

[8]So far, the evidentiary record consists of: Johnson's complaint, addenda to the complaint dated Sep. 18, and Oct. 30, 2008, and statement filed June 16, 2009; Hurwitz's amended answer, and statement dated June 22, 2009; Meyer's answer, and affidavits dated May 11 and June 19, 2009; Kerry Marshall's amended answer, and statements filed March 2, April 23 and June 20, 2009; and Todd Marshall's answer, and statements filed April 9, May 9 and June 20, 2009. Also, in light of the defaults by Sterling, Stephen Miles, and Miles, Incorporated, the purported destruction of Sterling records, and the gauzy recollections of Sterling's principals, I have taken official notice of NFA records regarding the registration and disciplinary history of the respondents, and I have subpoenaed documents and affidavits from the carrying broker for the Sterling account, Comtrust, Incorporated., and from the clearing broker for the Miles, Incorporated account, Alaron Trading Corporation. The subpoenaed evidence includes account-opening documents for the Sterling account, complete sets of account statements and equity runs for the Sterling and Miles, Inc. accounts, and affidavits from a principal of Comtrust concerning Sterling. In the near future, these documents will be made available to the complainant and non-defaulting respondents. *See Ricci v. Commonwealth Financial Group, Inc.*, Comm. Fut. L. Rep. (CCH) ¶26,917, at 44,444 (CFTC 1996) (In cases involving *pro se* litigants, it is appropriate for a presiding officer to take an active role in highlighting the relevant issues and fully developing the factual record.)

introducing broker ("IB") from August 2001 to July 2008. During the relevant time, Sterling introduced its customer accounts to Comtrust, Incorporated, a futures commission merchant ("FCM") located in southern Florida.

Sterling was started up by Stephen Miles, who was its first registered principal. After a few months, Todd Marshall came on board as a principal of the firm, and eventually became the sole owner. Todd Marshall was first registered with the NFA in early 1998. Many of the firms for whom Todd Marshall had worked before he bought into Sterling had been disciplined by the NFA or CFTC for fraudulent sales practices: American Financial Trading Corp.; Concorde Trading Group; Group One Financial Services, Inc.; and Barkley Financial Corp.

Todd Marshall would essentially take over as account executive for the Johnson account on or about May 11, 2007. According to Johnson, during his first conversation with Todd Marshall, after Johnson complained that he had been trying unsuccessfully for about a month to contact Miles in order to limit his losses and close the account, Todd Marshall would be less than forthcoming and merely reply that "[Miles] is not here," without clearly and accurately confirming that Miles, in fact, had quit, or been terminated, almost a month earlier. Also, during this conversation, Marshall would somehow change Johnson's mind about closing the account and convince Johnson to approve one last trade. During Marshall's tenure as account executive -- from May 11 to May 29 -- the account liquidation value would drop an additional $2,462, to $3,490.

Kerry Marshall, Todd Marshall's brother, was registered as an associated person with Sterling from April 7, 2006, to August 28, 2007. Kerry Marshall also was briefly registered as a principal in February 2007, "for purposes of an NFA audit." Kerry Marshall had no previous futures or options experience. He has not been registered since June 2008. According to

Johnson, Kerry Marshall would become his primary contact at Sterling after May 29, 2007, and in that capacity would offer commission rebates to Johnson that diminished over time, from $1,500 promised by Todd Marshall in late May, to $1,400 offered by Kerry Marshall in late June, to $1,000 paid by Sterling in early August.

During the life of Johnson's Sterling/Comtrust account -- December 28, 2006 to June 22, 2007 – Sterling employed 16 associated persons at its two offices. Six of these associated persons were "tainted" brokers who had worked at firms that had been disciplined by the CFTC or the NFA for fraudulent sales and trading practices. One defining characteristic of these sanctioned firms is that the vast majority of their customers lost most or all of their investments, largely because the firms pushed dubious high risk trading strategies that generated excessive commissions. The core of experienced brokers at Sterling was made up almost exclusively of tainted brokers. Notably, Miles was the one experienced Sterling broker who was not tainted at the time of his employment at Sterling. In this connection, Meyer has stated that he routinely solicited and opened accounts that were then transferred to more experienced brokers. When the NFA audit of Sterling commenced in February 2007, Sterling employed seven associated persons at its main office, and nine associated persons at its branch office. Miles, Hurwitz, Meyer, and Kerry and Todd Marshall worked at the main office.

During the two years before Sterling agents cold-called Johnson, Sterling customer accounts typically were depleted by excessive commissions, and thus typically realized substantial losses. In 2005, only five out of 119 Sterling customer accounts (4%) realized an over-all net profit, and Sterling customers paid $1,075,788 in aggregate commissions and realized $1,797,314 in aggregate net losses. In 2006, a larger number of Sterling customer accounts, 45 out of 233 (20%), realized an over-all net profit. However, profits in these winning

accounts paled in comparison to the losses in the losing accounts: overall, in 2006, Sterling customers paid $3,827,706 in aggregate commissions and realized $2,846,768 in aggregate net losses. Similarly, during the time that Johnson maintained his Sterling account -- the first half of 2007 -- Sterling customers paid $891,432 in aggregate commissions, and realized $827,192 in aggregate net losses.

On June 28, 2007 – about a month after Todd Marshall had closed out the viable options in Johnson's account and returned the account balance -- the National Futures Association Business Conduct Committee brought a disciplinary action against Sterling, Todd Marshall, and Stephen Miles and two other Sterling agents. The NFA alleged that Marshall, and Miles and the other Sterling agents had made misleading sales solicitations. The NFA also alleged that Marshall, and Miles and the other Sterling agents rushed customers through account-opening documents and risk disclosures, down-played the importance of the account-opening compliance review, pressured customers to invest ever-increasing funds, and disregarded customer complaints. The NFA further alleged that Sterling systematically churned its customers' accounts by steering them into extremely high risk and patently abusive trading strategies that generated excessive commissions, and thus rarely realized significant net profits. Furthermore, the NFA alleged that its February 2007 audit had found: that Sterling had not instituted any procedures for preventing, detecting and curing abusive and fraudulent sales practices by its agents; that Sterling had not instituted adequate procedures to ensure that the individuals and firms with which it did business were properly registered and/or NFA members; and that Sterling had failed to maintain current books and accounts.

