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DANIEL J. EMILY,
Complainant,

v.

GUY K. GLEICHMANN, and
UNITED STRATEGIC INVESTORS
GROUP LLC,
Respondents.

CFTC Docket No. 14-R007
Served electronically

INITIAL DECISION ON REMAND

Daniel Emily, the Complainant, brought these reparations proceedings on January 1, 2014, alleging that Guy Gleichmann, a registered commodity trading advisor (CTA) during the relevant time period, and his company United Strategic Investors Group, LLC (USIG), (1) entered into risky trades on his behalf without his authorization, and (2) churned his account. Compl. at 1-2 (Jan. 1, 2014); Compl. Addendum (Feb. 21, 2014). Former Judgment Officer (JO) McGuire held a telephonic hearing regarding the merits on March 24, 2016, and issued an Initial Decision on May 23, 2017.

In that Initial Decision, JO McGuire found that Gleichmann had churned Emily's account, but ruled that Emily was entitled to damages only for January and February 2012 by virtue of the statute of limitations. Initial Decision at 3-5. Emily was therefore awarded $1,121 in damages plus pre- and post-judgment interest of

1.10% compounded annually from February 29, 2012, as well as the $125 fee for filing these proceedings. *Id.* at 1, 6. In addition, JO McGuire found that Emily had failed to establish any violations other than churning with respect to Gleichmann's trades because of the general deference given to a CTA's trading strategies. *Id.* at 6.

Gleichmann timely appealed this decision, and the Commission remanded this matter on October 31, 2017 to this Office to explain how each element of churning as set forth in *Ferriola v. Kearse-McNeil* has been met. Commission Order at 1 (citing 2000 WL 873653 at *9 (CFTC June 30, 2000)). Before I completed my review on remand, I was appointed by the Commission as its Judgment Officer on April 9, 2018. Pursuant to that appointment, I issued a Notice of Appointment on April 23, 2018, in which the parties were "directed to submit any <u>new evidence</u> relevant to my reexamination of the record by May 9, 2018."[1] *See* Appointment Order at 1 (emphasis added).

Gleichmann filed two email responses on May 9, 2018, and one more email response on May 10, 2018. Emily filed an email response after my deadline, on June 4, 2018, to which Gleichmann responded on October 20, 2018. None of these arguments make any new points not found in the record below or Gleichmann's appellate briefs. Accordingly, they were resolved by the remand and none require an independent reconsideration. Having undertaken the churning analysis under the framework required by the Commission, for the reasons that follow, I find that

[1] In that same Order, I extended my own deadline to reconsider the record and issue a new decision until September 14, 2018. Appointment Order at 2. I extended it again until November 5, 2018. Order (Oct. 24, 2018).

Respondents did not churn Emily's account, and REVERSE the finding and associated damages award.

Legal Analysis and Conclusions

In its Remand Order, the Commission directed this Office to explain its analysis with respect to the churning claim. Remand Order at 1. The churning claim itself is limited to conduct in January and February 2012, since the statute of limitations bars recovery for any prior misconduct—a finding that the Commission did not overturn. Thus the scope of this decision on remand is limited to analyzing the facts under the relevant case law with respect to churning for those two months.

"Churning occurs when a broker who has control over a customer's account trades the account excessively for the purpose of generating commissions, without regard to the customer's interests." *Fields v. Cayman Associates, Ltd.*, CFTC Dkt. Nos. R 79-201, 79-355, 1985 WL 56217, at *1 (CFTC Jan. 2, 1985). As the Commission stated in its Order, to prove churning, a complainant must show that the respondent: (1) controlled the level and frequency of trading in the account, (2) chose an overall volume of trading that was excessive in light of the complainant's trading objectives, and (3) acted with either intent to defraud or in reckless disregard of the customer's interests. *Ferriola*, 2000 WL 873653, at *9; *Fijolek v. Salimian*, CFTC Dkt. No. 99-R115 2001 WL 1136058, at *10 (CFTC Sept. 26, 2001) (same). Although Gleichmann controlled Emily's account, Emily has not shown, by a preponderance of the evidence, that Gleichmann traded Emily's account excessively.

