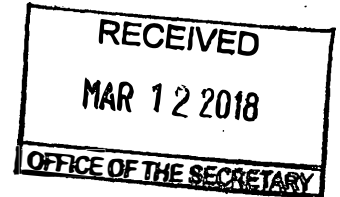


HARD COPY

UNITED STATES OF AMERICA
BEFORE THE
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C.



In the Matter of the Application of
The Association of Robert J. Escobio
With Southern Trust Securities, Inc.
For Review of Denial of Registration by
FINRA
Admin. Proc. File No. 3-18143 - (FINRA SD-2130)

**ROBERT ESCOBIO'S REQUEST THAT THE COMMISSION TAKE OFFICIAL
NOTICE OF APPELLANTS' PETITION FOR PANEL REHEARING
FILED MARCH 6, 2018 WITH THE UNITED STATES
COURT OF APPEALS FOR THE ELEVENTH CIRCUIT**

Robert J. Escobio, ("Mr. Escobio"), by and through his undersigned counsel, requests that the Commission take official notice of the attached Appellants' Petition for Panel Rehearing filed in response to the decision of the Eleventh Circuit Court of Appeals in the *U.S. Commodity Futures Trading Association v. Southern Trust Metals, Inc., Loreley Overseas Corporation, and Robert Escobio*, dated January 22, 2018. See 17 C.F.R. § 201.323, (explaining that the Commission may take notice "of any material fact which might be judicially noticed by a district court of the United States"), see also *Anthony Fields*, Exchange Act Release No. 74344, 2015 SEC LEXIS 662, at *6n.3 (Feb. 20, 2015);

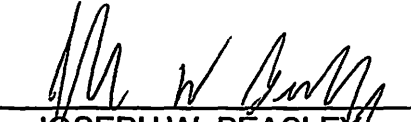
Thomas R. Alton, 52 S.E.C. 380, 386 n.24 (1995). This timely filed petition renders the Eleventh Circuit's decision, for which FINRA requested Official Notice on January 23, 2018, non-final.

Dated: March 9, 2018

Respectfully submitted

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing has been served upon the following parties this 9th day of March, 2018 as follows:

VIA FAX & FEDEX:

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United States Securities & Exchange
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By: _____


Joseph W. Beasley

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Case: 16-16544 Date Filed: 03/06/2018 Page: 1 of 59

**IN THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT**

APPEAL NO. 16-16544

**U.S. COMMODITY FUTURES
TRADING COMMISSION,
Plaintiff-Appellee,**

v.

**SOUTHERN TRUST METALS, INC.,
LORELEY OVERSEAS CORPORATION,
and ROBERT ESCOBIO,
Defendants-Appellants.**

**ON APPEAL FROM THE UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA
CASE NO. 1:14-CV-22739-JLK**

APPELLANTS' PETITION FOR PANEL REHEARING

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**CERTIFICATE OF INTERESTED PARTIES AND CORPORATE
DISCLOSURE STATEMENT**

Pursuant to FRAP 26.1 and 11th Cir. R. 26.1-1, *et seq.*, Defendants-Appellants Southern Trust Metals, Inc., Loreley Overseas Corporation, and Robert Escobio file this Certificate of Interested Persons and Corporate Disclosure Statement:

Burden, Ashley J. – Counsel for the U.S. Commodity Futures Trading Commission (“CFTC”).

Escobio, Robert – Defendant-Appellant.

Figueroa, Janet—paralegal in District Court proceedings for Robert Escobio, and for Appellants on appeal.

Herron Ortiz – counsel in District Court proceedings for Southern Trust Metals, Inc. and Loreley Overseas Corporation.

Hollinger, Rosemary – Counsel for CFTC.

Homer Bonner Jacobs, P.A. – counsel in District Court proceedings for Robert Escobio, and for Appellants on appeal.

Homer, Peter W. – counsel in District Court proceedings for Robert Escobio, and for Appellants on appeal.

King, Christopher John – counsel in District Court proceedings for Robert Escobio, and for Appellants on appeal.

King, Hon. James Lawrence – U.S. District Court Judge presiding.

Konizeski, Joseph A. – Counsel for CFTC.

Lechich, Brian John – Counsel in District Court proceedings for Southern Trust Metals, Inc. and Loreley Overseas Corporation.

Loreley Overseas Corporation – Defendant-Appellant, formerly registered with the British Virgin Islands Financial Services Commission, 100% owner of Southern Trust Metals, Inc.

Metzger, Carlin R. – Counsel for CFTC.

Ortiz, Jose Antonio – Counsel in District Court proceedings for Southern Trust Metals, Inc. and Loreley Overseas Corporation.

Sinclair, Gary – Counsel in District Court proceedings for Southern Trust Metals, Inc. and Loreley Overseas Corporation.

Southern Trust Metals, Inc. – Defendant-Appellant, registered with the Florida Department of State, administratively dissolved.

Southern Trust Securities Holding Corporation (ticker symbol “SOHL”)—100% owner of Loreley Overseas Corporation, registered with the Florida Department of State, publicly traded OTC.

Southern Trust Securities, Inc.—wholly owned subsidiary of Southern Trust Securities Holding Corporation, registered with the Florida Department of State.

Stukes, Anne – Counsel for CFTC on appeal.

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Appellants (“Defendants”) timely petition this Court for panel rehearing pursuant to Federal Rule of Appellate Procedure 40 and 11th Circuit Rule 40-3.¹

I. Introduction

The Court’s Opinion makes a crucial factual error that utterly changes the proximate cause analysis on the leveraged metals transactions. The Opinion states the metals transactions Southern Trust Metals engaged in were “futures” contracts. That is objectively not the case. From the Complaint through closing argument, the CFTC consistently maintained the leveraged metals transactions were over-the-counter spot contracts that were pegged to the market price of silver. Spot contracts, a type of derivatives contract, are not futures contracts, as many decisions have held. (Indeed, the Opinion cites the landmark case on this topic, *C.F.T.C. v. Zelener*, 373 F.3d 861 (7th Cir. 2004), *see slip op.* at 32). Account statements and other record evidence also clearly showed the metals transactions were not futures contracts. The district court never ruled otherwise, and the CFTC never altered its position. Even at oral argument, when the Panel asked the question of both sides, the CFTC maintained that the metal transactions were over-the-counter derivatives, while the undersigned explicitly stated they were not futures contracts. In short, no one – neither the CFTC, the trial court nor

¹ The Rules allow 45 days from the date of judgment to petition for rehearing in a case such as this where a federal agency is a party.

Defendants – ever asserted, much less agreed, that the metals transactions were futures.

The error turns out to be case dispositive. There *was* a set of futures and options transactions at issue, but they were separate from the metals transactions. Only eight customers traded futures and options, and the CFTC never doubted the legality of those transactions. The sole violation alleged for the futures and options trades was an alleged failure to register. The Opinion correctly holds registration violations and alleged omissions in connection with the futures and options transactions did not proximately cause any customer loss in this case, and accordingly vacates the restitution award dealing with the futures and options trades. The Court came to a different conclusion for the metals transactions, but only because it incorrectly understood them to be futures contracts. Respectfully, Defendants submit that once that error is corrected, the Court's proximate cause analysis requires vacatur or reversal of the restitution award for the metals transactions as well. Further, the Opinion neglects to address that the CFTC never succeeded in admitting into evidence any calculations to support the claimed restitution amount for the metals transactions. This fatal evidentiary shortcoming also merits rehearing.

II. Summary of Proceedings

The CFTC brought this enforcement action alleging Commodity Exchange Act (“CEA”) and CFTC regulation violations with respect to two distinct groups of transactions. Southern Trust Metals engaged in leveraged physical metals transactions that, according to the Complaint, were actually “OTC [over the counter] contracts which tracked the value of the underlying commodities being sold (gold, silver, platinum or palladium.)” Doc 1 p. 11. These transactions were made through highly-regulated London financial firms, Hantec and Berkeley. The second group of transactions comprised futures and options trades eight customers made in their Berkley sub-accounts. The CFTC sought, and the district court awarded, statutory restitution under 7 U.S.C. § 13a-1(d)(3) for both groups of transactions: \$559,727 on the futures and options transactions, and \$1,542,892 on the metals transactions—though the CFTC introduced no calculations supporting these totals.

Defendants appealed. One argument asserted that the district court applied a discredited foreseeability causation standard. The error was reversible, Defendants maintained, because the record lacked any evidence showing the claimed violations proximately caused customer loss, as required for restitution under 7 U.S.C. § 13a-1(d)(3). This Court mostly agreed. The Court rejected the district court’s foreseeability standard, following the U.S. Supreme Court’s decision in

Bank of America Corp v. City of Miami, 137 S. Ct. 1296 (2017). The Opinion finds § 13a-1(d)(3) “surely demands more than foreseeability alone,” and that Congress “has given no indication, either in the CEA’s text or otherwise, that it intended to depart from the common-law conception of proximate cause.” Slip op. at 26 (citing *Bank of America*, 137 S. Ct. at 1305). Applying prevailing directness principles, the Court vacated the restitution award on the futures and options transactions, finding no record evidence that a failure to register (the sole alleged violation on these transactions) proximately caused any customer loss. *Id.* at 29. The same held for the CFTC’s alleged omissions theory on its fraud-based claims. The Opinion accurately finds no record evidence that “losses flowed from the Defendants’ omissions regarding the roles of Loreley, Berkeley, or Hantec.” *Id.* at 29.