The respondents filed answers generally denying the NFA's allegations. However, by consent order dated July 9, 2008, Todd Marshall and Sterling agreed to a variety of sanctions,

including a permanent membership bar for Sterling and a three-year membership bar for Marshall.[9]

3. Miles, Incorporated, located in Boynton Beach, Florida, was a registered introducing broker from May 31, to November 30, 2007. Miles, Inc. was guaranteed by Alaron Trading Corporation. Stephen Robert Miles was the sole owner and principal of Miles, Inc.

4. Stephen Robert Miles, whose last known addresses were in Chase City, Virginia and Boynton Beach, Florida, was first registered with the NFA in May 2001. Miles was the first registered principal of Sterling, from August 2001 to September 2002. He was also registered as an associated person with Sterling August 2001 through December 2002, and again from August 9, 2006, to May 4, 2007.

Comtrust account statements and equity runs indicate that Sterling had assigned Johnson's account to Miles from January 16, 2007, until the last options expired worthless on June 22, 2007. This last date was: well past mid-April 2007, when Miles had stopped returning Johnson's calls and left Sterling to start up his own firm; well past May 4, 2007, when Todd Marshall submitted a Form 8T terminating Miles' registration as an associated person with Sterling; well past May 11, 2007, when Todd Marshall had made one last trade for the Johnson account, after Johnson had told him that for over a month he had been trying unsuccessfully to contact Miles to close out his account without any help from any of the Sterling employees who had been handling his thwarted calls; and well past May 29, 2007, when Todd Marshall had closed out all viable options and returned the account balance.

---

[9] The NFA allegations are recited here merely as background information, and do not form the basis for any default conclusion concerning the solicitation and trading of Johnson's Sterling/Comtrust account. However, the issuance of the NFA complaint in late June 2007-- after an apparently confrontational NFA audit in February 2007 -- was a significant event in the factual circumstances during the two-month -- late May to early August -- delay in the promised payment of the modest commission rebate. Thus, the anticipated issuance of the NFA complaint may have been a factor in Miles' departure in mid April, and in Sterling's purported prevarications after Johnson had called Sterling to close his account.

Johnson's experience with Miles indicates that although Miles had effectively stopped working at Sterling well before May 4, he would remain in fairly constant contact with someone knowledgeable at Sterling throughout May and June. When Miles spoke to Johnson in mid May from his new Virginia phone number, he would open the conversation by telling Johnson that he already knew that Johnson was unhappy and trying to close his Sterling account; and in early June, Miles would tell Johnson that he already knew that Johnson had finally succeeded in closing the account and received a refund of the account balance.

From 2001 to 2007, Miles' business affairs had at least occasionally been intertwined with those of Todd Marshall and Kerry Marshall. As noted above, in 2001 Miles brought Todd Marshall into Sterling, and in 2006 Todd Marshall returned the favor and hired Miles. In early June 2007, after Todd Marshall had promised to pay Johnson $1,500 unconditionally "out of my own pocket" to partially compensate Johnson for the losses he had incurred after he first tried to close the account, Miles would promise Johnson that Marshall "was good for it." Also, simultaneous with his second tenure at Sterling, Miles had been registered, from December 15, 2006, to May 15, 2007, as an associated person with Vanguard Trading Group, another south Florida introducing broker, which apparently was inactive at that time. However, when Sterling subsequently went out of business in July 2008, its remaining customers' accounts would be transferred to Vanguard, and three Sterling associated persons would transfer to Vanguard, including respondents Michael Hurwitz and Kerry Marshall.

When Miles took control of Johnson's account, he would introduce himself as "one of the best brokers on the East Coast." This statement was patently designed to deceive an unsophisticated investor like Johnson into believing that Miles had consistently made big money for his clients. This statement also doubled as inside joke for Miles and his colleagues at

Sterling: in actuality, Miles was one of the best at converting funds from his customers to his employer who happened to be located on the east coast of southern Florida. In the first few months after Miles had started his second stint with Sterling -- from early August 2006 to the end of December 2006 -- seventy-four out of seventy-seven of the Sterling accounts assigned to Miles (94%) had lost money, with losses totaling $179,669, and commissions totaling $287,638. During the time that Miles was responsible for Johnson's Sterling account -- the first half of 2007 -- Miles' customers realized $240,524 in aggregate net losses and paid $515,576 in aggregate commissions. Thus, during his second eight-month stint with Sterling in 2006 and 2007, Miles was noticeably productive for Sterling, but just as noticeably destructive for his customers: realizing for his customers aggregate net losses of $420,193, while generating for Sterling a total of $803,214 in commissions.

Miles would take over as Johnson's Sterling broker on January 16, 2007, a couple of weeks after two other Sterling agents had solicited and opened the account and recommended the initial trades. Miles would convince Johnson to deposit a total of $31,595 in his Sterling/Comtrust account, most of which was funded from a home equity line of credit or diverted from funds in Johnson's savings account that were intended for a year-end transfer to Johnson's IRA. Over twelve weeks, Miles would place a total of 18 trades for the Johnson account: most of which were concentrated in the first six weeks, all of which involved deep or substantially out-of- the-money options, and five of which were spreads. Miles' trades for the Sterling/Comtrust account would generate $14,840 in commissions, which quickly consumed almost half of the funds that Miles had convinced Johnson to commit. The commission-to-premium-paid ratios for these trades would range from 28% to 83%, with the ratios for nine of

the trades over 40%.[10] In mid-April of 2007, Miles would leave Sterling without warning Johnson, and start up his own firm, Miles, Incorporated.

In mid May 2007, Miles would learn from Sterling that Johnson had been told that he was no longer at Sterling, and begin trying to convince Johnson to open a new account with his new firm. In early June 2007, after learning from Sterling that Johnson had closed his Sterling/Comtrust account, Miles would use false guarantees to recoup his Sterling losses to convince Johnson to re-invest his Sterling refund with Miles, Incorporated. The trades recommended by Miles for Johnson's new Miles/Alaron account would quickly generate $2,000 in commissions and realize $6,213 in losses.

As noted above, on June 28, 2007 – shortly after Johnson had closed his Sterling account and opened his Miles, Inc. account -- the NFA Business Conduct Committee brought a disciplinary action against Miles, along with Todd Marshall, Sterling and other Sterling agents. The NFA alleged that Miles had made misleading sales solicitations that exaggerated the profit potential of trading options, that minimized the risk of loss of trading options and spreads, and that failed to disclose that the vast majority of his and Sterling's customers had lost money in the years immediately prior to the solicitations. By consent order dated July 9, 2008, Miles agreed to a variety of sanctions, including a one-year membership bar.

