

N.A.S.D. AWARD

NATIONAL ASSOCIATION OF SECURITIES DEALERS

In the Matter of the Arbitration Between

Name of Claimants

Jane Gale
Tony and Lorraine Sherman
Mona and David Montonaro

Consolidated No.s:

91-00611; [REDACTED]
91-00712

Name of Respondents

Mutual Service Corporation
John M. Culbertson

REPRESENTATION OF PARTIES

For Claimants: Steve Samson, Esq., Chicago, Illinois.

For Respondent Mutual Service Corporation: Robert J. Jonker,
Esq. of Warner, Norcross & Judd, Grand Rapids, Michigan.

Respondent John M. Culbertson failed to appear at the hearing.

CASE INFORMATION

Jane Gale's Statement of Claim filed: on or about February 19, 1991.

Claimant's Submission Agreement signed on: February 19, 1991.

Statement of Answer filed by Respondent, Mutual Service Corporation on: May 1, 1991.

Respondent Mutual Service Corporation's Submission Agreement signed on: March 15, 1991.

Statement of Answer filed by Respondent, John M. Culbertson on: June 19, 1991.

Respondent John M. Culbertson failed to file a Submission to Arbitration.

Claimant, Jane Gale's Amended Statement of Claim filed: October

10, 1991.

Answer of Mutual Service Corporation to the Amended Statement of Claim filed: November 13, 1991.

Claimants, Tony and Lorraine Sherman's Statement of Claim filed: February 27, 1991.

Statement of Answer filed by Respondent, Mutual Service Corporation on: May 22, 1991.

Respondent Mutual Service Corporation's Submission Agreement signed on: April 18, 1991.

Claimants, Tony and Lorraine Sherman's Amended Statement of Claim filed: October 10, 1991.

Answer of Mutual Service Corporation to the Amended Statement of Claim filed: November 13, 1991.

Respondent John M. Culbertson failed to file an Answer and a Submission to Arbitration.

Claimants, Mona and David Montonaro's Statement of Claim filed: March 4, 1991.

Statement of Answer filed by Respondent, Mutual Service Corporation on: May 9, 1991.

Respondent Mutual Service Corporation's Submission Agreement signed on: April 18, 1991.

Claimants, Tony and Lorraine Sherman's Amended Statement of Claim filed: October 10, 1991.

Answer of Mutual Service Corporation to the Amended Statement of Claim filed: November 13, 1991.

Statement of Answer filed by Respondent, John M. Culbertson on: June 19, 1991.

Respondent John M. Culbertson failed to file a Submission to Arbitration.

HEARING INFORMATION

Pre-Hearing conference date: February 5, 1992. 1 session.

Hearing dates: April 15, 1992. 2 sessions.
April 16, 1992. 1 sessions.

Hearing Location: Chicago, Illinois.

CASE SUMMARY

Claimant, Jane Gale, ("Claimant") alleged: misrepresentations and omissions; conversion; failure to supervise; violation of Section 10 (b) of the Exchange Act and Rule 10b-5 promulgated thereunder; violation of Section 20 of the Exchange Act (15 U.S.C. Section 78t); violation of Section 27, Article 3 of the Rules of Fair Practice of the NASD; violation of RICO, 18 U.S.C. Section 1961, et seq.; violation of 18 U.S.C. Sections 1341 and 1343; violation of 18 U.S.C. Section 1962 (c); violation of Section 1962 (a) and (c) of RICO, 18 U.S.C. Section 1961 (a) and (c), and breach of fiduciary duty by respondents John M. Culbertson ("Culbertson") and Mutual Service Corporation ("MSC"). The allegations arose out of the transactions in the following securities: Metro International Mortgage Pool; and Metro Mortgage Bond Pool which had allegedly been purchased for Claimant's account between February and June of 1985.

Claimant alleged having no knowledge or sophistication, and alleged complete reliance on the decisions of Culbertson. Claimant further alleged that she told Culbertson that the investments must have limited or no risk, must be liquid, and were for retirement. Claimant went on to allege that Culbertson represented to her that: He was a registered representative, and authorized agent and branch manager of MSC; MSC provided access to all stock exchanges, investment vehicles, and research for the sale of securities to investors; MSC maintained supervisory responsibility for compliance; MSC provided insurance for investors under SIPC and liability insurance; Culbertson was a specialist in retirement investments; and that all investments made with him were safe and liquid. These practices, statements, or omissions were alleged to be material or alleged to have been done with the specific intent to deceive or defraud or were alleged to have been false when made. Based on these representations, Claimant reasonably believed them to be true, and relied on them to make the investments listed above. Claimant had also alleged that Culbertson and MSC had failed to provide them with details of all investments, and had also failed to pay over all securities/monies in their account. Claimant next alleged that Culbertson converted the monies invested through him, and such conversion was done with the usual course of business for MSC, and within the scope of his employment. Lastly, Claimant asserted that MSC knew or should have known of the conversion through internal supervision, and that MSC failed to maintain and enforce a proper system of internal supervision.

