

N.A.S.D. AWARD

NATIONAL ASSOCIATION OF SECURITIES DEALERS

In the Matter of the Arbitration Between

Name of Claimants

Edward & Reine Penzer

vs.

Case #92-00400

Name of Respondents

Advest, Inc.
Gruntal & Co., Inc
William Kravitz

REPRESENTATION

For Claimants, Edward & Reine Penzer, ("Claimants") Lawrence A. Steckman, Esq., from the law firm of Camhy Karlinsky & Stein.

For Respondent, Gruntal & Co., Inc. ("Gruntal") and William Kravitz ("Kravitz") for the period Kravitz was in Gruntal's employ, Cynthia A. Feigin, Esq. from the law firm of Davis, Scotts, Weber & Edwards, P.C.

For Respondents, Advest, Inc. ("Advest") and Kravitz, for the period Kravitz was in Advest's employ, Emilio M. Demio, Esq. in-house counsel.

CASE INFORMATION

Statement of Claim filed was filed on February 7, 1992.
Claimant's Submission Agreement was signed on January 14, 1992.
Amended Statement of Claim was filed on December 13, 1992 to add Advest as a Respondent.

Joint Statement of Answer was filed by Gruntal and Kravitz on May 28, 1992.
Kravitz Submission Agreement was signed on May 5, 1993.
Gruntals' Submission Agreement was signed on May 5, 1993.

Joint Answer to First Amended Statement of Claim was filed on March 5, 1993.

Joint Statement of Answer was filed by Advest and Kravitz on March 5, 1993.

Advest's Submission Agreement was signed on May 7, 1993.

Answer to First Amended Statement of Claim was filed on March 5, 1993.

HEARING INFORMATION

Hearing Dates/Hearing Sessions: May 4, 1993 - Two Sessions
 May 5, 1993 - Two Sessions
 May 12, 1993 - Two Sessions
 June 8, 1993 - Two Sessions
 July 7, 1993 - Two Sessions

Hearing Location: National Association of Securities Dealers, Inc. offices located at 33 Whitehall Street, New York.

CASE SUMMARY AND DECISION

Claimants filed a claim against William Kravitz and Gruntal on January 30, 1991. The claim was amended to include Advest as an additional Respondent on December 30, 1992. The amended claim seeks compensatory damages in the sum of at least \$160,000.00 together with appropriate treble damages and attorneys fees, and is based upon alleged violations of federal securities laws, common law duties, NASD Rules of Fair Practice, and the Racketeer Influenced and Corrupt Organization Act ("RICO"). Specifically, Claimants have alleged that their broker, Kravitz, made unsuitable recommendations concerning the purchase by Claimants of certain securities in violation of Section 10(b) of the Securities Exchange Act of 1934 (the "1934 Act") and Rule 10b-5 promulgated thereunder, certain common law duties and obligations, and Section 2 of the NASD Rules of Fair Practice (suitability); and that Mr. Kravitz made misrepresentations and omissions of material fact, again in violation of Section 10(b) of the 1934 Act and Rule 10b-5, common law duties and obligations, and Sections 2 (suitability) and 18 (manipulative or fraudulent devices) of the NASD Rules of Fair Practice. Claimants further allege that the

actions of Respondents constitute RICO violations. With respect to Advest and Gruntal, Claimants assert liability on the basis of respondeat superior, failure to adequately supervise Mr. Kravitz, and by reason of Advest and Gruntal's status as control persons under the 1934 Act.

This matter came before the undersigned arbitrators for hearing on May 4, 1993, May 5, 1993, May 12, 1993, June 8, 1993, and July 7, 1993. On July 7, 1993, Claimants concluded the presentation of their evidence and rested. Several motions have been filed by the Respondents seeking to dismiss Claimants' claims. Specifically, Respondents have filed motions seeking to dismiss the 1934 Act and the RICO claims based on their applicable statutes of limitations; claims based on violations of the NASD Rules of Fair Practice on the ground that no private right of action exists; the RICO claims on the ground, inter alia, that Claimants failed to prove scienter; the breach of fiduciary duty claims and all claims by Co-Claimant Reine Penzer on the ground of failure of proof; and all claims to the extent that they are barred by Section 15 of the "Code of Arbitration Procedure" (six-year period within which to file claim).