However, this Court affirmed the restitution award with respect to the metals transactions, on the purported basis that customers were not buying leveraged physical metals as represented but futures contracts. The description of the leveraged metals transactions supposedly being futures contracts permeates the Opinion. *See* slip op. at 2 (stating Southern Trust Metals “promised to invest customers’ money in precious metals but instead invested the funds in futures”); *id.* at 5 (“nor did [Southern Trust Metal] inform customers who wished to invest in metals...that their money was being invested in futures”); *id.* at 8 (“instead of issuing loans to those customers and investing their money in metals, the

Defendants took the customers' money and invested it in futures"); *id.* at 19 (those documents, as well as the monthly account statements that Escobio received, make clear that Loreley was investing the customers' money in futures, not metals."); *id.* at 22 ("Defendants, for example, represented that they were investing customers' money in metals when in fact they were investing it in futures."). But the error features most prominently in the restitution analysis.

The Court reasoned that for customers who "wished to invest in metals ... there is no question that the Defendants' unilateral act of investing the funds in futures was a 'substantial' or 'significant contributing' cause of the loss." Slip op. at 31 (emphasis added). The Court even examined the "crucial differences between metals and futures," pointing out that the use of leverage in futures transactions could cause "losses greater than a customer's investments of funds," that futures contracts almost always have expiration dates, and that futures investors cannot "ride out" unfavorable market movements as a result. The assumption of a futures contract, therefore, played an integral role in the Court's decision to affirm the restitution award on the leveraged metals transactions. *Id.* at 31-33.

Defendants also appealed the amount of the restitution award on the basis that the CFTC presented no calculations at trial (the district court barred it from

doing so as a result of discovery abuses). The Opinion affirms the restitution amount without discussion of this crucial shortcoming in the CFTC’s case.

III. Argument

A. The metals transactions were not futures contracts.

It is undisputed the leveraged metals transactions were not futures contracts. The CFTC admitted as much in its Complaint, describing Southern Trust Metals’ product as “OTC contracts which tracked the value of the underlying commodities beings sold....” Doc 1 p. 11, ¶ 42. The CFTC throughout the district court case, and continuing through this appeal, distinguished what it alleged were these illegal off-exchange leveraged metals transactions in OTC spot contracts, and the legal futures and options transactions eight customers engaged in at Berkeley. *See id.* p. 7 ¶ 51; Appellee Br. p. 12, 21. The evidence highlighted clear differences between the futures and the metals transactions. The account statements for the eight customers who engaged in futures transactions, for example, literally say “FUTURE,” or the abbreviated, “FUT”:

KEY: FUT-Future OPT-Option EXO-Exercised Opt ASO-Assigned Opt CSH-Future Cash Settle EPP-Exch for Physical EPS-Exch for Swap

TRADE DATE	TRAD TYPE	TRADE NUMBER	QUANTITY	DELIVERY	EXE BRK	STRIKE PRICE	TRADE PRICE/ PREMIUM	OPEN POSN VALUATION	COMMISSION / CHARGES	REFERENCE
CBOT 10 YEAR US TREASURY NOTE FUTURE Delivery SEP-11 Currency USD										
Last Trading Date 21-SEP-11										
29-JUL-11	FUT	1999722	-1	SEP-11	HSE		125-06.00/32	(500.00)	(10.00)USD	
		NETT	-1		SETTLEMENT PRICE		125-22.00/32		(500.00)	
CHE STANDARD AND POORS 500 E-MINI FUTURE Delivery SEP-11 Currency USD										
Last Trading Date 16-SEP-11										
29-JUL-11	FUT	1999819	1	SEP-11	HSE		1282.7500	282.50	(10.00)USD	
		NETT	1		SETTLEMENT PRICE		1288.4000		282.50	

Supp. Appx. 68.

Statements for the leveraged metals transactions, in contrast, contain totally different information, including the symbol for silver, “XAG,” the specific quantity bought (“.20,” viz. 1,000 oz.), and the market price (in U.S. dollars):

Open Trades:

Ticket	Open Time	Type	Size	Item	Price	S/L	T/P	Price	Commission	R/O Swap	Trade P/L
783247	2011.08.24 16:03	buy	0.20	xagUSD	40.69	0.00	0.00	41.52	0.00	-6.30	830.00
									0.00	-6.30	830.00
								Floating P/L:			823.70

Appx. 1153.

Further confirming that the metals transactions were not futures contracts, Berkeley’s head trader wrote Southern Trust Metals during the trading that the leveraged metals accounts “only traded in OTC silver bullion and never traded any futures contracts,” Defs’ Ex. 50 (emphasis added). The parties disputed whether the phrase “OTC silver bullion” meant physical silver or derivative OTC spot contracts in silver. But no one ever questioned the truth of the statement that the leveraged metals accounts “never traded any futures contracts.” Erasing any doubt about this at all, the CFTC in its trial court closing argument contended, “What those [Hantec and Berkeley] statements show ... are margin derivatives trading of spot contracts pegged to the value of gold or silver.” Appx. 556:1-5 (emphasis added).

Spot contracts (also sometimes referred to as “forward contracts”) are not futures contracts, as courts have uniformly held . See, e.g., *Zelener*, 373 F.3d at

867; *C.F.T.C. v. Erskine*, 512 F.3d 309, 325 (6th Cir. 2008) (finding “six elements” distinguishing the foreign currency transactions at issue as forward contracts and not futures contracts); *C.F.T.C v. Sterling Trading Group, Inc.*, 605 F. Supp. 2d 1245, 1265 (S.D. Fla. 2009) (finding foreign currency transactions “were spot sales, not futures contracts.”). The CFTC’s unambiguous allegations of a spot contract “pegged” to the value of the underlying metal, therefore, concede the metals transactions were not futures contracts.

The idea that the leveraged metals transactions might be something *other* than what the CFTC claimed (OTC spot contracts) or what Defendants maintained (actual physical metals trades), arose for the first time at oral argument, in questions from the Panel. The Panel asked if the metals transactions were options. The undersigned answered unequivocally they were neither options nor futures, and there had never been a single allegation to the contrary in the entire case. *See* Oral arg. recording at 3:50; 4:48-5:03; 5:20-5:30; 7:45-7:59. When the Panel posed a similar question to the CFTC, asking if there was a difference between “derivatives contracts” and “options,” counsel answered, just as unequivocally, that there *is* a difference, and that Hantec and Berkley were trading over-the-counter derivatives (i.e., spot contracts). *See id.* at 20:38-40; 22:05-25.

The CFTC’s unwavering allegations of over-the-counter spot transactions waived any argument that the metals transactions were futures contracts. *See, e.g.,*

In re Pan Am. World Airways, Inc., Maternity Leave Practices & Flight Attendant Weight Program Litig., 905 F.2d 1457, 1462 (11th Cir. 1990) (stating that “if a party hopes to preserve a claim, argument, theory, or defense for appeal, she must first clearly present it to the district court, that is, in such a way as to afford the district court an opportunity to recognize and rule on it”). The CFTC would in any case be judicially estopped from characterizing the transactions as futures contracts now. *See Slater v. U.S. Steel Corp.*, 871 F.3d 1174, 1176 (11th Cir. 2017) (describing the “equitable doctrine of judicial estoppel is intended to protect courts against parties who seek to manipulate the judicial process by changing their legal positions to suit the exigencies of the moment.”). As it stands, the CFTC has never taken this position, and neither the record evidence nor any argument supports that the leveraged metals transactions were futures contracts.

B. Acknowledging that the leveraged metals transactions were not futures contracts changes everything about the proximate cause analysis.

The CFTC’s repeated assertion that the metals transactions were spot contracts “tracking” or “pegged” to the value of silver was the lynchpin for Defendants’ proximate cause argument. Representations to customers that they were trading leveraged physical silver could not have *proximately caused* any loss even if what they were actually trading was OTC “spot contracts pegged to the value of silver.” Their trades correlated exactly to the market price of silver either way, as even the testifying customers and the CFTC conceded. If customers lost

money, market movements in silver prices were the sole of cause of it. The alleged misrepresentation therefore was not “a ‘substantial’ or ‘significant contributing’ cause of the loss.” Slip op. at p. 31. It was no cause at all. This proximate causation argument should have prevailed.

