

N.A.S.D. AWARD

NATIONAL ASSOCIATION OF SECURITIES DEALERS

In the Matter of the Arbitration Between

Name of Claimants

W. Fox & Company, Inc.:
Eric Hilton, Jr. and Don Weiler

92-00383

Name of Respondents

Merrill Lynch, Pierce Fenner & Smith, Inc.;
Don Spivey

REPRESENTATION

For Claimant: W. Fox and Company, Inc., Eric Hilton, Jr. and Don Weiler were represented by Joseph A. McDermott, III, Esq. of Soape Brown McDermott, located in Houston, Texas.

For Respondent: Merrill Lynch, Pierce, Fenner & Smith, Inc. and Don Spivey were represented by Kathy D. Patrick, Esq. and Barrett H. Reasoner, Esq. of Gibbs & Ratliff, L.L.P., located in Houston, Texas.

CASE INFORMATION

Statement of Claim filed: January 31, 1992.

Claimant W. Fox and Company, Inc.'s Submission Agreement signed on: February 13, 1992 by Eric Hilton, Jr., Vice-President, W. Fox and Company, Inc.

Claimant Eric Hilton, Jr.'s Submission Agreement signed on: January 24, 1992.

Claimant Don Weiler's Submission Agreement signed on: January 24, 1992.

Joint Statement of Answer filed by Respondents Merrill Lynch, Pierce, Fenner & Smith, Inc. and Don Spivey on: April 15, 1992.

Respondent Merrill Lynch, Pierce, Fenner and Smith, Inc.'s Submission Agreement signed on: May 11, 1992 by Michael J. Stewart, First Vice-President, Merrill Lynch, Pierce, Fenner & Smith, Inc.

Respondent Don Spivey's Submission Agreement signed on: June 8, 1992.

HEARING INFORMATION

Pre-Hearing Conference: None Held.
Hearing Dates/Sessions: October 26, 1992 for Two (2) sessions:
October 27, 1992 for Two (2) sessions:
November 23, 1992 for Two (2) sessions.

Hearing Location: Houston, Texas.

CASE SUMMARY

Claimants W. Fox and Company, Inc. ("W. Fox") and the owners of W. Fox, Eric Hilton, Jr. ("Hilton") and Don Weiler ("Weiler") alleged that Respondent Don Spivey ("Spivey"), while employed by or acting as an agent for Respondent Merrill Lynch, Pierce, Fenner & Smith, Inc. ("Merrill Lynch"), entered into a civil conspiracy with Claimants' accountant to convert funds by depositing checks into an unauthorized account, or alternatively, was grossly negligent in the handling of Claimants' funds. In furtherance of their Claim, Claimants specifically alleged that:

1. Claimants contracted with an independent certified public accountant to provide accounting services to W. Fox. Unbeknownst to Claimants, the accountant began a scheme to embezzle an unknown sum of money from Claimants;
2. Part of the embezzlement scheme consisted of the accountant drawing checks written on a W. Fox bank account, presenting the checks to Hilton or Weiler for signature with a notation for an apparently legitimate business purpose, and then depositing the checks into an unauthorized Merrill Lynch account opened in the name of W. Fox through Spivey with the use of the forged signature of Hilton;
3. The accountant withdrew funds from the unauthorized Merrill Lynch account through the use of checks and a Visa card associated with the account;
4. Spivey was the broker for the Claimants' legitimate accounts, and knew or should have known the address of the unauthorized account was not that of W. Fox, but of the accountant. In addition, Claimants had been introduced to Spivey by the accountant, and Spivey knew or had reason to know that the accountant was not authorized to establish the bogus W. Fox account nor was he authorized to fund the account with W. Fox monies; and
5. Many of the unauthorized checks deposited into the unauthorized account bore notations such as "payroll taxes", and since Merrill Lynch was not acting as a payroll tax depository for W. Fox, these checks should have been a "red flag" for anyone exercising ordinary care in the processing of the items.

Based upon the above allegations, the Claimants asserted claims for violation of the Texas Business and Commerce Code; breach of fiduciary duty; civil conspiracy to convert funds

belonging to Claimants: gross negligence; and breach of contract.

