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NATIONAL FUTURES ASSOCIATION
LEGAL DOCKETING

**NATIONAL FUTURES ASSOCIATION**
**BEFORE THE**
**BUSINESS CONDUCT COMMITTEE**

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|---|---|---|
| In the Matter of: | ) | |
| | ) | |
| TRADINGEDGE CAPITAL MANAGEMENT (NFA ID #424519), | ) | |
| | ) | |
| and | ) | NFA Case No. 12-BCC-013 |
| | ) | |
| TIMOTHY J. KARLIN (NFA ID #424911), | ) | |
| | ) | |
| Respondents. | ) | |

## COMPLAINT

Having reviewed the investigative report submitted by the Compliance Department of National Futures Association ("NFA"), and having reason to believe that NFA Requirements are being, have been, or are about to be violated and that the matter should be adjudicated, NFA's Business Conduct Committee issues this Complaint against TradingEdge Capital Management ("TCM") and Timothy J. Karlin ("Timothy Karlin").

## ALLEGATIONS

### JURISDICTION

1. At all times relevant to this Complaint, TCM was a commodity trading advisor ("CTA") NFA Member located in Topeka, Kansas. As such, TCM was and is required to comply with NFA Requirements and is subject to disciplinary proceedings for violations thereof.

2. At all times relevant to this Complaint, Timothy Karlin was TCM's sole associated person ("AP") and listed principal and an NFA Associate. As such, he was required to comply with NFA Requirements and is subject to disciplinary proceedings for violations thereof.

## BACKGROUND

3. TCM has been a registered CTA since November 29, 2010. On September 2, 2011, TCM was also approved as a forex firm. TCM has never had a disclosure document accepted by NFA.

4. On January 18, 2012, TCM attempted to list Jerome DeFries ("DeFries") as a principal of the firm. However, NFA's registration system flagged DeFries' application as a result of a 1999 complaint filed against DeFries by the U.S. Securities and Exchange Commission ("SEC") which alleged that DeFries carried out an eight million dollar Ponzi-style fraud and also obstructed the SEC's investigation. After NFA asked Timothy Karlin for more information regarding the SEC's action against DeFries, TCM withdrew DeFries' principal application on January 27, 2012.

5. Given DeFries' possible involvement in TCM, NFA commenced an unannounced audit of TCM on February 13, 2012.

## APPLICABLE RULES

6. NFA Compliance Rule 2-36(b)(2) provides that no Forex Dealer Member ("FDM") or Associate of an FDM engaging in any forex transaction shall willfully make or cause to be made a false report, or willfully to enter or cause to be entered a false record in or in connection with any forex transaction.

7. NFA Compliance Rule 2-39(a) provides that except for Members who meet the criteria in Bylaw 306(b) and Associates acting on their behalf, Members and Associates who solicit customers, introduce customers to a counterparty, or manage accounts on behalf of customers in connection with forex transactions shall comply with Sections (a), (b), (c), (d), (e), (h), and (l) of Compliance Rule 2-36.

8. NFA Registration Rule 208 provides, in pertinent part, that an applicant for registration as a CTA must comply with the provisions of Rule 204(a)(2) for each individual who is a principal of the applicant at the time the applicant files its application for registration; and within 20 days after any person becomes a principal of an applicant or registrant subsequent to the filing of Form 7-R in accordance with Rule 204, the applicant or registrant must, if the new principal is an individual, comply with the provisions of Rule 204(a)(2) for each new principal.

9. NFA Compliance Rule 2-36(e) provides that each FDM shall diligently supervise its employees and agents in the conduct of their forex activities for or on behalf of the FDM. Each Associate of an FDM who has supervisory duties shall diligently exercise such duties in the conduct of that Associate's forex activities for or on behalf of the FDM.

## COUNT I

## VIOLATIONS OF NFA COMPLIANCE RULE 2-36(b)(2): DISTRIBUTING FALSE TRADING STATEMENTS TO TCM'S LENDERS.

10. The allegations contained in paragraphs 1 through 7 are realleged as paragraph 10.

11. During NFA's audit of TCM, NFA reviewed the firm's bank statements and noticed a series of deposits into the firm's operating account from a number of individuals. When NFA questioned Timothy Karlin regarding these deposits, he said that that they were loans to him and his brother, Michael Karlin, for the purpose of starting TCM. The loans totaled approximately $77,000 and were made by John F. McGivern, John A. McGivern, Mark McGivern and Daniel Cain (hereafter collectively referred to as lenders). Collectively, the lenders have been repaid about $16,000 and are still owed approximately $61,000.

12. Approximately $20,000 of the loan proceeds were used as an initial deposit to open a forex trading account with the goal of developing a performance track record for TCM. Michael Karlin was the designated trader for the account. The account eventually suffered trading losses of $19,994 – nearly 100% of the $20,000 initially deposited in the account.

13. Rather than disclose this nearly 100% trading loss to the lenders, Michael Karlin, while acting on behalf of TCM, prepared and distributed to the lenders falsified trading statements which showed that the account had a gain of $9,419 (i.e., a return of 47%).

14. Timothy Karlin -- who represented that he was unaware that the trading account had sustained trading losses or that his brother, Michael, had distributed falsified statements to the lenders – notified the lenders that the statements previously provided to them by TCM and Michael Karlin were false and that the trading account had actually suffered a loss of nearly 100%. He also informed

the lenders that Michael Karlin had repaid TCM approximately $18,000 of the $20,000 originally deposited into the account.