As this Court and many cases have observed, futures contracts have distinct characteristics. When people trade futures contracts, they “buy and sell contracts,” not the underlying commodities themselves. *E.g., Zelener*, 373 F.3d at 865. Futures contracts trade on regulated exchanges that guarantee obligations; futures contracts are standardized and fungible; they have a fixed quantity, a fixed price, and a fixed settlement (or expiration) date for delivery. *Id.* at 865-66; *see Erskine*, 512 F.3d at 325. These characteristics stand in stark contrast to spot or forward contracts. Spot transactions trade in the actual commodity itself at the market price; they trade over-the-counter and not on exchanges; they are bought and sold in any quantity at any time; there is no expiration date, as buyers can hold (or “roll over”) their positions indefinitely. *See id.*

The dispute in this case was never over the difference between owning physical leveraged metal versus futures contracts. That difference is great, as this Court explained. The dispute here was over the difference between owning leveraged physical metal and, according to the CFTC, owning leveraged positions in “spot contracts pegged to the value of gold or silver.” Appx. 556:1-5. That

difference is virtually nonexistent. Judge Easterbrook made exactly this point in *Zelener*. Customers buying and holding foreign currency positions in a spot contract, he observed, “could have engaged in the same price speculation by taking delivery and holding the foreign currency in bank accounts.” *See Zelener*, 373 F.3d at 863–64 (emphasis added). For customers who only want to speculate in precious metals price changes (as all Southern Trust Metals customers did), there is no difference in terms of economics and risk. Nor is there any *legal* difference, for that matter, as both leveraged metals transactions and spot contracts require registration under Dodd-Frank (with exceptions not discussed here). *See* 7 U.S.C. § 2(c)(2)(D).

As a result, none of the “crucial differences between metals and futures” the Opinion discusses are applicable. The record contains no evidence that leveraged spot contracts put customers at risk of “losses greater than a customer’s investments of funds,” as happens with futures contracts. Nor was there any evidence that the leveraged metals positions here had “expiration” dates prohibiting customers from holding positions long term. Indeed, the CFTC’s first witness bought 1,000 oz. of silver in 2011 and held that same position for over a year-and-a-half. *See* Appx. 2090; testimony of J. Jefferies Appx. 929-939 at 1:23-24; 11:9-10. She could have held the position longer than that, but she gave the order to sell after market silver prices declined. Appx. 941 at 13:19-20. She, like

all testifying customers, admitted this market movement in the price of silver was the reason for her loss. Appx. 952-53 at 24:17-25:5. Whether it was physical silver held in a depository or a spot contract pegged or tied to silver prices made no difference. Customers taking positions in spot contracts can “ride out” unfavorable market movements (though this particular customer chose not to) the same as customers buying physical metals. *See Erskine*, 512 F.3d at 313 (finding “no designated time for closing the trade ... unlike futures contracts where the contract must be liquidated at a fixed date determined at the time of purchase.”) (emphasis added).

The CFTC never claimed (nor could it) that there is a meaningful difference in terms of risk and ability to profit between owning the physical metal and owning a position through spot transactions in the physical metal. No evidence at trial or in this record supported any such difference, and there is no practical difference. The district court’s findings of fact, which the CFTC wrote, even explicitly recognized “[t]he fact that Defendants’ customers’ positions would have declined regardless of whether Defendants purchased physical silver (as they had promised to do) or derivatives contracts (as they actually did).” Doc 166 p. 23. It dismissed this fact as being “of no moment” only because of the erroneous foreseeability standard it adopted. *See id.* That was the CFTC’s entire strategy—to push a foreseeability

standard that would allow recovery of customer loss restitution without demonstrating proximate cause. This Court properly rejected this argument.

This Court's correct analysis on the direct relation proximate cause requirement for restitution under § 13a-1(d)(3) therefore requires reversal or vacatur of the restitution judgment on the leveraged precious metals transactions. Just as the alleged lack of registration proximately caused no customer losses, so too the lack of any meaningful difference between trading leveraged physical metal and trading leveraged spot contracts pegged to the value of the metal caused no proximate loss.

C. The Opinion overlooks the lack of admitted evidence supporting the purported customer loss calculations.

Though Defendants made it one of their core arguments, the Opinion assumes without discussion the accuracy of the CFTC's customer loss calculations. But it was error not to require the CFTC to present any calculations or computations of purported customer loss numbers to support the restitution award. The district court prohibited opinion testimony and charts of the calculations at trial as a sanction for discovery abuses. *See* Doc 146. Raw data came in the form of thousands of pages of account statements, but the calculations did not. The only charts the CFTC presented came *post*-trial, that the CFTC disingenuously slipped into a post-trial brief. However, Judge King had specifically sustained Defendants' objections to the admissibility of those charts. Yet, in response to a question from

the Panel at oral argument, appellate counsel for the CFTC led the Panel to believe that the CFTC's post-trial summaries had been admitted into evidence or requested by the district court. Oral arg. Recording at 25:13-26:23. In fact, they had not, and Defendants had no chance to respond to those charts as Judge King had forbade responses to post-hearing briefs. Doc 159 p. 104:9-107:16. The undersigned demanded that CFTC appellate counsel, consistent with the ethical duty of candor requiring corrections of false statements of material fact made to a court², correct this material fact after oral argument. Outrageously, for a federal agency charged with policing misrepresentations or omissions of material fact, CFTC's appellate counsel refused to correct the material factual misimpression she had knowingly created at oral argument. *See* Ex. A hereto. In any case, the CFTC's purported calculations never were admitted into evidence. Defendants had the right to discovery, cross-examination, and rebuttal of the CFTC's purported calculations. Awarding the full amount without those most basic of due process opportunities, Defendants respectfully submit, was and is manifest reversible error.

IV. Conclusion

The Court erred in assuming that the leveraged metals transactions were futures contracts. When that fact is corrected, the rest of the opinion requires

² *See, e.g.*, Florida Rule of Professional Conduct 4.3.3(a)(1) ("A lawyer shall not knowingly: (1) make a false statement of fact ...to a tribunal or fail to correct a false statement of material fact ...previously made to the tribunal by the lawyer").

reversal or vacatur of the restitution award consistent with the proximate cause analysis the Opinion sets forth. That result moots the issue of the inadequacy and inadmissibility of the CFTC's customer loss calculations. Otherwise, the manifest lack of record evidence of restitution calculations supporting the amount of alleged customer losses merits reversal. Defendants therefore respectfully request that the Panel rehear this matter to correct the threshold error and vacate or reverse the restitution judgment on the leveraged metals transactions accordingly.

Respectfully submitted:

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CERTIFICATE OF COMPLIANCE WITH RULE 32(a)

Counsel for Defendants-Appellants hereby submits its Certificate of Compliance with Type-Volume Limitation, Typeface Requirements, and Type Style Requirements pursuant to Fed. R. App. P. 32(a), and certify:

1. This petition complies with the type-volume limitation of Fed. R. App. P. 40(b) because the petition contains 3,210 words.
2. This petition complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because this petition has been prepared in a proportionally spaced typeface using Microsoft Word in 14-point font, Times New Roman.

CERTIFICATE OF SERVICE

I hereby certify that on March 6, 2018, I served the foregoing Appellants' Petition for Panel Rehearing on Anne W. Stukes (astukes@cftc.gov) and Carlin R. Metzger (cmetzger@cftc.gov), counsel for the CFTC, using this Court's CM/ECF system.

By: /s/ Christopher J. King

ADDENDUM

[PUBLISH]

IN THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

No. 16-16544

D.C. Docket No. 1:14-cv-22739-JLK

U.S. COMMODITY FUTURES TRADING COMMISSION,

Plaintiff - Appellee,

versus

SOUTHERN TRUST METALS, INC.,
LORELEY OVERSEAS CORPORATION,
ROBERT ESCOBIO,

Defendants - Appellants.

Appeal from the United States District Court
for the Southern District of Florida

(January 22, 2018)

Before JORDAN, HULL, and GILMAN,* Circuit Judges.

GILMAN, Circuit Judge:

This is a commodities-fraud case. The U.S. Commodity Futures Trading Commission (CFTC) began investigating Southern Trust Metals, Inc., Loreley Overseas Corporation, and Robert Escobio (collectively, the Defendants) in response to an investor's complaint. That complaint also prompted the National Futures Association (NFA)—a private, self-regulatory organization for the futures industry—to open an investigation, which proceeded in tandem with the CFTC's. The NFA's investigation ended in a settlement. Afterwards, the CFTC filed this lawsuit, alleging that the Defendants violated the Commodities Exchange Act (CEA) when they failed to register as futures commission merchants, transacted the purchase and sale of contracts for the future delivery of a commodity (futures) outside of a registered exchange, and promised to invest customers' money in precious metals (metals) but instead invested the funds in futures. The district court, after a bench trial, entered judgment for the CFTC on all claims.

For the reasons set forth below, we **AFFIRM** the judgment of the district court except as to the restitution award for the group of investors whose losses were associated solely with the registration violations. As to that portion of the

* Honorable Ronald Lee Gilman, United States Circuit Judge for the Sixth Circuit, sitting by designation.

restitution award, we **VACATE** the judgment and **REMAND** with instructions to consider other equitable remedies.

I. BACKGROUND

A. Factual background

Escobio is the Chief Executive Officer (CEO) and largest shareholder of the Southern Trust Securities Holding Corporation (Holding Corporation). The Holding Corporation owns Loreley, a British Virgin Islands corporation, which in turn owns Southern Trust, a Florida corporation. Escobio formed Southern Trust to provide commodities investment services, and he serves as its director and CEO.

