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UNITED STATES DISTRICT COURT
NORTHERN DISTRICT CALIFORNIA

COMMODITY FUTURES TRADING COMMISSION, Plaintiff, vs. DENARI CAPITAL, LLC, TRAVIS CAPSON, ARNAB SARKAR, Defendants.	)	Case No: 19-cv-07284-EMC PLAINTIFF'S MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF ITS MOTIONS FOR PRELIMINARY INJUNCTION AND APPOINTMENT OF TEMPORARY RECEIVER Hearing Date: December 29, 2019 Hearing Time: 1:30 p.m.

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I. INTRODUCTION

Since at least 2012, Defendants Travis Capson ("Capson"), Arnab Sarkar ("Sarkar") and their company Denari Capital, LLC ("Denari") (together, "Defendants") have fraudulently solicited and accepted at least $8,300,000 from at least twenty-eight participants whose funds were commingled in a pooled investment scheme that included leveraged off exchange foreign currency ("forex") transactions. Funds from at least nine of the participants were accepted explicitly for the purpose of trading forex in Denari's pooled account. Denari also solicited and accepted millions of dollars from at least sixteen other participants based on "promissory notes" to Denari. Denari used this money to place forex trades, for real estate investments, for various securities transactions, and personal expenses. Denari commingled the funds it received from investors in its bank and trading accounts, making it impossible to attribute specific pool participants' funds to specific transactions or investments. As of the end of July 2019, Denari's obligations to its participants exceeded $5,200,000. Denari does not have sufficient funds or liquid assets to pay these obligations.

Denari lost money over time in its forex trading account. But Denari consistently reported profits in statements to its investors. Capson and Sarkar lied to customers and prospects about the past profitability of Denari's forex trading activity, and the profits customers were making on their interests in Denari's pooled forex account (the "Pool"). Denari also issued false account statements to participants that misrepresented the profitability of their respective interests in the Pool.

Because Denari, Capson and Sarkar solicited funds to engage in forex trading in a pooled account, Defendants acted as a Commodity Pool Operator ("CPO") and Associated Persons ("APs") of a CPO, respectively, without being registered with the Commission as required.

Denari and Capson belatedly filed registration applications with National Futures Association ("NFA") on April 1, 2019.[1] Shortly thereafter, NFA commenced an examination of Denari based on information contained in these applications. During that examination, Capson provided false information to NFA investigators. Specifically, Capson falsely told NFA staff that Denari had been trading forex with its own money since 2015, and that Denari did not use third party funds to trade in Denari's forex trading account until after it had applied for and become registered with NFA in May 2019. In fact, Denari had been trading forex with third-party funds for years.

Plaintiff Commodity Futures Trading Commission ("CFTC" or "Commission") brought this action because Defendants have violated the anti-fraud and registration provisions of the Commodity Exchange Act ("Act"), 7 U.S.C. §§ 1-26 (2012), and Commission Regulations ("Regulations") promulgated thereunder, 17 C.F.R. pts. 1-190 (2019). Specifically, Defendants have:

(a) Committed fraud in violation of Sections 4band 4*o* of the Act, 7 U.S.C. §§ 6b, 6*o* (2012), and Regulation 5.2, 17 C.F.R. § 5.2 (2019);

(b) violated the registration requirements set forth in Sections 4m(1) and 4k(2) of the Act, 7 U.S.C. §§ 6m(1) and 6(k)(2) (2012), and Regulation 5.3, 17 C.F.R. 5.3 (2019); and

(c) commingled participant funds and failed to provide disclosure documents in violation of Regulations 4.20, 4.21, 4.24 and 4.25, 17 C.F.R. §§ 4.20, 4.21, 4.24, 4.25 (2019); and

(d) made false statements to NFA in violation of Section 9(a)(4) of the Act, 7 U.S.C. § 13(a)(4) (2012).

[1] NFA is the industrywide, self-regulatory organization for the U.S. derivatives industry. It has been ddesignated by the CFTC as a registered futures association pursuant to Section 17(a) of the Act, 7 U.S.C. § 21(a) (2012), and its mission is to safeguard the integrity of the derivatives markets, protect investors and ensure NFA Members meet their regulatory responsibilities.

Accordingly, pursuant to Section 6c(b) of the Act, 7 U.S.C. 13a-1(b) (2012), the CFTC moves for entry of a preliminary injunction: (1) prohibiting Defendants from destroying or refusing to permit the CFTC from inspecting and copying, when and as requested, all books and records or other documents; (2) freezing Defendants' assets; (3) compelling an accounting from Defendants; and (4) appointing a temporary receiver to administer the preliminary injunction. In conjunction with this motion, the CFTC is also moving for an order granting leave to conduct expedited discovery pursuant to Fed. R. Civ. P. 26(d).[2]

II. THE PARTIES

The CFTC is an independent federal regulatory agency charged by Congress with administering and enforcing the provisions of the Act, 7 U.S.C. §§ 1-26 (2012), and the Regulations promulgated thereunder, 17 C.F.R. pts. 1-190 (2019).

Denari Capital, LLC is a California limited liability company with a business address of 3100 Oak Road, Suite 380, Walnut Creek, California. (Capson Tr. 13:14-23; Wahls Dec. ¶ 4; Wahls Ex. 1, p. 14.) Capson and Sarkar incorporated Denari in 2012. (*Id.*) Approximately seven years later, on May 1, 2019, Capson and Sarkar registered Denari with the CFTC as a CPO and a Commodity Trading Advisor ("CTA"), and with NFA as a forex firm, on May 1, 2019. (*Id.*)

Defendant Travis Capson is a principal and co-owner of Denari. (Wahls Dec. ¶ 5; Wahls Ex. 2, pp. 8-9.) Capson is a resident of Kanab, Utah. (Capson Tr. 14:3-13.) Capson became registered with the CFTC as an AP of Denari, and was listed as a principal of Denari, on May 1,

[2] The CFTC submits with this Memorandum an Appendix of Declarations and Exhibits in Support of its Motion for Preliminary Injunction, which includes the declaration of NFA Compliance Manager Nichole Wahls ("Wahls"), the declaration of a pool participant, and the transcripts of testimony of Capson and Sarkar. References to declaration paragraphs appear, for example, as follows: Wahls Dec. ¶ 1. References to exhibits to the declarations and appear as follows: Wahls Ex. 1, or Capson Ex. 1. References to testimony page and line numbers appear, for example, as follows: Capson Tr. 5:12-15.

2019. (Wahls Dec. ¶ 5 and Wahls Ex. 2, pp. 8-9.) Arnab Sarkar is a resident of El Cerrito, California. (Sarkar Tr. 11:14-18.) Sarkar is a principal and co-owner of Denari along with Capson. (Wahls Dec. ¶ 6 and Wahls Ex. 3, pp. 8-9)

III. JURISDICTION AND VENUE

This Court has jurisdiction over this action under 28 U.S.C. § 1331 (2012) (federal question jurisdiction) and 28 U.S.C. § 1345 (2012) (district courts have original jurisdiction over civil actions commenced by the United States or by any agency expressly authorized to sue by Act of Congress). Section 6c(a) of the Act, 7 U.S.C. § 13a-l(a) (2012), authorizes the Commission to seek injunctive relief against any person whenever it shall appear that such person has engaged, is engaging, or is about to engage in any act or practice that violates any provision of the Act or any rule, regulation, or order promulgated thereunder. In addition, this Court has jurisdiction over the forex transactions described in the Complaint pursuant to Section 2(c)(2)(C) of the Act, 7 U.S.C. § 2(c)(2)(C) (2012), which subjects the forex solicitations and transactions at issue to, *inter alia*, Sections 4b and 4o of the Act, 7 U.S.C. §§ 6b, 6o (2012).