A. Gleichmann controlled Emily's account.

"Generally, where a customer has granted power of authority to the Respondent, control is presumed." *See, e.g.*, *Cazzetta v. Robbins Futures Inc.*, CFTC Dkt. No. 13-R014, 2017 WL 7789741, at *7 (CFTC Dec. 11, 2017); *Gile v. First Futures of Arizona, Inc.*, CFTC Dkt. No. 89-R124, 1990 WL 282923, at *3 (CFTC Aug. 14,1990); *Ball v. Shearson Hayden Stone, Inc.*, CFTC Dkt. No R 77-100, 1981 WL 26102, at *2-3 (CFTC Apr. 2, 1981); *Smith v. The Siegel Trading Company, Inc.*, CFTC Dkt. No. R 77-42, 1980 WL 15709, at *5 & n.7 (CFTC Sept. 3, 1980). Because Emily maintained a discretionary account with Gleichmann and signed a power of attorney to effectuate that discretion in October 2008 (and again in January 2012), control is presumed. *See* Compl. Ex. Customer Agreement and Related Sections ¶ 5; Answer Addendum ¶ 5.

B. Gleichmann did not trade an excessive amount in light of Emily's trading objectives.

The second criterion—evidence of excessive trading—can be found in a variety of ways, including: (1) high commission to equity ratios (the monthly commission divided by the average daily balance of account equity for the same month); (2) high percentage of day trades (trades established and offset within the same day); (3) a broker's departure from previously agreed upon trading strategy; (4) trading in an account when it is under-margined; and (5) reestablishment of a previously liquidated position in the same or related futures contract without any apparent trading strategy. *Cazzetta*, 2017 WL 7789741 at *7; *Fields*, 1985 WL 56217 at *2. "A finding of excessiveness does not require the presence of all of the above indicators." *Id.* The Commission has "emphasized that an analysis of excessiveness cannot be reduced to a mechanical rule or formula." *In the Matter of Murlas Commodities, Inc.*, CFTC Dkt. No. R 85-29, 1995 WL 523563, at *4 (CFTC Sept. 1, 1995). The Commission has also held that "evidence of customer trading objectives plays a more substantial role in evaluating issues of excessiveness." *Id.*

In the instant case, I find that only the first three factors are relevant, and an evaluation of them as well as a consideration of other facts does not support a finding of excessive trading by a preponderance of the evidence.

1. The monthly commission-to-equity ratios were not high in January or February 2012, suggesting that trading was not excessive.

As the Initial Decision noted, the monthly fees per net liquidating value, captured at the end of the month, were presumptively high for February 2012 at 28%. *See* February Monthly Statement at 4 (Commissions & Fees of $676.92/Net Liquidating Value of $2,438.62); Initial Decision at 3-4. However, month-end net liquidating value is less informative than the average daily equity in a month, since the former reflects an ephemeral snapshot of account value in time and the latter reflects a more accurate picture of what the account value and activity looked like overall in a given month when the fees were being generated. *Cf. In the Matter of Lincolnwood Commodities, Inc. of Calif.*, CFTC Dkt. No. 78-48, 1984 WL 48104, *23-*24 (CFTC Jan. 31, 1984) (explaining utility and means of calculating monthly commission-to-equity ratio). Emily's commissions to average daily equity ratio for

February 2012 was 13%,[2] under the 18% threshold generally considered a benchmark in deciding whether an account has been churned. *Id.* The ratio for January 2012 was somewhat higher at 15%, but still under the 18% benchmark.

2. There were a high percentage of day trades, but the trading volume was too low to support a finding of excessive trading.

As the Initial Decision stated, Gleichmann's trading in certain months included a high number of day trades. For example, Gleichmann began executing a comparatively large number of day trades in crude oil starting in March 2011. He began doing the same with natural gas in September 2011. This pattern remained relatively consistent through February 2012. And in fact, in February 2012, the vast majority of positions were liquidated within the same or the next day.

However, the "Commission has specifically rejected the theory that numerous day trades in a managed account constitute prima facie evidence of churning." *Seith v. Van Alen*, CFTC Dkt. No. 83-R782, 1985 WL 55278, at *5 (CFTC June 24, 1985). And day trading will be of limited probative value if "profiting from short-term market trends" is part of the customer's trading objectives. *In the Matter of Paragon Futures Ass'n*, CFTC Dkt. No. 88-18, 1992 WL 74261, at *11 (CFTC April 1, 1992). In the instant case, as will be discussed below, making a "quick profit" was in fact

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[2] To arrive at this figure, I used the sum of the net equity on the days there was any account activity and debited or credited any relevant fees, option premiums, and other realized gains and losses to arrive at a daily net equity for those days. I then divided the sum of this number by the number of days on which there was account activity to arrive at the daily average equity for the month of February. *See Leal v. Prestige Capital Investments Corp.*, CFTC Dkt. No. 89-R37, 1989 WL 242015, at * 7 (CFTC July 7, 1989). For a starting equity number, I used the ending cash balance for January 2012, since that figure excludes the value of any open market positions, which I also excluded from the February analysis. Had I included the value of open positions in net equity, the commission to equity ratio would have been even lower.

one of Complainant's trading objectives, limiting the utility of examining the high number of day trades.