The testimony revealed that since at least 1983, Dr. Penzer and his wife employed the services of Respondent, Kravitz, -- first, when he was with Advest, and after November 1987, when he moved to Gruntal. (R. at 85, 135). Dr. Penzer is an educated man with a Ph.D. in psychology and human relations, a practicing psychoanalyst, and a licensed clinical psychologist. (R. at 55-56.) Nevertheless, Dr. Penzer alleges that he is an unsophisticated investor who reposed complete trust and confidence in Mr. Kravitz. (R. at 114.) He alleges that he told Mr. Kravitz on numerous occasions that he only wanted to invest in safe and secure investments, and that Mr. Kravitz repeatedly assured him that his investments were "as good as the federal government." (R. at 92-93, 111, 113-14, 152.) Dr. Penzer and his wife signed the forms necessary to open their accounts at both Advest and Gruntal, but those forms did not indicate that the Penzers had decided to limit their investments to only those that were absolutely as safe and secure as the federal government.² Moreover, the record revealed that almost from the outset, investments were made in Dr. Penzer's accounts that could not be characterized as safe

The amended claim also alleges that Mr. Kravitz made unauthorized purchases of securities for Claimants' accounts in violation of the 1934 Act, Rule 10b-5, the common law, and the NASD Rules of Fair Practice. It appears that only one unauthorized purchase was made, and that that situation was immediately corrected. (R. at 112-13, 389-91.) Dr. Penzer admitted that on that one occasion he did not tell Mr. Kravitz that he did not want the unauthorized security or take other action to cancel the purchase, despite his awareness of the unauthorized purchase at the time of the transaction. (R. at 390). Prior to completion of Claimants' case, they presented no additional evidence of unauthorized purchases, and so, it appears from the record that Claimants are not pursuing independent claims based upon unauthorized purchases.

Indeed, the record reveals that Dr. Penzer signed agreements to open option accounts. (R. at 108-09, 139-40, 369, 381, 383; Claimants' Exhibits 2E, 6A, 6B.)

and secure "as the federal government." Thus, for example, between opening his account at Advest in April 1983 and December 1983, at least four allegedly "unsuitable" securities were purchased. See Claimants' Exhibits 3B and 18. The largest single investment was an investment in Hydro Optics in June 1983, an investment that declined in value from \$6,400.00 to \$2,300.00 in six months. See Claimants' Exhibit 3B. The Penzers allege that numerous and frequent unsuitable transactions occurred through 1989. Claimants' Exhibit 18.

It should also be noted that none of Dr. Penzer's accounts were discretionary accounts, nor is there any allegation that there were, with the one single exception noted above, supra note 1, any unauthorized trades. (R. at 113.)

From the beginning, Dr. Penzer received, and admits reviewing, appropriate confirmation slips and monthly account statements. (R. at 111-112, 116, 127-28, 152-53, 412, 456.) This, we believe, is the fundamental problem with Claimants' case. Although professing to be an unsophisticated investor, these confirmations and monthly statements are not contended to have misrepresented the actual status of the trading in Claimants' accounts or the account balances at any particular time, with the result that from the beginning Claimants could see what was happening in their accounts and the description of the securities being purchased.³ As shown above, it is not as though Dr. Penzer is an illiterate person of below-average intelligence. Further, Dr. Penzer has not insignificant financial-based abilities. Thus, he admits taking care of the books for his own business. (R. at 361-62.) He admits on at least one occasion to finding an error in his account and calling it to Mr. Kravitz's attention (R. at 412-14; Gruntal's Exhibit H.) He also admits understanding his brokerage statements sufficiently so that on one occasion when he discovered that securities were transferred from Advest into the wrong Gruntal account, he called that error to Mr. Kravitz's attention. (R. at 160.) Compare Claimants' Exhibits 7A and 3A.