Venue in this Court is proper pursuant to this Court's Local Rules and Section 6c(e) of the Act, 7 U.S.C. § 13a-l(e) (2012), because Defendants transacted business in this District, and the acts and practices in violation of the Act have occurred, are occurring, or are about to occur within this District. Denari's office and Sarkar's residence are in Contra Costa county**.**

IV. FACTS

A. The Denari Scheme

Capson and Sarkar formed Denari to offer investments in forex and real estate. (Capson, Tr. 7:22-8:18.) In promotional materials, they described Denari as a "fund" that would give investors "the opportunity to diversify their investment portfolio into alternative markets that are not available through the traditional investment platforms." (Capson Tr. 151:16-152:25; Capson Ex. 8.) Shortly after starting Denari in 2012, Capson and Sarkar also began investing funds they

solicited for Denari in various mining companies and related securities, and offering interests in those mining companies and related securities to Denari investors. (Capson Tr. 29:15-36:15.)

Capson and Sarkar are the two managing partners of Denari, and each holds a 50% ownership interest in the firm. (Sarkar Tr. 7:2-8; Capson Tr. 8:8-18.) Capson and Sarkar began operating Denari in 2012, while they were still working for an investment firm registered with the Financial Institution Regulatory Authority ("FINRA"). (Wahls Dec. ¶¶ 7-8; Capson Tr. 54:8-55:7; Sarkar Tr. 10:22-25 and 95:19-96:22.) Capson and Sarkar settled a FINRA proceeding based on this conduct in June 2014, for their failure to disclose outside business activities and engaging in a private securities transaction without providing prior written notice to the FINRA member firm where they worked.[3] (Wahls Dec. ¶¶ 7-8; Wahls Ex. 4a and 4b.)

Between 2012 and the present, Capson and Sarkar solicited individuals to invest with Denari. (Wahls Dec. ¶ 23; Wahls Exs. 11, 12; Capson Tr. 8:6-12, 166:21-167:16; Sarkar Tr. 6:20-23.) Capson and Sarkar solicited participants for various investments, including forex trading, real estate, and investment in a gold mining company, among other investments. (Capson Tr. 7:23-8:5; 30:1-5; Sarkar Tr. 29:23-31:7.) In promotional brochures provided to investors and prospects, Denari claimed, among other things, that "over the past 10 years we have developed a disciplined investment strategy that has earned positive returns in 36 of the past 40 quarters." (Capson Tr. 152:4-25 and Ex. 8; Wahls Dec. ¶¶ 25-28, Wahls Exs. 20a, 20b, 20c and 21). Denari also represented that it "charges no management fees. We will pay all expenses associated with the fund management, performance reporting and market research. By

[3] Neither Capson nor Sarkar disclosed the FINRA settlement to certain Denari participants, and only disclosed it to participants who confronted them about it after learning about the settlement themselves, or who requested an explanation as to why Capson and Sarkar left their prior investment firm. (Sarkar Tr. 97:2-6; 115:7-10; Capson Tr. 58:18-59:5.) Specifically, one participant confronted Capson about the settlement after finding it on the internet, and Capson inaccurately informed the participant that "we didn't have to pay the fine or serve any suspension," and "we don't have a single client, past or present, that has lost money," among other things. (Oyler Dec. ¶ 11; Oyler Ex. 4.)

not passing any of these expenses on to our clients through traditional quarterly fees we are compensated through performance, not assets under management." (*Id.*) Denari's promotional materials included claimed annual rates of return for 2017 of 50.22% and for 2018 of 36.33%, and portrayed Denari as never having a losing year. (*Id.*)

However, actual trading in Denari's forex trading account for 2017 and 2018 does not support the claimed rates of return. (Wahls Dec. ¶¶27-29; Wahls Exs 20b, 20b.) The forex trading account experienced a negative return of more than 46% in 2017 and a positive return of 8% in 2018, which, while positive, was based upon a relatively low amount of assets and just half of what Denari's promotional materials claimed. (Wahls Dec. ¶ 29 and Wahls Ex. 15.) Denari's promotional material also contained monthly "trading results" for January through July 2018 that are inconsistent with the actual monthly trading results realized in its trading account.[4] (Wahls Dec. ¶ 30 and Ex. 15.) Additionally, Denari could not produce any of the required forex pool disclosure documents when asked to do so during the course of NFA's examination. (Wahls Dec. ¶ 25.)

B. Participant Contributions to the Denari Pool

Capson and Sarkar documented at least some of the Denari participants' contributions of funds to the Denari pool with "Joint Venture Agreements" and/or "Promissory Notes." (Capson Tr. 44:3-25.) Since September of 2012, at least nine participants signed "Joint Venture Agreements" with Denari. (Wahls Dec. ¶ 14 and Ex. 11; McCormack Dec ¶ 15.) Capson also signed these agreements as managing partner of Denari. (*See, e.g.*, Wahls Dec. ¶ 14 and Ex. 11.) These agreements state that, "the Joint Venturers have agreed to make contributions to a common fund for the purpose of investing under the direction of Denari Capital, LLC." (*Id.*)

[4] Specifically, Denari's promotional material claimed rates of return of 3.79%, 3.55%, 3.43%. 3.09%, 3.53%, 0.94% and 2.47% for January through July 2018 respectively, while its actual monthly trading results for this time period was -7.27%, -1.79%, -4.82%, 7.71%, 16.80%, -0.72% and 3.75%. (Wahls Dec. ¶30; Wahls Exs. 20a, 20b, 20c and 15).

The agreements also state that Denari could acquire "any assets, which may include but are not limited to real estate, foreign currency," or other business interests, in connection with the venture. (*Id.*) Some of the Denari Joint Venture Agreements provide that "Denari Capital, LLC will be solely responsible for all investment decisions and will receive a portion of the investment earnings equal to the percentage agreed upon by each of the Joint Venturers." (*Id.*) Denari received at least $3,700,000 from participants who signed the Joint Venture Agreements. (McCormack Dec. ¶ 15.)

At least sixteen participants signed Promissory Notes with Denari, pursuant to which Denari received at least $3,200,000. (McCormack Dec. ¶ 16.) Capson signed the Promissory notes as managing partner of Denari. (*See, e.g.*, Wahls Dec. ¶ 31; Wahls Ex. 22.) The Promissory Notes state that Denari agrees to repay the loans, usually with 10% to 12% interest annually. (*Id.*) Most of the loans had a one-year term with an option to renew at the lender's choice. (*Id.*) For example, one of the Promissory Notes involved a $100,000 loan made by an individual on November 1, 2018 to Denari. (*Id.*) The note had a one-year term, with a promise for the principle to be repaid upon demand at the end of any month after November 2019. (*Id.*) The note also provided for monthly interest payments at a rate of 12% annually on the outstanding principle balance. (*Id.*)

Denari deposited and commingled participant funds received pursuant to the Joint Venture Agreements and Promissory Notes into bank accounts in Denari's name and subsequently transferred some of these funds into forex trading accounts for the purpose of trading forex. (Wahls Dec. ¶¶ 17, 32; McCormack Dec. ¶ 19.) Of the at least $8,300,000 that Denari solicited and accepted, at least $3,200,000 was received from participants who signed promissory notes, at least $3,700,000 was received from participants who signed Joint Venture

Agreements, and at least $1,450,000 was received from participants for the purpose of other investments. (McCormack Dec. ¶¶ 15, 16, 17, 20.)

