

N.A.S.D. AWARD

NATIONAL ASSOCIATION OF SECURITIES DEALERS

In the Matter of the Arbitration Between

Name of Claimant

Robert F. Merriman, Individually and as Trustee
of the Robert F. Merriman, M.D., P.A. Profit Sharing
Plan and Trust

93-01482

Name of Respondents

Shearson Lehman/American Express Inc., n/k/a
Smith Barney Shearson, Inc.;
Lester Pound

REPRESENTATION

For Claimant: Robert F. Merriman, Individually and as Trustee of the Robert F. Merriman, M.D., P.A. Profit Sharing Plan and Trust ("Merriman") was represented by A.W. SoRelle, III, Esq. of Underwood, Wilson, Berry, Stein & Johnson, P.C., located in Amarillo, Texas.

For Respondents: Shearson Lehman/American Express, Inc., now known as Smith Barney Shearson, Inc. ("Shearson") and Lester Pound ("Pound") were represented by Victor A. Machinski, Jr., Esq., Smith Barney Shearson, Inc., New York, New York.

CASE INFORMATION

Statement of Claim filed: April 14, 1993.

Claimant's Submission Agreement signed on: March 30, 1993 by Robert F. Merriman, Individually and as Trustee of the Robert F. Merriman, M.D., P.A. Profit Sharing Plan and Trust.

Statement of Answer filed by Respondents Shearson and Pound on: June 25, 1993.

Respondent Shearson's Submission Agreement signed on: June 25, 1993 by Victor A. Machinski, Jr., Vice President, Shearson Lehman Brothers, Inc.

Respondent Pound did not file an executed submission agreement.

Claimant's Motion for Leave to File a Supplemental Pleading filed: February 14, 1994.

Opposition to Motion for Leave to File a Supplemental Pleading filed February 25, 1994.

Respondents' Motion to Dismiss filed: February 4, 1994.

Claimant's Response to Motion to Dismiss filed: February 12, 1994.

Respondents' Reply Memorandum in Support of Motion to Dismiss filed: February 25, 1994.

HEARING INFORMATION

Pre-Hearing Conference: None Held.
Hearing Dates/Sessions: June 14, 1994 for Two (2) sessions;
June 15, 1994 for Two (2) sessions; and
June 16, 1994 for Two (2) sessions.

Hearing Location: Albuquerque, New Mexico.

CASE SUMMARY

Claimant Merriman alleged that Respondent Pound, while employed by or acting as an agent for Respondent Shearson, placed Merriman in unsuitable securities, such as limited partnerships, even though he was advised that Merriman wanted to preserve principal and did not want the trust assets invested in risky limited partnerships. Merriman specifically alleged that:

1. In 1986, Merriman, as trustee, gave Respondents discretionary authority to direct the investments of the Trust and thereafter, Respondents selected the specific investments and directed Merriman and the Custodian to make specific investments. Respondents knew that Merriman was relying upon them to select the investments and determine a proper investment strategy;
2. Merriman advised Pound that he was concerned about safety of principal and did not want the account invested in risky limited partnerships. Merriman was led to believe that the investments were backed by Shearson and were the equivalent of high quality debt instruments such as bonds. Pound failed to disclose the risk, lack of liquidity, and lack of diversity of the investments and Respondents benefitted by selecting investments with high up-front commissions and other benefits;
3. Respondents directed and caused almost the entire corpus of the Trust to be invested in non-liquid limited partnerships and funds. Given Merriman's age and stated objectives, the investment portfolio selected by Respondents was highly inappropriate, and appeared to have been selected with Respondents' benefit in mind; and

4. Merriman was unaware of the lack of market for these investments due to the manner in which the investments were routinely reported. Because he relied upon Respondents to select appropriate investments, Merriman did not inquire about the liquidity and propriety of the investments until he reviewed his plan in anticipation of retirement. The needs of Merriman and the Trust require near term liquidity and more appropriate diversity, while currently no market exists for these assets at or near their stated value.

— Based upon the above allegations, Merriman asserted claims for breach of fiduciary duty; breach of fiduciary duty under §404(a) 29 U.S.C. §1104 (a) of ERISA; violation of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b), and Rule 10b-5 (17 C.F.R. 240), the Tex. Bus. & Comm. Code §27.01 and the Texas Securities Act, Vernon's Ann. Civ.St. Art. 581-33 , and violation of Deceptive Trade Practices-Consumer Protection Act of the State of Texas ("DTPA"), codified as part of the Texas Business and Commerce Code, §§17.41 et seq.