In addition, the overall trading volume per month was relatively low in every month since March 2011. For example, in January 2012, there were six trades executed in the month. In February 2012, there were 27 trades executed in the month. In this case, given the absence of other factors indicating churning, this is too low a trading volume to detect churning. *See, e.g., Birkner v. ContiCommodity Svcs. Inc.*, CFTC Dkt. Nos. R 81-947, R 82-128, 1986 WL 65827, at *6 (CFTC July 17, 1986) (noting that 39 transactions, with roughly 50% of those being day or overnight-traded, was too small a trading level on which to find churning); *cf. Parciasepe v. Shearson, Hayden, Stone, Inc.*, CFTC Dkt. Nos. R 79-795, 80-123, 1985 WL 56215, at *1 (CFTC Jan. 2, 1985) (noting that Respondent had executed up to 596 round turn trades in one month). If in fact churning the account was a motivating factor, one would expect to see more trades in general.

Because the trading volume overall was low, and because day trading is of limited probative value here, I find that the day trades do not support a churning finding.

3. Gleichmann did not depart from Emily's trading objectives.

An evaluation of whether Gleichmann departed from Emily's trading objectives necessarily requires identifying those objectives. In this case, Emily had a long trading history with Gleichmann and his objectives, as described in his testimony, stayed consistent throughout this history.

Emily began trading with Gleichmann in 2004 with USIG, which was a registered Introducing Broker from 2004 through 2008, and a registered Commodity Trading Advisor from 2008 through 2013. Hearing Tr. at 18:18-19:7 (Gleichmann). While USIG was registered as an IB, Emily maintained a nondiscretionary trading account. That is, an account where the client makes all the trading decisions. But on October 24, 2008, upon the change from IB to CTA, Emily signed an updated disclosure agreement and gave Gleichmann power of attorney granting him discretionary trading authority. Answer Ex. (Wavelength Disclosure Document); Hearing Tr. at 22:25-23:5 (Gleichmann).[3]

After transitioning from a nondiscretionary account to a discretionary one, Emily committed a total of $7,500 through deposits made in December 2008 and March 2009, when trading began. Hearing Tr. at 22:6-8 (Gleichmann). Emily made a net profit of $11,462 from 2009 through 2011. Emily Production Ex. 3 (Jan. 6, 2016). He realized a loss of $2,000 in 2012. *Id.*

During this time, Emily stated that he traded "commodities, currencies, financial (treasuries), and stock market indices," and explained that his "strategy included both buying and selling of options/futures. A common strategy of mine involved selling out-of-the-money options with the intention of collecting the premium." Emily Production Ex. 2 (January 6, 2016). In addition, throughout his trading history, from 2004 through 2013, Emily's agreed-to trading concentrated on energy contracts on the NYMEX. *Id.* at 10:1-11:2.

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[3] Emily signed an updated Disclosure Document on January 13, 2012. Answer Ex. (Wavelength Disclosure Document).

Emily testified that he "probably had losses overall," but that he was drawn to these products because "[i]t seem[ed] like a good way to make some, make some quick profit . . . if it worked out." Hearing Tr. at 8:24-9:13 (Emily). Emily understood the "high risk" nature of this kind of trading. *Id.* at 9:14-17.

Upon review of the monthly account statements, it appears that Gleichmann adhered to Emily's trading objectives fairly closely. He traded various commodity options and energy futures, which is consistent with Emily's objectives and own trading style. He did begin day trading, as discussed above, sometime in March 2011, but that trading was not contrary to Emily's interests. This is therefore unlike Commission cases finding churning where the customer's trading strategies were ignored. *See, e.g., Parciasepe,* 1985 WL 56215, at *2 (customer understood there would be trading in five or six commodities but Respondent traded in more than twenty commodities); *Piskur v. Int'l Precious Metals Corp.*, CFTC Dkt. Nos. R 80-1186, 81-142, 1985 WL 56214, at *5 (CFTC Jan. 2, 1985) (complainant's objectives were "conservative," but the level of trading in his account "was consistent only with the most aggressive of speculative trading objectives").