C. Capson and Sarkar Create a Denari Forex Pool

In August of 2012, Capson and Sarkar opened a forex trading account in Denari's name with FXCM, at the time a futures commission merchant and a retail foreign exchange dealer ("RFED") registered with the CFTC. (Capson Tr. 17:24-19:14, 100:13-101:10; Capson Ex. 5.) Capson was the primary trader on the account. (Capson Tr. 20:18-21:4.) Denari made periodic deposits to and withdrawals from its forex trading account at FXCM (Capson Ex. 5) that were funneled through Denari's bank account, where Denari co-mingled funds from all of its investors (Capson Tr. 105:11-20, 144:23-145:9). Denari's account opening application documents with FXCM falsely claimed that it was only investing proprietary funds, and not funds of third parties. (Wahls Dec. ¶ 39; Wahls Ex. 26.) In fact, Denari used third-party investor funds to trade forex in its FXCM account.

In February 2017, Denari transferred its trading account held at FXCM to a different RFED, Gain Capital Group LLC ("Gain"). (Capson Tr. 17:24-19:14; Wahls Dec. ¶9.) Capson remained the primary trader for Denari on its account at Gain. (Sarkar Tr. 17:18-18:6; Capson Tr. 20:18-21:4.) In addition to the nearly $9,000 opening transfer balance in February 2017, Denari made seven additional deposits to the Gain account through June 2019. (Wahls Dec. ¶ 18, Wahls Ex. 15.) The deposits ranged in amounts from $20,000 to $700,000 and totaled $1,662,000. (*Id.*)

Despite Denari's claims of profitability in promotional materials and in account statements issued to Denari customers, Denari's forex account at FXCM suffered overall losses of more than $228,000 before the remaining account balance was transferred to GAIN in 2017. (Wahls Dec. ¶ 40.) Denari's forex trading account at Gain also suffered losses, despite Denari's

representations of consistent trading profits. Out of 30 months traded at Gain, at least 15 months experienced trading losses. (Wahls Dec. ¶ 18; Wahls Dec. Ex. 15.)

D. Denari Issued False and Misleading Account Statements to Participants

Denari issued periodic account statements to participants that misrepresented the value of their respective investments and interests in the Pool, and exaggerated the returns of the Pool. (Wahls Dec. ¶23; Wahls Ex. 19.) The statements reflected that Denari participants' funds were earning consistent profits with no losses. For example, on March 2, 2018, Capson sent one participant an email attaching a first quarter 2018 account statement, and noted in his email that "February was another consistent month for us with 3.55% fund performance. After March, we will readjust the trade sizes based on the new account value." (Oyler Dec. ¶19 and Oyler Ex. 12.) However, Denari's forex trading account at Gain had a return of -1.79% in February 2018, and fared no better in January or March of 2018 with returns of -7.27% and -4.82% respectively. in March 2018 resulting in losses each month during the first quarter of 2018. (Wahls Dec. ¶30; Wahls Ex. 15.)

Denari improperly calculated the Pool's net asset value ("NAV"). Denari failed to factor in the impact of unrealized losses in its forex trading account and, therefore, inflated its performance results. (Wahls Dec. ¶¶ 24, 29; Wahls Ex. 15.) Moreover, Denari regularly closed out profitable positions to recognize gains, while continuously rolling forward losing positions. **(***Id.*) Denari then issued account statements to Denari participants reflecting consistent profits, with no losses. (*See, e.g.*, Oyler Dec. ¶¶ 17-27, Oyer Exs. 10-21.)

E. Capson Made False Statements to NFA During the July 2019 Examination

NFA conducts periodic audits and examinations of NFA members In furtherance of its official duties under the Act as a means of monitoring and assuring compliance with NFA rules, the Act, and the Regulations. In July 2019, NFA began an examination of Denari. (Wahls Dec.

¶ 8.) On July 15, 2019, NFA sent Capson a document request and spoke to him by telephone. (*Id.*) During that phone call, Capson told NFA representatives including Compliance Department Manager Nicole Wahls that Denari has been trading forex with its own, proprietary funds since approximately 2015, and that Denari did not trade forex for third-party investors until after Denari became registered as a CPO in 2019. (Wahls Dec. ¶ 10.) Capson's representations are false. (Wahls Dec. ¶¶ 11-12.) Denari has been operating a forex pool and trading third party funds since at least 2012.

F. Denari Has Insufficient Funds To Cover Its Obligations To Participants

Denari lacks sufficient funds to cover its obligations to its participants. As of June 30, 2019, Denari's forex trading account at Gain had a net liquidating value ("NLV") of approximately $1,000,000. (Wahls Dec. ¶ 21.) However, according to a June 30, 2019 Denari financial statement, the value of Denari's forex pool participants' interest was approximately $1,600,000. (Wahls Dec. ¶ 33, Wahls Ex. 24.) In addition to the NLV of approximately $1,000,000 in Denari's forex trading account as of June 30, 2019, Denari's only other liquid asset consisted of a bank account that had a balance of approximately $200,000 as of June 30, 2019. (Wahls Dec. ¶¶21, 33.) Therefore, as of June 30, 2019, Denari did not have sufficient liquid assets to cover its forex pool participants' interests in the Pool. (Wahls Dec. ¶21.)

Denari's bank records also show deposits from a least five pool participants to a Denari bank account since January 1, 2017. (Wahls Dec. ¶¶ 17, 18 and Wahls Exs. 14a, 14b, 8, 17a, 18b, and 15.) Denari and Capson distributed funds from one or more Denari bank accounts to participants as purported profit and interest payments. (Wahls Ex. 15; Capson Tr. 45:4-22, 69:21-71:1, 76:17-77:5.) Capson also took regular monthly draws from Denari's bank account, where they had co-mingled the funds of Pool investors, regardless of losses suffered in Denari's forex trading or other purported investments. (Capson Tr. 156:22-157:7.) Capson and Sarkar

withdrew funds from Denari bank accounts for their personal use, including paying for Capson's personal American Express credit card bills, to pay for meals at restaurants, to purchase gas, to pay for gym memberships, and to invest in Capson's personal cryptocurrency trading account, among other things. (Capson Tr. 83:21-84:14, 168:10-18; Sarkar Tr. 117:7-21; Wahls Exs. 14a and 17a; McCormack Dec. ¶ 18.) Additionally, Capson and Sarkar paid themselves $10,000 per month each from the Denari bank accounts. (Capson Tr. 77:14-19; Sarkar Tr. 15:11-13.) Capson and Sarkar did not disclose these withdrawals and payments to participants. (Capson Tr. 78:24-79:2.)

As of July 31, 2019, the NLV of Denari's account at Gain declined to approximately $530,000. (Wahls Dec. ¶22; Wahls Exs. 18a and 18b.) Meanwhile, Denari's bank account balance totaled approximately $300,000 as of July 22, 2019, for combined liquid assets of approximately $830,000. *Id.* Combining all of Denari's liquid assets and even attributing them all to the Denari forex pool, the Denari forex pool had a shortfall of at least $400,000 as of June 30, 2019. (Wahls Dec. ¶21; Wahls Ex. 17a and 17b.)

Additionally, Denari's June 30, 2019 balance sheet indicates that the firm owes more than $5,200,000 in "business loans," which, according to Defendants, represents the firm's obligation to the forex pool participants, promissory note holders and others. (Wahls Dec. ¶33; Wahls Ex. 24.) Excluding the approximately $1,600,000 that Denari and Capson have represented is owed to forex pool participants as of June 30, 2019, Denari, Capson and Sarkar appear to owe more than $3,600,000 to the promissory noteholders and others whose funds were commingled with the pool participants' funds. Id. On information and belief, Defendants misappropriated some or all of these funds. Denari does not have sufficient liquid assets to meet its current liabilities to its participants nor, on information and belief, does it have sufficient assets liquid or non-liquid to satisfy its current obligations to its participants. (Wahls Dec. ¶21.)

