

N.A.S.D. AWARD

NATIONAL ASSOCIATION OF SECURITIES DEALERS

In the Matter of the Arbitration Between

Name of Claimants

Walter & Gertrude Schaberg

91-02375

Name of Respondents

Shearson Lehman Hutton, Inc.
Richard Rogers

REPRESENTATION

For Claimants: Walter and Gertrude Schaberg were represented by Michael Salcido, Esq. of Burch & Cracchiolo, P.A., located in Phoenix, Arizona.

For Respondents: Shearson Lehman Hutton, Inc., now known as Shearson Lehman Brothers, Inc., and Richard Rogers were represented by Michael C. Licosati, Esq. of Keesal, Young & Logan, located in Long Beach, California.

CASE INFORMATION

Statement of Claim filed: August 2, 1991.

Claimants' Submission Agreement signed on: April 6, 1990.

Joint Statement of Answer filed by Respondents Shearson Lehman Hutton, Inc., now known as Shearson Lehman Brothers, Inc. and Richard Rogers on: December 16, 1991.

Respondent Richard Rogers appeared at the hearing and subsequently executed a Submission Agreement on: July 6, 1992.

Respondent Shearson Lehman Hutton, Inc., now known as Shearson Lehman Brothers, Inc., did not file an executed submission agreement, but is required to submit to arbitration pursuant to Section 12 of the NASD Code of Arbitration Procedure.

HEARING INFORMATION

Pre-Hearing Conference: None Held.

Hearing Date/Sessions: June 25, 1992 for three (3) sessions.

Hearing Location: Scottsdale, Arizona.

CASE SUMMARY

Claimants Walter and Gertrude Schaberg ("Schabergs") alleged that Respondent Richard Rogers ("Rogers"), while employed by or acting as an agent for Respondent Shearson Lehman Hutton, Inc., now known as Shearson Lehman Brothers, Inc. ("Shearson"), misrepresented certain investments in annuities and common stocks, thereby placing the Schabergs in investments which were unsuitable given the Claimants' investment objectives and needs. The Schabergs specifically alleged as follows:

1. The Schabergs were unsophisticated investors who were totally dependent upon Respondents' advice and who explained to Rogers that their investment objectives were low risk, safety of principal, income and liquidity;
2. In 1983, Respondents invested \$38,900.00 of the Schabergs' investment funds into the Executive Life Single Premium Annuity and 500 shares of Tucson Electric Power;
3. The annuities had interest rate guarantees of between 10.5 percent to 8.5 percent; however, these guaranteed rates were valid only if the funds were left in the contract for the full 10 years;
4. In early 1987, the Schabergs explained to Respondents that they needed more income as their monthly expenses had increased to approximately \$2,000.00 versus an income from all sources, including stock dividends, of \$1,538.00;
5. In July of 1987, Respondents placed \$70,351.83 of the Schabergs' investment funds, which were substantially all of the Schabergs' life savings, in the Immediate Joint and Survivor Annuity issued by the Manufacturer's Life Insurance Company;
6. The two important characteristics of the Manufacturer's Life annuity were that there was absolutely no access to principal, even in case of emergencies and that principal was being invaded on a regular basis, much of returning to the Schabergs as the "income payment";
7. This investment was unsuitable given the Schabergs' investment objectives, required the close out of the Executive Life annuities and a Single Premium Deferred Annuity from National Home Life

Insurance Company in order to pay for the new annuity, and furthermore, resulted in payment of "surrender charges" for the funds drawn; and

8. The Respondents misrepresented the transaction by: a) stating the transaction would yield 10.5 percent interest, risk free; b) stating that the investment was consistent with the Schabergs' objectives; c) failing to disclose the surrender charges or the options to avoid them; d) failing to state that Respondents would receive a sizeable commission for effectuating this transaction; e) failing to provide all the material and information contained in the prospectus or offering memoranda; f) failing to adequately explain alternatives that would provide similar income and meet their objectives; g) failing to explain that a substantial portion of the money received monthly was actually the Schabergs' own investment; h) failing to explain that at the end of the annuity's terms, there would be no money left for their estate; and, i) failing to explain to the Schabergs that by entering into this investment, they would lose all access to their funds.

Based upon the above allegations, the Schabergs asserted claims for fraud, securities fraud, and civil racketeering, violating A.R.S. Par. 44-1991 and A.R.S. Par. 13-2301(D)(4)(r) and (t); breach of fiduciary duty; breach of contract; negligence; and negligent misrepresentation.