More importantly, there is a disconnect between Emily's churning allegations and what actually occurred in his account. Emily believes that Gleichmann began churning his account when Emily gave Gleichmann discretionary trading authority. For example, he states: "I was reluctant to change over to a discretionary account. . . . Once the switch was made, however, everything changed quickly. Almost as if someone had flipped a switch Mr. Gleichmann launched into a wild flurry of trades which destroyed the account in a short period of time." Emily Production Ex. 2 (Jan. 6, 2016). But the change from nondiscretionary to discretionary was made in 2008, and yet Emily did not complain about it until 2012, having testified that he discovered it in December 2011. Hearing Tr. at 25:20-26:9 (Emily). And in fact Emily did not bring this litigation until January 1, 2014. Not only does that foreclose all claims before 2012, as JO McGuire found, *see* Initial Decision at 5, but it suggests that Emily was complaining more about the losses that started accruing around the same time than potential churning.

And here, the lateness of the complaint was not due to Emily's lack of awareness. The Commission has found repeatedly that "the nature of churning is such that it rarely lends itself to ready detection by the customer." *Piskur*, 1985 WL 56214 at *6. This is why ratification is not usually a defense to churning. *Id.* However, evidence "which shows that the customer possessed sufficient sophistication and experience to enable him to discover that his account was being overtraded" will undercut any assumption that the complainant in fact did not detect the churning previously. *Id.*

I find Emily was an informed and sophisticated investor. Emily considered himself an "informed" investor who read the *Financial Times* and listened to and read other relevant sources. Hearing Tr. at 24:15-25:8 (Emily). He admitted he was receiving account statements regularly after switching from a non-discretionary to a discretionary account in late 2008, and generally had a brief telephone call with Gleichmann once a week. Hearing Tr. at 23:6-24:11 (Emily). Thus the record supports a finding that he was aware of what was going on in his account ever since the time it was converted to a discretionary account in October 2008. And importantly, the trading strategy starting in December 2011 does not look appreciably different than the preceding months.[4]

Emily does point to one fact indicating that Gleichmann was trading outside his preferred strategy. He identified a particular set of transactions on February 7, 2012 with a realized profit that was outstripped by the fees. On this day, Gleichmann entered into a set of round turns on natural gas futures that yielded a profit of $60. But the fees on these two round turn transactions were $199, and so in fact Emily lost $139 on this "winning" trade though Gleichmann made money. *Compare* February 2012 Monthly Statement at 1, *with id.* at 3. But other round turn transactions executed this same month were actual winning trades, and it is a stretch to assume the barely winning or losing trades were entered into for the purposes of churning on such an inconsistent record with little trading activity.

On balance, the evidence in the record does not support a finding of excessive trading. Rather, this is more like *Halterman v. Eastern Capital Corporation* in

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[4] Moreover, it is not clear that Emily was in fact unhappy with the way his account was being handled in December 2011. At the hearing, Emily's recollection of when he realized there were problems in his account was poor and inconsistent. For example, he first claimed he asked Gleichmann to cease trading in, and in fact close, his account in early January 2012. Hearing Tr. 27:20-24 (Emily). He later testified that in fact he reached out to Gleichmann to close his account in February 2012. Hearing Tr. 28:8-11; 34:5-9; 37:4-25 (Emily). But in his Complaint Addendum, Emily stated that he reached out to Gleichmann to close his account sometime in early March 2012. Compl. Addendum at 2 (Feb. 24, 2014). And if in fact Emily was unhappy with his account as early as December 2011, as he testified, it is unclear why he renewed his discretionary trading relationship with him in mid-January 2012, *see* Hearing Tr. 33:8-22 (Gleichmann); Answer Ex. (Wavelength Disclosure Document), and why he never attempted to close his account again until July 2012. Hearing Tr. 31:21-32:15; July 2012 Monthly Statement (Gain Capital production in response to JO McGuire's subpoena) (Jan. 6, 2016).

which the Commission decided there was no churning where the customer "was in frequent contact with [Respondent] during the alleged churning period but there is no evidence that he had any complaints until the losses accrued in December." CFTC No. 85-R38, 1988 WL 232290, at *2 (CFTC April 15, 1988).

C. <u>There was no intent to defraud.</u>

Because I do not find that the record supports a finding that Respondents excessively traded Emily's account, there is no need to consider the third element of the churning claim—that is whether any excessive trading was done with an intent to defraud the customer.

ORDER

For the reasons discussed above, I find that Respondents did not churn Emily's discretionary account in January and February 2012. Gleichmann is therefore not liable to Emily for any damages or filing fees and the complaint is dismissed

Dated: November 5, 2018

Kavita Kumar Puri
Judgment Officer