Denari's June 30, 2019 balance sheet also included other assets purportedly valued at more than $6,100,000. (Wahls Dec. ¶34.) These assets consist of stock in three mining-related companies and a real estate holding in Nevada. *Id.* However, Denari has not been able to substantiate its ownership of these assets nor the value Denari assigns to them. (Wahls Dec. ¶¶35, 36.) Additionally, Denari, Capson and Sarkar hold ownership interests in or have roles with the mining entities listed as Denari's assets. (Wahls Dec. ¶34.) These assets include penny stock in one company that is insolvent; stock in a privately-held company of which Denari and Sarkar are majority shareholders; and stock in a third company in which Denari and Capson regularly engage in buying and selling the stock by privately arranging transactions in the stock. *Id.* The real estate holding in Nevada is not in Denari's name, and Denari also included on its balance sheet Capson's and Sarkar's personal shares in the mining-related companies, which had the effect of improperly increasing the assets listed on the firm's balance sheet. *Id.*

NFA confronted Capson and Sarkar, on July 30, 2019 about the difference between the firm's liquid assets and its financial obligations to its participants. (Wahls Dec. ¶35.) Capson and Sarkar were uncertain whether they could immediately repay these obligations and said they would liquidate the stock they own to make everyone whole. (*Id.*) NFA filed a member responsibility action ("MRA") against Denari and Associate Responsibility Action ("ARA") (together "MRA/ARA") against Capson, on August 6, 2019, suspending them from NFA membership; prohibiting them and anyone acting on their behalf from soliciting or accepting any funds for any investment in Denari; prohibiting them from disbursing or transferring any funds from accounts in the name of Denari or over which Denari or Capson have control without prior approval of NFA; prohibiting them from placing any commodity interest trades, including forex; requiring Denari to hire a qualified third party to calculate the amount owed to each joint venture investor and each promissory noteholder and to notify each investor of their respective valuation;

and requiring Denari and Capson to provide copies of the MRA/ARA to all joint venture investors and promissory noteholders, all NFA members that have an investment over which Denari or Capson exercise control, and any banks or financial institutions that maintain accounts in the name of Denari or Capson or over which they exercise control. (Wahls Dec. ¶¶37-38, Wahls Ex. 25).

V. ARGUMENT

A. Legal Standard for Preliminary Injunctive Relief

Pursuant to Section 6c(b) of the Act, 7 U.S.C. § 13a-1 (2012), the CFTC seeks a preliminary injunction against Defendants prohibiting, among other things, future violations of the Act or Regulations under which they have been charged. 7 U.S.C. § 13a-1(b) (2012) provides in pertinent part that "[u]pon a proper showing, a . . . temporary injunction . . . shall be granted without bond." 7 U.S.C. § 13a-1(a) (2012) authorizes the CFTC to seek injunctive relief against any person "[w]henever it shall appear to the Commission" that such person or entity "has engaged, is engaging, or is about to engage in any act or practice constituting a violation of any provision" of the Act or Regulations; *see also CFTC v. Co Petro Marketing Group, Inc*., 680 F.2d 573, 583 (9th Cir. 1982) (recognizing district court's authority "to issue permanent or temporary injunctions or restraining orders" under 7 U.S.C. § 13a-1); *CFTC v. Yu*, 2012 WL 3283430, at *4 (N.D. Cal. Aug. 10, 2012, No. 12-cv-3921) ("the CFTC is entitled to injunctive relief upon a *prima facie* showing that a violation of the law has occurred and that 'there is some reasonable likelihood of future violations'") (quoting *CFTC v. Hunt*, 591 F.2d 1211, 1220 (7th Cir. 1979)). Injunctive relief under 7 U.S.C. § 13a-1 "is remedial in nature, and is designed to prevent injury to the public and to deter future illegal conduct." *Yu*, 2012 WL 3283430, at *4. Therefore, restrictions ordinarily associated with private litigation, such as irreparable injury or inadequacy of other remedies, are inapplicable. *See Hunt*, 591 F.2d at 1220; *Yu*, 2012 WL 3283430, at *4.

The CFTC is entitled to preliminary injunctive relief upon a *prima facie* showing that: (1) a violation of the Act or Regulations has occurred; and (2) there is a reasonable likelihood of future violations. "Once a violation is demonstrated, the moving party need show only that there is some reasonable likelihood of future violations." *CFTC v. Wilson*, 2011 WL 6398933, at *2 (No. 11-cv-1651, S.D. Cal. Dec. 20, 2011) (citing *Hunt*, 591 F.2d at 1220) (internal quotations omitted); *see also CFTC v. Valois*, 2015 WL 12684303, at *2 (No. 15-cv-130, C.D. Cal. Feb. 13, 2015) (granting preliminary injunction where record constitutes *prima facie* showing of Defendants' violations and a "reasonable likelihood of future violation" exists). In assessing the reasonable likelihood of future violations of the Act and Regulations, "a court must look to the totality of the circumstances," including whether a defendant's past violations "require a showing of knowledge of wrongdoing, were persistent or recurrent, or occurred over a long span of time." *Yu*, 2012 WL 3283430, at *4. As a result, the Court may infer a reasonable likelihood of future violations from a defendant's past unlawful conduct. *Hunt*, 591 F.2d at 1220.

Moreover, "because the commodities trading area is a highly regulated, 'highly sensitive area of public trust,'" any circumstances suggesting that a defendant may repeat or continue his activity in violation of CFTC registration requirements "strongly favor entry of an injunction." *Yu*, 2012 WL 3283430, at *4 (citing *CFTC v. British Am. Commodity Options*, 560 F.2d at 142).

B. *Prima Facie* Violations of the Act and Regulations

The record before the Court establishes a *prima facie* showing that Defendants violated the antifraud and registration provisions of the Act and Regulations, and that a reasonable likelihood of future violations exists. Defendants' violations strike at the heart of market integrity and the orderly functioning of the CFTC's registration process. Defendants: acted as an unregistered CPO (and APs of a CPO) by soliciting, accepting, and receiving at least $8,300,000 from at least twenty eight participants, whose funds were commingled in a pooled investment

scheme including for forex trading; provided false and misleading promotional material to participants; issued false account statements to participants; lied to NFA representatives about the source of the funds in Denari's forex trading account during an examination; and misappropriated participants' funds. Defendants' conduct demonstrates that they are likely to continue to engage in such unlawful conduct unless enjoined by this Court. Therefore, the granting of the preliminary injunctive relief requested by the CFTC is warranted.

C. The Commission Has Jurisdiction Over the Forex Transactions

Denari accepted funds from participants and pooled those funds for trading in an account at a "Retail Foreign Exchange Dealer" ("RFED"), in which Denari engaged in retail forex transactions as a retail forex CPO. Under § 2(c)(2)(C) of the Act, 7 U.S.C. § 2(c)(2)(C) (2012), the CFTC can pursue an action involving forex transactions that are: (1) offered to or entered into with a person who is not an eligible contract participant ("ECP"); (2) offered to or entered into on a leveraged basis or financed by the offeror on a similar basis; and (3) do not result in delivery within two days or create an enforceable obligation to make or take delivery. *CFTC v. Trimble*, No. 11-cv-02877-PAB-KMT, 2013 WL 317526, at *6 (D. Colo. Jan. 28, 2013); *CFTC v. Cook*, No. 09-3332 (MJD/FLN), 2016 WL 128131, at *3 (D. Minn. Jan. 12, 2016). Pursuant to Section 2(c)(2)(C)(ii)(I) of the Act, these retail forex transactions are subject to certain provisions of the Act, including anti-fraud provisions. In addition, for the purposes of retail forex transactions, a CPO is defined in Regulation 5.1(d)(1), 17 C.F.R. § 5.1(d)(1) (2019), "as any person who operates or solicits funds, securities, or property for a pooled investment vehicle that is not an eligible contract participant as defined in Section 1(a)(18) of the Act, 7 U.S.C. § 1a(18) (2012), and who engages in retail forex transactions." Section 1a(18)(A)(xi) of the Act sets a high dollar-value threshold requirement for individuals to be an ECP. For individuals, it is generally limited to those who have amounts invested on a discretionary basis, the aggregate of

which is in excess of $10 million. Pursuant to Section 1a(18)(A)(iv)(II) of the Act, the Denari pool cannot be an ECP because at least some of its participants did not possess the requisite assets to be ECPs.[5] (Oyler Dec. ¶ 29.)

