

N.A.S.D. AWARD

NATIONAL ASSOCIATION OF SECURITIES DEALERS

In the Matter of the Arbitration Between

Name of Claimant

City of Englewood

93-03625

Name of Respondents

Murchison Investment Bankers, Ltd.
Kenneth Schulte

REPRESENTATION

For Claimant City of Englewood ("Claimant") appeared Michael P. McNamee, Esq. of Buren, Turner & McNamee located in Dayton, OH.

For Respondents Murchison Investment Bankers, Ltd. ("Murchison") and Kenneth Schulte ("Schulte") appeared Dennis H. Taylor, Esq. of the law firm of Taylor & Associates located in Houston, TX.

CASE INFORMATION

Statement of Claim filed on September 15, 1993. In addition, Claimant filed a First Amended Statement of Claim, Second Amended Statement of Claim, and a Third Amended Statement of Claim. Claimant's Submission Agreement was signed on September 13, 1993.

A Joint Statement of Answer was filed by Respondents Murchison and Schulte on November 22, 1993. Respondent Murchison's Submission Agreement was signed on November 19, 1993 and Respondent Schulte's Submission Agreement was signed on November 18, 1993.

HEARING INFORMATION

Hearing Dates/Session:	May 11, 1994	-	Three Sessions
	May 12, 1994	-	Two Sessions

The hearing was held at the Marriott Hotel located in Cincinnati, Ohio.

CASE SUMMARY

The City of Englewood, Ohio ("Claimant") alleged that Respondent Kenneth Schulte ("Schulte") as an agent of Respondent Murchison Investment Bankers, Ltd. ("Murchison") contacted and represented to Joan M. Huls ("Huls"), Finance Director of Claimant, and Eric A. Smith ("Smith"), City Manager, that Schulte could increase the yield of Claimant's portfolio by purchasing government securities which had yields much higher than any securities then held in Claimant's portfolio; that on approximately July 13, 1990, in reliance upon the representations made by Respondents, Claimant purchased an FNMA stripped mortgage Trust 51 ("Security I") for \$100,489.65; that on approximately December 13, 1990, upon the advice and recommendation of Schulte, Claimant sold Security I for \$99,970.95 and purchased a second FNMA stripped mortgage Trust 50 ("Security II") for \$99,341.36; that on approximately July 16, 1993, due to the rapid repayment on the underlying mortgages, Claimant had no option but to sell Security II for \$8,494.99; that during the ownership of Security II, Claimant received interest payments totalling \$39,851.68.

Claimant also alleged that Respondents violated Section 12(1) of the 1933 Act, 15 U.S.C. Section 77e(a)(1) by failing to register Security I and Security II; that Respondents violated Section 12(2) of the 1933 Securities & Exchange Act, 15 U.S.C. Section 77(1) by making false communications and omissions of material facts necessary to avoid misleading Claimant; that Respondents violated Section 17(a) of the 1933 Securities & Exchange Act, 15 U.S.C. Section 77q(a) for acting with the intent to defraud Claimant; that Respondents violated Section 10(b) of the 1934 Securities & Exchange Act, and SEC Rule 10(b)(5) promulgated thereunder by using instrumentalities of interstate commerce and the mails to defraud Claimant who relied on Respondents' statements and representations; and that Respondents violated the NASD Rules of Fair Practice, Article III, Section 1 and Section 2 by recommending, marketing, and selling the securities misrepresented as "risk-free" investments which were backed and guaranteed by the United States Federal Government. Claimant further alleged that Murchison breached its duty to supervise and review the actions of Schulte as required by the NASD Rules of Fair Practice, Article III, Section 27(a); that Respondents made misrepresentations on which Claimant relied when inducing Claimant to purchase the aforementioned securities, in violation of Ohio Rev. Codes Section 17097.44(B)4 and 1707.44 (G), and Ohio Common law fraud; that Respondents negligently failed, and alternatively, had a duty to disclose material information concerning those investments; that Respondents breached their fiduciary duty with Claimant by such conduct; and that as a result of such violations, Respondent proximately injured and damaged Claimant in the amount of \$50,994.69 of its principal investment, plus loss of invested money and other consequential damages, for a total of approximately \$90,846.37.