5. Michael Hurwitz and Matthew Meyer were both involved at various points during the solicitation, account opening, first deposit, and first round of trades in the Johnson account -- a period that stretched from late November 2006 to mid-January 2007.

[10] The *commission-to-premium ratio*, based on the commissions paid to initiate a long option trade, or the net premiums paid to initiate an option spread trade, reflects the rate at which an option trade must appreciate to overcome the cost of the commissions, and break even. A higher ratio indicates a greater barrier to potential profitability. Thus, the higher the ratio, the greater the chance will be that the trade will fail to realize a profit. Similarly, as trades with high commission-to-premium ratios multiply, the greater the chance that an account will be rapidly depleted via commissions.

Hurwitz, who had no previous commodities or derivatives experience, was a registered associated person with Sterling from March 27, 2006 to May 14, 2008. Thus, Hurwitz had worked at Sterling for eight months before the first contact with Johnson, and would remain at Sterling during the entire life of Johnson's account.

Meyer, who similarly had no previous commodities or derivatives experience, was a registered associated person with Sterling from September 1, 2005 to May 6, 2008. Meyer states that, in that capacity, he routinely opened accounts that were subsequently transferred to more senior Sterling brokers. There were two brief gaps in Meyer's registration with Sterling: first, from October 9 to 13, 2006; and second, from December 26, 2006 to January 22, 2007. Due to the apparent unreliability of Sterling's record-keeping and its apparently lax regulatory compliance, it cannot be reliably established that Meyer actually had ceased working at Sterling during these brief gaps. In any event, Miles had worked at Sterling for over a year before the first contact with Johnson, and essentially would remain at Sterling during the entire life of Johnson's account.

Johnson concedes that he is not sure exactly when he spoke to Meyer and when he spoke to Hurwitz, before Miles took control of the account. Conversely, Meyer, Hurwitz, and Kerry and Todd Marshall have offered little or nothing on this issue, claiming to have lost almost all memory of the factual circumstances from November 2006 to August 2007. Since the account-opening package that was sent to Johnson included Meyer's business card, it is reasonable to conclude -- for purposes of this default order -- that it was Meyer who would take the lead in the solicitation. Since Comtrust account statements indicate that the account was assigned to Hurwitz, and not Meyer, from December 28, 2006 to January 12, 2007, it is reasonable to conclude -- for purposes of this default order -- that it was Hurwitz who would recommend the

first two trades on December 28, 2006. During the time that the account was assigned Hurwitz, Johnson would deposit $3,000 and two trades would be placed in the account, both of which involved out-of-the-money options and one of which was a spread.

Either Meyer or Hurwitz would introduce Miles to Johnson. Meyer, Hurwitz and Johnson agree that neither Meyer nor Hurwitz would speak to Johnson after Miles abruptly took over the Sterling account on January 16, 2007.

Hurwitz has not been registered since August 2008. Meyer currently is registered as an associated person and principal with a southern Florida introducing broker, Vista Trading.

The accounts

6. Johnson maintained two separate and consecutive accounts with different sets of firms, but which both featured Stephen Miles as the primary account executive.

The first account, introduced by Sterling International Commodities and carried by Comtrust, Incorporated, was opened on December 28, 2006, and essentially closed on May 29, 2007, when Todd Marshall closed out all viable option positions and returned the account balance. On June 22, 2007, the few remaining options expired worthless. Comtrust account statements indicate that Sterling first assigned the account to Hurwitz, and then re-assigned it to Miles on January 16, 2007. The account remained assigned to Miles until the last options expired worthless on June 22, 2007, despite the fact that Miles had left Sterling in mid-April, 2007, and that by May 11, 2007, Todd Marshall had effectively taken control of the account.

The Sterling/Comtrust account realized an aggregate net loss of $20,943. The $15,860 charged in commissions accounted for the lion's share of this loss. For this account, Johnson made a total of $31,595 in deposits: $3,000 on December 29, 2006; $3,250 on January 22; $28,000 on February 12; and $345 on April 10, 2007. Johnson received back a total of $13,356

in refunds: $8,324 on March 6; $229 on April 4; $303 on May 17; $3,490 on May 30; and $1,000 on or about August 4, 2007.

The circumstances around Sterling's payment of $1,000 to Johnson on or about August 4, 2007 remain murky and dubious: none of the respondents has owned up to any first-hand knowledge or any responsibility for the purported "release" signed by Johnson in connection with that payment; [11] and Johnson claims that Todd and Kerry Marshall tricked and coerced him into signing a bogus release in order to receive a portion of the $1,500 commission rebate that they had been promising -- for over two months -- after he had complained to them about excessive commissions and Miles.[12] Therefore -- for purposes of this default order -- Sterling's August 4th payment is treated as no more than a much delayed rebate based on a modest commission credit adjustment.

7. Johnson's second account, introduced by Miles, Incorporated and carried by Alaron Trading Corporation, Incorporated, was opened on June 6, and closed on August 29, 2007. Stephen Miles acted as the account executive for this second account. For the Miles/Alaron account, Johnson deposited a total of $6,500 -- $3,000 on June 6, $1,500 on June 19, and $2,000 on August 20, 2007 – and received back $287 on August 29, 2007, for a net loss of $6,213. In addition, on or about December 10, 2008, before this case was forwarded to my docket, Alaron Trading Company, the guarantor of Miles, Inc., paid Johnson $2,000 to settle out as a respondent in this matter.

---

[11] When asked about the circumstances around Sterling's payment of the $1,000, the non-defaulting respondents have essentially donned Sgt. Schultz's helmet and asserted "I know nothing. I see nothing. I hear nothing. I remember nothing."

[12] Johnson understands the document that Sterling agents directed him to sign before he could receive even a portion of Marshall's promised payment to be a "Notary Public."