15. By reason of the foregoing acts and omissions, TCM is charged with violations of NFA Compliance Rule 2-36(b)(2), as incorporated by and through NFA Compliance Rule 2-39(a).

## COUNT II

## VIOLATIONS OF NFA REGISTRATION RULE 208: FAILING TO LIST MICHAEL KARLIN AS A PRINCIPAL OF TCM.

16. The allegations contained in paragraphs 1 through 5 and 8 are realleged as paragraph 16.

17. Michael Karlin was jointly and severally liable, along with his brother, Timothy Karlin, for the loans they received from the lenders. Michael Karlin, together with his brother, was also jointly responsible for the firm's operations. Moreover, Michael Karlin was solely responsible for the trading in the firm's forex trading account.

18. As evidenced by these circumstances, Michael Karlin exerted a controlling influence over TCM and, therefore, should have been listed as a principal of the firm, but he was not so listed.

19. By reason of the foregoing acts and omissions, TCM is charged with violations of NFA Registration Rule 208.

## COUNT III

**VIOLATIONS OF NFA COMPLIANCE RULE 2-36(e): FAILING TO DILIGENTLY SUPERVISE TCM'S OPERATIONS.**

20. The allegations contained in paragraphs 1 through 5, 7 and 9 are realleged as paragraph 20.

21. Timothy Karlin, as the only AP and principal of TCM, had a duty to diligently supervise the activities of TCM, which included listing Michael Karlin as a principal of TCM, monitoring the trading activity in the forex account, and ensuring that TCM accurately reported the account's performance to TCM's lenders.

22. However, as alleged above, Timothy Karlin failed to list Michael Karlin as a principal of TCM, and he was totally unaware of the trading losses in the forex account or that lenders had received false trading statements. These shortcomings evidence a failure on the part of Timothy Karlin and TCM to diligently supervise TCM.

23. By reason of the foregoing acts and omissions, Timothy Karlin and TCM are charged with violations of NFA Compliance Rule 2-36(e), as incorporated by and through NFA Compliance Rule 2-39(a).

## PROCEDURAL REQUIREMENTS

## ANSWER

You must file a written Answer to the Complaint with NFA within thirty (30) days of the date of the Complaint. The Answer shall respond to each allegation in the Complaint by admitting, denying or averring that you lack sufficient knowledge or information to admit or deny the allegation. An averment of insufficient knowledge or

information may only be made after a diligent effort has been made to ascertain the relevant facts and shall be deemed to be a denial of the pertinent allegation.

NFA staff is authorized to grant such reasonable extensions of time in which an Answer may be filed as it deems appropriate.

The place for filing an Answer shall be:

National Futures Association
300 South Riverside Plaza, Suite 1800
Chicago, Illinois 60606
Attn: Legal Department-Docketing

E-Mail: Docketing@nfa.futures.org
Facsimile: 312-781-1672

Failure to file an Answer as provided above shall be deemed an admission of the facts and legal conclusions contained in the Complaint. Failure to respond to any allegation shall be deemed an admission of that allegation. Failure to file an Answer as provided above shall be deemed a waiver of hearing.

**POTENTIAL PENALTIES, DISQUALIFICATION AND INELIGIBILITY**

At the conclusion of the proceedings conducted as a result of or in connection with the issuance of this Complaint, NFA may impose one or more of the following penalties:

(a) expulsion or suspension for a specified period from NFA membership;

(b) bar or suspension for a specified period from association with an NFA Member;

(c) censure or reprimand;

(d) a monetary fine not to exceed $250,000 for each violation found; and

(e) order to cease and desist or any other fitting penalty or remedial action not inconsistent with these penalties.

The allegations herein may constitute a statutory disqualification from registration under Section 8a(3)(M) of the Commodity Exchange Act. Respondents in this matter who apply for registration in any new capacity, including as an AP with a new sponsor, may be denied registration based on the pendency of this proceeding.

Pursuant to the provisions of Commodity Futures Trading Commission ("CFTC") Regulation 1.63, penalties imposed in connection with this Complaint may temporarily or permanently render Respondents who are individuals ineligible to serve on disciplinary committees, arbitration panels and governing boards of a self-regulatory organization, as that term is defined in CFTC Regulation 1.63.

**NATIONAL FUTURES ASSOCIATION**
**BUSINESS CONDUCT COMMITTEE**

Dated: 04/13/2012

By: _____
Chairperson

/jac(Complaints\TradingEdge_Karlin 2012)

**AFFIDAVIT OF SERVICE**

I, Nancy Miskovich-Paschen, on oath state that on April 13, 2012, I served a copy of the attached Complaint, by sending such copy by e-mail, overnight mail and regular mail, first-class delivery, in envelopes addressed as follows to:

TradingEdge Capital Management
1320 SW 27th Street
Apt. J68
Topeka, KS 66611
Attn: Timothy Karlin
E-mail: tkar@sbcglobal.net

Nancy Miskovich-Paschen

Nancy Miskovich-Paschen

Subscribed and sworn to before me
on this 13th day of April 2012.

Mary A. Patton

Notary Public

OFFICIAL SEAL
MARY A PATTON
NOTARY PUBLIC, STATE OF ILLINOIS
MY COMMISSION EXPIRES 08/28/2013