But Dr. Penzer's admitted sophistication goes beyond that. He also admits investing in tax shelters recommended by his accountant. (R. at 77-78.) This fact raises yet another disturbing aspect of Dr. Penzer's testimony. Dr. Penzer testified that he filed income tax returns prepared by an accountant who, the evidence showed, took an active interest in Dr. Penzer's investments and recommended at least one tax shelter to Dr. Penzer. (R. at 356-359.) Dr. Penzer nevertheless asserted that he never reviewed his tax returns to see what securities losses or gains were being reported to the federal government (R. at 287-88, 457), and we are impliedly asked to assume that the accountant, although concerned with Dr. Penzer's investments, never alerted Dr. Penzer to the fact that he was losing money on speculative investments.

³ Despite Dr. Penzer's purported ignorance of the stock market, the arbitrators cannot help but notice that in testifying as to his pre-Advest investment history, Dr. Penzer testified that after owning AT&T stock, he then held some "over the counter" stocks for a short period. (R. at 68.) This is not the language or terminology of a completely market illiterate investor.

Continuing this same theme. Dr. Penzer also testified that he never read any of the brokerage account forms that he signed. (R. at 144; 386.) When confronted with the fact that he must have known that he had a margin account (and signed an appropriate form to open a margin account), Dr. Penzer denied having read the form and explained that the fact that he wrote checks against his account and noted the word "borrowed" on the checks simply meant that he was borrowing in some sense other than on margin. (R. at 386, 442.) See Advest's Exhibit L; Gruntal's Exhibit A.

The sum and substance of Dr. Penzer's case is that he never read anything that he signed, he never understood his confirmations or brokerage statements, he never read his income tax returns and, in essence, just believed that Mr. Kravitz was following purported instructions to invest in only safe and secure investments.

As to the purported instruction to Mr. Kravitz that he only invest in safe and secure investments, there are several problems in crediting Dr. Penzer's testimony. First, one must assume that he never observed a variance from those instructions in all of the confirmations and monthly statements that he received, or that if he did observe what was being purchased, he chose to ignore it. Second, the instructions would be contrary to the forms that were signed. Third, the instructions would have been at least somewhat contrary to his prior investment history. Testimony revealed that in 1982 Dr. Penzer invested approximately one-half of his then liquid assets in a business that returned 400% on his investment in less than three years, an investment that could hardly be classified as nonspeculative and as safe as the federal government. (R. at 75-76.)⁴ As noted above, tax strategic investments were also made, again somewhat inconsistent with the purported instructions. (R. at 287-89, 355-56.) Finally, Dr. Penzer admitted that a recent stroke may have negatively impacted his memory (including, we must assume, his memory with respect to the precise instructions he gave Mr. Kravitz). (R. at 493)⁵ We simply cannot credit, under these circumstances, the testimony that Dr. Penzer placed his complete, unquestioning trust and confidence in Mr. Kravitz.

In light of the foregoing, we believe that in the exercise of reasonable diligence, Dr. Penzer should have initially discovered no later than December of 1983 that Mr. Kravitz had

⁴ Likewise, Dr. Penzer made a unilateral decision to invest in Nutri Bevco in August of 1985 on the advice of the inventor of the product. He was so intent upon making this investment, that when Mr. Kravitz was unavailable, Dr. Penzer opened an account at Rooney Pace in order to complete the transaction. Mr. Kravitz advised Dr. Penzer that this was not an appropriate investment, and indeed, the company went out of business and Dr. Penzer suffered a loss. (R. at 318-22.)

⁵ Dr. Penzer also testified that his personal attitudes toward money may have compromised his memory. (R. at 468.)

violated the purported instructions to invest in only investments as safe and secure as the federal government.

First, as to the 1934 Act claims, these claims are barred by the applicable statute of limitations. Pursuant to Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson, 111 S. Ct. 2773, 2781 (1991), Dr. Penzer must have filed a claim within one year of discovering facts constituting the violations or, in all events, within three years of the alleged violations. Here the evidence establishes that the Claimants received brokerage statements up to the time they left Gruntal in December of 1989, brokerage statements that would have revealed the most recent of the alleged securities laws violations. Since this action was commenced over one year later on January 30, 1991, the securities fraud claim must be dismissed.