D. Defendants Engaged in Fraud

Defendants violated Section 4b(a)(2)(A)-(C) of the Act by (1) making material misrepresentations and omissions to pool participants, (2) issuing false account statements to pool participants, and (3) misappropriating pool participants' funds for use on personal and improper business expenses. Section 4b(a)(2)(A)-(C) of the Act (which applies to Defendants' retail forex transactions pursuant to 7 U.S.C. § 2(c)(2)(C) as discussed in the previous subsection of this brief) makes it unlawful:

> for any person, in or in connection with any order to make, or the making of, any contract of sale of any commodity for future delivery, or swap, that is made, or to be made, for or on behalf of, or with, any other person, other than on or subject to the rules of a designated contract market
>
> (A) to cheat or defraud or attempt to cheat or defraud the other person;
>
> (B) willfully to make or cause to be made to the other person any false report or statement or willfully to enter or cause to be entered for the other person any false record;
>
> (C) willfully to deceive or attempt to deceive the other person by any means whatsoever in regard to any order or contract or the disposition or execution of any order or contract, or in regard to any act of agency performed, with respect to any order or contract for or, in the case of paragraph (2), with the other person[.] (emphasis added).

This is a broad anti-fraud provision that encompasses Defendants' fraudulent solicitations based on a fabricated forex trading history of Denari, misleading promotional materials touting

[5] In addition, pursuant to Section 1a(18)(A)(iv)(I)-(II) of the Act, the term ECP encompasses a commodity pool that has total assets exceeding $5 million and is formed by a person subject to regulation under the Act. Denari's pool account has never had total assets exceeding $5 million, so if defined by the size of the actual pool account, Denari would not be an ECP.

fictitious rates on Denari's actual forex trading activity, false account statements issued to participants with fabricated returns, and the misappropriation of participant funds. *See, e.g., Hirk v. Agri-Research Council, Inc.*, 561 F.2d 96, 103-04 (7th Cir. 1977) ("Section 4[b] encompasses conduct 'in or in connection with' futures transactions. The plain meaning of such broad language cannot be ignored."); *see also CFTC v. Gresham*, No. 3:09-CV-75, 2011 WL 8249266, at *3 (N.D. Ga. Sept. 8, 2011) (ruling that Section 4b encompasses fraudulent misrepresentations "in connection with" promissory notes given to secure funds used to trade forex).

"The elements of a fraud action under [Section] 4b are derived from the common law action for fraud." *Puckett v. Rufenacht, Bromagen & Hertz, Inc.*, 903 F.2d 1014, 1018 (5th Cir. 1990). To establish that Defendants violated Section 4b(a) of the Act through misrepresentations and omissions, the Commission must prove that: (1) misrepresentations or omissions were made; (2) the misrepresentations or omissions were material; and (3) Defendants acted with scienter. *CFTC v. R.J. Fitzgerald & Co., Inc.*, 310 F.3d 1321, 1328–29 (11th Cir. 2002). All three elements are established here.

1. The Defendants Made Material Misrepresentations and Omissions

Defendants made numerous material misrepresentations and omissions. "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 (citing *Hammond v. Smith Barney Harris* Upham *& Co.*, CFTC No. 86-R131, 1990 WL 282810, at *4 & n.12 (Mar. 1, 1990)). A representation or omission is material if "a reasonable investor would consider it important in deciding whether to make an investment." *R.J. Fitzgerald*, 310 F.3d at 1328–29. This includes representations about past success and experience, *e.g., CFTC v. Commonwealth Fin. Grp., Inc.*, 874 F. Supp. 1345, 1353–54 (S.D. Fla. 1994) ("It amounts to a misrepresentation when salespeople emphasize the profits enjoyed by customers without

mentioning any of the losses."); account balances, *e.g.*, *CFTC v. Rosenberg*, 85 F. Supp. 2d 424, 447 (D.N.J. 2000); and risk of loss and opportunity for profit, *e.g.*, *R.J. Fitzgerald*, 310 F.3d at1330; *see also CFTC v. Noble Wealth Data Info. Servs., Inc.*, 90 F. Supp. 2d 676, 686 (D. Md. 2000) ("Indeed, misrepresentations concerning profit and risk go to the heart of a customer's investment decision and are therefore material as a matter of law."), *aff'd in part, vacated in part sub nom. CFTC v. Baragosh*, 278 F.3d 319 (4th Cir. 2002); *CFTC v. Lake Shore Asset Mgmt. Ltd.*, 2008 WL 1883308, at *8 (N.D. Ill. Apr. 24, 2008) ("misrepresentations or omissions about experience, historical success, and profitability are material and may constitute fraud."); *CFTC v. Hunter Wise Commodities*, 21 F. Supp. 3d 1317, 1345-46 (omissions of historical losing track record of trading are material).

Defendants' fraudulent solicitations included, among other things, the following oral and written misrepresentations:

- Denari had "earned positive returns in 36 of the past 40 quarters;"
- "we don't have a single client, past or present, that has lost money,"
- Denari's annual rates of return for 2017 and 2018 were 50.22% and 36.33% respectively;
- That Denari could provide a guaranteed interest payment of 10% or 12% on promissory notes; and
- Participants were earning consistent profits with no losses.

Defendants also misrepresented in their promotional material the forex Pool's monthly trading results for 2018 and, prior to issuance of NFA's action against Denari and Capson on August 6, 2019, disclose to pool participants that Denari did not have sufficient funds or assets to meet its obligations to them. Defendants also failed to disclose to at least some participants and prospects that Capson and Sarkar were sanctioned by FINRA. All of these misrepresentations

and omissions were material to prospective and actual pool participants, who would necessarily need to know that the Pool was risky, was not profitable, could not satisfy its financial obligations to participants, and was being run by individuals who were previously sanctioned by FINRA.

2. Defendants Acted with Scienter

Defendants acted with the requisite scienter to establish a violation of Section 4b(a) of the Act. Scienter requires that an individual's acts be performed "with knowledge of their nature and character." *Wasnick v. Refco, Inc.*, 911 F.2d 345 (9th Cir. 1990) (citation omitted). The Commission need only demonstrate that Defendant's actions were "intentional as opposed to accidental." *Lawrence v. CFTC*, 759 F.2d 767, 773 (9th Cir. 1985); *see also CFTC v. Noble Metals Int'l, Inc*., 67 F.3d 766, 774 (9th Cir. 1995) (for a Section 4b claim, the Commission must show that a defendant either "intentionally violated the Act or acted with 'careless disregard' of whether his actions violated the Act"); *Drexel Burnham Lambert Inc. v. CFTC*, 850 F.2d 742, 748 (D.C. Cir. 1988) (holding that recklessness is sufficient to satisfy scienter requirement). Conduct involving "highly unreasonable omissions or misrepresentations . . . that present a danger of misleading [retail customers] which is either known to the Defendant or so obvious that [the] Defendant must have been aware of it" have been found to meet the scienter requirement. *CFTC v. Hunter Wise Commodities, LLC*, 21 F. Supp. 3d 1317, 1339 (S.D. Fla. 2014) (citing *R.J. Fitzgerald*, 310 F.3d at 1328).

