

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF FLORIDA

CASE NO. 11-60702-CIV-COOKE/TORRES

SECURITIES AND EXCHANGE COMMISSION,

Plaintiff,

v.

COMMODITIES ONLINE, LLC, and
COMMODITIES ONLINE MANAGEMENT,

Defendants.

**RECEIVER'S MOTION FOR COURT APPROVAL
OF PROPOSED CLAIMS PROCESS**

David S. Mandel, the Court-appointed Receiver of Commodities Online LLC and Commodities Online Management, LLC (together, "Commodities Online," "COL," or the Defendants), hereby moves this Court to approve the proposed procedure for use in determining claims asserted by victim/investors and other creditors including the Claim Form to be sent to those victim/investors and creditors. At this point, the Receiver is not asking the Court to resolve any issues about the claims, such as what types of claims will be recognized or how the assets of the Receivership Estate should be distributed.

Background

This Receivership resulted from the action brought by the Securities and Exchange Commission against the Defendants, charging them with violating federal securities laws by "duping investors into funding a fraudulent scheme and violating the antifraud and registration provisions of the federal securities laws." [D.E. 1]. Commodities Online, through its controlling members including convicted felons Louis N. Gallo III and James C. Howard, III, and others, conspired to defraud approximately 700 investors by making materially false and fraudulent

representations and omissions to induce victims to invest and/or purchase ownership interests in purportedly “pre-sold” commodities contracts. In reality, no contracts existed and the investors’ funds were commingled in Commodities Online accounts. The co-conspirators also falsely represented that COL had a track record of profits when, in fact, Commodities Online never made a profit and was insolvent at all times. A true Ponzi scheme by nature, any payments Commodities Online made to investors were made by using funds received from newer investors. Moreover, COL’s principals diverted the majority of the investors’ funds to themselves, to other co-conspirators, or to other companies they controlled.

At the outset of this case, the Court granted the Commission’s emergency motion for a temporary restraining order, and appointed the Receiver over the Defendants (“Receivership Order”). [D.E. 3 and 5]. On April 6, 2011, both Defendants consented to the entry of permanent injunctions and other relief, and on April 8, 2011, the Court entered judgments for disgorgement and civil penalties. [D.E. 8]. On August 23, 2011, the Court granted the Receiver’s motion requiring James C. Howard and Sutton Capital LLC to turn over and disgorge \$1,450,000 of investor funds to the Receiver. [D.E. 39]. After approximately one year of litigation, during which time Howard avoided complying with the Court’s order and never paid any money to the Receivership, on August 2, 2012, Howard filed for bankruptcy, and all creditors’ actions against him were stayed. [D.E. 213]. In addition, several individuals, including COL’s principals Louis Gallo and James Howard and others, pleaded guilty to conspiracy or other crimes in the federal criminal case *United States v. Howard, et al.*, 12-23620-Cr-Lenard, relating to their involvement in the COL fraud; in particular, Gallo and Howard were sentenced to lengthy prison terms, and each was ordered to pay financial penalties and restitution of approximately \$19 million.

In furtherance of his duties, the Receiver has acted to recover as much of the victim/investors funds as possible, including recovering funds from certain entities and

individuals, and bringing separate legal actions as appropriate. The details of the Receiver's efforts are set forth more fully in his periodic status reports.¹

Due to the illegal and/or fraudulent misconduct of Commodities Online's principals and co-conspirators, the Commodities Online Receivership has limited funds, substantially less than the amounts invested by the victim/investors. While Commodities Online investors have suffered substantial losses, the Receivership Estate's assets will be insufficient to make the investors whole. The purpose of the Receivership is to preserve and recover the assets that rightfully should belong to the Receivership Estate, with the ultimate goal of distributing those assets to the victims/investors and creditors who have suffered losses. [D.E. 5 at ¶¶1, 2, 24]. From the time the Receiver was appointed, he has recovered approximately \$950,000, through the prosecution and resolution of litigation claims against various parties who were responsible for the Receivership Entities' losses and other asset recovery efforts.² The turnover of approximately \$2,434,315 in funds from the frozen accounts in addition to the aforementioned \$950,000 raised the total receipts to approximately \$3,388,190. The payment of receivership expenses and professional fees totaling approximately \$1,480,291 has left a balance of approximately \$1,907,898 remaining in the Estate.

