

NASD REGULATION, INC. AWARD

NASD REGULATION, INC. - OFFICE OF DISPUTE RESOLUTION

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In the Matter of the Arbitration Between

Name of Claimants

Ilene and Steven Schwartz

92-01588

Name of Respondents

CoreStates Securities Corporation  
Kevin Kelly

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**REPRESENTATION**

For Claimants Ilene and Steven Schwartz ("Claimants"): Steven Schwartz

For Respondents CoreStates Securities Corporation ("CoreStates") and Kevin J. Kelly ("Kelly"): Elizabeth Hoop Fay, Esq. and Gregory M. Harvey, Esq. of the law firm of Morgan, Lewis & Bockius, Philadelphia, PA

**CASE INFORMATION**

Statement of Claim filed: January 17, 1991.

Claimants' Submission Agreement signed on: January 28, 1992.

Joint Answer of Respondents CoreStates Securities Corporation and Kevin Kelly (collectively referred to as "Respondents") filed on: August 11, 1992.

Respondent CoreStates Submission Agreement executed by James B. Warden, President, CoreStates Securities Corporation on: August 6, 1992.

Respondent Kelly's Submission Agreement signed on: July 29, 1992.

**HEARING INFORMATION**

Preliminary Hearing with the Full Panel: January 18, 1995 - one session

Hearing Dates/Sessions:

September 24, 1996 - two sessions  
September 25, 1996 - two sessions  
September 26, 1996 - two sessions

October 21, 1996 - two sessions  
October 22, 1996 - two sessions  
October 23, 1996 - one session  
October 24, 1996 - two sessions  
November 7, 1996 - two sessions  
November 8, 1996 - two sessions  
November 18, 1996 - one session  
January 13, 1997 - two sessions  
January 14, 1997 - two sessions  
March 3, 1997 - two sessions  
March 6, 1997 - two sessions  
April 15, 1997 - two sessions  
April 16, 1997 - two sessions  
April 17, 1997 - two sessions  
April 18, 1997 - two sessions  
April 22, 1997 - two sessions  
April 29, 1997 - two sessions  
April 30, 1997 - two sessions  
May 22, 1997 - one session  
May 28, 1997 - two sessions  
July 7, 1997 - two sessions  
July 24, 1997 - two sessions  
August 12, 1997 - two sessions  
August 13, 1997 - two sessions  
August 14, 1997 - two sessions  
August 15, 1997 - two sessions  
September 5, 1997 - two sessions  
September 11, 1997 - two sessions  
September 12, 1997 - two sessions  
October 8, 1997 - two sessions  
October 9, 1997 - two sessions

Total Number of hearing sessions with the full panel = 66

Hearing Location: NASD Regulation, Inc., District Office, Philadelphia, PA

CASE SUMMARY

Claimants alleged, among other things, on January 26, 1985 they opened an account with Philadelphia

National Bank doing business as PNB Discount Brokerage Services "PNB". PNB is now known as CoreStates Securities Corporation and will be referred to as "CoreStates". Claimant alleged that Respondents solicited Claimants' business and promised Claimants that they would have virtually instantaneous execution of trades. Claimants alleged that in November of 1985 they began trading options with Respondents but that Respondents failed to timely sell Claimants' options, forcing Claimants to execute on their 221 November 135 calls on IBM. Claimants alleged that based on this experience Claimants virtually stopped trading options with Respondents. Claimants alleged that once again Respondents actively solicited Claimants to trade options, claiming that Respondents would provide direct access to the trading floor for all option trades. Claimants alleged that Respondents gave them a special telephone line and were told that no other customers had access to this line. Claimants' alleged that based on Respondents' representations that Claimants resumed trading options with Respondents. Claimants alleged that between April 25, 1986 and November 28, 1986, Claimants account diminished, the majority of the decline in Claimants' account was caused by Respondents' fraudulent and negligent trading practices and delays in placing orders. Claimants alleged that in September of 1986, Respondents actively solicited Claimants to trade index options, even though Kelly, the person primarily responsible for Claimants' account was not licensed to trade index options. Claimants alleged that they did not receive timely execution of their index option trades and that such delays caused Claimants to suffer losses. Claimants alleged that they later learned that Respondents were not sending their trades directly to the floor but that their trades were wired to an intermediary, National Financial Service Corporation ("NFSC"), who Claimants maintained delayed the orders and would wait an inordinate amount of time before wiring orders to Pershing Division of Donaldson Lufkin & Jenrette Securities Corporation ("Pershing"). Claimants alleged that when Respondents were confronted with the problem of untimely executions, Kelly promised to give Claimants substantial monetary adjustments. Claimants alleged that CoreStates reneged on this promise and that Kelly's position was subsequently "eliminated".