Defendants knew that the Pool was not making consistent profits through forex trading or earning the returns reflected in their promotional material and account statements and that Pool participants' funds were being misappropriated, yet chose to misrepresent the true nature of the Pool. Accordingly, Defendants' conduct involved making highly unreasonable misrepresentations and omissions to Pool participants, with scienter.

3. Fraud by Misappropriation

Defendants also violated Section 4b(a) of the Act through misappropriation of pool participants' funds. Misappropriation constitutes "willful and blatant" fraud. *CFTC v. Am. Bullion Exch. Abex Corp.*, No. SACV 10-1876 DOC, 2014 WL 12603558 (C.D. Cal. Sept. 16, 2014); *Noble Wealth*, 90 F. Supp. 2d at 687; *see also In re Slusser*, CFTC No. 94-14, 1999 WL 507574, at *12 (July 19, 1999) (consent order) (respondents violated Section 4b of the Act by surreptitiously retaining money in their own bank accounts that should have been traded on behalf of investors), *aff'd in relevant part Slusser v. CFTC*, 210 F.3d 783 (7th Cir. 2000); *CFTC v. Morse*, 762 F.2d 60, 62 (8th Cir. 1985) (defendant's personal use of customer funds violated Section 4b of the Act).

Defendants solicited money for a pooled investment in forex as well as other types of investments, but misappropriated participant funds for their personal and other uses including purchases on Amazon, meals at restaurants, gym memberships and gas, among other things. Capson also took regular monthly draws from Denari's bank account, where they had co-mingled the funds of Pool investors, regardless of losses suffered in Denari's forex trading or other purported investments. As of July 22, 2019, Defendants had liquid assets of approximately $830,000, but owe more than five million dollars to participants. Defendants' acts of misappropriation of pool participants' funds are a clear example of "willful and blatant" fraud in violation of Section 4b of the Act.

4. False Account Statements

Defendants also violated Section 4b(a) of the Act when they created and issued false account statements to pool participants. *See, e.g.*, *CFTC v. Weinberg*, 287 F. Supp. 2d 1100, 1107 (C.D. Cal. 2003) (false and misleading statements as to amount and location of investors' money violated Section 4b(a) of Act); *Noble Wealth*, 90 F. Supp. 2d at 686 (defendant's profit claims constituted false reports and fraud within the meaning of the Act); *CFTC ex rel. Kelley v.*

Skorupskas, 605 F. Supp. 923, 932-33 (E.D. Mich. 1985) (defendant violated Section 4b(a) by issuing false monthly statements to customers).

Pool participants received quarterly statements via mail and email. (McCormack Dec. ¶ 9.) The statements were created (or caused to be created) by the Defendants. Since at least 2013, these account statements reflect consistent profits with no losses. The statements purport to provide, among other things, the pool participants' "investment results," "quarterly interest payments" and balance at the beginning of each quarter.

These account statements are false. For 2017, the Pool experienced a negative trading returns of at least 49%. However, Denari's account statements issued to participants showed only positive returns for 2017. Additionally, Defendants improperly calculated the Pool's NAV. Defendants failed to factor in the impact of unrealized losses in its forex trading account and, therefore, inflated its performance results. Moreover, Defendants regularly closed out profitable positions to recognize gains, while continuously rolling forward losing positions. Consequently, Defendants provided false account statements to pool participants.

5. Defendants Violated Regulation 5.2(b)(1)-(3)

Defendants are liable for violating Regulation 5.2(b)(1)-(3), 17 C.F.R. § 5.2(b)(1)-(3) (2019), for the same reasons that they are liable for violating Section 4b(a)(2)(A)-(C) of the Act. Regulation 5.2(b) provides, in relevant part, that

> [i]t shall be unlawful for any person, by use of the mails or by any means or instrumentality of interstate commerce, directly or indirectly, in or in connection with any retail forex transaction: (1) [t]o cheat or defraud or attempt to cheat or defraud any person; (2) [w]illfully to make or cause to be made to any person any false report or statement or cause to be entered for any person any false record; or (3) [w]illfully to deceive or attempt to deceive any person by any means whatsoever.

Regulation 5.2(b) adds only one additional element not found in the anti-fraud provision in Section 4b(a)(2)(A)-(C): that defendant's conduct must involve "use of the mails or by any

means or instrumentality of interstate commerce." Here, Defendants used the telephone and email to solicit participants, and sent false account statements to participants via mail and email. Also, much of the money was transferred to bank accounts through wire transfers, or other means or instrumentalities of interstate commerce. Finally, Defendants used email and the Internet to open the Pool's trading account and to carry out their trading activity.

A. Defendants Engaged in Forex Pool Fraud in Violation of Section 4*o*(1)(A)-(B) of the Act

1. Denari is a Commodity Pool Operator

Denari is a CPO. A "commodity pool" is defined in part under Section 1a(10)(A) of the Act, 7 U.S.C. § 1a(10)(A) (2012), as "any investment trust, syndicate, or similar form of enterprise operated for the purpose of trading in commodity interests," including for the trading of futures or forex. A CPO is defined under Section 1a(11)(A)(i) of the Act as any person—

> engaged in a business that is of the nature of a commodity pool, investment trust, syndicate, or similar form of enterprise, and who, in connection therewith, solicits, accepts, or receives from others, funds, securities, or property, either directly or through capital contributions, the sale of stock or other forms of securities, or otherwise, for the purpose of trading in commodity interests, including any—
>
> (I) commodity for future delivery, security futures product, or swap; [or]
> (II) agreement, contract, or transaction described in section 2(c)(2)(C)(i) of this title or section 2(c)(2)(D)(i) of this title[.]

In addition, pursuant to Regulation 5.1(d)(1), subject to certain exceptions not relevant here, any person who operates or solicits funds, securities, or property for a pooled investment vehicle and engages in retail forex transactions is defined as a retail forex CPO. During the Relevant Period, Denari solicited, accepted, and received from others funds for the Pool.

2. Defendants Capson and Sarkar Are Associated Persons of Denari

Regulation 1.3, 17 C.F.R. § 1.3 (2019), defines an AP of a CPO as a natural person associated with a CPO:

> as a partner, officer, employee, consultant, or agent (or any natural person occupying a similar status or performing similar functions), in any capacity which involves (i) the solicitation of funds, securities, or property for a participation in a commodity pool or (ii) the supervision of any person or persons so engaged[.]

Pursuant to Regulation 5.1(d)(2), any person associated with a CPO as defined by Regulation 5.1(d)(1) "as a partner, officer, employee, consultant or agent (or any natural person occupying a similar status or performing similar functions), in any capacity which involves: (i) [t]he solicitation of funds, securities, or property for a participation in a pooled vehicle; or (ii) [t]he supervision of any person or persons so engaged" is defined as an AP of a retail forex CPO.

Defendants Capson and Sarkar were associated with a CPO as a partner, officer, employee, consultant, or agent in a capacity that involved the solicitation of funds for the Denari Pool, or the supervision of any person or persons so engaged. Therefore, Defendants Capson and Sarkar were APs of a CPO as defined by Regulation 1.3.