Respondents Shearson and Rogers denied the material allegations of the Statement of Claim, alleging that:

1. Rogers performed a comprehensive review of Claimants' financial situation and explained numerous investment alternatives which would be suitable for the Schabergs' financial objectives prior to the Schabergs' decision to invest in the Executive Life Single Premium Annuity and the 500 shares of Tucson Electric Power;

2. By the summer of 1987, the Schabergs' initial investment of \$38,900.00 made in 1983 had increased in value to approximately \$71,000.00, representing a growth of approximately 84% in four years;

3. Pursuant to the Schabergs' request for more income, Rogers spent a great deal of time explaining the various suitable investments, though it was impossible for Rogers to guarantee a stable monthly payment sufficient to satisfy their stated requirements without depleting principal, and the Schabergs directed Rogers to purchase an immediate joint and survivor annuity issued by Manufacturer's Life, which had one of the highest ratings of all insurance companies;

4. The surrender of the annuities to effectuate the purchase was done at an expense of \$1,957.75, or about 2.7% of the combined annuity value, which Rogers believed was outweighed by the strengths and reliability of placing the proceeds in a single

annuity with Manufacturer's Life;

5. Rogers received absolutely no commission for the surrender of the policies, but received \$1,407.04 net out of the gross sales commission for the purchase of the Manufacturers' annuity and never made the transaction for the purpose of obtaining increased commissions;

6. After the investment, the Schabergs still had 650 shares of Tucson Electric Power trading at approximately \$56.00 per share with a total market value of \$36,500.00, an increase of \$22,000.00 in four years; and

7. The Statement of Claim is barred by the applicable statute of limitations because the Claimants are seeking to recover damages for investments made on July 1, 1987, over four years from the date of filing.

In addition, Respondents asserted the following affirmative defenses, requesting that the Statement of Claim be dismissed:

1. The Statement of Claim fails to state claims upon which relief can be granted;

2. The alleged losses were proximately caused by Claimants' own conduct or negligence, or the conduct or negligence of a third party;

3. The Claimants completely failed to mitigate their damages;

4. Respondent Shearson maintained an adequate and reasonable system of supervision and control over its employees; and Respondents at all times acted in good faith and did not, directly or indirectly, induce any acts constituting a cause of action;

5. The claim is barred on the ground of laches;

6. The Schabergs expressly ordered, approved, authorized, participated in and ratified the acts and transactions complained of, and the Claimants are precluded from recovery;

7. The Schabergs, through their conduct, approved, authorized and ratified the actions and transactions complained of, and are estopped from recovery;

8. All risks were fully explained to the Schabergs and they knowingly, willingly and voluntarily assumed the risk involved;

9. Claimants, by their conduct, waived any and all rights they may have against Respondents; and

10. Claimants are guilty of unclean hands.

RELIEF REQUESTED

Claimants requested that the arbitrators enter an award against the Respondents, jointly and severally, for compensatory damages of approximately \$70,351.83; treble damages pursuant to A.R.S. Par. 13-2314(A); punitive damages; attorneys' fees and costs; and pre- and post-judgment interest.

Respondents Shearson and Rogers requested that the arbitrators dismiss all claims and that they be awarded attorneys' fees and costs.

OTHER ISSUES CONSIDERED & DECIDED

The parties have agreed that the Award in this matter may be executed in 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. The Statement of Claim is hereby dismissed and denied in its entirety;
2. Claimants Walter and Gertrude Schaberg are liable for and shall pay to Respondents Shearson Lehman Hutton, Inc., now known as Shearson Lehman Brothers, Inc., and Richard Rogers the sum of \$500.00 as attorneys' fees. In determining to award attorneys' fees to Respondents Shearson Lehman Brothers, Inc. and Richard Rogers, the panel considered the arguments presented by the parties and Arizona law and determined that authority existed for an award of attorneys' fees in favor of Respondents;
3. The parties shall each bear all of their other costs of arbitration, except for those specifically enumerated herein.

FORUM FEES

Pursuant to Section 43(c) of the Code of Arbitration Procedure, the following total Forum Fees are assessed: Three sessions (3) x \$750.00 hearing session deposit = \$2,250.00.

The National Association of Securities Dealers, Inc. (NASD) shall retain the claim filing fee of \$200.00 and the hearing session deposit of \$750.00

previously deposited by the Claimants Walter and Gertrude Schaberg. Claimants Walter and Gertrude Schaberg are liable for and shall pay to the NASD additional forum fees in the sum of \$1,500.00.

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

CONCURRING ARBITRATORS' SIGNATURES

Dated:

Irving Lowe
Irving Lowe, Esq.
Public Arbitrator
Chairperson

August 17, 1992

Thomas S. Barsuk
Thomas S. Barsuk
Public Arbitrator

August 14, 1992

Richard B. Bequette
Richard B. Bequette
Industry Arbitrator

August 17, 1992

Date of Service by the NASD:

August 25, 1992