In order to fulfill his responsibilities, the Receiver proposes that the Court approve and adopt the claims process as set forth below.

¹ The Receiver's status reports are filed at Docket Entries 11, 22, 116, 159, 197, 221, 232, 246, 260, 274, 290, 300, and 302.

² This total does not include any future restitution that may be paid by Defendants Howard or Gallo, the judgments against George Saliba and Francisco Ortiz-Gonzalez, or the settlement with Martin Vegas.

Identification of Commodities Online Investor-Victims

The Receiver, his counsel and his forensic accountants reviewed the numerous files and the computer databases seized from Commodities Online as well as the subpoenaed financial records to identify the Commodities Online investors, when they invested in Commodities Online, and how much money they invested. In addition, many individuals have contacted the Receiver by both telephone and email regarding their investments in Commodities Online. This information has been compiled into a comprehensive database.

From January 1, 2010, when Commodities Online's bank accounts were opened, until April 1, 2011, when the Court entered the Receivership Order and froze Commodities Online's assets, approximately 700 individuals invested approximately \$19,119,805. Having consulted with counsel as well as with his forensic accountant Soneet Kapila, the Receiver believes that those persons who invested money in Commodities Online during that period should be entitled to receive a *pro rata* distribution from the Receivership Estate.

PROPOSED CLAIMS PROCESS

A. The Basis for Investor Claims.

The majority of the claims which the Receiver expects will be made against the Receivership estate are claims by defrauded investors. The Receiver proposes that the Claim Form that will be sent out to each investor should include pre-printed information as to the investor's total amount of money invested and the dates of investment. *See* Sample Claim Form attached hereto as Exhibit A. This process will be less burdensome for the investor, and less costly for the Receivership. If an investor disputes either the information provided on the Claim Form or the basis for their claim, the Form allows them to state any challenge and provide any supporting documents. This type of claims process has been recognized as providing sufficient protection to the due process rights of creditors. *See, e.g., SEC v. Hilton*, No. 12-cv-81033, D.E.

183 (S.D. Fla. Jun. 19, 2015) (Middlebrooks, J.) (granting receiver's motion to approve proposed claims process using same type of claim form); *SEC v. Homeland Communs. Corp.*, No. 07-cv-80802, 2010 U.S. Dist. LEXIS 57961, at *2-3 (S.D. Fla. May 24, 2010) (Marra, J.) (noting approval of receiver's recommended claim form where receiver recommended claim amount) (citing to D.E 121 Mar. 12, 2009, Order Approving Claims Process); *SEC v. TLC Investments and Trade Co.*, 147 F. Supp. 2d 1031, 1037 (C.D. Cal. 2001) ("regarding the pay out of claims to investors, the Receiver will initially contact the investors with a suggestion as to the amount of their claim based on the Receiver's reconstruction of the TLC entities' records. If an investor disagrees with that amount, he or she can inform the Receiver and ask for reevaluation").

Regarding the basis for the claims, although the Court need not decide this issue now, at the conclusion of the claims process the Receiver intends to assert that the most equitable and reasonable basis for determining the investors' claims is the amount of their investment and whether they invested in Commodities Online during the time period alleged in the Complaint. As is well established, the basis for investor claims should not include the amount the investor may have expected to make as a return on the investment, or the lost time value of their delayed investment return, or other expectancy-type damages claims. It is generally recognized that an investor in a fraudulent scheme is entitled to the return of his/her investment, but is not entitled to realize a profit from such a scheme. *See, e.g., CFTC v. Equity Financial Group, LLC*, 2005 U.S. Dist. LEXIS 20001, at *76-77 (D. N.J. Sept. 2, 2005) (adopting receiver's recommendation that "claims be recognized only for actual dollar amounts invested," and agreeing that "recognizing profits or other earnings in claims for distributions would be to the detriment of later investors and would therefore be inequitable"); *United States CFTC v. Wilson*, 2013 U.S. Dist. LEXIS 99992, at *18 (S.D. Cal. Jul. 17, 2013); *In re Receiver*, 2011 U.S. Dist. LEXIS 71961, at *7-8 (D. S.C. Jul. 1, 2011); *SEC v. Parish*, 2010 U.S. Dist. LEXIS 11757, at *16-24 (D. S.C. Feb. 10, 2010).

