

FILED

DEC - 2 2010

NATIONAL FUTURES ASSOCIATION
BEFORE THE
HEARING PANEL

NATIONAL FUTURES ASSOCIATION
LEGAL DOCKETING

| | | |
|---------------------|---|-------------------------|
| In the Matter of: |) | |
| |) | |
| FOREX LIQUIDITY LLC |) | |
| (ROBERT F. GRAY |) | NFA Case No. 08-BCC-023 |
| NFA ID #196740), |) | |
| |) | |
| Respondent. |) | |

DECISION

On July 7, 2010, a designated Panel of the Hearing Committee held a hearing to consider the charges against Robert F. Gray (Gray). The Panel issues the following Decision under National Futures Association (NFA) Compliance Rule 3-10.

I

PROCEDURAL BACKGROUND

On September 26, 2008, NFA's Business Conduct Committee issued a one-count Complaint against Forex Liquidity LLC (Forex Liquidity) and Gray.¹ The Complaint charged that Gray violated NFA Compliance Rules 2-5, 2-36(b)(5), 2-36(c) and 2-36(e) because he failed to cooperate with NFA's investigation of Forex Liquidity's capital condition; failed to maintain current books and records for Forex Liquidity; provided false and misleading information to NFA; failed to uphold high standards of commercial honor and just and equitable principles of trade; and failed to supervise Forex Liquidity's financial condition, or its preparation and maintenance of required

¹ Forex Liquidity was not a party in this hearing because the firm is currently under the control of a receiver and therefore NFA has stayed its proceeding against the firm.

books and records. On October 29, 2008, Gray filed an Answer, where he denied the material allegations in the Complaint.

II

EVIDENCE PRESENTED AT THE HEARING

NFA presented one witness at the hearing and introduced a number of documents into evidence. Gray testified on his own behalf. A summary of the evidence follows:

Jennifer Sunu

Jennifer Sunu (Sunu), a Director in NFA's Compliance Department, testified substantially as follows:

Forex Liquidity has been an NFA Member futures commission merchant (FCM) since February 2006. Gray is a listed principal of Forex Liquidity, as well as a registered associated person (AP) of the firm and an NFA Associate. Forex Liquidity stopped doing business in December 2007 because NFA issued a Member Responsibility Action (MRA) against the firm. An MRA is an emergency action, and NFA took this action against Forex Liquidity because Forex Liquidity was unable to demonstrate that it was in compliance with the capital requirements of a forex dealer member (FDM). The MRA effectively prevents the firm from doing any business. In particular, the MRA prohibited Forex Liquidity from accepting any new customers or funds from existing customers, from placing any trades except to rollover existing trades, disbursing any funds from any of its accounts without NFA's approval and required Forex Liquidity to transfer assets that were held at other financial institutions to either its account at U.S. Bank or to an NFA Member FCM. Finally, the MRA required Forex Liquidity to produce financial statements including net capital computations as of

December 4, 2007 and provide support for the balances listed on those financial statements.

At the time of the MRA, an FDM's capital requirement was \$1 million. However, NFA had recently notified FDMs that over the next eighteen months, the capital requirement would be increasing from approximately \$5 million (effective December 31, 2007) to \$20 million (effective May 2009).

NFA began an audit of Forex Liquidity in August 2007. As part of the audit, NFA tested the firm's June 30, 2007 financial statement. NFA also reviewed March, April and May 2007 financial statements that were submitted to NFA in the months prior to the June 30 statement in order to identify any trends or unusual financial circumstances. In reviewing these statements, staff noticed that there was a significant increase in current assets between the March 2007 and the April 2007 financial statements. Specifically, beginning in April 2007 and carrying through to the June 2007 statement, Forex Liquidity's current assets included \$35 million in firm securities purportedly owned by the firm. The net effect of this current asset balance was to increase the firm's adjusted net capital from approximately \$2.8 million in March to over \$38 million in June.

When NFA asked Gray about the increase in Forex Liquidity's capital, he indicated that he personally had received a corporate bond issued by ABN-AMRO in the amount of \$50 million, and that he had given the bond to Forex Liquidity for it to use for its capital. Gray also told NFA that he listed the bond's value as \$35 million on Forex Liquidity's financial books because he wanted to be able to withdraw some of the funds without having to report to the Commodity Futures Trading Commission (CFTC) a substantial decrease in Forex Liquidity's adjusted net capital.

In addition, Gray told NFA that he had received the bond from a company called Swiss Imperial Trust (SIT), which was located in Switzerland. He had entered into an agreement with this company to begin doing forex retail business in China. The bond was supposed to cover the cost of certain projects outlined in the agreement.