Southern Trust represented that it was able to facilitate customers' investment in precious metals. Its website and brochure stated that customers "can take physical possession of [their] metals in New York or London." The company's brokers told customers much the same story—that the customers were purchasing metals stored in places like New York, London, and Hong Kong. At least one of Southern Trust's brokers told customers that Southern Trust charged "storage fees" for the metals. To open a trading account at Southern Trust, customers completed an account-opening form containing language that "[p]hysical precious metals can either be delivered directly to the customer's designated point of delivery or to a recognized depository, which provides insured

non-segregated storage.” Southern Trust also represented that it could loan customers money to purchase metals.

But Southern Trust did not in fact deal in metals; it dealt only in contracts for the future delivery of metals. Such contracts are a type of derivative investment. Southern Trust, however, was not registered with the CFTC as a futures commission merchant and thus could not trade futures on registered exchanges. So Escobio, through Loreley, engaged two foreign brokerages—Berkeley Futures Limited and Hantec Markets Limited—to handle the transactions.

Escobio opened trading accounts at Berkeley and Hantec in Loreley’s name, not in the names of Southern Trust’s customers. The accounts were numbered, and Southern Trust maintained records linking its customers to the specific numbered accounts.

Opening these accounts required Escobio to review documents describing Berkeley’s and Hantec’s investment products. One of Hantec’s account-opening documents, the “Product Disclosure Statement,” explains that “bullion trading” “operates in the same manner as foreign exchange trading” in that “[w]hat you are actually buying is a [c]ontract” that “derives its value from” a “physical underlying asset” such as “Loco London Gold.” That document’s “Glossary” defines “Loco London Gold” to “mean[] not only that the gold is held in London but also that the

price quoted is for delivery there.” Elsewhere, the document explains that in “bullion trading,” “[Hantec] do[es] not deliver the physical underlying assets (i.e. gold or silver) to you, and you have no legal right to it.” The Berkeley documents similarly confirm that the account holder intends “to speculate in derivative products.” None of the account-opening documents mention making loans for the purchase of metals.

After setting up the trading accounts at Berkeley and Hantec, Southern Trust sent its customers’ money to Loreley, which in turn invested the funds, through Berkeley and Hantec, in futures. Escobio received monthly account statements showing that all investments were in futures, not metals. Those statements do not reflect any loans to Southern Trust’s customers.

Southern Trust never informed its customers that their money was being transferred to Loreley, Berkeley, or Hantec. Nor did it inform customers who wished to invest in metals (the group comprising the vast majority of its customers) that their money was instead being invested in futures. Southern Trust still charged those customers interest on fictitious loans, which it falsely told them were made in order to facilitate their investment in metals.

After receiving a complaint from one of Southern Trust’s customers, the NFA opened an investigation. Around the same time, Escobio asked Berkeley and Hantec about the nature of Loreley’s investments. Escobio contended at trial that

he did so simply to confirm his understanding that Loreley was investing in metals. The CFTC maintained, however, and the district court ultimately concluded, that Escobio had done so in anticipation of litigation, and that he had carefully framed his inquiries to elicit responses that would support the defense he later asserted—that he did not know that his customers’ money was being invested in futures.

In response to Escobio’s inquiry, Hantec’s CEO said: “I can confirm that you hold accounts with us that only trade Silver Bullion.” Hantec’s CEO clarified at his deposition, however, that “Silver Bullion” is industry lingo for contracts for the future delivery of silver and that he could not have intended any other meaning because trading in “physical metals is not something that Hantec does.”

A Berkeley employee similarly responded to Escobio’s inquiry, writing that “all Loreley accounts with the prefix XILOR were silver bullion accounts” that “only traded in OTC [off-exchange] silver bullion and never traded any futures contracts.” But Berkeley’s CEO testified at his deposition that Berkeley had never delivered metals to any of its customers, including Loreley, nor stored any metals on their behalf. He also testified that, despite Escobio’s contrary assertion, he never told Escobio that the trades Berkeley handled for Loreley would lead to the storage of metals.

None of Southern Trust’s investments led to the delivery of metals. Hantec’s CEO testified that he told Escobio that Hantec could arrange for the

delivery of metals, but that he did so only in response to a hypothetical question. According to Hantec's CEO, Escobio inquired in the abstract about Hantec's ability to arrange delivery: "It's an inquiry from a client. Robert [Escobio] did not tell me, 'I would like to deliver metal.' He asked me, 'If I wanted to deliver a metal, can you arrange it?' and I said, 'Let me go find out.'" Hantec's CEO continued: "I talked to . . . one of my contacts at Standard Chartered bank who gave me information and I went back to Robert and explained" that Hantec could arrange delivery. This response was memorialized in a letter to Escobio, stating that "any Gold or Silver you purchase from us is held for your account and upon full payment we are able to arrange delivery for you when requested." But the Defendants never asked Hantec to arrange delivery, and no delivery ever occurred.

The NFA's investigation ended in a settlement. Although the NFA's and the CFTC's investigators had cooperated with each other, their investigations were independent. The Defendants' settlement agreement with the NFA therefore does not mention the CFTC or the CFTC's investigation.

As the CFTC's investigation moved forward, the Defendants continued to produce documents in response to its requests. The Defendants' lawyers knew at the time of the NFA settlement that the CFTC might bring its own enforcement action, but they did not suggest to the CFTC or to anyone else that such an action would violate their settlement agreement with the NFA.

B. Procedural background

In July 2014, the CFTC filed its complaint, seeking equitable relief and penalties under the CEA. The complaint alleges that the Defendants engaged in two illegal schemes, which we will refer to as the “unregistered-futures scheme” and the “leveraged-metals scheme.”

As to the unregistered-futures scheme, the complaint alleges that, even though the Defendants were not registered as futures commission merchants, they accepted money from customers who wished to invest in futures. Because the Defendants were unregistered, moreover, they could not trade futures on a registered exchange. They therefore sought to trade indirectly, through intermediaries. To that end, the Defendants funneled the customers’ money through Loreley to foreign brokerage firms—Berkeley and Hantec—licensed to trade futures. Those brokerage firms made the actual investments.

As to the leveraged-metals scheme, the complaint alleges that the Defendants accepted money from customers who wished to invest in metals with borrowed money. But instead of issuing loans to those customers and investing their money in metals, the Defendants took the customers’ money and invested it in futures. No loans existed, but the Defendants charged loan interest anyway.

At the summary-judgment stage of the case, the parties filed dueling motions. The district court granted the CFTC’s motion in part, holding that the

Defendants had conducted off-exchange transactions and had failed to register as futures commission merchants. It denied the Defendants' motion in full, rejecting their affirmative defenses that (1) their settlement with the FTA equitably estopped the CFTC from bringing suit, and (2) they actually delivered metals so as to bring their transactions within an exception to the CEA's registration requirements.

The CFTC's fraud claim then proceeded to trial. After a bench trial, the district court found that the Defendants had engaged in fraud, ordered them to pay restitution in the full amount of the customers' losses, and imposed fines. The court also permanently enjoined the Defendants from employment in the commodities-trading industry. On appeal, the Defendants challenge the court's rulings both on summary judgment and at trial.

II. ANALYSIS

A. Standard of review

On an appeal from a judgment in a bench trial, we review the district court's conclusions of law de novo. *HGI Assocs., Inc. v. Wetmore Printing Co.*, 427 F.3d 867, 873 (11th Cir. 2005). We also review de novo the district court's application of law to facts. *United States v. Frank*, 599 F.3d 1221, 1228 (11th Cir. 2010). The district court's findings of fact, on the other hand, are evaluated under the clear-error standard. *HGI*, 427 F.3d at 873. "We will not find clear error unless our review of the record leaves us 'with the definite and firm conviction that a

mistake has been committed.” *Coggin v. Comm’r of Internal Revenue*, 71 F.3d 855, 860 (11th Cir. 1996) (quoting *United States v. Gypsum Co.*, 333 U.S. 364, 395 (1948)). Finally, when the district court has issued a permanent injunction, we review the scope of the injunction under the abuse-of-discretion standard. *Commodity Futures Trading Comm’n v. Wilshire Inv. Mgmt. Corp.*, 531 F.3d 1339, 1343 (11th Cir. 2008).

B. Equitable estoppel does not bar the CFTC’s claims.

To start with, the Defendants challenge the district court’s summary-judgment ruling that their settlement with the NFA does not preclude the CFTC’s claims. The district court held that equitable estoppel does not apply because (1) the Defendants do not dispute that the NFA is a private, nongovernmental organization through which the commodities-trading industry regulates itself; (2) the CFTC was not a party to the settlement; and (3) settlements with private, nongovernmental organizations do not preclude subsequent claims by government regulators.

Although this circuit has not yet addressed whether a settlement between a nongovernmental regulator and a regulated company may preclude subsequent claims by a governmental regulator, the circuits that have addressed the issue have uniformly answered in the negative. *See, e.g., Graham v. S.E.C.*, 222 F.3d 994, 1007 n.25 (D.C. Cir. 2000) (“Of course, even if the NASD had done something to

bind itself, that would not have bound the SEC.”); *Jones v. S.E.C.*, 115 F.3d 1173, 1179–81 (4th Cir. 1997) (“We have found no statutory, regulatory, or historical reference to support [the] argument that NASD discipline of its members was intended to preclude this disciplinary action by the SEC itself against a securities professional.”).