In addition, the logistics of attempting to determine the claims of lost profits would be extremely burdensome, and speculative. Even if the business of Commodities Online had been conducted legitimately, the investors had no guaranty that their investment would yield any particular return at any particular time; the true opportunity cost on an individual basis is thus impossible to quantify. Accordingly, the Receiver believes that each Commodities Online investor's claim should include only the amount of the actual cash investment.

B. Non-Investor/Creditor Claims.

Although the majority of claims that will be asserted against the Receivership Entities will be from the Commodities Online investors, there are others who may wish to assert claims as well. The non-investor claims could include trade creditors such as vendors, suppliers, and other potential claimants. Such claims would need to include the supporting documentation or other information corroborating the amount of the claim asserted (*e.g.*, invoices for any goods supplied or services rendered for which the payment was not received due to the institution of the Receivership).

It is clear, however, that the amount of money available for distribution in the COL Receivership will fall short significantly of the total needed to fully compensate the defrauded investors. As a result, the Receiver will likely seek the subordination or rejection of all non-investor claims at the conclusion of the claims process. In addition, even if the Court recognizes such claims, there are legal limitations on which assets currently held by the Receiver may be used for such claims. Most significantly, any funds from the disgorgement and penalties imposed upon the Defendants in the SEC action may only be distributed to the victim-investors, not to creditors. *See, e.g.*, 15 U.S.C. Section 7246.

Whether or not these claims are ultimately recognized by the Court, however, the Receiver submits that these non-investor claimants should be given the opportunity to file Claim Forms.

C. The Process for Resolving Claims.

The Receiver proposes that, after the Court approves the text and format for the Claim Form, the Receiver will send the Claim Form to all known investors and creditors within 20 days of the entry of the Order Approving the Claims Process. The Receiver proposes to send the Claim Form by email to all investors who have previously provided an email address as an accepted means of communication with them. *See, e.g., SEC v. Global Online Direct, Inc.*, 2007 U.S. Dist. LEXIS 88819, at *2-4 (N.D. Ga. Nov. 29, 2007) (finding receiver's email notice of claims process to investors in receivership entities satisfied due process where receiver possessed proper email addresses of investors); *SEC v. Hilton*, No. 12-cv-81033, D.E. 183 at 4 (S.D. Fla. Jun. 19, 2015) (granting receiver's motion to approve proposed claims process and allowing receiver to provide claims form by email to all investors who have previously provided their email address to the receiver). The Receiver will send the Claim Form to all other investors and other creditors by U.S. mail, or, if they reside outside the U.S., by priority international mail.

The Receiver recommends setting a 60-day period for returning all Claim Forms. The deadline, or the Claims Bar Date, will be printed on the Claim Form, and posted on the Receivership website. The Receiver will also publish a blank copy of the Claim Form on the website with instructions on how to complete and timely submit the form. Claimants will have the option to return the form by email, by fax, or by mail. For those investors to whom the Receiver will mail the Claim Form, the Receiver will include a pre-addressed return envelope to return the Claim Form. The envelope will not be pre-stamped or pre-paid for cost considerations. The Receiver will also publish a notice of the Claims Bar Date in South Florida newspapers or other South Florida publications.

As the Claim Forms are returned, the Receiver will attempt to resolve any potential objections to the claims based on insufficient or inaccurate information from the claimants. For

example, an investor may submit a claim form without his or her signature or may request an amount different from the Receiver's records. The Receiver will try to resolve these issues with the investor without raising a formal objection with the Court.

