

ORIGINAL
DISTRICT OF NEBRASKA

UNITED STATES DISTRICT COURT
FOR THE
DISTRICT OF NEBRASKA

2004 MAY -4 AM 10:16

GARY D. MCFARLAND
CLERK

COMMODITY FUTURES
TRADING COMMISSION

CIVIL ACTION NO. 4:04CV3184

Plaintiff,

COMPLAINT FOR
INJUNCTIVE AND
OTHER EQUITABLE
RELIEF AND FOR A
CIVIL MONETARY PENALTY

v.

Commercial Hedge Services,
d.b.a. Prime Trading
Company, Prime Trading
Company, and Lawrence
Joseph Volf

Defendants.

SUMMARY

1. Since April 2002 through at least March 2003, defendants Commercial Hedge Services (“CHS”), Prime Trading Company (“PTC”), and Lawrence Joseph Volf (“Volf”) (collectively, “defendants”) executed unauthorized trades in approximately 90 Nebraska farmers’ commodity futures hedge accounts. The farmers opened these accounts to protect themselves from a decrease in the price of their corn crops. Despite the fact that the farmers’ account opening documents clearly indicated that the accounts were hedge accounts, to be used only for the purpose of executing bona fide hedge transactions, defendants executed speculative trades that the farmers did not authorize. During most of the months in question defendants, without the farmers’ authorization, fraudulently initiated overall long positions that increased the farmers’ risk of a decrease in the price of corn. Defendants disregarded the hedge agreements in the

farmers' account opening documents and executed unauthorized speculative trades that ultimately caused the farmers to lose approximately \$5.1 million.

2. Moreover, defendants fraudulently led the farmers to believe that they were hedging their corn crop, in particular, that they were decreasing their risk of a fall in the price of corn. In reality, however, defendants executed a trading strategy that consistently increased the farmers' price risk.

3. By virtue of these acts, defendants have engaged in acts and practices that violate Sections 4b(a)(2)(i) & (iii), 4c(1) and 4c(b) of the Commodity Exchange Act, as amended ("Act"), 7 U.S.C. §§ 6b(a)(2)(i) & (iii), 6c(1) and 6c(b) (2002), and Sections 33.10 and 166.2 of the Commission's Regulations ("Regulations"), 17 C.F.R. §§ 33.10 and 166.2 (2004).

4. Accordingly, pursuant to Section 6c of the Act, 7 U.S.C. § 13a-1, the Commission brings this action to enjoin defendants' unlawful acts and practices and to compel their compliance with the Act and the Regulations. In addition, the Commission seeks civil monetary penalties, restitution to farmers for losses caused by defendants' fraud, disgorgement of defendants' ill-gotten gains, a trading prohibition and such other relief as this Court may deem necessary or appropriate.

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

JURISDICTION AND VENUE

6. This Court possesses jurisdiction over this action pursuant to Section 6c of the Act, 7 U.S.C. § 13a-1, which provides that whenever it shall appear to the Commission that any person has engaged, is engaging, or is about to engage in any act or practice constituting a violation of

any provision of the Act or any rule, regulation, or order promulgated thereunder, the Commission may bring an action in the proper District Court of the United States against such person to enjoin such practice or to enforce compliance with the Act.

7. Venue properly lies with this Court pursuant to Section 6c(e) of the Act, 7 U.S.C. § 13a-1(e), because defendants are found in, inhabit, or transact business in the District of Nebraska, and the acts and practices in violation of the Act have occurred within this District, among other places.

THE PARTIES

8. **Plaintiff Commodity Futures Trading Commission** is the independent federal regulatory agency charged with the administration and enforcement of the Act, 7 U.S.C. §§ 1 *et. seq.*, as amended, and the Regulations promulgated thereunder, 17 C.F.R. §§ 1.1 *et. seq.* The Commission's main office is located at 1155 21st Street, NW, Washington, DC 20581.

9. **Defendant Commercial Hedge Services, Inc.** is currently registered with the Commission as an Introducing Broker ("IB") and with the Securities and Exchange Commission as Notice Broker Dealer. CHS is guaranteed by R. J. O'Brien, a Futures Commission Merchant registered with the Commission. CHS has offices at 1510 E. 4th Street, Suite 1, North Platte, Nebraska 69101.

10. **Defendant Prime Trading Company** was a d.b.a. for CHS. In or about January 2000, PTC was acquired by Sherman County Bank and Lawrence Joseph Volf. PTC continued to operate as a branch of CHS until August 2003 when it applied for a license as an IB; that license was granted in January 2004. PTC has offices at 717 O Street, Loup City, Nebraska 68853.