In *Jones*, the Securities and Exchange Commission (SEC) brought administrative claims against a securities trader after the trader settled a claim by the National Association of Securities Dealers (NASD). 115 F.3d at 1180. The Fourth Circuit rejected the trader’s argument that the settlement precluded the SEC’s claims, reasoning that private and public regulators “represent distinct interests” and “bring two separate vantage points to enforcement efforts—one from the industry itself and the other from the regulator.” *Id.*

This outcome accords with the courts’ general reluctance to apply principles of equitable estoppel to the government. “The Supreme Court has never established that the doctrine of equitable estoppel can be applied against the government and, in fact, has implied that it can not be.” *Tovar-Alvarez v. U.S. Atty. Gen.*, 427 F.3d 1350, 1353–54 (11th Cir. 2005) (citing *Office of Pers. Mgmt. v. Richmond*, 496 U.S. 414, 422 (1990)). “[I]t is well settled that the [g]overnment may not be estopped on the same terms as any other litigant.” *Heckler v. Cmty. Health Servs. of Crawford Cty.*, 467 U.S. 51, 60 (1984).

This circuit has repeatedly opined that, even assuming that equitable estoppel could apply against the government, “it would require a showing of affirmative misconduct on the government’s part.” *Tovar-Alvarez*, 427 F.3d at 1354; *see also Sanz v. U.S. Sec. Ins. Co.*, 328 F.3d 1314, 1319–20 (11th Cir. 2003) (“[E]ven if estoppel is available against the Government, it is warranted only if affirmative and egregious misconduct by government agents exists.”).

The present case is analogous to *Jones*. Here, the uncontradicted evidence shows that the NFA, like the NASD, is a private, nongovernmental organization and that the CFTC was not a party to the Defendants’ settlement with the NFA. The record, moreover, contains no evidence of affirmative misconduct by the government. So even if equitable estoppel theoretically could apply to the government, it does not apply here.

A second, independent ground also exists for affirming the district court’s denial of summary judgment based on the Defendants’ estoppel defense: the record reflects a genuine dispute of material fact regarding the element of reasonable reliance. *See Heckler*, 467 U.S. at 59 (noting that “the party claiming the estoppel must have relied on its adversary’s conduct” and that the “reliance must have been reasonable”). Especially noteworthy is the fact that the settlement agreement makes no mention of the CFTC or its investigation, so the Defendants’ purported reliance lacks a textual basis. The only language in the agreement that

even arguably suggests reliance is a clause providing that the agreement “shall resolve and terminate all complaints, investigations and audits relating to [the Defendants].”

But interpreting this language to embrace the CFTC’s investigation is unreasonable. For one thing, the notion that the NFA would agree to terminate investigations outside its control—and that the Defendants would accept such an unfulfillable obligation as consideration for their own concessions—defies common sense. Further, a literal interpretation of “all complaints, investigations and audits relating to [the Defendants]” would impose on the Defendants obligations that they surely did not intend, such as the obligation to terminate their own routine, internal accounting audits. Such audits would, after all, be “audits relating to [the Defendants].”

The lack of textual support for the Defendants’ estoppel argument creates a genuine dispute concerning the *reasonableness* of their reliance. At the same time, other evidence creates a genuine dispute about whether there was any reliance at all. First, the Defendants continued to produce documents in response to requests from the CFTC’s investigators after the settlement. This fact tends to negate any reliance because the Defendants presumably would not have continued cooperating with the CFTC if they had truly believed that their settlement with the NFA had terminated the CFTC’s investigation. Second, the Defendants’ lawyers, while

preparing to defend against that action, never suggested to the CFTC or anyone else that such an action might violate the settlement agreement with the NFA. For these reasons, we find no error in the district court's denial of the Defendants' motion for summary judgment based on the affirmative defense of equitable estoppel.

C. Summary judgment in favor of the CFTC on its claims for registration violations was appropriate.

We now turn to the merits of this case. The CEA imposes registration requirements on commodities traders and the exchanges where they trade. Section 6d of the CEA makes it “unlawful for any person to be a futures commission merchant unless . . . such person shall have registered [as such] . . . with the [CFTC].” 7 U.S.C. § 6d(a)(1). The statute also requires that all transactions be “conducted on or subject to the rules of a board of trade which has been designated or registered by the [CFTC].” *Id.* § 6(a). Together, these provisions require that only registered traders handle transactions and that they do so on a registered exchange.

An exception exists, however, for transactions that result in “actual delivery within 28 days.” *Id.* § 2(c)(2)(D)(ii)(III)(aa). Actual delivery means “giving real and immediate possession” of the commodity “to the buyer or the buyer’s agent.” *U.S. Commodity Futures Trading Comm’n v. Hunter Wise Commodities, LLC*, 749 F.3d 967, 979 (11th Cir. 2014) (internal quotation marks omitted). “‘Actual’ is

that which ‘exist[s] in fact’ and is ‘real,’ rather than constructive.” *Id.* (quoting *Black’s Law Dictionary* 494 (9th ed. 2009)).

This exception is an affirmative defense on which the commodities trader bears the burden of proof. *See Schlemmer v. Buffalo, R & P R Co*, 205 U.S. 1, 10 (1907) (explaining that the “general rule of law is[] that a proviso carves special exceptions only out of the body of the act; and those who set up any such exception must establish it”); *see also Corning Glass Works v. Brennan*, 417 U.S. 188, 196–97 (1974) (“[T]he application of an exemption under the Fair Labor Standards Act is a matter of affirmative defense on which the employer has the burden of proof.”); *Mulhall v. Advance Sec., Inc.*, 19 F.3d 586, 590 (11th Cir. 1994) (“[T]he exceptions granted within the EPA constitute affirmative defenses.”).

The Defendants concede that they were not registered as futures commission merchants and that the trades at issue did not occur on a registered exchange. But they seek refuge in the exception for transactions resulting in actual delivery.

As set forth in the factual background of this opinion, however, there is no basis in the record for the Defendants’ contention that actual delivery ever occurred. The record instead supports the holding of the district court that the Defendants failed to establish their affirmative defense of “actual delivery.” *See Hunter Wise Commodities*, 749 F.3d at 979. We therefore find no error in the

court's grant of summary judgment in favor of the CFTC on its claims that the Defendants engaged in off-exchange transactions and failed to register as futures commission merchants.

D. The district court did not err in concluding that the Defendants committed fraud under 7 U.S.C. §§ 6b(a) and 9, and under 17 C.F.R. § 180.1.

We next turn to the issue of fraud. For our purposes, 7 U.S.C. § 6b(a), 7 U.S.C. § 9, and 17 C.F.R. § 180.1 are redundant. Section 6b(a) makes it “unlawful . . . for any person . . . in connection with . . . any contract of sale of any commodity . . . for future delivery . . . to cheat or defraud or attempt to cheat or defraud the other person . . . [or] willfully to make . . . any false report or statement . . . [or] willfully to deceive or attempt to deceive the other person by any means whatsoever.” 7 U.S.C. §§ 6b(a). Section 9 of the same chapter is similar, providing that “[i]t shall be unlawful for any person . . . to use . . . in connection with any . . . contract of sale of any commodity . . . for future delivery . . . any manipulative or deceptive device or contrivance.” *Id.* § 9(1). Finally, 17 C.F.R. § 180.1(a) declares it “unlawful for any person . . . in connection with any . . . contract of sale of any commodity . . . or contract for future delivery . . . to intentionally or recklessly . . . use . . . any manipulative device, scheme, or artifice to defraud; . . . [or] [m]ake . . . any untrue or misleading statement of a material fact or to omit to state a material fact necessary . . . to make the statements made

not untrue or misleading; . . . [or] [e]ngage . . . in any act . . . which operates . . . as a fraud or deceit upon any person.”

The CFTC must prove the same three elements to establish liability under each of the above provisions: “(1) the making of a misrepresentation, misleading statement, or a deceptive omission; (2) scienter; and (3) materiality.” *Commodity Futures Trading Comm’n v. R.J. Fitzgerald & Co., Inc.*, 310 F.3d 1321, 1328 (11th Cir. 2002). “Unlike a cause of action for fraud under the common law of [t]orts, ‘reliance’ on the representations is not a requisite element” *Id.* at n.6.

1. Misrepresentation, misleading statement, or deceptive omission

The district court’s factual findings on the “misrepresentation” element reflect no clear error. With the many references to “physical metals,” “physical possession,” and “storage,” Southern Trust’s brochure, website, brokers, and account-opening documents collectively represented that the company offered investments in metals. Abundant evidence shows, however, that after accepting the customers’ money, Southern Trust sent the funds to Loreley, which in turn sent them to Berkeley and Hantec for investment in futures. The Defendants do not dispute that the accounts at Berkeley and Hantec were in Loreley’s name, not in the names of Southern Trust’s customers. Moreover, the evidence shows that Southern Trust never informed its customers that their money was being

transferred to Loreley, Berkeley, or Hantec and, consequently, that the customers did not know that those firms held their money.