In its Answer to Claimant, Jane Gale's Statement of Claim, MSC denied each and every material allegation contained therein. In addition, MSC asserted the following defenses:

1. Claimant's cause of action involves two "investments" allegedly acquired in 1985 with reliance on alleged statements made by Respondent Culbertson. In 1985, Respondent Culbertson had no affiliation at all with MSC, and was a registered

representative of F.S.C. Securities Corp.. Claimant had no cause of action against MSC based on alleged conduct of Respondent Culbertson, who did not become a registered representative of MSC until January of 1987.

2. Claimant's cause of action, if any, lies exclusively against Culbertson. Claimant did not deal with MSC, never deposited any funds with MSC, and never acquired any securities through MSC. MSC did not in any way defraud or otherwise harm the Claimant.

3. If Claimant's allegations as to Culbertson are true, MSC is not vicariously liable for the fraud perpetrated by Culbertson. Culbertson was never an employee of MSC, and so the doctrine of respondeat superior is completely inapplicable. Culbertson was a registered representative of MSC who worked as an independent contractor. Culbertson's alleged dealings with the Claimants did not in any way involve MSC. Claimant's check was not payable to or received by MSC.

4. Even if the doctrine of respondeat superior were applicable, the alleged conduct of Culbertson could not be vicariously attributed to MSC because it would not be in support of MSC. See, e.g., Gibaldi v. Lamson, 205 Ill. App. 3d 1025, 1029-30, 563 N.E.2d 956, 960 (1990). MSC never received any commissions or other remuneration based on the alleged interactions between Culbertson and Claimant.

5. Claimant never actually purchased or sold a security. Accordingly, an essential claim of a securities fraud action is missing: namely, that the Claimant's alleged loss be "in connection with" the purchase or sale of a security.

6. Claimant's RICO claims are also legally insufficient (as well as factually baseless as against MSC). Claimant attempts to allege MSC is both an "enterprise" under RICO and a liable person under 18 U.S.C. Section 1962(c). The enterprise and a liable party under this section cannot be the same person. See, e.g., Harco, Inc. v. American National Bank & Trust Co., 747 F.2d 384 (7th Cir. 1984), aff'd on other grounds, 105 S.Ct. 3291 (1985). Moreover, MSC never received income from any alleged racketeering activity in this case, and so Claimant's claim under 18 U.S.C. Section 1962(a) is also flawed. Finally, the Claimant has failed to allege the requisite pattern of activity to which RICO applies. See H J Inc. v. Northwestern Bell Telephone Co., 109 S.Ct. 2893, 2902 (1989); and Azurite Corp. v. Amster & Co., 730 F.Supp. 571, 581 (S.D.N.Y. 1990).

7. Claimant's charge that MSC failed to exercise adequate supervision over Culbertson is also without merit. MSC conducted and continues to conduct all reasonable and necessary supervision of activity undertaken by registered representatives in securities transactions that involve MSC. In this case, the Claimant's alleged loss has nothing to do with a securities

transaction that involves MSC.

8. Claimant's cause of action, if any, is barred by the applicable statute of limitations.

For his Statement of Answer, Culbertson did not deny the allegations set forth in Claimant, Jane Gale's Statement of Claim.

In her Amended Statement of Claim, Claimant reasserted the claims and allegations as set forth in her original Statement of Claim. In addition, Claimant alleged that Respondents MSC and Culbertson continually, actively, and fraudulently concealed from Claimant material facts giving rise to the conversion of their money. Claimant further alleged that because they had received: interest payments until October of 1990; fraudulent statements of account to showing their investments were safe; assurances their investments were safe each time Culbertson was questioned, and letters sent by Culbertson concerning the alleged investments made by Culbertson, Claimant had no way of knowing of the fraud until November of 1990. In addition, Claimant alleged that all of the acts of Culbertson were within the scope and course of his employment with MSC, and Claimant alleged justification in reliance upon the appearance of authority respecting Culbertson's actions.