Gray gave NFA statements from an entity called Malory Investments (Malory). The statements included both statements for Gray's personal account and statements for Forex Liquidity's account. The February 2007 statement for Gray's account purports to show that he had net assets of \$50 million, which was made up of \$50 million in ABN-AMRO securities. Gray's March 2007 statement shows that the portfolio value is \$0 because there was a \$50 million withdrawal on March 14. On that day, there was a transfer of the ABN-AMRO bond from Gray's account to Forex Liquidity's account. Forex Liquidity's March 2007 statement shows net portfolio assets of \$43.8 million. The statement shows that on March 14, there was a deposit of \$50 million labeled ABN-AMRO bond and then a transfer out of the account of \$6.1 million to another Malory account. Forex Liquidity's monthly statements for April, May and June 2007 show the same \$43.8 million balance.

After NFA received these statements, staff sent a confirmation request to Malory seeking its confirmation of the existence and value of the bond. On August 13, 2007, NFA received a response from Robert Stein, Malory's president, confirming that Malory was holding an ABN-AMRO bond in the account of Forex Liquidity with an approximate value of \$43.8 million.

In November 2007, FINRA contacted NFA regarding its investigation involving Malory Investments and a series of transactions involving Malory and Forex Liquidity. In particular, FINRA was concerned about the dollar amounts of the

transactions because Malory had historically been a relatively inactive firm that did not hold customer funds. The FINRA representative also told NFA that FINRA had questioned Malory about the \$50 million ABN-AMRO bond and that Malory told them that the bond was in an account in Malory's name at SIT.

FINRA provided NFA with copies of statements from SIT. The statements purported to show that Malory had an account at SIT and that Malory had the bond deposited in that account.

After receiving these documents, Sunu called Gray and told him that NFA was concerned that it appeared that the bond had never actually left Switzerland, that Malory was not holding the bond, and although Forex Liquidity was reporting the bond as a current asset, Forex Liquidity did not actually have control over the bond. Given these concerns, NFA notified Forex Liquidity through Gray that in order for Forex Liquidity to be in compliance with NFA's capital requirement, the firm had to move the bond from SIT to a U.S. regulated financial institution by 5:00 p.m. on November 30, 2007. On December 1, Gray sent NFA an e-mail indicating that he had transferred the bond. Gray subsequently told NFA that the bond was being held at Commonwealth Financial Network (CFN) and provided NFA with the account number. CFN, however, informed NFA that it did not have an account in Forex Liquidity's name. The next day, NFA received a letter from an individual named Tom Smith on letterhead entitled Commonwealth Financial P.M.S. The letterhead also included a website address, which was the website for CFN. In that letter, Smith confirmed that Forex Liquidity had deposited the bond at the firm. After NFA received this letter, staff again contacted CFN. A CFN representative indicated that Commonwealth P.M.S. was not an affiliate or subsidiary and that he was not familiar with the firm. Sunu then contacted Smith at the

telephone number listed on the letter. Smith stated that Commonwealth P.M.S. was an affiliate of CFN and was registered as a broker-dealer and he provided NFA with a CRD number for Commonwealth P.M.S. Smith also told Sunu that although Forex Liquidity had an account with Commonwealth P.M.S., he could not verify the amount of funds that Forex Liquidity had on deposit with the firm because privacy laws prevented him from doing so. Smith also claimed that privacy laws prevented him from giving Sunu any information on his supervisors. NFA did not have any direct evidence that Gray fraudulently procured the letter to provide NFA.

When Sunu attempted to verify the CRD number with FINRA, FINRA staff indicated that that CRD number had not been in use since 1991 and had never been associated with Commonwealth P.M.S. FINRA staff also indicated that Commonwealth P.M.S. had never been a FINRA member or registered as a broker-dealer.

Given this set of circumstances, NFA instructed Gray to transfer the bond to Forex Liquidity's account at U.S. Bank. Gray indicated, however, that he did not believe that he needed to include the bond as an asset in order to meet Forex Liquidity's capital requirement. Gray provided NFA with two net capital computations for November 30, 2007. One calculation included the bond and the other did not. Although the calculation without the bond indicated that Forex Liquidity was in compliance with its capital requirement, NFA was concerned with some of the assets that made up the firm's capital.