Soliciting and opening the Sterling/Comtrust account

8. According to Johnson, in late November or early December 2006, he was cold called by two Sterling agents, in the first of a series of several persistent conversations. Johnson told them that he was a carpenter, that he knew nothing about commodity futures or options, that he had an IRA and that he was focused on saving for retirement. The Sterling agents told him that they had a suitable and lucrative investment for his retirement, and guaranteed that they would get him "fantastic returns" trading options on unleaded gasoline futures, because gasoline was going up to four dollars a gallon. They made a rudimentary presentation about supply and demand and seasonal price changes in the energy markets, and strongly implied that they had consistently made money for their customers. They mentioned that options trading was generally risky, but undercut that disclosure by emphasizing the size and certainty of profits, and otherwise said nothing that accurately reflected the reality that Sterling customers typically lost most of their investments. They did not discuss in any meaningful detail the trading strategies favored by Sterling -- for example, they did not mention that they would be recommending multi-contract out-of-the-money option trades -- and did not reveal that these trading strategies would generate substantial commissions in the hundreds and thousands of dollars, since Sterling charged commissions on a per-contract basis.

The two Sterling agents also did not reveal that, after Johnson made his first deposit and approved his first set of trades, he should expect to be quickly handed off to a more senior broker, who in turn would pressure him to commit ever larger sums of money. As a result, when they did hand him over to Miles a few weeks later, Johnson would be surprised and confused, and feel "betrayed," at least until Miles won him over.

At first, Johnson was initially reluctant, principally because he knew nothing about commodity options, but the Sterling agents kept him intrigued by emphasizing the tremendous profits to be made, and kept up the pressure with multiple calls. Eventually, they wore down and convinced Johnson to commit $3,000, which was a substantial amount for him.

The Sterling agents spent minimal time discussing the account-opening documents, and essentially just showed him where to sign. One of the Sterling account-opening documents – the "Notification of Fees and Commissions" -- was a model of deception through disclosure of a partial truth: although it featured the technically correct disclosure that Sterling charged $240 in commission and fees per contract, it did not even hint that typical commissions and fees would be substantially larger per trade, because Sterling routinely recommended multi-contract trades.[13]

9. On December 28, one of the two Sterling agents advised Johnson to approve two trades: The first was the purchase of two out-of-the-money July wheat calls, and the second was an out-of-the-money June summer blend gasoline call spread. The commissions for these trades totaled $880, which immediately consumed almost a third of Johnson's initial modest deposit. The commission-to-premium ratios for the trades were 36% and 69%, respectively.

According to Johnson, the Sterling agent: did not clearly state the total amount of commissions for each trade, did not clearly break down the total costs for each trade (*i.e.*, total premiums, total commissions and total cost), which would at least have indirectly revealed the onerous commission-to-premium ratios, and did not mention that the options were out-of-the-money.

[13] Out of the twenty-one total trades in the Johnson account, for only three trades would the commissions and fees total around $240. For fourteen trades, the commissions per trade would be about $500; for one additional trade, the commissions would be well over $1,000; and for another three trades, the commissions would be over $2,000.

Miles takes control

10. A few days later, one of the Sterling agents told Johnson that Stephen Miles would be taking over as his account executive, and described Miles as a "good guy." Miles falsely introduced himself as "one of the best commodity brokers on the East Coast." Johnson told Miles that he was concerned about saving enough for his retirement and that he still did not remotely understand commodity options. Miles offered a cursory discussion of matters like supply and demand, the difference between puts and calls, and the effect of well known current events on the prices of various commodities. Miles emphasized the huge profits to be made with him at the helm, rarely if ever mentioned any risk of loss, and played to Johnson's concerns:

- "I can see you're ten years behind on your retirement."
- "One day you'll hold your head up high and be wealthy."
- "You're going to help people with all of the money you are going to make."
- "You're going to make 60 to 80 thousand dollars on soybeans this year."

By Friday, January 12, 2007, the aggregate liquidation value of Johnson's options had declined from $1,953 to $1,637. However, Miles never mentioned to Johnson that his first trades were not appreciating as guaranteed by the other Sterling agents.

On Tuesday, January 16, 2007, Miles convinced Johnson to approve a new round of trades, and empty out his savings account with a second deposit of $3,750 (which would be received by Comtrust a week later on January 22):

> Miles . . . said "if you send me more money. You'll have a [better] spread and have a [better] chance of making money." Miles talked about corn and wheat. How drought, flood and ice change crops from one year to the other. Miles smooth talked me right out of 3250 one night. That was the last of my savings. Miles said, "You're going to make some money now with your bigger account." That's when I started to not sleep at night and felt what I was into was not for me, it was for gamblers.

The three trades (July corn calls, May soybean puts and November soybean calls) that Miles steered Johnson into generated another $960 in commissions and fees. Thus, at this point, Johnson had paid $1,180 in cumulative commissions and fees.

11. For Johnson, the opening of his first-ever commodity options account coincided with the purchase of his first personal computer. Johnson focused his attention on learning how to operate the computer, so that he could read the confirmation statements that Comtrust was sending electronically. As a result, it would not be until early March that he sufficiently mastered the computer that he could track the status of the account and realize the magnitude of the commissions charged to his account.

12. By Friday, February 2, 2007, the account liquidation values had declined to $2,732. Thus, Johnson's $6,250 investment had quickly lost $3,518. Approximately a third of this loss could be attributed to the commissions and fees. At no point, did Miles ever advise Johnson that his account had been depreciating.

On Monday, February 6, Miles urged Johnson to quintuple his investment:

> Miles and I were getting friendly as two people can get over the phone. Talk about outside [non-business] issues. Miles also told me he had more clients in the Bend area, my home town. Miles [assured] me with 6250 in my account. I was doing the right thing. Miles told me, "It looks like your several years behind on your retirement. If you'll stick with me, you will drop those nail bag in 5 years and hold your head up high and be able to help people someday, because of your wealth." The relationship between Miles and myself was good. I became very interested in commodities. I felt I was learning something new. But then, I was very interested in just getting my money back.
>
> On [February 6], Miles called me. Talking about "bring your account up to a bigger static [status?], play some hardball, your behind on your retirement, do you want true wealth." Miles said, "I'm taking a select few [customers] and we're going into soybean. A bushel of soybean is going to skyrocket. If corn ethanol takes off. Like I think it will. You, Robert, could stand to make 60 to 80 thousand dollars, due to the shortage of soybean being planted in the U.S.A." Miles asked me, "Do you have more money to send me [?]" My reply "absolutely NO! You have $6250.00 of

my money. I want to see it returned. That's all the money I had. I shouldn't have to send any more money."