In its Answer to the Amended Statement of Claim, MSC denied each and every material allegation contained therein. MSC also reasserted its defenses as originally raised in its answer to the Statement of Claim. In addition, MSC raised the additional defenses that:

1. The Illinois Consumer Fraud Deceptive Business Practices Act does not properly apply to the alleged purchase or sale of securities regulated by other state and federal statutes. See Vanek v. Cosmano, No. 85C 0334 (N.D. Ill. Jan 24, 1986); Coron, Inc. v. American Heritage savings 7 Loan Assoc. No. 85C 6380, 1986 Westlaw 2072 (N.D. Ill. Feb. 3, 1986). Cf. Mercer v Jaffe, Sneider, Raitt and Heuer, 713 F.Supp. 1019, 1029-30 (W.D. Mich. 1989). Contra, Wislow v. Wong, 713 F.Supp. 1103, 1107 (N.D. Ill. 1989). Moreover, MSC's compliance with applicable securities laws defeats a purported claim under this Act in any event.

2. The Amended Statement of Claim should be stricken as untimely.

Claimants, Tony and Lorriane Sherman, ("Claimants") alleged: misrepresentations and omissions; conversions; failure to supervise; violation of Section 10 (b) of the Exchange Act and Rule 10b-5 promulgated thereunder; violation of Section 20 of the Exchange Act (15 U.S.C. Section 78t); violation of Section 27, Article 3 of the Rules of Fair Practice of the NASD; and breach of fiduciary duty by Respondents John M. Culbertson ("Culbertson") and Mutual Service Corporation ("MSC"). The

allegations arose out of transactions in the following securities: Metro Mortgage Pool; Metro GNMA Bond Pool; Metro GNMP Bond Pool 86; J.P. Moyan Notes; Metro Bond Pool; Bond Fund; Australian Bond Fund; Kleinwest-Benson; Metro International Bond Pool; Metro Equity Plus Money Fund which had allegedly been purchased for Claimants' account between August of 1985, and May of 1990.

Claimants alleged that they had no knowledge or sophistication, and alleged their complete reliance on the decisions of Culbertson. Claimants further alleged that they told Culbertson that the investments must have limited or no risk, must be liquid, and were for retirement. Claimants went on to allege that Culbertson represented to them that: He was a registered representative, and authorized agent and branch manager of MSC; MSC provided access to all stock exchanges, investment vehicles, and research for the sale of securities to investors; MSC maintained supervisory responsibility for compliance; MSC provided insurance for investors under SIPC and liability insurance; Culbertson was a specialist in retirement investments; and that all investments made with him were safe and liquid. These practices, statements, or omissions were alleged to be material or alleged to have been done with specific intent to deceive or defraud or were alleged to have been false when made. Based on these representations, it was alleged that Claimants reasonably believed them to be true, and relied on them to make the investments listed above. Claimants have also alleged that Culbertson and MSC had failed to provide them with details of all investments, and had also failed to pay over all securities/monies in his account. Claimants next alleged that Culbertson converted the monies invested through him, and such conversion done within the usual course of business for MSC, and within the scope of his employment. Lastly, Claimants asserted that MSC knew or should have known of the conversion through internal supervision, and that MSC failed to maintain and enforce a proper system of internal supervision.

In its Answer to Claimants, Tony and Lorraine Sherman's Statement of Claim, MSC denied each and every material allegation contained therein. In addition, MSC asserted the same defenses that were raised in the case of Jane Gale v. John M. Culbertson and Mutual Service Corporation, No. 91-00611, and which are set forth more fully above. However, MSC did not assert the defense in point set forth above.

In their Amended Statement of Claim, Claimants reasserted the claims and allegations as set forth in their original Statement of Claim. In addition, Claimants alleged that Respondents MSC and Culbertson continually, actively, and fraudulently concealed from them material facts giving rise to the conversion of their money. Claimants further alleged that because they had received: interest payments until October, 1990; fraudulent statements of account; assurances that his investments were safe each time Culbertson was questioned; and letters from Culbertson

concerning the alleged investments made by Culbertson, Claimants had no way of knowing of the fraud until November of 1990. In addition, Claimants alleged that all of the acts of Culbertson were within the scope and course of his employment with MSC, and Claimants alleged their justification in reliance upon the appearance of authority respecting Culbertson's actions.