11. **Defendant Lawrence Joseph Volf** resides at 1120 West 4th Street, North Platte, Nebraska 69101. Volf has been registered as a Principal and Associated Person ("AP") of CHS

since 1988, and as a Branch Manager of CHS since 1999. Volf is a registered Principal and AP of PTC.

FACTUAL BACKGROUND

Trading Activity in 90 Hedge Accounts

12. Since April 2002 through at least March 2003, defendants introduced to R. J. O'Brien approximately 90 managed hedge accounts for farmers located in and around Sherman County, Nebraska. The farmers produced corn and, therefore, were long the cash corn market. In order to protect against price fluctuations in the corn market, each farmer opened hedge-trading accounts at R. J. O'Brien, a futures commission merchant registered with the Commission. These hedge accounts were only to be used for the purpose of executing bona fide hedge transactions. In or about February 2003, at the behest of R. J. O'Brien, the farmers executed powers of attorney in favor of PTC.

13. Defendants held a number of group informational meetings throughout 2002 that some farmers with managed hedge accounts, among others, attended. At those meetings, Defendants fraudulently led the farmers to believe that they were hedging on the farmers' behalf, when, in fact, they were actually speculating. In particular, defendants fraudulently led the farmers to believe that their exposure to price risk would be decreased when, in fact, defendants' trading strategy consistently increased the farmers' price risk.

14. Defendants executed trades for or on behalf of the farmers, placed batch orders for those trades, and allocated the executed trades on a pro-rated basis among the hedge accounts. Defendants primarily traded in options on futures contracts, which they occasionally exercised, resulting in the assignment of futures contracts to the hedge accounts. On occasion, they also purchased futures contracts.

15. From April 2002 through at least March 2003, rather than reducing the farmers' price risk, defendants fraudulently initiated net long positions in the hedge accounts that increased the farmers' downward price risk in nine of the twelve months of trading. Moreover, defendants fraudulently initiated positions in the hedge accounts – by purchasing futures contracts and buying and selling puts and calls (options) – that resulted in net long positions, thereby increasing the farmers' price risk.

16. The farmers' hedge accounts were traded in a fraudulent manner not authorized by their owners. The farmers' purpose in engaging the services of defendants was to hedge the farmers' corn crops. The farmers never requested nor authorized defendants to make speculative trades in their accounts. The farmers never requested nor authorized defendants to increase their net long positions. Defendants' unauthorized trading and fraud caused the farmers to lose \$5.1 million.

17. Prior to approximately February 2003, none of the farmers' accounts were discretionary accounts. Despite this, defendants did not obtain prior authorization for each trade as required by Commission Regulation 166.2. Rather, defendants held periodic group meetings (between three and four per year) in which defendants outlined their general trading strategy.

18. Defendants did not, prior to the purchase or sale, tell each farmer the precise commodity interest or the exact amount of the commodity interest that they were going to buy or sell for the farmer.

19. Prior to the purchase or sale, defendants did not obtain from each farmer the precise commodity interest or the exact amount of the commodity interest that the farmer wished to buy or sell for his hedge account.

VIOLATIONS OF THE COMMODITY EXCHANGE ACT AND REGULATIONS

COUNT I

**VIOLATION OF SECTION 166.2 OF THE COMMISSION'S REGULATIONS,
17 C.F.R. § 166.2
UNAUTHORIZED TRADING**

20. Paragraphs 1 through 19 above are realleged and incorporated herein by reference.
21. Section 166.2 of the Regulations, 17 C.F.R. § 166.2 makes it unlawful for any futures commission merchant, introducing broker or any of their associated persons to directly or indirectly effect a transaction in a commodity interest for the account of any customer unless before the transaction the customer, or person designated by the customer to control the account:
- (a) Specifically authorized the futures commission merchant, introducing broker or any of their associated persons to effect the transaction (a transaction is "specifically authorized" if the customer or person designated by the customer to control the account specifies (1) the precise commodity interest to be purchased or sold and (2) the exact amount of the commodity interest to be purchased or sold); or (b) Authorized in writing the futures commission merchant, introducing broker or any of their associated persons to effect transactions in commodity interests for the account without the customer's specific authorization; Provided, however, That if such futures commission merchant, introducing broker or any of their associated persons is also authorized to effect transactions in foreign futures or foreign options without the customer's specific authorization, such authorization must be expressly documented.
22. As described in paragraphs 1 through 21 above, defendants effected transactions in commodity interests for the accounts of customers without obtaining, before the transaction: (a) specific authorization of the customers, or persons designated by the customers to control the account, in that neither the customers nor persons designated by the customers to control the