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

1. At the time the account was opened in 1986, Merriman advised Pound that he would have to work at least ten more years. This disclosure was used in establishing time horizons for the investments as well as Merriman's liquidity needs and Pound recommended investments with an anticipated time to maturity of six to eight years, which was satisfactory and acceptable to Merriman;
2. The trust account was not a discretionary account. Merriman was fully informed and was an active participant in selecting and directing each of the investments made;
3. Of the four investments at issue that are not subject to a class action or which have been liquidated with returns in excess of the investment, all are viable and have substantial current value;
4. Pound discussed with Merriman the pertinent risk factors regarding the limited partnership investments, including the holding period and the illiquidity when making his recommendation. Merriman responded that illiquidity was not a factor because the funds would not be withdrawn until his retirement in 1996. Merriman was presented with a prospectus for each limited partnership which set forth all necessary disclosures and at no time did Respondents withhold or misrepresent information concerning the investments;
5. Because of the events of 1987, Merriman was concerned about the volatility of the stock and bond markets, and considered various investment alternatives which he asked Pound to recommend. Merriman's aversion to stocks and bonds

and his retirement plans made him suitable for the limited partnership investments. Each investment was made with his express authorization after discussion of objectives and holding period; and

6. The funds invested were not needed for current expenses, the investments were diversified among a number of limited partnerships, and the investments were consistent with the investment objectives and financial capabilities of Merriman at the time they were made. Therefore, the limited partnerships were in all respects suitable for him and suitability cannot be measured by profitability.

In addition, Respondents asserted several affirmative defenses, including the following:

1. The Statement of Claim failed to state a claim upon which relief could be granted;
2. Claimant was a competent, well-educated and experienced investor who had or should have had all material facts regarding the investments made, including the associated risks. Any loss or diminution of value was the result of unforeseen market fluctuations and was within the risk Merriman assumed;
3. The damages claimed have no causal relationship with any act committed or attributable to Respondents;
4. The claims, in whole or in part, are barred by the principles of laches, waiver, estoppel and ratification, and are time barred; and
5. The damages allegedly sustained were caused, in whole or in part, by Merriman's failure to mitigate his damages.

In addition, Respondents brought a Counterclaim against Merriman individually for indemnification, contribution or set-off, claiming that Merriman, as Trustee, controlled the transactions and that if the Respondents incurred any liability to the Trust, the liability would be due to the acts and misconduct of Merriman as Trustee.

RELIEF REQUESTED

Claimant Merriman requested entry of an award against Respondents for damages in excess of \$300,000.00; recovery of all benefits received by Respondents as a result of their violations of ERISA in an amount in excess of \$100,000.00; two times the amount of their actual damages not exceeding \$1,000.00 and three times all damages exceeding \$1,000.00; recovery of damages in accordance with Section 17.50 of the DTPA; all costs associated with the lawsuit and arbitration; all attorneys' fees and expenses; interest; and such further relief as the Claimant was

entitled.

Respondents requested that the Statement of Claim be dismissed in all respects; Respondents be awarded the relief requested in their counterclaim; and Respondents be awarded their fees and expenses, including attorneys' fees, forum fees and all other costs of this proceeding.

OTHER ISSUES CONSIDERED & DECIDED

Respondent Pound 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.

Upon review of the Motion for leave to File a Supplemental Pleading and all responses thereto, the Panel determined on June 14, 1994 that the Motion would be denied.

Pursuant to a stipulation of the parties signed March 3, 1994 and filed June 1, 1994, claims regarding the investment in Stamford Towers Limited Partnership were excluded from any claim for damages. Based upon this stipulation, the Motion to Dismiss filed February 4, 1994 by Respondents is moot.

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 post hearing submissions, 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 with prejudice and denied in its entirety;
2. Respondents' Counterclaim is hereby dismissed with prejudice and denied in its entirety;
3. The parties shall bear their own costs of arbitration, including attorneys' fees, except for those specifically enumerated herein;
4. Any relief not specifically granted is hereby denied.

OTHER COSTS

The NASD shall retain the \$750.00 postponement fee paid by Respondents on November 19,

1993.

FORUM FEES

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

The National Association of Securities Dealers, Inc. shall retain the \$200.00 non-refundable claim filing fee and the \$800.00 hearing session deposit previously deposited by the Claimant, Robert F. Merriman, individually and as Trustee of the Robert F. Merriman, M.D., P.A. Profit Sharing Plan and Trust. Respondent Shearson Lehman/American Express Inc., n/k/a Smith Barney Shearson Inc. and Lester Pound is liable for and shall pay to Claimant Robert F. Merriman, individually and as Trustee of the Robert F. Merriman, M.D., P.A. Profit Sharing Plan and Trust the sum of \$1,000.00 as reimbursement of the claim filing fee and the hearing sessions deposit. In addition, Respondent Shearson Lehman/American Express Inc., n/k/a Smith Barney Shearson Inc. and Lester Pound is liable for and shall pay to the NASD forum fees in the sum of \$3,700.00.

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

Concurring Arbitrators' Signatures

Name

Date

/s/ Barry H. Barnett, Esq.
Barry H. Barnett, Esq.
Public Arbitrator
Chairperson

September 13, 1994

/s/ Peter J. Broullire, III
Peter J. Broullire, III
Public Arbitrator

September 14, 1994

/s/ Mike Edward Mimovich
Mike Edward Mimovich
Industry Arbitrator

September 27, 1994

For NASD Use Only

Date of Decision: September 27, 1994