Respondents Merrill Lynch and Spivey denied the material allegations of the Statement of Claim alleging that:

1. The Claimants were aware, before they began trading with Merrill Lynch, that the accountant had embezzled some \$10,000.00 from them, and despite this act, retained the accountant and instructed Merrill Lynch and Spivey that the accountant would handle the day to day details of the account;
2. Neither Claimants or the accountant told Merrill Lynch or Spivey of the accountant's wrongful actions and Respondents were unaware of these prior actions until after W. Fox discovered that it had been cheated again. The only people who knew or should have known of the accountant's wrongful actions were the Claimants;
3. The account Claimants complain of was not an unauthorized account, but one that Claimants traded in regularly and often spoke to Spivey about the account's performance and strategy;
4. Respondents did not violate the Texas Business and Commerce Code because the Respondents had no notice that the checks drawn on the W. Fox bank account were not authorized and Claimants' signature on the checks was a statement to Respondents indicating that the checks were authorized;
5. There is no fiduciary duty between a broker and its customer, and therefore no breach of fiduciary duty;
6. At all times, Spivey acted, in accordance with the instructions received from the Claimants and he did not know of any wrongdoing by the accountant nor did he enter into a conspiracy with him; and
7. Respondents were not negligent because Claimants' own signatures were on the items deposited in their accounts and they continually stated their support for the accountant.

In addition, Respondents asserted the following affirmative defenses:

1. Under the Uniform Commercial Code, the Claimants' signature on checks was a warranty that they authorized them, and Respondents were entitled to rely upon that warranty in honoring the checks. Claimants cannot now assert that Merrill Lynch and Spivey were responsible for the losses asserted;
2. Claimants were guilty of comparative and contributory negligence because they were aware that the accountant had previously stolen from them, had never advised Respondents of this fact and retained the accountant even though they

were aware of the fraud, signed checks with scrutinizing there true purpose and failed to supervise the accountant even though the knew there was reason to believe he would injure them if left to his own devices;

3. The claims are barred by the doctrines of estoppel, ratification, waiver, accord and satisfaction, and by the applicable statutes of limitations; and

4. Upon information or belief, Claimants entered into a full and complete settlement with the accountant that makes them entirely whole.

RELIEF REQUESTED

Claimants W. Fox, Hilton and Weiler requested that the panel issue an award against Respondents for Claimants actual damages and for punitive damages in the amount of \$500,000.00; for attorneys' fees in the amount of \$250,000.00; for pre- and post-judgment interest at the highest applicable rate; for restitution for fiduciary breach; and for all such other and further relief to which the Claimants would show themselves to be justly entitled.

Respondents Merrill Lynch and Spivey requested that the panel enter an award that Claimants take nothing by their action.

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 and the arbitration briefs, the undersigned arbitrators have decided in full and final resolution of the issues submitted for determination as follows:

1. Respondents Merrill Lynch, Pierce, Fenner & Smith, Inc. and Don Spivey are jointly and severally liable for and shall pay to Claimants W. Fox and Company, Inc., Eric Hilton, Jr. and Don Weiler the sum of \$8,237.50;

2. In addition, Respondents Merrill Lynch, Pierce, Fenner & Smith, Inc. and Don Spivey are jointly and severally liable for and shall pay to Claimants W. Fox and Company, Inc., Eric Hilton, Jr. and Don Weiler the sum of \$3,300.00 as attorneys' fees in this arbitrations. In determining to award attorneys' fees to Claimants, the panel considered the authorities cited in the arbitration briefs submitted by the parties, as well as the arguments of the parties, and determined that authority existed for an award of attorneys' fees to the Claimants;

3. The parties shall bear their own costs of all items not specifically enumerated

herein.

FORUM FEES

Pursuant to Section 43(c) of the Code of Arbitration Procedure, the following Forum Fees are assessed: Six (6) sessions x \$750.00 per session = \$4,500.00.

The National Association of Securities Dealers, Inc. ("NASD") shall retain the \$200.00 claim filing fee and the \$750.00 hearing session deposit previously deposited by the Claimants, W. Fox and Company, Inc., Eric Hilton, Jr. and Don Weiler. In addition, Claimants W. Fox and Company, Inc., Eric Hilton, Jr. and Don Weiler are jointly and severally liable for and shall pay to the NASD additional forum fees in the sum of \$1,500.00. Respondents Merrill Lynch, Pierce, Fenner & Smith, Inc. and Don Spivey are jointly and severally liable for and shall pay to the NASD forum fees in the sum of \$2,250.00.

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

Concurring Arbitrators' Signatures

Name:

Dated:

Judith A. Swinney, Esq.
Judith A. Swinney, Esq.
Public Arbitrator
Chairperson

January 25, 1993

Victor B. Russek, Jr.
Victor B. Russek, Jr.
Public Arbitrator

January 22, 1993

Thomas H. Vann
Thomas H. Vann
Industry Arbitrator

January 22, 1993

Date of Service on Parties: 2-2-93