The district court correctly applied the law to these facts. “Whether a misrepresentation has been made depends on the ‘overall message’ and the ‘common understanding of the information conveyed.’” *R.J. Fitzgerald*, 310 F.3d at 1328 (quoting *Hammond v. Smith Barney Harris Upham & Co.*, Comm. Fut. L. Rep. (CCH) 36,657 & n.12 (CFTC Mar. 1, 1990)). We find the case of *U.S. Commodity Futures Trading Commission v. Hunter Wise Commodities, LLC*, 21 F. Supp. 3d 1317 (S.D. Fla. 2014), squarely on point. The district court in *Hunter Wise* concluded, after a bench trial, that the defendant “misrepresented facts about the precious metals transactions it oversaw” and provided a deceptive “‘overall message’” when it “led the retail customers to believe metals were stored on their behalf.” *Id.* at 1338 (quoting *R.J. Fitzgerald*, 310 F.3d at 1328). Moreover, the court found that the defendant “failed to inform [the retail customers] that the metals it purchased were on a financed basis, it did not own the metals, and the metals, if there were any at all, were not in the retail customers’ names.” *Id.*; see also *U.S. Commodity Futures Trading Comm’n v. Hunter Wise Commodities, LLC*, 749 F.3d 967, 980–82 (11th Cir. 2014) (affirming the district court’s issuance of a preliminary injunction because the CFTC presented a prima facie case of fraud under 7 U.S.C. § 6b).

Southern Trust orchestrated a nearly identical scheme in the present case. It misrepresented to customers the fundamental nature of their investments, telling them that they were investing in metals when in fact they were investing in futures, and charging a fictitious storage fee despite the customers having no metals to store. Finally, Southern Trust failed to tell the customers that it passed their money through Loreley to Berkeley and Hantec, with the customers having no knowledge of or relationship with these entities. The district court therefore did not err in concluding that the CFTC satisfied its burden, under the preponderance-of-the-evidence standard, to prove the first element necessary to establish fraud.

2. Scienter

Regarding the element of scienter, Escobio does not dispute that he was the CEO of both Southern Trust and the Holding Corporation, and that he had substantial prior experience in commodities trading. He also does not dispute that he signed the account-opening documents for Loreley's trading accounts at both Berkeley and Hantec. Those documents, as well as the monthly account statements that Escobio received, make clear that Loreley was investing the customers' money in futures, not metals. Further, Escobio knew that the accounts at Hantec and Berkeley bore Loreley's name, not the names of Southern Trust's customers. Based on these facts, the district court did not clearly err in finding that Escobio knew that he was investing his customers' money in futures.

Nor did the district court clearly err in finding that Escobio knew that Berkeley and Hantec did not make any loans to Southern Trust's customers, even though Southern Trust charged its customers interest on the purported loans. Neither the account-opening documents nor the monthly statements from Berkeley or Hantec reflect any loans from those companies. Moreover, the Defendants point to no evidence—other than Escobio's uncorroborated testimony—of any loans from Berkeley or Hantec, and the district court discounted Escobio's testimony on that point, as on others, because it determined that he lacked credibility. This circuit applies a "strong rule of deference" in reviewing a district court's determination of a witness's credibility at a bench trial. *Childrey v. Bennett*, 997 F.2d 830, 834 n.5 (11th Cir. 1993). Given this standard, as well as the numerous conflicts between Escobio's testimony and the documentary evidence, the court was entitled to find that Escobio lacked credibility and to discount his testimony accordingly.

The district court also correctly applied the law to these facts. "[S]cienter is established if Defendant intended to defraud, manipulate, or deceive, or if Defendant's conduct represents an extreme departure from the standards of ordinary care." *Commodity Futures Trading Comm'n v. R.J. Fitzgerald & Co., Inc.*, 310 F.3d 1321, 1328 (11th Cir. 2002). Adapting "federal securities law" to the commodities-fraud context, this circuit has stated that scienter is shown "when

Defendant's conduct involves 'highly unreasonable omissions or misrepresentations . . . that present a danger of misleading [customers] which is either known to the Defendant or so obvious that Defendant must have been aware of it.'" *Id.* (quoting *Ziemba v. Cascade Int'l, Inc.*, 256 F.3d 1194, 1202 (11th Cir. 2001)).

The evidence shows that the Defendants either intended to mislead Southern Trust's customers or made highly unreasonable misrepresentations that posed an obvious danger of misleading them. Escobio's deep involvement in managing the futures-trading accounts at Berkeley and Hantec, as well as his extensive industry experience, support the inference that he knew that he was investing his customers' money in futures. Hantec's CEO, at his deposition, put it this way: "Under no circumstance is [it] plausible" that Escobio believed that he was trading in metals. Escobio also surely knew that Berkeley and Hantec had made no loans to Southern Trust's customers and, therefore, that the customers were being charged interest on loans that did not exist. The district court thus did not err in concluding that the CFTC had proved scienter.

3. Materiality

This brings us to the third and final element—materiality. "A representation or omission is 'material' if a reasonable investor would consider it important in deciding whether to make an investment." *Fitzgerald*, 310 F.3d at 1328–29. The

Defendants' briefing on this element addresses only the materiality of their omission that the customers' money would pass through Loreley to Berkeley and Hantec. If that were the only omission or misrepresentation in this case, we might need to examine the materiality element more closely. But other misrepresentations found by the district court easily qualify as material. The Defendants, for example, represented that they were investing customers' money in metals when in fact they were investing it in futures. Moreover, the Defendants represented that customers owed interest on loans used to purchase metals, but the loans did not exist. A reasonable investor would consider each of these misrepresentations important in deciding whether to invest. Accordingly, the district court did not err in concluding that these misrepresentations were material. We therefore agree with the district court's overall conclusion that fraud was established under 7 U.S.C. §§ 6b(a) and 9, and under 17 C.F.R. § 180.1.

E. The district court did not err in permanently enjoining the Defendants from employment in the commodities-trading industry.

Turning now to the propriety of the injunction issued against the Defendants, we note that a district court's issuance of an injunction is reviewed under the abuse-of-discretion standard. *Commodity Futures Trading Comm'n v. Wilshire Inv. Mgmt. Corp.*, 531 F.3d 1339, 1347 (11th Cir. 2008) (applying this standard to a permanent injunction issued under the CEA). "[S]o long as [the district court's] decision does not amount to a clear error of judgment[,] we will not reverse even if

we would have gone the other way had the choice been ours to make.” *S.E.C. v. ETS Payphones, Inc.*, 408 F.3d 727, 733 (11th Cir. 2005).

“[U]pon a proper showing,” the CEA allows a district court to grant “a permanent or temporary injunction.” 7 U.S.C. § 13a-1(b). “[T]he ultimate test [for an injunction] is whether the defendant’s past conduct indicates that there is a reasonable likelihood of further violations in the future.” *Wilshire*, 531 F.3d at 1346 (quoting *SEC v. Caterinichia*, 613 F.2d 102, 105 (5th Cir. 1980)). This test entails weighing the following six factors:

the egregiousness of the defendant’s actions, the isolated or recurrent nature of the infraction, the degree of scienter involved, the sincerity of the defendant’s assurances against future violations, the defendant’s recognition of the wrongful nature of his conduct, and the likelihood that the defendant’s occupation will present opportunities for future violations.

SEC v. Carriba Air, Inc., 681 F.2d 1318, 1322 (11th Cir. 1982). A court need not make a finding on every factor. See *Wilshire*, 531 F.3d at 1346–47 (holding that a district court that considered only three of the six factors did not abuse its discretion in issuing an injunction).

Escobio argues that the injunction should be vacated because the district court, in weighing the *Carriba Air* factors, erred in not concluding that his cooperation with the NFA’s investigation resolved the last three factors in his favor. But the court had discretion in how to interpret Escobio’s cooperation with the NFA. This discretion would have allowed the court, for example, to interpret

Escobio's cooperation not as contrition, but as a self-interested effort to strike a favorable deal with the NFA and, perhaps, to avoid criminal prosecution. Escobio's denial of wrongdoing at his deposition, at trial, and throughout the NFA's and the CFTC's investigations further belies his acceptance of responsibility. The same is true of his attempt to deflect blame onto Berkeley and Hantec, which he claims duped him into trading futures. In sum, the court applied the correct legal standard, and its factual findings contain no clear error. We therefore find no fault in its issuance of a permanent injunction.

F. Restitution is proper only for losses sustained in the leveraged-metals scheme, not for losses sustained in the unregistered-futures scheme.

This brings us to the final issue in this case—restitution. The district court awarded restitution for losses arising from both schemes. First, it awarded \$1,543,892 for losses sustained in the leveraged-metals scheme, in which the Defendants accepted customers' money for investment in metals but instead invested the funds in futures. Second, the court awarded \$559,725 for losses sustained in the unregistered-futures scheme, in which the Defendants accepted customers' money for investment in futures—and actually invested the funds in futures through Loreley's accounts at Berkeley and Hantec—but failed to register as futures commission merchants or to conduct the transactions on a registered exchange. The Defendants challenge both awards, arguing that the CFTC failed to

prove, as required by the CEA, that the Defendants' violations of the CEA proximately caused their customers' losses.

1. The district court relied on a definition of proximate cause subsequently rejected by the Supreme Court.

Under the CEA, a “court may impose . . . on any person found in the action to have committed any violation[] equitable remedies including . . . restitution to persons who have sustained losses proximately caused by such violation (in the amount of such losses).” 7 U.S.C. § 13a-1(d)(3). This statutory language, by its terms, permits restitution only for losses proximately caused by a violation.