When Steve Miles told me I should send 28,000 dollars, I was in shock. "I don't have that kind of money." Miles asked "Can you borrow the money?" I replied, "Absolutely no. I have a Home Equity line of Credit. I will never use credit." Miles told me. "All investors use their lines of credit." He said, "Don't you want a new car." Miles and I debated over money for a good 2 to 3 hours. Well Miles is a very good manipulator and persuader. After so much hammering back and forth, the stress and anxiety had me at tears. I caved in, and said "yes" to writing a check out of my HELOC for $28,000.

Miles made a guarantee with me, "You're doing the right thing, You're going to make 60 to 80 thousand. All you're going to have to do is make 2 or 3 monthly payments on your Home Equity line of Credit and you'll have your $28,000 back in two months. You're in the big leagues now. You're not going to regret this move."

Miles then convinced Johnson to approve four trades, involving a total of 33 contracts, which generated an additional $7,920 in commissions. Afterwards, Johnson wrote the check for $28,000, which Comtrust would receive a week later.

13. Between February 26 and March 2, Miles closed out various positions, all at losses, and used the collected premiums to initiate six more trades. Three of these trades were spreads, and Miles in turn used the premiums collected for the short legs of the spreads to fund additional positions. During this time, Miles assuaged Johnson's anxiety about his investment by assuring him: "I guarantee you'll have your money back in two months."

On or about March 2, Miles had sufficiently mastered his PC to realize that he had paid about $12,000 in cumulative commissions.

I called and asked what that was about. Miles told me "That's the price of doing business." I replied that, "I thought that this was a retirement account." He then told me "You have to hit the bottom before you get rich."

Miles assured Johnson that he had made him a $8,300 profit on a soybean trade. However, none of the soybean trades remotely made that profit. Only one of seven soybean trades realized a net profit, and that was for $3,750. The net losses on the six losing soybean trades totaled $6,950.[14]

Miles vanishes and Johnson tries to cut his losses

14. After March 2, the frequency of Miles calls to Johnson decreased as did the life span of option positions, with Miles typically liquidating option positions a week or two after opening them.

By April 19, which was when Johnson would last speak to Miles in his capacity as a Sterling account executive, the commissions and fees had totaled $15,720. After this conversation, Miles would leave Sterling, without Miles or anyone else at Sterling telling Johnson.

Remarkably, even though Johnson made multiple calls to Sterling over almost four weeks asking to speak to Miles, no one at Sterling would tell Johnson that Miles had left until on or about May 11, when Todd Marshall first spoke to Johnson. From Johnson's last conversation with Miles in mid April to his conversation with Todd Marshall in mid May, the account liquidation value declined from $6,746 to $5,454, a drop of $1,192.

After Miles left, Todd Marshall would essentially take over as broker for Johnson's account. However, he would not take any apparent action until on or about May 11, 2007 -- about a week after he had submitted to the NFA the form 8T terminating Miles registration as an associated person with Sterling. By this point, Johnson had lost all patience with Miles'

[14] Sterling's customers were compelled to rely on their Sterling account executives to provide fair and accurate verbal reports of the net profits or net losses for trades, because Comtrust's written, and electronic, statements only reported the gross profit or loss (*i.e.*, the "net premium" collected or paid) when the position was closed out, but did not report the net profit or loss (*i.e.*, the gross profit or loss, less the considerable costs of the commissions and fees which were charged when the position was opened).

unexplained failure to return his calls and insisted on speaking to someone responsible, and was handed to Todd Marshall. All that Marshall can recall about his conversations with Johnson is that he felt "sympathetic" for Johnson's frustrating experience with Miles. In contrast, Johnson distinctly remembers speaking to Todd Marshall in May.

Johnson asserts that he complained to Marshall that he had been trying unsuccessfully for almost a month to contact Miles and close his account so that he could limit his losses, and that he also complained about the ensuing decline in account value, about excessive commissions, and about the fact that Miles had convinced him to draw $28,000 from his home equity line of credit. Johnson also asserts that it was Todd Marshall who closed out the account on May 29, 2007, who advised Johnson that he would be sending the resulting account cash balance of $3,490, and who promised Johnson an additional $1,500 for his recent frustrations.[15] Although Johnson remembers this as a single conversation, documentary evidence suggests that Johnson and Todd Marshall spoke twice in May: on the 11th and the 29th.

The first conversation between Todd Marshall and Johnson was on or about May 11, 2007, when Johnson insisted on speaking to a responsible Sterling agent after Miles had failed to return several calls. On this date, the account liquidation value was $5,952. Johnson asserts that during his initial conversation with Marshall, Johnson complained that he had been trying for almost a month to contact Miles and close out his account, and Marshall merely replied "He's not here," without clearly indicating whether he had quit or been terminated, or when or why.

> I spoke to Todd Marshall. I never was told by Miles or in the telephone conversation with Todd Marshall that Todd Marshall was the owner of Sterling. I told Todd Marshall, "I've been trying to get in contact with Steve Miles." Todd replied, "He's

---

[15] Thus, the promised $1,500 commission reimbursement essentially compensated Johnson for the drop in account value between his last conversation with Miles and his first conversation with Todd Marshall, but did not compensate Johnson for the $2,300 in drop account value between Johnson's first conversation with Todd Marshall when he told Marshall that he had been trying for a month to close the account, and the second conversation with Marshall when Johnson renewed or repeated his instruction to close the account.

> not here." I told Todd Marshall, "My account a month ago was between 5,000 and 6,000 dollars. All along I have been trying to get a hold of Miles, to get out of the market to save what I had left in the account."

Somehow, Marshall disregarded or deflected Johnson's complaint about Miles, and Johnson's intention to close the account, and obtained Johnson's approval to partially liquidate a spread and a long trade to collect a total of $893 in premiums, and in turn opened one last trade for the account at a total cost of $409.[16] Marshall also returned to Johnson $303.