One line item was \$11.2 million being held at Malory. Given the problems NFA uncovered with respect to the bond being held at Malory, NFA was concerned that the \$11.2 million might not be at Malory. As a result, NFA instructed Gray to move the funds at Mallory to Forex Liquidity's bank account at U.S. Bank. At that point, Gray told

NFA that the funds were not actually at Malory, but were held at a company called Profi, which is a forex dealer located San Marino, a country near Italy. Gray told NFA, however, that Profi would be returning those funds directly to Forex Liquidity. Over the next several days, approximately \$4 million was transferred from Profi to Forex Liquidity's account at U.S. Bank. A few days later, however, Forex Liquidity's attorney provided NFA with a copy of a letter from Profi to Forex Liquidity, which indicated that Profi had been instructed by Malory that the funds could not go directly to Forex Liquidity, but had to be sent through Malory. Profi indicated that they would not be transferring the remaining \$7 million and they requested that Forex Liquidity return the \$4 million already sent. Given the uncertainty of whether Forex Liquidity would ever receive the additional \$7 million and the claim against the \$4 million, NFA determined that Forex Liquidity should not include any of the \$11 million for capital purposes.

NFA was also concerned that the November 30, 2007 capital calculation showed liabilities that were approximately \$10 million less than the prior month's reported liabilities. When NFA asked Gray to provide evidence that this reduced liability number was correct, Gray told NFA that the November 30 number was not correct because they had failed to include the liabilities owed to other forex dealers. As a result of these two adjustments, Forex Liquidity was severely undercapitalized.

NFA did not have any evidence that Gray was involved in creating the Malory statements. NFA also did not have any evidence to establish unquestionably that the bond did not exist, except for the fact that Gray and Forex Liquidity were never able to move the bond from Malory or SIT to Forex Liquidity's account.

NFA did not attempt to confirm the existence of the bond with SIT. Since NFA was unfamiliar with the entity and would not be sure that any information it provided was accurate, NFA felt the most prudent action would be to require Forex Liquidity to move the bond to a U.S. institution. Sunu acknowledged that NFA could not definitively prove that the bond did not exist. However, if Gray was including the bond on Forex Liquidity's financial statements as a current asset, he should have had evidence that he or Forex Liquidity had control of the asset.

Robert Gray

Gray testified substantially as follows:

The agreement between Gray and SIT was a loan agreement. Under the agreement, Gray could borrow up to \$50 million from SIT. Gray and Forex Liquidity were planning on expanding Forex Liquidity's forex business in China. SIT provided Gray with this bond for Forex Liquidity to use to meet capital so that Forex Liquidity's cash could be used to expand in China. During the course of the contract, Gray and Forex Liquidity paid approximately \$1.5 million in interest to either SIT's counsel or its financial office.

Forex Liquidity's insurance company referred Gray to Malory. Gray believes he opened a personal account, as well as an account for Forex Liquidity at Malory prior to February 2007, when he entered into the agreement with SIT. Before opening the accounts, Gray checked Malory's status and background on their regulator's website.

Gray and Forex Liquidity had been doing business in Beijing since April or May 2006 with a firm in China called FXA. This company put Gray in touch with SIT. Gray did not meet with any representatives from SIT prior to entering into the agreement with the firm.

After NFA told Gray that he had to move the bond to a U.S. financial institution, Gray instructed Malory to do so. Malory decided to move the bond to Commonwealth P.M.S. Gray had never spoken to anyone at Commonwealth P.M.S. until he called Smith and asked for some type of confirmation that the bond had been deposited with Commonwealth P.M.S. Gray did not ask many questions about where Malory was transferring the bond. He was satisfied that Malory was transferring it to Commonwealth, which he understood to be a U.S. broker-dealer regulated by FINRA. Malory did not refer to it as Commonwealth P.M.S. and when he checked FINRA's website for the name Commonwealth, it indicated that Commonwealth had offices throughout the U.S. Gray never picked up on the distinction between Commonwealth and Commonwealth P.M.S., even after he received a copy of the letter sent from Tom Smith on letterhead that indicated the firm was Commonwealth P.M.S.

Gray denied that Sunu ever instructed him to have the bond transferred from Commonwealth P.M.S. She did, however, tell him that he had to transfer all of Forex Liquidity's counterparty funds to U.S. Bank.

Gray does not know what happened to the \$50 million. He never withdrew the funds from Commonwealth P.M.S. He did hire an investigator to investigate Commonwealth P.M.S. and Malory. From this investigation, he learned that Malory had been suspended from doing business in California and had numerous actions pending in other states for selling questionable investment products.