In its restitution analysis, the district court concluded that the “Defendants’ violations proximately caused their customers’ losses” because those losses “were a reasonably foreseeable result of the Defendants’ violations.” The court derived this foreseeability-based formulation of proximate cause from a recent decision of this court holding that, for proximate cause to exist under the Fair Housing Act (FHA), “[t]he defendant must have been reasonably able to foresee the kind of harm that was actually suffered.” *See City of Miami v. Bank of Am. Corp.*, 800 F.3d 1262, 1282 (11th Cir. 2015).

That decision, however, was subsequently reversed by the Supreme Court in *Bank of America Corp. v. City of Miami*, 137 S. Ct. 1296 (2017). The Court concluded that, “[i]n the context of the FHA, foreseeability alone does not ensure the close connection that proximate cause requires” between the complained-of

conduct and the alleged harm. *Id.* at 1306. As the Court explained, the FHA incorporates the concept of proximate cause developed at common law, where “directness principles” apply. *Id.* Proximate cause under the FHA thus “requires ‘some direct relation between the injury asserted and the injurious conduct alleged.’” *Id.* (quoting *Holmes v. Sec. Inv’r Protection Corp.*, 503 U.S. 258, 268 (1992)). Such a “direct relation” usually does not exist “beyond the first step” in a causal chain. *Id.* (quoting *Hemi Group, LLC v. City of New York, N.Y.*, 559 U.S. 1, 10 (2010)).

We have found no circuit court opinion examining proximate cause under the CEA, but the statute surely demands more than foreseeability alone. Section 13a-1(d)(3) of the CEA, like the FHA provision examined in *Bank of America*, “sounds basically in tort” because it defines a new legal duty and authorizes the courts to award compensation for injuries caused by a defendant’s wrongful breach. *See Curtis v. Loether*, 415 U.S. 189, 195 (1974) (explaining why a damages action under the Civil Rights Act of 1964 “is analogous to a number of tort actions recognized at common law”).

Congress, moreover, has given no indication, either in the CEA’s text or otherwise, that it intended to depart from the common-law conception of proximate cause. *See Bank of America*, 137 S. Ct. at 1305 (“We assume Congress ‘is familiar with the common-law rule and does not mean to displace it *sub silentio*’ in federal

causes of action.” (quoting *Lexmark Int’l, Inc. v. Static Control Components, Inc.*, 134 S. Ct. 1377, 1390 (2014))). We thus conclude that the common-law rules governing proximate cause apply here. Those rules include the notion that proximate cause encompasses cause in fact, requiring proof of “but-for” causation. W. Page Keeton et al., *Prosser and Keeton on the Law of Torts* § 30 (5th ed. 1984).

2. The district court erred in finding that the registration violation alone proximately caused any loss.

With regard to the unregistered-futures scheme, the district court’s finding of proximate cause rested on the premise that the Defendants’ “business was illegal from the outset” and that the Defendants “never should have accepted customer funds for the purpose of trading futures transactions without first registering as a futures commission merchant with the CFTC.” The court reasoned that because the transactions were illegal, the losses were foreseeable. But such reasoning mistakes correlation for causation. As a general matter, losing money is a foreseeable result of investing with an unregistered trader, but this is not because a trader’s failure to register will itself cause any loss. More likely, any loss will result from some other factor, such as the trader’s incompetence or dishonesty, which the failure to register correlates with but does not cause. The intrinsic qualities of the trader—not his or her failure to register—would be the likely cause of the loss, to say nothing of market fluctuations.

Consider the analogous circumstance of a client being represented by an unlicensed lawyer. The lawyer's lack of licensure might indicate incompetence or a lack of integrity, but normally it will not in and of itself cause a client's loss in court. Indeed, a client might well prevail in court despite the lawyer's status. Or, if there is a loss, the loss could flow from factors wholly unrelated to the lawyer's status, such as an unfavorable precedent, a judicial error, or a jury's caprice.

A recent decision from this court illustrates the point that a fraudster's failure to observe registration requirements does not necessarily cause his victim's loss. In *Alvarez v. United States*, 862 F.3d 1297, 1300 (11th Cir. 2017), a group of federal employees sued the defendant for negligence per se after he sold them fraudulent, unregistered securities. The court rejected the plaintiffs' argument that the seller's failure to register the securities had caused the losses, concluding instead that the losses had occurred because the securities were fraudulent. This point was made by the *Alvarez* court in the following passage:

As the district court correctly explained, "had the FEBG Bond Fund been legitimate, the fact of its being unregistered would have had no effect on plaintiffs. And conversely, if McLeod had registered the fraudulent securities (lying about them to do so since they didn't exist), plaintiffs would still have suffered the same harm. Plaintiffs' injuries flow from the securities and McLeod's representations which underlay them being fraudulent, not because they were unregistered."

Id. at 1302 (quoting the district court's opinion).

The same logic applies here. In the unregistered-futures scheme, the Defendants invested their customers' money in futures through Loreley's accounts at Berkeley and Hantec. The customers who lost money in this scheme intended to invest in futures, and the CFTC does not dispute that the Defendants in fact facilitated the investments that those customers wished to make. According to the district court, the Defendants' only CEA violations in the unregistered-futures scheme were their failure to register as futures commission traders and their failure to disclose the roles of Berkeley, Hantec, and Loreley in making the investments.

But the record contains no evidence that the customers who lost money in the unregistered-futures scheme did so because of these violations. As in *Alvarez*, there has been no showing that the registration violations caused the losses. Nor has the CFTC pointed to any evidence that the losses flowed from the Defendants' omissions regarding the roles of Loreley, Berkeley, or Hantec. The CFTC has not shown, for instance, that the customers who intended to invest in futures would have refrained from doing so if they had known of Loreley's, Berkeley's, or Hantec's involvement. Nor has the CFTC shown that those entities' involvement delayed the execution of the trades or otherwise caused the investors to receive anything less than what they had bargained for.

Because the CFTC did not prove that the Defendants' violations in the unregistered-futures scheme caused any loss, we vacate the restitution award

related to that scheme and remand the issue to the district court with instructions to consider whether any other equitable remedy is appropriate. We particularly note the statutory subsection under which the court may order the disgorgement of gains, in appropriate circumstances, without regard to proximate cause. *See* 7 U.S.C. § 13a-1(d)(3) (“[T]he court may impose . . . on any person found . . . to have committed any violation[] equitable remedies including . . . disgorgement of gains received *in connection with* such violation.” (emphasis added)). The district court may, but need not, consider on remand whether disgorgement is appropriate in the present case.

3. Sufficient evidence supports the award of restitution for losses sustained in the leveraged-metals scheme.

The district court did not err, however, in awarding restitution for losses in the leveraged-metals scheme, in which the Defendants promised to invest the customers’ money in metals but instead invested the funds in futures. To constitute a proximate cause, the fraud must stand in “direct relation” to the loss. *Bank of Am. Corp. v. City of Miami*, 137 S. Ct. 1296, 1306 (2017). This does not mean that the fraud must be the “sole and exclusive cause” of the loss; it means only that the fraud must be a “substantial” or “significant contributing cause.” *FindWhat Investor Group v. FindWhat.com*, 658 F.3d 1282, 1309 (11th Cir. 2011) (citing *Robbins v. Koger Properties, Inc.*, 116 F.3d 1441, 1447 (11th Cir. 1997)). The courts’ “general tendency” when considering whether a but-for cause

qualifies as a proximate cause is “not to go beyond the first step” in the causal chain. *Bank of Am. Corp.*, 137 S. Ct. at 1306 (quoting *Hemi Group, LLC v. City of New York, N.Y.*, 559 U.S. 1, 10 (2010)).

In the present case, the fraud is directly related to the losses because the Defendants took their customers’ money and, contrary to the customers’ instructions, invested the funds in futures. But the customers wished to invest in metals, not futures, so there is no question that the Defendants’ unilateral act of investing the funds in futures was a “substantial” or “significant contributing” cause of the loss. Whether additional causes exist is irrelevant. Moreover, the Defendants’ act of investing the customers’ funds in futures is inextricable from the fraud because that act rendered false the Defendants’ representations about the nature of the investments being made and directly led to the investors’ losses when market conditions deteriorated.

The Defendants argue, however, that market conditions should be viewed as the sole proximate cause of the losses on the theory that the drop in metals prices would have caused the same losses even if their customers’ money had been invested in metals. But this argument ignores crucial differences between metals and futures. For one thing, futures involve an element of leverage, which magnifies gains and losses:

When you speculate in the futures markets, you have the ability to purchase contracts on margin. This means you can control a large

amount of metal at a fraction of its value. Leverage can amplify returns and risk. Small price swings in either direction could mean significant gains, or you could lose significantly more than you initially invested.