3. Defendants Violated Section 4*o*(1) Through Their Fraud

Pursuant to Section 2(c)(2)(C)(ii)(I) of the Act, 7 U.S.C. § 2(c)(2)(C)(ii)(I) (2012), "[a]greements, contracts, or transactions" in retail forex and accounts or pooled investment vehicles "shall be subject to . . . section[ ] 4o [of the Act]," except in circumstances not relevant here. Defendants violated Section 4*o*(1) of the Act by making material misrepresentations and omissions to participants, by misappropriating participants' funds for use on personal and other expenses, and by issuing false account statements. Section 4*o* of the Act is a parallel statute to Section 4b of the Act in that the same conduct that violates Section 4b can violate Section 4*o*. *CFTC v. Driver*, 877 F. Supp. 2d 968, 978 (C.D. Cal. 2012). The only additional element set forth in Section 4*o*(1) is that Defendants' conduct must involve use of the mails or any means or instrumentality of interstate commerce, which it did. While acting as CPOs and APs of CPOs, Defendants used various means of interstate commerce (i.e., the Internet, telephone, email, and wire transfers), to defraud and deceive pool participants. Section 4*o*(1) of the Act applies to all

CPOs, among others, whether registered, required to be registered, or exempt from registration. *Skorupskas*, 605 F. Supp. at 932.

B. Defendants Failed To Register with the Commission in Violation of Sections 4k(2), and 4m(1) of the Act and Regulation 5.3(a)(2)

Although required to by the Act and Regulations, Defendant Denari did not register as a CPO, and Defendants Capson and Sarkar did not register as APs of CPOs. Section 4m(1) of the Act provides that it is unlawful for a commodity pool operator, unless registered, to make use of the mails or any means or instrumentality of interstate commerce in connection with his business as a commodity pool operator. Similarly, Section 2(c)(2)(C)(iii)(I)(cc) of the Act states that a person shall not operate or solicit funds for any pooled investment vehicle in connection with forex transactions, unless registered pursuant to Commission regulations. Regulation 5.3(a)(2)(i) requires forex CPOs, as defined by Regulation 5.1(d)(1) to register as such with the Commission. Section 4k(2) of the Act states that APs of CPOs who are soliciting for participation in a pool must register with the Commission. "The intent of the congressional design is clear; persons engaged in the defined regulated activities within the commodities business are not to operate as such unless registered . . . and the Commission is empowered to seek injunctive prohibitions against violations of any provisions of the Act, including registration provisions." *CFTC v. British Am. Commodity Options*, 560 F.2d 135, 139 (2d Cir. 1977). "Registration is the kingpin in this statutory machinery, giving the Commission the information about participants in commodity trading which it so vitally requires to carry out its other statutory functions of monitoring and enforcing the Act." *Id.* at 139–40.

Defendant Denari was acting as a CPO by, among other things, soliciting, accepting, and receiving funds from others for forex trading in the Pool. Denari had never been registered with the Commission in any capacity until May 1, 2019, and was not otherwise exempt or excluded from registration. Because Denari was not registered with the Commission as a CPO during the

Relevant Time until May 1, 2019, it violated Sections 4m(1) of the Act and Regulation 5.3(a)(2)(i).

Capson and Sarkar were acting as APs of CPOs by, among other things, soliciting, accepting and receiving funds from others for forex trading in the Denari Pool. Capson and Sarkar had never been registered with the Commission in any capacity until May 1, 2019, and they are not otherwise exempt or excluded from registration. Because they were not registered with the Commission as APs of CPOs during the Relevant Time until May 1, 2019, they violated Section 4k(2) of the Act and Regulation 5.3(a)(2)(ii).

C. Defendants Failed To Properly Receive and Commingled Pool Participant Funds in Violation of Regulation 4.20(a)-(c)

Defendants did not operate the Denari Pool as an entity cognizable as a legal entity separate from its CPO, received funds in names other than the Denari Pool and also commingled pool funds with non-pool funds. (McCormack ¶ 13, 14 and 18.) Regulation 4.20(a) requires that a CPO operate its commodity pool as an entity cognizable as a legal entity separate from its operator; Regulation 4.20(b) prohibits CPOs, whether registered or not, from receiving pool funds in any name other than that of the pool[6]; and Regulation 4.20(c) prohibits a CPO, whether registered or not, from commingling the property of any pool it operates with the property of any other person.

During the Relevant Period, Denari, while acting as a CPO for the Pool, violated Regulation 4.20(a) by failing to operate the Pool as a separate legal entity from the CPO and violated Regulation 4.20(b) by receiving pool funds that were not in the name of the Pool when they deposited pool funds into the bank and trading accounts of Denari. Defendants violated Regulation 4.20(c) by commingling pool funds with non-pool funds when they transferred pool funds into accounts that held non-pool funds and transferred non-pool funds into accounts that held pool funds.

[6] Regulation 5.4, 17 C.F.R. § 5.4 (2019), states that Part 4 of the Regulations, 17 C.F.R. pt. 4, applies to any person required to register as a CPO pursuant to Part 5 of the Regulations relating to forex transactions. 17 C.F.R. pt. 5.

D. Defendants Failed To Provide Pool Participants with Disclosure Documents in Violation of Regulations 4.21, 4.24 and 4.25

CPOs are required to provide pool participants with certain disclosures. Regulation 4.21, 17 C.F.R. § 4.21 (2019), provides that

> each commodity pool operator registered or required to be registered under the Act must deliver or cause to be delivered to a prospective participant in a pool that it operates or intends to operate a Disclosure Document for the pool prepared in accordance with §§ 4.24 and 4.25 by no later than the time it delivers to the prospective participant a subscription agreement for the pool . . . .

Regulation 4.24, 17 C.F.R. § 4.24 (2019), outlines in detail twenty-three types of general disclosures required for pools. Regulation 4.25, 17 C.F.R. § 4.25 (2019), outlines in detail the performance disclosures required for pools, including performance disclosures for different points in time of the pool's operating history.

Denari, Capson, and Sarkar failed to provide prospective participants with a pool disclosure document in the form specified in Regulations 4.24 and 4.25. Defendants Joint Venture Agreements and Promissory Notes do not include the required cautionary statement to participants or a full and complete risk disclosure, including the risks involved in retail forex trading. In addition to Defendants' lack of cautionary statements and risk disclosures, Defendants also failed to provide participants with additional required information, including but not limited to fees and expenses incurred by the pool, past performance disclosures, and a statement that the CPO is required to provide all participants with monthly or quarterly account statements, as well as an annual report containing financial statements certified by an independent public accountant. Therefore, Defendants violated Regulations 4.21, 4.24 and 4.25.

E. Capson Made Misrepresentations to NFA

Section 9(a)(4) of the Act makes it unlawful for any person willfully to falsify, conceal, or cover up by trick, scheme, or artifice a material fact, or to make any false, fictitious, or fraudulent statements or representations, or to make or use any false writing or document

knowing the same to contain any false, fictitious, or fraudulent statement or entry to a registered entity, board of trade, swap data repository, or futures association designated or registered under the Act and acting in furtherance of its official duties under the Act. This provision applies to the representations made by Capson to NFA in this case, since NFA is a futures association designated or registered under the Act, acting in furtherance of its official duties under the Act. *See, e.g., U.S. Commodity Futures Trading Comm'n v. Crombie*, 914 F.3d 1208, 1212 (9th Cir. 2019).

Capson violated Section 9(a)(4) of the Act by willfully concealing material facts and by making false statements or representations to NFA, a futures association registered under the Act, in connection with an examination that NFA conducted of Denari beginning in July 2019 in furtherance of NFA's official duties under the Act. Capson lied to NFA about the source of the funds in Denari's trading account in order to conceal that Denari was using third-party investor funds to trade in its forex pool, and was operating an unregistered commodity pool.