However, this was not exactly what Johnson had in mind when he had begun his conversation with Marshall. So, a couple of weeks later on May 29, a fed-up Johnson more insistently repeated or renewed his instruction to close the account, and Marshall liquidated all viable open positions and refunded the account balance. By this time the account liquidation values had further declined, to about $3,490. Also -- according to Johnson -- Marshall promised to pay him $1,500 as partial compensation for his recent problems with Miles:

> Todd Marshall replied by saying, "Well, I will close your account out and send you your 3,500 dollars, and I will also send you 1,500 dollars out of my pocket." I thought to myself, "Todd must have some authority with Sterling to send money out of pocket." Todd and I had a verbal agreement on the 1,500 dollars. Todd also said," if you can't afford trading in the commodities market, you should never use your home equity line of credit." Todd said, "you know, 90% percent of people lose their money, on the first go around." Michael Hurwitz, Matthew Meyers and Steve Miles never told me those percentages. . . . I received my 3,500 dollars a short time later. The account was closed. I was waiting on the 1,500 dollars Todd and I agreed on.

Comtrust would quickly refund the $3,490 account balance. However another two months would pass – with, according to Johnson, multiple delays, false excuses, broken promises and implied threats by Kerry Marshall -- before Sterling would send a portion of the $1,500 that Johnson asserts was promised by Todd Marshall.

---

[16] This trade realized a gross profit of $130, which was wiped out by $139 in commissions and fees. Thus, this last trade served as a final refrain of Johnson's experience: a money-loser for Johnson, but a money-maker for Sterling.

Miles' reprise

15. Although Stephen Miles had stopped communicating with Johnson from the Sterling office, he stayed in touch with the Sterling office and thus quickly learned in mid May that Johnson wanted to close his account, and quickly learned in early June that Johnson had successfully closed his Sterling account and received a refund of the account balance. At some point in April, Miles had sent Johnson a personal card with a Virginia phone number. Thus, for the first couple of weeks in May, Johnson tried to reach Miles both at Sterling's Florida office and at Miles' Virginia number.

Finally, on May 15 -- a few days after Johnson had learned from Todd Marshall that Miles "is not here" -- Miles answered Johnson's call to his Virginia phone number. When Johnson complained about him disappearing for a month, Miles merely explained that he was starting up a new firm. During this conversation and a second conversation on May 17, Miles guaranteed to recoup Johnson's losses if he opened a second account with Miles' new firm Miles, Incorporated.

In a third conversation, on June 3, Miles assured Johnson that Marshall "was good" for his promise to send the $1,500 rebate, and also convinced Johnson to re-invest the bulk of his refund from Sterling:

> [I told Miles]: "I just lost 22,000 [sic] dollars, Miles. I feel I have to sell my house now." Miles replied, "Don't. I can get your money back. 22,000 dollars is nothing. It's going to probably take a year. If we work slow and together on trades, we will make your money back." I agreed to send Miles more money. I opened up an Alaron, Miles, Inc. account with 3000 dollars. Miles put me in Soybean, RBOB, Cocoa and Currencies. The problem was I would come home from work, just to find Miles, again and again, moving and bouncing the account around without my input or knowledge. I was losing money. Once more, I sent another 1500 dollars and lost that. I was a mess. The last time I spoke with Steve Miles was on or around Aug. 12/07. Miles was telling me to "play hardball" once again with a large sum of

> money. I replied, "NO WAY! I'm done." Miles did it again. He persuaded and manipulated me out of another 2000 dollars. . . . But this time, all of Steve Miles phone numbers were disconnected. I called Alaron's main office. I forget who I talked to. I asked the man, "Where's my $2000.00? The man replied, "Money has way of disappearing in the commodities market and I have never heard of a Steve Miles."

Johnson deposited a total of $6,500 in the Miles/Alaron account ($3,000 on June 6, $1,500 on June 21, and $2,000 on August 20, 2007), and received a refund of $287 on August 30, 2007, for a net loss of $6,223.

Miles placed twelve out-of-the-money options trades for the second account, often without consulting Johnson. Only one trade realized a net profit: a miniscule $30. Commissions totaled almost $2,000, and by August 29 had consumed over 35% of Johnson's deposits in the second account.

The last run-around

16. In the meantime, Johnson was experiencing yet another round of frustrations with Sterling, which stretched from late May to early August 2007. According to Johnson:

> After a week [*i.e.*, in the first week of June 2007], I phoned Sterling International. Kerry Marshall answered the phone. I asked "Is Todd there?" Kerry Marshall said "Todd's not here." For the next three months Todd was never there. I asked Kerry "Is my 1500 on the way?" Kerry replied, "We're working on it." I called Kerry Marshall once a week for two months. [He'd tell] me, "It's on the way. It's on my desk. We're working on it." I started feeling I was getting the run-a-round. Finally, I received a document with the amount of 1400 that needed to be signed and notarized. I signed and notarized the document. I sent it back to Sterling. I was very disappointed, [because] the 100 dollar short-fall felt like the 22,000 [sic] dollars I had just lost to Sterling. I waited another two weeks.

When the promised check for $1,400 did not arrive, Johnson called Comtrust to complain. Soon afterwards, he received from Sterling, not a check, but a new document titled "release" which stated that Sterling agreed to pay Johnson an even smaller amount: $1,000.

According to Johnson, when he called to complain about this newly reduced offer, Kerry Marshall told him that he and Todd had decided to further reduce the amount because Johnson had "gotten [Comtrust] involved":

> Finally I received another document, not 1400 dollars, the document was for 1000 dollars to be signed and notarized. I waited so long for my 1500 dollars. I just signed and notarized the 1000 dollar document. I just want my money and it all behind me.

After a couple more weeks, Sterling sent the check for $1,000.

Discussion

Stephen Miles and other agents of Sterling defrauded Johnson during the solicitation and the trading of his account principally by using high-pressure tactics to convince him to commit ever increasing amounts of money and to fund these deposits from his savings and home equity line of credit, by grossly distorting the relative risks and rewards of following their trading advice, and by churning his account.