More fundamentally, however, Dr. Penzer was required to demonstrate scienter to prevail on his RICO and 10b-5 claims and, for that matter, his common law fraud claim. Ernst & Ernst v. Hochfelder, 425 U.S. 185, 193, 96 S. Ct. 1375, 1381 (1976); Cosmas v. Hasset, 886 F.2d 8, 13 (2d Cir. 1989); Katara v. D.E. Jones Commodities, Inc., 835 F.2d 966, 970-71 (2d Cir. 1987). The evidence produced by Dr. Penzer failed completely to support the allegations that there was any intention on the part of Mr. Kravitz or on the part of Advest or Gruntal to defraud the Penzers. Even viewing the standard for scienter as requiring only proof of recklessness, Claimants have failed to demonstrate that the Respondents' conduct was highly unreasonable in any respect. Given the evidence set forth at length above which demonstrates that Dr. & Mrs. Penzer permitted this rather consistent course of conduct to continue for a period of six years, during which time they continued to receive confirmations and monthly statements, we are not prepared under these circumstances to say that Mr. Kravitz or Advest or Gruntal acted unreasonably.

For very much the same reason, we also hold that the RICO claims are barred by the statute of limitations to the extent they are based on injury that occurred more than four years before the claims were instituted. The Supreme Court has held that RICO claims are covered by four-year statute of limitations. Agency Holding Corp. Malley-Duff & Assocs., Inc., 483 U.S. 143, 156, 107 S. Ct. 2759, 2767 (1987). The Second Circuit has held that a RICO claim accrues "each time plaintiff discovers or should have discovered an injury caused by defendants' [RICO] violation...." Bankers Trust Co. v. Rhoades, 859 F.2d 1096, 1105 (2d Cir. 1988), cert. denied, 490 U.S. 1007, 109 S. Ct. 1642 (1989).

The Claimants have asserted that the cause of action does not accrue under the Bankers Trust doctrine until after the Claimant becomes aware of the fact that he has been the victim of a RICO violation and he has suffered an injury (i.e., a stock loss alone is not enough to start the statute of limitations running). The Respondents argue that knowledge of the loss is sufficient. In support of their position, Claimants cite the panel to the decision of Judge Stanton in Dayton Monetary Assocs. V. Donaldson, Lufkin, Jenrette Securities Corp., Nos. 91 Civ. 2050, 91 Civ. 4944, 91 Civ. 5000, 91 Civ. 5622, 91 Civ. 6432, 1992 W.L. 204374 (S.D.N.Y. 1992). In that

case. Judge Stanton, in connection with a Rule 12(b)(6) motion, determined that issues of fact existed on that motion precluding any finding that as a matter of law the plaintiffs knew or should have known of the fraud there at issue. He recognized that the critical question was when did the Claimant "actually know, or in the exercise of due diligence should have known, of the fraudulent activities..". Id. at *3. In that case, on a motion to dismiss, Judge Stanton could not make that determination. Here, however, Claimants' case is complete, and they have submitted all of their evidence. What we are left with, is our conclusion that in the exercise of due diligence, Dr. Penzer should have discovered the purportedly fraudulent activities of the Respondents no later than December of 1983. It was at that point that Dr. Penzer should have realized that his purported instructions to Mr. Kravitz were not being obeyed. We believe that by their continued course of conduct, Claimants waived their right to complain about Mr. Kravitz's actions.

Looked at in another way, and as noted above, Claimants' failure to object to the way in which their accounts were managed precludes any finding of scienter on the part of Respondents. For the same reason Claimants were not free thereafter to complain about Advest or Gruntal. We note parenthetically that absolutely no evidence was ever submitted against Advest or Gruntal implicating in any way the supervision that they exercised over Mr. Kravitz. In any event, the claims here against all three Respondents fail because of the manner in which Claimants chose to shut their eyes to what was going on.⁶ See Goodman v. Shearson Lehman Bros., Inc., 698 F. Supp. 1078, 1083 (S.D.N.Y. 1988); Appel v. Kidder Peabody & Co., 628 F. Supp. 153, 157 (S.D.N.Y. 1986).

With respect to the claims based upon alleged violations of the NASD Rules of Fair Practice, case law supports the conclusion that no private right of action exists for breach of NASD Rules. SSH Co. v. Shearson Lehman Bros., Inc., 678 F. Supp. 1055, 1058 (S.D.N.Y. 1987). In any event, Claimants' counsel conceded during the hearings that unless Claimants could show breach of fiduciary duty, there was no private civil cause of action for violation of NASD Rules of Fair Practice, and that unless he could demonstrate fraud or scienter, he would have to show a breach of fiduciary duty in order to prevail. (R. at 266-272.)