Gray did receive a copy of the MRA issued by NFA on December 4. However, until the time of this hearing he had never looked at paragraph 5 of the MRA, which instructed Forex Liquidity to transfer any and all assets not currently held at U.S. Bank or an NFA Member FCM to U.S. Bank or an NFA Member FCM by 3:00 p.m. on December 5.

During the ten-day period between when the MRA was filed and the receiver took over, Gray did not give NFA corrected capital computations because Forex Liquidity was redoing its financial information internally and it hadn't completed this process. Gray still believes that the firm was in capital compliance. Although Sunu's affidavit indicated that Forex Liquidity had \$19 million in assets, this was wrong because the firm had \$29 million in cash. Forex Liquidity had at least \$3 million in excess capital.

Gray did not believe that SIT, Malory and Commonwealth P.M.S. were initially in collusion to defraud him and Forex Liquidity. He does believe, however, that at some point they became connected with each other. Neither SIT, nor any other entity has come after him for "repayment" of the bond. Gray is not really sure what really happened to the bond or if it ever existed. He thinks he became overly aggressive and tried to expand too quickly.

III

FINDINGS, CONCLUSIONS AND PENALTY

Gray was an NFA Associate and a registered AP of Forex Liquidity during the period covered by the Complaint. Therefore, he was required to comply with NFA Requirements, and NFA has jurisdiction over him for purposes of this action.²

² See NFA Bylaw 301(b) and NFA Compliance Rule 2-14.

NFA's case against Gray was based primarily on the testimony of Sunu. Sunu provided a detailed chronology of the events leading up to NFA's MRA against Forex Liquidity, which also forms the basis of this Complaint. During NFA's investigation of the alleged bond that made up a substantial portion of Forex Liquidity's capital, Gray repeatedly provided NFA with information that upon investigation turned out not to be true. First, Gray told NFA that the bond was held at Malory Investments. When NFA learned from FINRA that the bond was not being held at Malory and that Malory had represented that the bond was being held in an account in its name at SIT, NFA directed Gray to have the bond transferred to a U.S. financial institution if Forex Liquidity wanted to include it as a current asset for capital purposes. Gray then told NFA that the money had been transferred to CFN, a registered broker-dealer, and provided NFA with an account number. When NFA followed up with CFN, however, NFA learned that the bond was not held there and that CFN did not have an account for Forex Liquidity. NFA then received a letter from an entity called Commonwealth Financial P.M.S. Although the letter confirmed that Forex Liquidity had over \$47 million on deposit at the firm, when NFA attempted to follow up with the firm, NFA was given more misleading information, including a representation that the firm was affiliated with CFN and a false CRD number.

When NFA told Forex Liquidity that it could not include this asset unless it was transferred to its account at U.S. Bank, Forex Liquidity represented that it could meet its capital requirement without the bond proceeds. Forex Liquidity provided NFA with a pro forma capital calculation that showed it had excess net capital of over \$11 million. However, when NFA reviewed the balances on the computation, it became

clear that some of these balances were inaccurate and that Forex Liquidity was not in capital compliance.

Gray did very little to refute the substance of Sunu's testimony. He admitted that he did little due diligence on firms that were purportedly holding a substantial portion of his firm's capital. Even when it should have been clear that NFA had grave concerns regarding his capital position, he took no real initiative to resolve the matters and gain control of funds supposedly belonging to the firm. Moreover, he submitted a capital computation to NFA without any attempt to verify its accuracy. It was clear that Gray had very little interest in the rules that governed his business. He even admitted that he had not fully read the MRA until the day of this hearing.

NFA's Complaint charged Gray with failing to cooperate promptly and fully with NFA, willfully submitting false and misleading information to NFA, failing to observe high standards of commercial honor and just and equitable principles of trade in conducting Forex Liquidity's forex business and failing to diligently supervise Forex Liquidity's financial condition and its preparation and maintenance of its financial records. There is no question that Gray failed to supervise Forex Liquidity's financial condition and its records. Gray permitted a substantial portion of the firm's net assets to be held at entities for which he did no due diligence. And, as noted above, even when it should have been apparent to Gray that there were significant issues with the existence of the bond, he did little or nothing to ascertain its existence. Moreover, when it should have been clear that NFA had serious doubts about Forex Liquidity's capital position, he provided NFA with a capital computation that was materially inaccurate. Based on this evidence, the Panel finds that Gray violated NFA Compliance Rule 2-36(e).

It's not surprising that the capital computation was materially inaccurate, however, since throughout NFA's investigation of Forex Liquidity Gray repeatedly gave NFA materially inaccurate information. Although Gray claims that he did not know that the information he provided to NFA was false, the Panel finds that if he wasn't purposefully providing NFA with false information, then he is completely inept at running a regulated business.