During the solicitation and trading of the account, Miles and the other Sterling agents created the false and misleading impression that Johnson could reasonably expect to make tremendous profits with minimal accompanying risk, at a cost of just $240 per trade. For example, Miles and the other Sterling agents: falsely represented that the trading strategies favored by Sterling were suitable for Johnson's conservative investment objectives; falsely guaranteed profits by exaggerating the profit potential and downplaying the substantial risk of loss of the option trading strategies favored by Sterling; falsely represented that Sterling customers typically enjoyed tremendous profits, when in fact the vast majority of Sterling customers had lost large portions of their investments in the two preceding years; emphasized well-known current events and seasonal tendencies deceptively suggesting that they were certain

to move the market in certain directions when in fact these factors had already been factored into the market price; deceptively downplayed the importance of the account-opening documents; failed to disclose that Sterling would be recommending trading strategies – multi-contract, out-of-the-money options and option spreads – that would quickly generate excessive, profit-killing commissions; failed to clearly disclose the amount of commissions; outright lied about the commissions, suggesting that they were normal and customary and that they were justified by the purportedly guaranteed profits, when in fact they were excessive and the primary factor in the substantial losses suffered by the majority of Sterling customers; failed to warn him that they would be pressuring him to invest ever increasing amounts of money, in total disregard of his financial status and investment objectives; and used similar deceptions to lull Johnson into maintaining his account in the face of mounting losses. It is "rudimentary" that these types of misrepresentations and omissions about profit potential and risks are material.[17]

Johnson's decision to open the account, deposit additional funds and continue trading was consistent with his assertions that he relied on Miles' and the other Sterling agents' confident, but unrealistic, message that he would quickly realize large profits with minimal accompanying risk. The conclusion that Johnson reasonably relied on respondents' misrepresentations and omissions to his detriment is supported by the fact that he was unsophisticated, with limited investment experience, no experience trading commodity options, and no familiarity with the commodity markets.[18] Respondents' written disclosures of general risks by themselves did not cure the false impression of guaranteed large profits created by Miles and the other Sterling agents, where the overall effect of respondents' intentionally deceptive

---

[17] *In re JCC, id.*, at 41,576 n.23.
[18] *See Ricci,* at 44,444.

statements substantially outweighed and vitiated the written risk warnings,[19] and where the commission disclosure itself deceptively suggested that commissions would be no more than $240 per trade.

To establish churning, Johnson must show: one, that respondents "controlled" the level and frequency of trading in the account; two, that respondents chose an overall volume of trading that was "excessive" in light of his trading objectives; and three, that respondents acted with either "intent" to defraud, or in "reckless disregard" of his interests.[20] Since Johnson did not execute a written power of attorney, he must show that respondents exercised *de facto* control over the trading in his account. Evidence of the following factors will establish *de facto* control: (1) the customer lacks sophistication; (2) the customer lacks prior commodity option trading experience and devotes a minimum of time to trading the account; (3) the customer reposes a high degree of trust and confidence in respondents; (4) a large percentage of the transactions are based on respondents' recommendations; (5) the customer does not approve transactions in advance; and (6) the respondents do not provide full, truthful and accurate information prior to obtaining customer approval for transactions.[21] Here, the record shows that Johnson lacked the requisite trading knowledge or experience, and that he remained generally confused from start to finish. The record also demonstrates that Johnson's acceptance of Miles' and the other Sterling agents' advice was influenced by their deceptions and distortions concerning the likelihood of profits, the results of trades, and the status of the account.

---

[19] *Ferriola*, at 50,153. Similarly, although Sterling has not produced a recording of the account-opening compliance review for Johnson's account, nothing in the record remotely suggests that Sterling would have instituted a compliance review that was genuinely designed to detect or cure the sort of fraud practiced by Miles. *See JCC, Incorporated v. CFTC,* Comm. Fut. L. Rep. (CCH) ¶ 26,492, at 43,217-43,218 (11th Cir. 1995) (A perfunctory compliance review cannot be used as "advance exoneration" of fraudulent misrepresentations omissions).
[20] *Ferriola,* at 50,154.
[21] *Id.*

Commission case law recognizes that customer objectives are one of the touchstones for an analysis of excessiveness.[22] Here, Johnson did not communicate a specific trading objective beyond an expectation that the trading strategies recommended by respondents would be consistent with his limited financial resources and his conservative retirement-oriented objectives, and that the strategies had a reasonable likelihood of profits with minimal risk of loss. It would be unreasonable to expect him to articulate much more of an objective given that: Johnson knew nothing about commodity options; Sterling agents had cold-called him; Miles and other Sterling agents left Johnson with little understanding about the mechanics and specific risks of Sterling's trading strategies; and Miles and other Sterling agents did not attempt to ascertain a more specific or sophisticated objective. In any event, the absence of a fully articulated specific trading objective does not justify the use of a trading strategy that emphasizes account executives' and firms' interests over the interests of their customer.[23]

Here, Miles and other Sterling agents recommended trading strategies that were patently designed to generate several hundreds and thousands of dollars in commissions in a short time, by using a combination of multiple contracts, out-of-the-money or deep-out-of-the-money options, option spreads, and short-term trades. The excessiveness is underscored: by the fact that the commission-to-premium ratios, or break-even rates, ranged up to 83%, which meant that the likelihood of profit was extremely remote; by the fact that commissions rapidly consumed large percentages of the funds deposited by Johnson; by the fact that Miles and other Sterling agents routinely urged Johnson to initiate trades before he had added sufficient funds; and by the fact that they repeatedly urged him to invest ever increasing amounts of money, in total disregard of his financial status and conservative investment philosophy.

---

[22] *In re Murlas Commodities, Inc.*, Comm. Fut. L. Rep. (CCH) ¶26,485, at 43,156-57 (CFTC 1985).
[23] *Ferriola,* at 50,154.

Miles' and the other Sterling agents' promises of certain profits failed to reflect the detrimental effect of Sterling's burdensome commissions on profit potential. Here, the commissions and fees charged to Johnson's account consumed nearly a half of his investment and resulted in a commission-to-premium-paid ratios of up to 83%, which represented a formidable barrier to profit potential. Thus, their unrestrained profit projections were materially deceptive:

> Because the size of a firm's commissions and fees affects the profit potential of an investment, it affects the kinds of representations that can be made about profitability. . . . All else being equal, customers of a firm with a high commission or fee structure will have a more difficult time making a profit than those who employ a less expensive firm. As a result, the firm charging higher commissions and fees is more limited in what it can claim regarding profit potential.[24]

By principally compensating its account executives with a cut of the commissions, Sterling supplied its brokers with the necessary motivation to make unrestrained profit projections and to convince Johnson to approve trading strategies that emphasized their interests over Johnson's interests. Moreover, the fact that the Sterling agents routinely transferred new customers like Johnson to more experienced brokers like Miles, and that Miles urged Johnson to invest more money and to make more trades indicates that pushing trades to generate commissions was a pervasive practice at Sterling.