In its Answer to the Amended Statement of Claim, MSC denied each and every material allegation contained therein. MSC also reasserted its defenses as originally raised in its answer to the Statement of Claim. In addition, MSC raised the additional defenses contained in its Answer to the Amended Statement of Claim in the case of Jane Gale v. John M. Culbertson and Mutual Service Corporation, No. 91-00611, and set forth more fully above.

Claimants, Mona and David Montenegro, ("Claimants") alleged: misrepresentations and omissions; conversion; failure to supervise; violation of Section 10 (b) of the Exchange Act and Rule 10b-5 promulgated thereunder; violation of Section 20 of the Exchange Act (15 U.S.C. Section 78t); violation of Section 27, Article 3 of the Rules of Fair practice of the NASD; violation of RICO, 18 U.S.C. Section 1961, et seq.; violation of 18 U.S.C. Sections 1341 and 1343; violation of 18 U.S.C. Section 1962 (c); violation of Section 1962 (a) and (c) of RICO, 18 U.S.C. Section 1961 (a) and (c), and breach of fiduciary duty by Respondents John M. Culbertson ("Culbertson") and Mutual Service Corporation ("MSC"). The allegations arose out of the transactions in the following securities: Metro Mortgage Pool; and J.P. Morgan Notes allegedly purchased for their account between November of 1984, and August of 1987.

Claimants alleged having no knowledge or sophistication, and alleged complete reliance on the decisions of Culbertson. Claimants further alleged that they told Culbertson that the investments must have limited or no risk, and were to be used for their retirement. Claimants went on to allege that Culbertson represented to them that: He was a registered representative, and authorized agent and branch manager of MSC; MSC provided access to all stock exchanges, investment vehicles, and research for the sale of securities to investors; MSC maintained supervisory responsibility for compliance; MSC provided insurance for investors under SIPC and liability insurance; Culbertson was a specialist in retirement investments; and that all investments made with him were safe and liquid. These practices, statements, or omissions were alleged to be material or alleged to have been done with specific intent to deceive or defraud or were alleged to have been false when made. Based on these representations, Claimants reasonably believed them to be true, and relied on them to make the investments listed above. Claimants had also alleged that Culbertson and MSC had failed to provide them with details of all investments, and had also failed to pay over all securities/monies in their account. Claimants next alleged that Culbertson converted the monies invested through him, and such

conversion was done within the usual course of business for MSC, and within the scope of his employment. Lastly, Claimants asserted that MSC knew or should have known of the conversion through internal supervision, and that MSC failed to maintain and enforce a proper system of internal supervision.

In its Answer to Claimant, Mona and David Montonaro's Statement of Claim, MSC denied each and every material allegation contained therein. In addition, MSC asserted the same defenses that were raised in the case of Jane Gale v. John M. Culbertson and Mutual Service Corporation, No. 91-00611, and which are set forth more fully above. However MSC did not assert the defense raised in point 1 set forth above.

In their Amended Statement of Claim, Claimants reasserted claims and allegations as set forth in Claimants' original Statement of Claim. In addition, Claimants alleged that Respondents MSC and Culbertson continually, actively, and fraudulently concealed from her material facts giving rise to the conversion of Claimants' money. Claimants further alleged that because they had received: interest payments until October, 1990; fraudulent statements of account; assurances that their investments were safe each time Culbertson was questioned; and letters from Culbertson concerning the alleged investments made by Culbertson, Claimants had no way of knowing of the fraud until November of 1990. In addition, Claimants alleged that all of the acts of Culbertson were within the scope and course of his employment with MSC, and Claimants alleged justification in reliance upon the appearance of authority respecting Culbertson's actions.

In its Answer to the Amended Statement of Claim, MSC denied each and every material allegation contained therein. MSC also reasserted its defenses as originally raised in its answer to the Statement of Claim. In addition, MSC raised the additional defenses in the case of Jane Gale v. John H. Culbertson and Mutual Service Corporation, No. 91-00611, and set forth more fully above.

RELIEF REQUESTED

Claimant, Jane Gale requested:

1. Compensatory damages in excess of \$25,000.00;
2. Any additional punitive and consequential damages Claimant may establish at the hearing, including treble damages pursuant to RICO;
3. Interest at the legal rate, forum fees, attorneys' fees and costs; and

4. Other proper and just relief.

Respondent Mutual Service Corporation requested that Claimant's claims be denied in their entirety.