account specified (1) the precise commodity interest to be purchased or sold and (2) the exact amount of the commodity interest to be purchased or sold; or, (b) authorization, in writing, for the futures commission merchant, introducing broker or any of their associated persons to effect transactions in commodity interests for the accounts without the customers' specific authorization; all in violation of Commission Regulation 166.2, 17 C.F.R. § 166.2.

23. Each act of unauthorized trading including but not limited to those specifically alleged herein at paragraphs 1 through 22 is alleged as a separate and distinct violation of Commission Regulation 166.2, 17 C.F.R. § 166.2.

COUNT II

VIOLATION OF SECTION 4b(a)(2)(i) and (iii) OF THE COMMODITY EXCHANGE ACT, 7 U.S.C. § 6b(a)(2)(i) and (iii) FRAUD IN CONNECTION WITH COMMODITY FUTURES CONTRACTS

24. Paragraphs 1 through 23 above is realleged and incorporated herein by reference.

25. Section 4b(a)(2)(i) and (iii) of the Act, 7 U.S.C. § 6b(a)(2)(i) and (iii), makes it unlawful for any person, in or in connection with any order to make, or the making of, any contract of sale of any commodity for future delivery, made, for or on behalf of any other person if such contract for future delivery is or may be used for (A) hedging any transaction in interstate commerce in such commodity or the products or byproducts thereof, or (B) determining the price basis of any transaction in interstate commerce in such commodity, or (C) delivering any such commodity sold, shipped, or received in interstate commerce for the fulfillment thereof -- (i) to cheat or defraud or attempt to cheat or defraud such other person; and (iii) willfully to deceive or attempt to deceive such other person by any means whatsoever in regard to any such order contract or the disposition or execution of any such order or contract, or in regard to any act of agency performed with respect to such order or contract for such person.

26. As described in paragraphs 1 through 25 above, defendants in or in connection with orders to make, or the making of, contracts of sale of commodities for future delivery, made, or to be made, for or on behalf of another person, where such contract for future delivery may be used for the purposes set forth in Section 4b(a)(2) of the Act: (i) cheated or defrauded or attempted to cheat or defraud such other person; and/or (iii) willfully deceived or attempted to deceive such other person by any means whatsoever in regard to any such order or contract or the disposition or execution of any such order or contract, in violation of Section 4b(a)(2)(i) and (iii) of the Act, 7 U.S.C. § 6b(a)(2)(i) and (iii).

27. Each fraudulent misrepresentation and omission, including but not limited to those specifically alleged herein at paragraphs 1 through 26 is alleged as a separate and distinct violation of Section 4b(a)(2)(i) and (iii) of the Act, 7 U.S.C. § 6(b)(a)(2)(i) and (iii).

COUNT III

VIOLATION OF SECTION 4c(b) OF THE ACT, 7 U.S.C. § 6c(b) AND COMMISSION REGULATION 33.10, 17 C.F.R. § 33.10: FRAUD IN CONNECTION WITH COMMODITY OPTIONS CONTRACTS

28. Paragraphs 1 through 27 are realleged and incorporated herein by reference.

29. Section 4c(b) of the Act, 7 U.S.C. § 6c(b), makes it unlawful to offer to enter into, enter into or confirm the execution of, any transaction involving any commodity regulated under the Act which is of the character of, or is commonly known to the trade as, an "option", "privilege", "indemnity", "bid", "offer", "put", "call", "advance guaranty", or "decline guaranty", contrary to any rule, regulation, or order of the Commission prohibiting any such transaction or allowing any such transaction under such terms and conditions as the Commission shall prescribe.

30. Commission Regulation 33.10, 17 C.F.R. § 33.10, makes it 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.

31. As described in paragraphs 1 through 30 above, defendants in connection with offers to enter into, the entry into, the confirmation of the execution of and the maintenance of commodity options transactions cheated or defrauded or attempted to cheat or defraud at least one other person; and deceived or attempted to deceive at least one other person by various other means, in violation of Section 4c(b) of the Act and Commission Regulation 33.10.