As part of this commission-generating scheme, Miles and the other Sterling agents recommended trades in positions that were out of the money ("OTM"), even when comparable in-the-money ("ITM") positions were available. These trades exponentially increased respondents' commission income, because Sterling charged Johnson commissions based on the number of contracts traded, rather than the value of the position, and because more OTM options

---

[24] *Johnson v. Fleck*, Comm. Fut. L. Rep. (CCH) ¶24,957, at 37,502 (CFTC 1990) (Gramm concurrence).

could be purchased since the premium for an OTM option is lower than the premium for a comparable ITM option.

Here, Sterling's unvarying insistence that Johnson trade out-of-the options cannot be justified where Johnson's trading objective included, at a minimum, a reasonable chance of profit. First, the value of a low-priced option is almost always less responsive to price changes in the underlying commodity or asset. Second, the total premium value represents the amount of risk, regardless of the number of contracts. And third, the profit potential of an OTM option, as measured by its delta, is lower than that of an ITM option of the same type.[25] For these reasons, the Commission has emphasized that "when customers are paying commissions on a per-contract basis, an account executive seeking to serve his customer's interests will purchase the lower-cost ITM position."[26] Thus, Miles' and the other Sterling agents' promises of certain profits failed to reflect the reality that the strategy of buying OTM options, compared to buying comparable ITM options, was significantly more risky and less profitable, and that the only real guarantee was that respondents' stream of commission revenue would be unnecessarily increased. Similarly Miles' unrestrained promise to recoup losses with more trades with his new firm was deceptive because it failed to reflect the fact that he would again be recommending OTM options.[27]

The intentional nature of Miles' and the other Sterling agents' fraud is underscored by their exploitation of Johnson's lack of trading experience, their blatant disregard of his confusion and conservative financial objectives, their reckless indifference to the source of his funds, their blatant lies that the commissions charged to Johnson were normal and customary, their failure to

---

[25] *See Ferriola,* at 50,154-50,155.
[26] *Id.*, at 50,155.
[27] *See Hinch v. Commonwealth Financial Group, Inc.*, Comm. Fut. L. Rep. (CCH) ¶27,056, at 45,021-45,022 (CFTC 1997).

provide a fair and accurate disclosure of Sterling's oppressive commission structure, the fact that they rushed him into approving additional trades and investing additional funds before he understood the size of the commissions, and the fact that they disregarded and discouraged his complaints.

For the Sterling/Comtrust account, the proper measure of damages for churning combined with fraudulent profit guarantees, where losses exceed commissions, is Johnson's out-of-pocket losses: $20,943. For the Miles, Incorporated/Alaron account, the proper measure of damages for unauthorized trading combined with fraudulent profit guarantees, where losses on losing trades exceed out-of-pocket losses, is the total losses for losing trades: $6,243.

Default Awards

In connection with Robert B. Johnson's account introduced by Sterling International Commodities and carried by Comtrust, Incorporated, it is concluded: one, Stephen R. Miles and other agents of Sterling International Commodities, working separately and together, used a combination of high-pressure tactics, deceptions, misrepresentations and omissions to perpetuate a load and churn scheme, and convert $20,943 of Johnson's funds for the enrichment of themselves and other respondents, in violation of Section 4c(b) of the Commodity Exchange Act and CFTC rule 33.10; two, that Stephen R. Miles fraudulently breached his fiduciary duty to Johnson by churning his account and by abandoning his account, in violation of Section 4c(b) of the Commodity Exchange Act and CFTC rule 33.10; three, that Sterling and Sterling agents aided and abetted the fraud of Miles and other Sterling agents, in violation of Section 13(a) of the Act; four, that Sterling and Sterling agents failed to adequately supervise Miles and other Sterling agents, in violation of CFTC rule 166.3; five, that these violations, separately and together, proximately caused $20,943 in damages; and six, that Sterling International

Commodities is liable for the violations of Miles and other Sterling agents pursuant to Section 2(a)(1)(B) of the Act.

In connection with Robert B. Johnson's account introduced by Miles, Incorporated, and cleared by Alaron Trading Corporation, it is concluded: one, that Stephen Miles used deceptive and fraudulent tactics to convince Johnson to open a second account and that Miles made numerous unauthorized trades, in violation of Section 4c(b) of the Commodity Exchange Act and CFTC rule 33.10; two, that these violations proximately caused $6,243 in damages; and three, that Miles, Incorporated is liable for Miles' fraud, pursuant to Section 2(a)(1)(B) of the Act.

Accordingly, two separate awards are hereby issued:

First, Stephen Robert Miles and Sterling International Commodities are ordered to pay to Robert B. Johnson reparations of $20,943, plus interest on that amount at 0.51% compounded annually from December 28, 2006,[28] to the date of payment, plus $50 in costs for the filing fee. Liability is joint and several.

Second, Stephen Robert Miles and Miles, Incorporated are ordered to pay to Robert B. Johnson reparations of $6,243, plus interest on that amount at 0.51% compounded annually June 6, 2007, to the date of payment, plus $50 in costs for the filing fee. Liability is joint and several. The total amount of this second award (*i.e.*, damages, plus interest, plus cost of filing fee) shall be reduced by the $2,000 that Alaron paid Johnson on or about December 10, 2008.[29]

Any motion to vacate these default awards must meet the appropriate standards set out in CFTC rule 12.23.

---

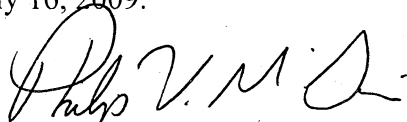
[28] Since Miles' is deemed to have admitted that he perpetuated the alleged fraud of the Sterling agents who solicited the initial deposit(s), and recommended the initial trade(s), Miles is liable for the entire amount of Johnson's out-of-pocket losses. Also, Johnson made his three deposits just a few weeks apart. Therefore, for administrative convenience, the interest for the entire award will begin to run from a single date, the date of the initial deposit.

[29] Alaron's payment shall not reduce the first award against Miles and Sterling.

These default findings and conclusions are <u>not</u> binding on the non-defaulting respondents, and these default awards do <u>not</u> establish the liability of any of the non-defaulting respondents.

The parties should note that Stephen Robert Miles is not currently registered, and that Miles, Incorporated and Sterling International Commodities are out of business. In these circumstances, successful collection of all or part of this default award may likely be a remote possibility, unless Miles re-applies for registration with the NFA.

Dated July 16, 2009.



Philip V. McGuire,
Judgment Officer