Next, we come to the breach of fiduciary duty. These claims are based on the notion that unsuitable recommendations were made by the Respondents. For the reasons set forth above, we are not prepared to credit Dr. Penzer's testimony that he instructed Mr. Kravitz to buy only safe and secure investments as good as the federal government, but that even if he did, by virtue of Claimants' conduct thereafter, they waived the right to complain about the purchases and sales that were made. Moreover, as described above, we conclude that Dr. Penzer did not repose

⁶ For these reasons, it is not necessary for us to determine when the injury claims accrue for RICO purposes. But see Testone v. Niagara Mohawk Power Corp., No. 91-CV-1042, 1992 W.L. 72145 (N.D.N.Y. 1992).

complete trust and confidence in Mr. Kravitz. Supra at p. 7; Ambrosino v. Rodman & Renshaw, Inc., 635 F. Supp. 968, 973 (N.D. Ill. 1986).

For the reasons set forth herein, Respondents' motions to dismiss all claims are granted.

FORUM FEES

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

Non-refundable Filing Fee:	\$250.00
Hearing Session Fees:	\$1,000.00 x 10 sessions = \$10,000.00

1. Claimants deposited \$1,250.00 and shall remit the balance, \$9,000.00, to the NASD.
2. Claimants requested and were granted two postponements, for hearings scheduled in October, 1992 and March, 1993. This panel assessed \$1,000.00 for each postponement which Claimants have already paid.

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

ARBITRATION PANEL

Harold G. Levison, Esq.	-	Public Chairperson
Felix Wroblewski, MD.	-	Public Panelist
Edward N. Gioiella, Esq.	-	Industry Panelist

CONCURRING ARBITRATOR'S SIGNATURE

Harold G. Levison
Harold G. Levison, Esq.

Date of Decision: November 5, 1993

Jersey
STATE OF NEW ~~YORK~~
COUNTY OF *MORRIS*

S.S:

On this *4th* day of November, 1993, before me personally appeared Harold G. Levison, Esq. known to me to be the individual described in and who executed the foregoing instrument and he duly acknowledged to me that he executed the same.

Harold G. Levison
Harold G. Levison
Notary Public

CONCURRING ARBITRATOR'S SIGNATURE



Felix Wroblewski, MD



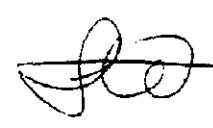
Date of Decision: November 5, 1993

STATE OF NEW YORK
COUNTY OF *Putnam*

S.S.:

On this *27th* day of October, 1993, before me personally appeared Felix Wroblewski, MD known to me to be the individual described in and who executed the foregoing instrument and be duly acknowledged to me that he executed the same.

ARLENE W. MICHELL
Notary Public, State of New York
No. 4030398
Qualified in Putnam County
Commission Expires April 22, 19*95*

 *in error* 

CONCURRING ARBITRATOR'S SIGNATURE

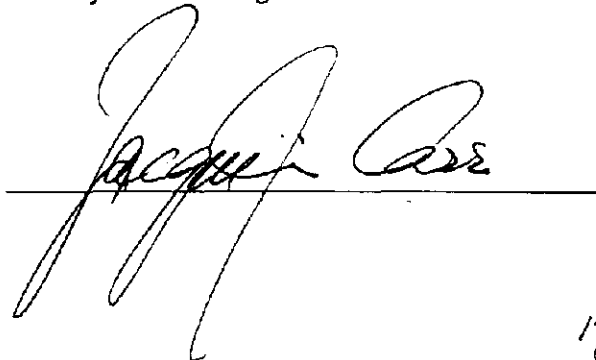

Edward N. Gioiella, Esq.

Date of Decision: November 5, 1993

STATE OF NEW YORK
COUNTY OF NEW YORK

S.S.:

On this day of October, 1993, before me personally appeared Edward N. Gioiella, Esq. known to me to be the individual described in and who executed the foregoing instrument and be duly acknowledged to me that he executed the same.



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