

[Securities Regulation Daily Wrap Up, COMMODITY FUTURES—S.D. Fla.: Purported precious metals dealer must pay for lies about physical purchases, \(Sept. 1, 2016\)](#)

Securities Regulation Daily Wrap Up

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By [Amy Leisinger, J.D.](#)

A Florida federal district court found in favor of the CFTC on its fraud claim against an individual and a firm that claimed to sell precious metals. According to the court, the defendants engaged in margined derivatives transactions while purporting to actually purchase precious metals on behalf of customers. The court enjoined the defendants from further violations and ordered payment of a \$375,000 penalty and restitution to the defrauded clients (*CFTC v. Southern Trust Metals, Inc.*, August 29, 2016, King, J.).

Fraud. According to the CFTC, a Florida resident solicited investors through his company, Southern Trust Metals, Inc., and offered financing to purchase physical precious metals. The defendant and his company told customers that Southern Trust made loans to them to purchase precious metals in connection with these transactions, but no loans were made and no metals were purchased or delivered. Instead, they managed their precious metals exposure through over-the-counter derivative trades in the name of an offshore subsidiary with two U.K.-based trading firms.

Prior proceeding. In a motion for summary judgment, the CFTC contended that the transactions were illegal under the Commodity Exchange Act because they were offered to non-eligible contract participants and were not executed on an exchange. The CFTC also argued that Southern Trust had illegally acted as an FCM without registration. The court [awarded](#) the CFTC partial summary judgment, finding that the defendants engaged in illegal off-exchange, financed retail commodity transactions in violation of the CEA. In addition, by accepting money and orders for the transactions, the court found that the firm had acted as a futures commission merchant without registration and that the individual was liable as a controlling person. The CFTC did not seek summary judgment on its claim that the defendants committed fraud in connection with the transactions.

Fraud liability. The court found that Southern Trust misrepresented to customers that they were purchasing physical metals held in depositories and that they were receiving loans to purchase those metals in multiple promotional materials and sales calls. Further, the defendants transferred funds through the holding company to the U.K.-based firms for margined derivatives contracts, never holding title to or possessing physical metals, without disclosing these practices to customers. These statements and omissions were false and misleading and also material, as a reasonable customer would have found it material that no metals or loans existed, the court stated. The defendants knew, or were reckless in not knowing, that no physical metals had been purchased via the U.K. firms, particularly in light of the account statements from the companies describing the actual arrangement. As a controlling person, the individual defendant is jointly and severally liable for Southern Trust's violations of the antifraud provisions of the CEA and its underlying regulations, the court held.

Sanctions. Given the defendants' expertise, it was egregious to accept customer funds and disguise the trading of metals derivatives as the purchase and sale of physical metals on a leveraged basis, the court found. Further, the court stated, there is a strong likelihood of opportunities for future violations. As such, the court determined to enter a permanent injunction against the defendants. The court also concluded that restitution of customer losses is appropriate in connection with both of the schemes, noting that a defendant who fraudulently induces participation in a transaction cannot later blame the market for customer losses. Finding that a treble penalty would be excessive in light of the other sanctions, the court decided to impose a civil penalty of just over \$375,000—one-third of the defendants' total gain.

The specific terms of the sanctions will be set out in a forthcoming final judgment order.

The case is [No. 1:14-CV-22739-KING](#).

Attorneys: Joseph A. Konizeski for the CFTC. Gary M. Sinclair (Gary Sinclair, Attorney at Law) and Jose Antonio Ortiz (Herron Ortiz, P.A.) for Southern Trust Metals, Inc. and Loreley Overseas Corp.

Companies: Southern Trust Metals, Inc.; Loreley Overseas Corp.

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