Claimants also alleged that throughout this time period, Respondents frequently obtained funds from other bank accounts held at CoreStates by Claimants, without Claimants prior knowledge or approval. Claimant alleged that they told Respondents to stop raiding their other accounts, but Kelly continued to do so. Claimants further alleged that during this time period Respondents violated federal requirements by allowing Claimants to buy options on margin. Claimants alleged that CoreStates maintained tapes of orders that were telephoned in and other matters, Claimants alleged that Respondents destroyed tape recordings of conversations with Claimant Steven Schwartz concerning this dispute.

Respondents categorically denied all allegations of wrongdoing in the Claimant Ilene Schwartz's ("Mrs. Schwartz") account. Respondents maintained, among other things, that Steven Schwartz, Mrs. Schwartz' son, had authority to trade in his mother's account, but that he does not have standing to sue Respondents for losses allegedly sustained in his mother's brokerage account. Respondents maintained that CoreStates is a discount brokerage firm and that all trades were ordered by either Mrs. Schwartz or Steven Schwartz. Respondents maintained that no trades were solicited by Kelly or any other representative of CoreStates. Respondents maintained that Claimants exercised complete control over Mrs. Schwartz account. Respondents maintained that they never solicited options transactions from Claimants. Respondents maintained that every order placed by Claimants was placed by CoreStates and Kelly in a timely manner. Respondents maintained that Claimants telephoned orders directly to CoreStates and the orders were immediately entered into NFSC's on-line order entry system, which routed the orders either directly to the floor of the appropriate exchange or to NFSC's block desk, depending on the size and type of the order being entered. Respondents maintained that at times, NFSC used Pershing to execute

orders. Respondents maintained that Claimants were never promised "virtually instantaneous execution of trades." Respondents maintained that they never represented to Claimants that CoreStates "would provide direct access to the trading floor for all option trades." Respondents maintained that Claimants knew that CoreStates cleared through NFSC. Respondents maintained that it is not uncommon for an order of substantial size to be executed in multiple parts because it is not possible to execute the entire order at the same time and price. Respondents maintained that Mrs. Schwartz' account was actively traded, CoreStates designated a particular telephone line on which Claimants could call in orders so that their calls would be answered more quickly than if they had come from a general line. CoreStates maintained that at the time Claimants were trading as CoreStates, the customers had knowledge that orders that were placed by telephone were tape recorded. Respondents maintained that no tapes of conversation with the Claimant were intentionally destroyed by Respondents; they were reused periodically as were all the tapes. Respondents denied Claimants allegation that Respondents failed to sell 221 IBM November calls before expiration. Respondents maintained that Ilene Schwartz promptly sold 22,100 shares of IBM purchased as a result of the exercise of the 221 calls at a profit of more than \$30,000. Respondents maintained that Claimants allegation that decreases in equity were due to trading losses or other losses caused by Respondents' handling of their orders was false. Respondents maintained that between April 1986 and November 1986, Claimants withdrew more than \$2.5 million from the account and deposited, during the same period of time, less than \$700,000 in the account. Respondents maintained that Claimants did not make purchases of options on margin; all option purchases were paid for in full with funds available in the account or by the deposit of additional funds into the account. Respondents maintained that in opening the brokerage account, Mrs. Schwartz instructed CoreStates in writing that when securities were sold in her account, the proceeds should be deposited in Philadelphia National Bank Account #0435-9619, and that when securities were purchased for her account, that same Philadelphia National Bank account should be charged in order to pay for the transaction. Respondents maintained that neither CoreStates nor Kelly ever offered to compensate Claimants for any trading losses that Mrs. Schwartz allegedly incurred.