F. Defendants Are Derivatively Liable for Each Other's Misconduct.

1. Capson and Sarkar Are Liable as Control Persons.

Section 13(b) of the Act, 7 U.S.C. § 13c(b) (2012) provides that "Any person who, directly or indirectly controls any person who has violated any provision of this Act or any of the rules, regulations, or orders issued pursuant to this Act may be held liable for such violation in any action brought by the Commission to the same extent as such controlled person. In such action, the Commission has the burden of proving that the controlling person did not act in good faith or knowingly induced, directly or indirectly, the act or acts constituting the violation." A "fundamental purpose" of the statute is "to reach behind the corporate entity to the controlling individuals of the corporation and to impose liability for violations of the Act directly on such individuals as well as on the corporation itself." *R.J. Fitzgerald*, 310 F.3d at 1334 (quoting *JCC, Inc. v. CFTC*, 63 F.3d 1557, 1567 (11th Cir. 1995)) (internal quotation marks omitted). To

establish controlling person liability under Section 13(b) of the Act, the Division must show: (1) control; and (2) lack of good faith or knowing inducement of the acts constituting the violation. *In re First Nat'l Trading Corp.*, CFTC No. 990-28, 1994 WL 378010, at *11 (Jul. 20, 1994), *aff'd without opinion sub nom. Pick v. CFTC*, 99 F.3d 1139 (6th Cir. 1996).

To establish control, a defendant must possess general control over the operation of the entity principally liable. *See, e.g., R.J. Fitzgerald*, 310 F.3d at 1334 (recognizing an individual who "exercised the ultimate choice-making power within the firm regarding its business decisions" as a controlling person). Evidence that a defendant is an officer, founder, principal or the authorized signatory on the company's bank accounts indicates the power to control a company. *In re Spiegel*, CFTC No. 85-19, 1988 WL 232212, at *8 (Jan. 12, 1988).

Here, Capson and Sarkar controlled Denari, and knowingly induced, directly or indirectly, all the conduct which constituted violations of the Act. Capson and Sarkar are the sole owners, principals and managers of Denari. Capson and Sarkar are and have been signatories on Denari's bank accounts, and controlled all decisions and all company funds. (McCormack Dec. ¶ 13.) They also controlled all aspects of Denari's solicitations and promotional materials, as well as the issuance of account statements. Capson and Sarkar clearly have general control over Denari.

The evidence also shows that Capson and Sarkar failed to act in good faith or knowingly induced the acts constituting the violations of Denari. To establish "that a controlling person knowingly induced conduct which violates the Act, the Division must show that the controlling person had actual or constructive knowledge of the core activities that constitute the violation at issue and allowed them to continue." *JCC, Inc.*, 63 F.3d at 1568. To support a finding of constructive knowledge of wrongdoing, the Commission must show that a defendant "lacked actual knowledge only because he consciously avoided it." *Id*. at 1569 (citations omitted).

Here, Capson and Sarkar were the only two people who operated all aspects of Denari's business. They had intimate knowledge of all of Denari's interactions with investors and all of Denari's transactions. Capson and Sarkar knew, for example, that: (1) Denari's promotional material contained inaccurate trading performance for the Pool; (2) not all funds deposited by certain participants specifically for pool trading would be used to trade, but rather that Capson and Sarkar would misappropriate them for their own uses; and (3) that the account statements issued by Denari were false. Consequently, pursuant to Section 13(b) of the Act, 7 U.S.C. § 13c(b) (2012), Capson and Sarkar knowingly induced Denari's violations, thus making them liable for all of the entity's violations of the Act.

2. Denari is Liable for the Acts of its Agents

Section 2(a)(1)(B) of the Act, 7 U.S.C. § 2(a)(1)(B) (2012), and Regulation 1.2, 17 C.F.R. § 1.2 (2014) provide that the "act, omission, or failure of any official, agent, or other person acting for any individual, association, partnership, corporation, or trust within the scope of his employment or office shall be deemed the act, omission, or failure of such individual, association, partnership, corporation, or trust, as well as of such official, agent, or other person."

Under Section 2(a)(1)(B) of the Act and Regulation 1.2, strict liability is imposed upon principals for the actions of their agents acting within the scope of their employment. *Dohmen-Ramirez v. CFTC*, 837 F.2d 847, 857-58 (9th Cir. 1988); *Rosenthal & Co. v. CFTC*, 802 F.2d 963, 966 (7th Cir. 1986). Because Capson and Sarkar committed the alleged violations while acting on behalf of Denari, Denari is liable for Capson and Sarkar's violations of the Act pursuant to Section 2(a)(1)(B) of the Act and Regulation 1.2.

V. APPOINTMENT OF A TEMPORARY RECEIVER

The CFTC requests that the Court appoint a temporary receiver to administer any preliminary injunctive relief ordered by this Court. The appointment of a temporary receiver is authorized by 7 U.S.C. § 13a-1(a) and pursuant to this Court's equitable authority, to administer the relief granted by a preliminary injunction order and to perform such other duties as the Court may consider appropriate. *E.g., CFTC v. Co Petro Marketing Group, Inc.*, 680 F.2d 573 (9th Cir.1982) ("We have little difficulty in finding that section 6c is broad enough to authorize the appointment of a receiver, an order requiring that the receiver have access to the firm's books and records, and an order for an accounting."); *Matter of McGaughey*, 24 F.3d 904, 907 (7th Cir.1994) ("[f]ederal courts have an inherent equitable power to appoint a receiver to manage a defendant's assets during the pendency of litigation"). The CFTC recommends the appointment of receivers in cases where the defendants have engaged in fraud. As the former Fifth Circuit recognized:

> The district court's exercise of its equity power in this respect is particularly necessary in instances in which the corporate defendant, through its management, has defrauded members of the investing public; in such cases, it is likely that, in the absence of the appointment of a receiver to maintain the status quo, the corporate assets will be subject to diversion and waste to the detriment of those who were induced to invest in the corporate scheme and for whose benefit, in some measure, the SEC injunctive action was brought.

SEC v. First Fin. Grp., 645 F.2d 429, 438 (5th Cir. Unit A 1981); *see also FTC v. U.S. Oil & Gas Corp.*, 748 1431, 1432 (11th Cir. 1984). The decision to appoint an equity receiver in enforcement actions under the Act is a matter within the sound discretion of the trial judge. *CFTC v. Am. Commodity Grp. Corp.*, 753 F.2d 862, 866 n.6 (11th Cir. 1984); *see also Noble Metals Int'l, Inc.*, 67 F.3d 766, 775 (9th Cir. 1995) (noting district court's discretion to fashion preliminary relief in CFTC enforcement action, including an asset freeze).

VI. CONCLUSION

For the foregoing reasons, the CFTC respectfully requests that the Court enter a preliminary injunction: (1) prohibiting Defendants from destroying or refusing to permit the CFTC from inspecting and copying, when and as requested, all books and records or other documents; (2) freezing Defendants' assets; (3) compelling an accounting from Defendants; and (4) appointing a temporary receiver to administer the preliminary injunction. The CFTC also has moved for entry of an order granting leave to conduct expedited discovery pursuant to Fed. R. Civ. P. 26(d) in a separate motion.

Date: November 8, 2019

/s/ Carlin R. Metzger

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CERTIFICATE OF SERVICE

I, Carlin Metzger, an attorney with the U.S. Commodity Futures Trading Commission, certify that I served the CFTC's Motion for Preliminary Injunction upon counsel for Defendants listed below, who have been representing Defendants in connection with the CFTC's investigation prior to the filing of the CFTC's action against Defendants, via e-mail, on November 8, 2019.

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