If the claimant and the Receiver cannot reach an agreement or if the Receiver has substantive objections to the nature of the claim (such as a claim for "lost profits"), the Receiver will collect those objections and prepare an Omnibus Claims Objection Notice for the Court to review. The Omnibus Claims Objection Notice will list all claims to which the Receiver objects by category, the basis for the Receiver's objections, and the amount (if any) that the Receiver has approved for the claim and recommends to the Court for approval. The Omnibus Claims Objection Notice will be served within 30 days after the Claims Bar Date for all claims to which the Receiver objects. The Receiver will post the Omnibus Claims Objection Notice prominently on the Receiver's website to expedite informing claimants of the objection(s).

A claimant who wants to challenge the Receiver's objection must communicate to the Receiver in writing (either by mail or email) within 30 days, stating any arguments and providing any supporting documentation. After an additional 30 day period, the Receiver will submit an omnibus filing to the Court listing all unresolved objections and attaching all communications. If a claimant does not respond to the Omnibus Claims Objection Notice, he or she should be deemed to have waived any challenge to the Receiver's objection and thereby consented to the amount of the claim set out by the Receiver. For the claimants who timely submit responses to the Receiver's objections, the Court (or the Magistrate Judge or a Special Master if the Court so chooses) will resolve any remaining disputes at a hearing or through another process to be determined by the Court. The manner of resolving any outstanding objections, whether by additional filings or by court hearing, will depend on their nature and number.

In summary, the Receiver's proposed time line for the claims process, after the Court enters an Order approving the process, would be as follows:

ACTION	TIME FRAME
The Receiver or designated claims administrator sends out claim forms to all known investors and creditors, posts blank claim form on Receivership website, and publishes commencement of claims process and Claims Bar date in appropriate publications.	Within 20 days of Court Order approving claims process
As Claim Forms are returned, the Receiver attempts to resolve disputed claims.	Ongoing
Claims Bar date (<i>i.e.</i> the date by which all Claim Forms must be submitted to Receiver)	90 days thereafter
The Receiver serves an Omnibus Claims Objection Notice on all claimants with disputed claims, including a list of disputed claims, the basis for the Receiver's objection, and the amount the Receiver recommends for the claim.	Within 30 days thereafter
The claimants who continue to disagree with Receiver's recommended amount must inform the Receiver in writing. Failure to respond timely to the Receiver's Omnibus Claims Objection Notice constitutes a waiver of objections and consent to the Receiver's recommendation. The Receiver will inform the Court of all unresolved objections, including all communications.	Within 30 days thereafter
Court hearing or other procedure to address unresolved objections	To be decided by the Court

ACTION	TIME FRAME
<p>The claimants who do not agree to Receiver's recommended amount recommended must inform the Receiver in writing. Those claimants who do not respond waive their objections and consent to Receiver's recommendation. At the end of the period, the Receiver files a report advising the Court of all unresolved objections, including all objection communications.</p>	<p>Within 30 days thereafter</p>
<p>Court hearing or other procedure to address unresolved objections</p>	<p>To be decided by the Court</p>

CONCLUSION

The Receiver respectfully requests that the Court approve the proposed claims process as set forth in this motion and the attached proposed Order. The Receiver also requests that the Court approve the proposed Claim Form for use in that process.

Respectfully submitted,

MANDEL & MANDEL LLP
Counsel for Receiver, David S. Mandel
 1200 Alfred I. duPont Building
 169 East Flagler Street
 Miami, Florida 33131
 Telephone: 305.374.7771
 Facsimile: 305.374.7776
nsmandel@mandel-law.com

By: /s/ Nina Stillman Mandel
 NINA STILLMAN MANDEL
 Florida Bar No.: 843016

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a true and correct copy of the foregoing was filed via CM/ECF
this 6th day of October, 2015.

/s/ Nina Stillman Mandel