Respondents asserted that Claimants' claims are barred in whole or in part by Pennsylvania's two-year statute of limitations on tort actions and four year statute of limitations on contract actions, as well as by principles of waiver, estoppel, ratification, and contributory negligence. Respondents maintained that to the extent that events occurred more than six years prior to the filing of this arbitration, those claims are barred by Rule 10304 of NASD Regulation, Inc.'s Code of Arbitration Procedure ("Code").

#### **RELIEF REQUESTED**

Claimants requested: damages in an amount of approximately \$1,000,000; the return or disgorgement of all commissions paid to Respondents.

Respondents requested: that Claimants' claim be dismissed.

#### **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 NASD Regulation.

On January 18, 1995, Respondents Pershing Division of Donaldson, Lufkin & Jenrette Securities Corporation and National Financial Services Corporation were dismissed as parties from this case.

There were two other major motions filed in this case, one by each side. Claimants filed a motion for judgment because of Respondents alleged repeated failure to comply with Claimants' discovery requests and the Panel's Orders. This motion was denied. Respondents filed a motion to dismiss Claimants' claim because the claim was not timely filed, based on the applicable statutes of limitations. This motion was also denied.

### AWARD

After considering the motions, pleadings, testimony and 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 Panel finds that Claimants have carried their burden of proving their claim by the fair weight and preponderance of the evidence and are awarded compensatory damages in the amount of \$402,500.00; plus interest at a rate of 3% for 10.5 years of \$126,800 for a total award against Respondents CoreStates Securities Corporation and Kevin Kelly jointly and severally in the amount of \$529,300.00.
2. Claimants' claim for punitive damages is denied.
3. The parties shall bear their respective costs and attorneys fees except as costs and forum fees are delineated below.
4. All other claims for relief not specifically addressed herein are denied in their entirety.

### FORUM FEES

Pursuant Rule 10332 of the Code of Arbitration Procedure, the following Forum Fees are assessed.

66 hearing sessions x \$1,000 = \$66,000

Forum Fees Assessed: 25% against Claimants, jointly and severally; 25% against Respondent Kevin Kelly; and 50% against Respondent CoreStates Securities Corporation.

Therefore the amount assessed against Claimants for forum fees, jointly and severally is \$16,500. The amount assessed against Respondent Kevin Kelly is \$16,500. The amount assessed against Respondent CoreStates Securities Corporation is \$33,000.

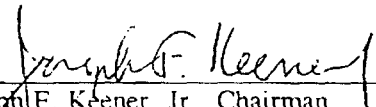
Schwartz Award  
Case No. 92-01588  
Page -6-

Fees are payable to NASD Regulation, Inc.

Date Award Signed

Concurring Arbitrators' Signatures

11-1-97

  
\_\_\_\_\_  
Joseph F. Keener, Jr., Chairman  
Public Arbitrator

\_\_\_\_\_  
John W. Lear, Panelist  
Public Arbitrator

Date Award Signed

Dissenting Arbitrator's Signature

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Charles W. Lake, Panelist  
Industry Arbitrator

Charles W. Lake dissents from all aspects of this award, liability, damages and forum fees.

Date Award Served by NASD Regulation, Inc. November 4, 1997

Schwartz Award  
Case No. 92-01588  
Page -6-

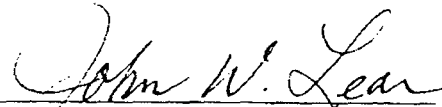
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Public Arbitrator

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John W. Lear, Panelist  
Public Arbitrator

Date Award Signed

Dissenting Arbitrator's Signature

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Charles W. Lake, Panelist  
Industry Arbitrator

Charles W. Lake dissents from all aspects of this award, liability, damages and forum fees.

Date Award Served by NASD Regulation, Inc. November 4, 1997

Schwartz Award  
Case No. 92-01588  
Page -6-

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Public Arbitrator

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\_\_\_\_\_  
John W. Lear, Panelist  
Public Arbitrator

Date Award Signed

Dissenting Arbitrator's Signature

11/1/97

Charles W. Lake  
Charles W. Lake, Panelist  
Industry Arbitrator

Charles W. Lake dissents from all aspects of this award, liability, damages and forum fees.

Date Award Served by NASD Regulation, Inc. November 4, 1997