U.S. Commodity Futures Trading Comm'n, *The Risks of Buying Gold, Silver & Platinum*, <http://www.cftc.gov/idc/groups/public/@cpfraudawarenessandprotection/documents/file/cppreciousmetalsfraudbrochure.pdf>; *see also* Thomas A. Russo & Marlisa Vinciguerra, *Financial Innovation and Uncertain Regulation: Selected Issues Regarding New Product Development*, 69 Tex. L. Rev. 1431, 1488 (1991) (explaining that “futures trading is inherently risky and involves the possibility of losses greater than a customer’s investments of funds”). Accordingly, the argument that the Defendants’ customers would have experienced losses of the same magnitude if their money had been invested in metals is flawed.

Another crucial difference between metals and futures is that metals can be held indefinitely, whereas futures almost always have expiration dates. *See Commodity Futures Trading Comm’n v. Zelener*, 373 F.3d 861, 867 (7th Cir. 2004) (noting that “normal futures contracts have defined expiration or delivery dates”); *see also* Patricia A. O’Hara, *The Elusive Concept of Control in Churning Claims Under Federal Securities and Commodities Law*, 75 Geo. L.J. 1875, 1894 n.55 (1987) (“[C]ommodity futures are by definition a short-term investment with a specified delivery date, generally not too removed in time. The trader must either close his position prior to the delivery date or perform the contract.”).

When metals prices fall, a metals investor can avoid losses by not selling the metals until prices (hopefully) recover. But a futures investor makes or loses money immediately when prices change. See Roberta Romano, *A Thumbnail Sketch of Derivative Securities and Their Regulation*, 55 Md. L. Rev. 1, 18 (1996) (explaining that “holders of futures contracts recognize gains and losses immediately because of the daily settlement process”); see also *id.* (“Margin accounts are adjusted daily in response to changes in the value of positions, a process that is called ‘marking to market.’ If a customer’s position experiences a gain, his account balance is increased and he may withdraw the profit from the account. If he experiences a loss, his account balance is reduced.”). This means that a futures investor cannot “ride out” unfavorable market movements in the same way as a metals investor.

Given the inherent differences between metals and futures, the Defendants’ argument that conditions in the metals market were the sole proximate cause of their customers’ losses is untenable. If the Defendants had placed their customers’ money in a slot machine instead of in the metals market, surely they could not escape liability by pointing to the unpredictable odds in a casino as the sole proximate cause for the losses. Crediting the Defendants’ argument would create perverse incentives for commodities traders. See *United States v. Turk*, 626 F.3d 743, 750 (2d Cir. 2010) (rejecting a similar argument because it would “encourage

would-be fraudsters to roll the dice on the chips of others, assuming all of the upside benefit and little of the downside risk”). We therefore find no error in the district court’s restitution award for losses sustained in the leveraged-metals scheme.

III. CONCLUSION

For all of the reasons set forth above, we **AFFIRM** the judgment of the district court except as to the restitution award for the group of investors whose losses were associated solely with the registration violations. As to that portion of the restitution award, we **VACATE** the judgment and **REMAND** with instructions to consider other equitable remedies.

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October 6, 2017

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Re: CFTC v. *Robert Escobio, et al*; 11th Circuit Case No.16-16544

Ms. Stukes:

I write to bring to your attention that you made at least three (3) material misrepresentations to the appellate court during the September 28th oral argument. Under Rule 4-3.3 of the Rules of Professional Conduct, a lawyer shall not make a false statement of fact or law to a tribunal or fail to correct a false statement of material fact or law previously made to the tribunal. Consistent with this ethical obligation, please send a letter to the appellate court by close of business Friday (October 6, 2017) correcting your material misstatements.

First, you stated that customers of Southern Trust Metals received “nothing”— neither derivatives nor options. You specifically told the appellate court that Southern Trust Metals’ customers “got thin air”; “they got their money stolen”; “there were no precious metals”; “there was no derivatives trading”; “they got snookered”; “customers were told they were buying metals and they were not buying anything”; and “they were buying the privilege of being ripped off.” These statements go far beyond the bounds of zealous advocacy. They are outright falsehoods. As counsel for the CFTC well knows (and the trial record establishes), Southern Trust Metals’ parent company, Loreley, maintained accounts at both Berkeley and Hantec (UK regulated financial services firms) and customer funds were deposited into numbered sub-accounts at those UK regulated firms for the precious metals transactions at issue. In fact, the

EXHIBIT A

CFTC produced (and moved into evidence at trial) all statements from Berkeley and Hantec regarding those transactions. Moreover, the CFTC has consistently maintained throughout this entire proceeding, in its complaint, at trial, in its proposed findings fact and conclusions of law, and even in its appellate briefs that Southern Trust Metals was not engaged in actual precious metals transactions but was instead engaged in trading precious metals derivatives. For you to knowingly tell the appellate court that customers “got thin air,” “there was no derivatives trading,” and that customers “were not buying anything” is an outrageous falsehood.

Second, in response to a question from the bench, you told the appellate court that the CFTC’s post-hearing brief exhibits, Doc 164-1, 2, 3, were summaries of account statements from which the trial court’s restitution figures could be derived. You even intimated these documents were admitted into evidence. That was false. Those summaries were not admitted into evidence. Indeed, Judge King sustained defense objections when CFTC trial counsel sought to elicit those figures from the CFTC’s in-house supposed expert. Certainly, your response omitted a material fact (that the exhibits did not come into evidence) necessary in order to make the statement you did make, in the light of the circumstances under which it was made, not misleading. This egregious omission of material fact needs to be corrected immediately.

Third, you told the appellate court that Southern Trust Metals had “destroyed records when under investigation” and that is why the CFTC supposedly could not ascertain the exact amount of customer losses. That statement was demonstrably false. In fact, Southern Trust Metals produced thousands of pages of documents, including bank statements and all customer statements in its possession. Southern Trust Metals did not destroy any records “when under investigation.” Moreover, the CFTC subpoenaed bank records and received complete account statements from Hantec and Berkeley which reflect a history of customer-by-customer deposits and the ensuing transactions.

We expect you to correct these misrepresentations in satisfaction of your duty of candor to the appellate court by close of business Tuesday (October 10, 2017).

Very truly yours,



Peter W. Homer



U.S. COMMODITY FUTURES TRADING COMMISSION
Case: 16-16544 Date Filed: 02/06/2018 Page: 59 of 59
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October 12, 2017

VIA ELECTRONIC MAIL

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Miami, FL 33131

Re: CFTC v. Robert Escobio, et al., Case No. 16-16544 (11th Cir.)

Dear Peter:

I am in receipt of your letter dated October 6, 2017, in which you posit that I have an ethical obligation to send the Eleventh Circuit a letter to “correct material misstatements” purportedly made during my oral argument on September 28. I see no basis for doing so. Every aspect of my argument is supported by the record. Moreover, your colleague Chris King had a full and fair opportunity to respond to my argument during his rebuttal. I have no intention of advocating your clients’ theory of the case in a post-argument letter to the court.

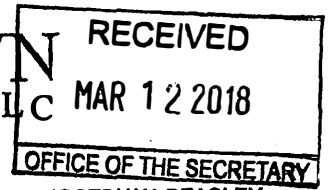
Moreover, I commend to you the ABA Committee on Ethics and Professional Responsibility’s Formal Opinion 94-383, which concludes that a threat by counsel to file disciplinary charges against an opponent to obtain an advantage in a civil case can itself violate one or more ethics rules. *Accord* D.C. Bar Ethics Opinion 220 (holding that threats to file disciplinary charges for the sole purpose of gaining advantage in a civil matter are a violation of the Rules of Professional Conduct); *see also In re Discipline of Eicher*, 661 N.W.2d 354 (S.D. 2003) (holding that an attorney, who threatened via letter to file a complaint with bar association’s disciplinary board if opposing counsel did not take suggested actions, violated professional conduct rules dealing with fairness to opposing counsel).

Sincerely,

/s/ Anne W. Stukes

HARD COPY

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March 9, 2018

VIA FAX (202)772-9324 & FEDERAL EXPRESS

Mr. Brent J. Fields, Secretary
U. S. Securities and Exchange Commission
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Mail Stop 1090-Room 10915
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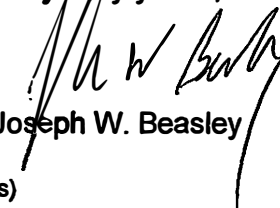
**Re: Administrative Proc. File No. 3-18143
FINRA SD-2130 Decision by FINRA NAC
In the Matter of the Continued Association of
Robert J. Escobio (CRD #703813) with
Southern Trust Securities, Inc., (BD#103781)**

Dear Mr. Fields:

Enclosed please find the original and three copies of Robert Escobio's Request that the Commission Take Official Notice in the above-captioned matter of Appellants' Petition for Panel Rehearing filed with the United States Court of Appeals for the Eleventh Circuit on March 6, 2018, regarding the Court's decision dated January 22, 2018, in the case styled *U.S. Commodity Futures Trading Commission v. Southern Trust Metals, Inc. Loreley Overseas Corporation and Robert Escobio*, Appeal No. 16-16544.

By copy of this letter, we have served the same on Andrew J. Love, Esq., Counsel for FINRA as described in the Certificate of Service.

Very truly yours,


Joseph W. Beasley

JWB/jm
Enclosures

cc: Andrew J. Love, Esq. (via e-mail, fax & Federal Express)
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