Therefore, even if the Panel accepts Gray's claim that he was unaware of the true situation and did not know he was providing NFA with false information, the Panel believes Gray acted with reckless disregard of his regulatory obligations, which is sufficient to find that he acted willfully. See *In re Squadrito*, [1990-1992 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 26,262 at 38,828 (CFTC March 27, 1992). As a regulated professional overseeing a regulated entity that holds customer funds, Gray had an obligation to ensure Forex Liquidity's assets were safe. Gray also had an obligation to make sure that Forex Liquidity was in compliance with its capital requirement and that any assets that were being reported as current were under Forex Liquidity's control. Gray, however, completely failed to execute these obligations. It is apparent from the overall circumstances and Gray's own testimony that he was more interested in expanding his business than ensuring that Forex Liquidity was in regulatory compliance. Gray had sufficient reason to doubt the information he was giving NFA, but he kept providing false information without attempting to determine whether any of it was true. Therefore, the Panel finds that Gray failed to cooperate promptly and fully with NFA in its investigation, willfully provided NFA with false and misleading information and failed to observe high standards of commercial honor and just and equitable principles of

trade in conducting Forex Liquidity's business, in violation of NFA Compliance Rules 2-5, 2-36(b)(5) and 2-36(c).

A number of factors must be considered when determining the appropriate sanction for this violation. One of the more significant is the nature of the violation. The evidence at the hearing showed that Gray repeatedly provided NFA with misleading information that hampered NFA's ability to complete its investigation of Forex Liquidity and its capital position. In addition, under Gray's control, Forex Liquidity was operating under its net capital requirement and Gray appeared not to understand the gravity of the situation. These are very serious violations and deserve a significant penalty.

Therefore, the Panel imposes the following sanction:

Gray may not be an NFA Member, Associate Member or principal of an NFA Member or act in a capacity that requires him to be listed as a principal for a period of ten years from the date of this Decision.

IV

APPEAL

Gray may appeal the Panel's Decision to the Appeals Committee of NFA by filing a written Notice of Appeal with NFA within fifteen days of the date of this Decision. Pursuant to NFA Compliance Rule 3-13(a), the Notice must describe those aspects of the disciplinary action to which exception is taken and must include any request to present written or oral arguments. The Decision shall be final after the expiration of the time for appeal or review unless it is appealed or reviewed.

V

INELIGIBILITY

Pursuant to the provisions of CFTC Regulation 1.63, this Decision and the sanctions imposed by it renders Gray ineligible to serve on a governing board,

disciplinary committee, oversight panel, or arbitration panel of any self-regulatory organization, as that term is defined in CFTC Regulation 1.63, until three years after the effective date of this Decision or until all of the sanctions and conditions imposed on Paul have been fulfilled, whichever is later.

**NATIONAL FUTURES ASSOCIATION
HEARING PANEL**

Dated: 12/02/2010

By: Wendy Robinson
Wendy Robinson,
Chairperson

(caw:BCC Cases/Forex Liquidity-Gray Decision)

AFFIDAVIT OF SERVICE

I, Nancy Miskovich-Paschen, on oath state that on December 2, 2010, I served copies of the attached Decision, by sending such copies in the United States Mail, postage prepaid, certified mail, return receipt requested, and by regular mail, first-class delivery, in envelopes addressed as follows:

David Stawick
Office of the Secretariat
Commodity Futures Trading
Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Terry Montgomery
Division of Enforcement
Commodity Futures Trading
Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

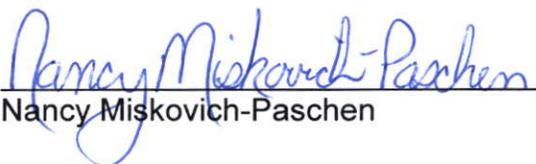
William Penner
Deputy Director
Commodity Futures Trading
Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Tempest Thomas
Proceedings Clerk
Office of Proceedings
Commodity Futures Trading
Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

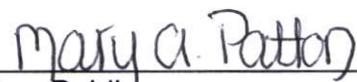
Dirk O. Julander, Esq.
Julander, Brown & Bollard
9110 Irvine Center Drive
Irvine, CA 92618

and by hand delivery to:

Ronald V. Hirst, Esq.
National Futures Association
300 South Riverside Plaza
Suite 1800
Chicago, IL 60606


Nancy Miskovich-Paschen

Subscribed and sworn to before me
on this 2nd day of December 2010.


Notary Public