32. Each fraudulent misrepresentation and omission, including but not limited to those specifically alleged herein at paragraphs 1 through 31 above is alleged as a separate and distinct violation of Section 4c(b) of the Act, 7 U.S.C. § 6c(b), and Commission Regulation 33.10, 17 C.F.R. § 33.10.

COUNT IV

VIOLATION OF SECTION 4o(1) OF THE ACT, 7 U.S.C. § 6o(1) FRAUD BY A COMMODITY TRADING ADVISOR

33. Paragraphs 1 through 32 are realleged and incorporated herein by reference.

34. A commodity trading advisor is defined, pursuant to Section 1a(6) of the Commodity Exchange Act, as any person who, for compensation or profit, engages in the business of advising others, either directly or through publications, writings, or electronic media, as to the value of or the advisability of trading in - any contract of sale of a commodity for future delivery made or to be made on or subject to the rules of a contract market or derivatives transaction

execution facility any commodity option authorized under section 6c of the Commodity Exchange Act.

35. As described in paragraphs 1 through 34 above defendants, for compensation or profit, engaged in the business of advising others, either directly or through publications, writings, or electronic media, as to the value of or the advisability of trading in - any contract of sale of a commodity for future delivery made or to be made on or subject to the rules of a contract market or derivatives transaction execution facility any commodity option authorized under Section 6c of the Act.

36. Section 4o(1) of the Act, 7 U.S.C. § 6o(1), makes it unlawful for a commodity trading advisor, associated person of a commodity trading advisor, among others by use of the mails or any means or instrumentality of interstate commerce, directly or indirectly - to engage in any transaction, practice, or course of business which operates as a fraud or deceit upon any client or prospective client.

37. As described in paragraphs 1 through 36 above, defendants, by use of the mails and other means or instrumentality of interstate commerce, directly or indirectly - engaged in transactions, practices, or courses of business that operated as a fraud or deceit upon clients or prospective clients in violation of Section 4o(1) of the Act, 7 U.S.C. § 6o(1).

38. Each fraudulent misrepresentation and omission, including but not limited to those specifically alleged herein at paragraphs 1 through 37 above is alleged as a separate and distinct violation of Section 4o(1) of the Act, 7 U.S.C. § 6o(1).

RELIEF

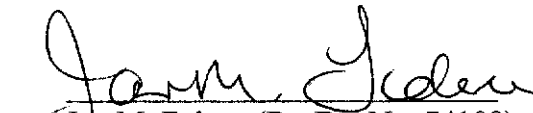
39. WHEREFORE, the Commission respectfully requests that this Court, as authorized by Section 6c of the Act, 7 U.S.C. § 13a-1, and pursuant to its own equitable powers, enter:

- a) an order finding that defendants violated Sections 4b(a)(2)(i) & (iii), 4o(1) and 4c(b) of the Act, 7 U.S.C. §§ 6b(a)(2)(i) & (iii), 6o(1) and 6c(b), and Sections 33.10 and 166.2 of the Regulations, 17 C.F.R. §§ 33.10 and 166.2;
- b) a permanent injunction prohibiting defendants from engaging in conduct violative of Sections 4b(a)(2)(i) & (iii), 4o(1) and 4c(b) of the Act, 7 U.S.C. §§ 6b(a)(2)(i) & (iii), 6o(1) and 6c(b) and Sections 33.10 and 166.2 of the Regulations, 17 C.F.R. §§ 33.10 and 166.2;
- c) an order prohibiting defendants from trading on or subject to the rules of any registered entity;
- d) an order directing defendants to disgorge, pursuant to such procedure as the Court may order, all benefits received from the acts or practices which constitute violations of the Act or Regulations, as described herein, and interest thereon from the date of such violations;
- e) an order directing defendants to make full restitution, pursuant to such procedure as the Court may order, to every customer whose funds were received by them as a result of acts and practices which constituted violations of the Act and Regulations, as described herein, and interest thereon from the date of such violations;
- f) an order directing defendants to pay a civil monetary penalty in the amount of not more than the higher of \$120,000 or triple the monetary gain to each defendant for each violation of the Act or Regulations; and
- g) such other and further remedial ancillary relief as the Court may deem appropriate.

Plaintiff requests that the trial be held in Lincoln, Nebraska.

Dated: May 3, 2004

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Jan M. Folena". The signature is written in a cursive style with a large, looping initial "J".

Jan M. Folena (Pa. Bar No. 74108)

Chief Trial Attorney

Commodity Futures Trading

Commission

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