Claimants, Tony and Lorraine Sherman requested:

1. Compensatory damages in excess of \$170,000.00;
2. Any additional punitive and consequential damages Claimant may establish at the hearing, including treble damages pursuant to RICO;
3. Interest at the legal rate, forum fees, attorneys' fees and costs; and
4. Other proper and just relief.

Respondent Mutual Service Corporation requested that Claimant's claims be denied in their entirety.

Claimants, Mona and David Montonaro requested:

1. Compensatory damages in excess of \$30,000.00;
2. Any additional punitive and consequential damages Claimant may establish at the hearing, including treble damages pursuant to RICO;
3. Interest at the legal rate, forum fees, attorneys' fees and costs; and
4. Other proper and just relief.

Respondent Mutual Service Corporation requested that Claimant's claims be denied in their entirety.

OTHER ISSUES CONSIDERED & DECIDED

Respondent John M. Culbertson did not file with the NASD a properly executed Submission to Arbitration but is required to submit to arbitration pursuant to Section 12 of the NASD Code of Arbitration Procedure. Respondent John M. Culbertson answered the claims numbered 91-00611, and 91-00712, however, Respondent Culbertson did not appear at the hearing. After review of the service attempts by the NASD and the parties, the fact that Respondent Culbertson had answered claims in the aforementioned consolidated cases, and deliberation, the panel ordered the hearing to proceed pursuant to Section 29 of the Code of Arbitration Procedure. Respondent John M. Culbertson shall be

bound by the determination of the arbitration panel on all issues submitted.

The parties have agreed that the Award in this matter may be executed by counterpart copies or that a handwritten, signed Award may be entered. In either case, the parties have agreed to receive conformed copies of the award while the originals remain on file with the NASD.

AWARD

After considering the pleadings, the testimony, and the evidence presented at the hearing, the undersigned arbitrators have decided in full and final resolution of the issues submitted for determination as follows:

1. Respondents Mutual Service Corporation and John M. Culbertson are jointly and severally liable for, and shall pay to Claimants, Tony and Lorraine Sherman the sum of \$62,100.00, as satisfaction of their claims herein.
2. Claimant, Jane Gale's claims against respondent Mutual Service Corporation are hereby denied and dismissed with prejudice.
3. Respondent John M. Culbertson is liable for, and shall pay to Claimant, Jane Gale the sum of \$10,000.00.
4. Claimants, Mona and David Montonaro's claims against respondent Mutual Service Corporation are hereby denied and dismissed with prejudice.
5. Respondent John M. Culbertson is liable for, and shall pay to Claimants, Mona and David Montonaro the sum of \$10,000.00.
6. Claimants, Jane Gale, Tony and Lorraine Sherman, and Mona and David Montonaro's claims for damages under RICO, punitive damages, and for attorney's fees are hereby denied and dismissed with prejudice.
7. Each claimant and respondent shall bear their own costs of this arbitration, except as set forth below.

FORUM FEES

Pursuant to Section 43 (c) of the NASD Code of Arbitration Procedure, the following forum fees are assessed:

- 1 pre-hearing conference sessions X \$300.00 = \$300.00
- 3 hearing sessions X \$1,000.00 = \$3,000.00

Pursuant to Section 43 (c) of the Code of Arbitration, the NASD shall retain the nonrefundable filing fee in the amount of

\$100.00, and shall retain the hearing session deposit in the amount of \$400.00 previously paid to the NASD by the claimant, Jane Gale.

Pursuant to Section 43 (c) of the Code of Arbitration, the NASD shall retain the nonrefundable filing fee in the amount of \$200.00, and shall retain the hearing session deposit in the amount of \$750.00 previously paid to the NASD by the claimants, Tony and Lorraine Sherman.

Pursuant to Section 43 (c) of the Code of Arbitration, the NASD shall retain the nonrefundable filing fee in the amount of \$100.00, and shall retain the hearing session deposit in the amount of \$400.00 previously paid to the NASD by the claimants, Mona and David Montonaro.

Additional forum fees in the amount of \$1,750.00 are assessed against respondent Mutual Service Corporation.

Fees are payable to the National Association of Securities Dealers, Inc.

CONCURRING ARBITRATORS

Dated:

June 16, 1992

/s/James S. Teborek
James S. Teborek
Presiding Chair
Public Arbitrator

June 12, 1992

/s/Burton Y. Weitzenfeld
Burton Y. Weitzenfeld
Public Arbitrator

July 7, 1992

/s/William J. Roberts
William J. Roberts
Industry Arbitrator