Respondents maintained that in July, 1990, Schulte recommended the FNMA investments as a more suitable purchase than the non cash-flowing CD which had

a lower yield, and as a hedge against rising interest rates. Further, Respondent maintained that Schulte recommended a purchase position of about \$100,000.00, representing 2.5 percent of Claimant's available funds for long term investments; that the investments were guaranteed by Fannie Mae, but not that it was risk free; that Schulte recommended and Claimant purchased Security I which was sold in December, 1990 after Claimant received interest payments of \$8,014; that Huls assured Schulte in response to his inquiry that purchasing these Securities did not violate any of the City's investment or regulatory policies; and that Schulte recommended the purchase of Security II because it had a higher projected yield than Security I. Moreover, Respondents maintained that Huls received monthly summaries of the current status of the investments; that as of May, 1991 Huls expressed no dissatisfaction with the December, 1990 purchase; that on July 12, 1991, Ron Pate, who handled the account at the time, that the Security II was no longer a satisfactory investment because of the unexpected decline in the interest rates and recommended another investment yielding 20% at the time; that Huls said that she was not interested in making any portfolio changes with Murchison and would "Play out" the disputed investment; that one year later, another Murchison representative telephoned Huls and discussed the current condition of the account and made the same recommendation as Pate; that after sending current information to Mark Brownfield, Counsel to the City of Englewood sent a demand letter to Murchison seeking restitution for the loss on the second investment; that Murchison counsel sent a letter dated June 24, 1993 and a second letter on July 2, 1993.

Respondents maintained that all claims against Respondents by Claimant should be dismissed as there is no private cause of action for violations of NASD Rules and Regulations nor for Section 17(a) of the Securities Act of 1933; that the claims are barred, in whole or in part, by the applicable statute of limitations and the doctrine of laches; that Huls was an experienced and knowledgeable investor who controlled and knowingly approved the investments in dispute; and that Schulte's recommended purchase was suitable under the then market conditions and factually supportable. Further, Respondent maintained that any losses to Claimant's account were directly and proximately caused by the changed interest rates which Huls was aware of no later than July 1991; that neither Murchison nor Schulte acted recklessly or with the requisite intent to deceive or conspire to defraud with respect to Claimant; that Schulte made no material misstatement or omission to Huls or anyone else associated with Claimant; that Respondents made good faith recommendations that were suitable to Claimant's needs; and that Claimant failed to mitigate its damages after Huls was specifically told in July, 1991 of the interest rate risk. In addition, Respondent maintained that Huls, fully aware of the volatility of the investments, assumed the interest market risk of the Security II purchase, even after being advised of the adverse effect on the security due to the declining interest rate.

RELIEF REQUESTED

Claimant requested an award in the amount of \$50,994.69 as a result of the loss of its principal investment, plus the loss of the use of the invested money and other consequential damages, for a total estimated damage amount of \$90,846.37 or such greater amount to be proven at the arbitration hearing, and hereby requests a joint and several award in that amount against Respondents. In addition, punitive damages and Attorneys' fees, as permitted under Ohio common law of fraud.

Respondents requested that Claimant's statement of claim be dismissed with costs assessed against Claimant.

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. Respondent Murchison be and hereby is liable and shall pay to the Claimant the sum of \$9,000.00, interest specifically excluded.
2. Respondent Schulte be and hereby is liable and shall pay to the Claimant the sum of \$4,500.00, interest specifically excluded.
3. All claims against the Respondents for punitive damages be and hereby are denied.
4. All claims against the Respondents for attorneys' fees be and hereby are denied.
5. Each party shall bear their respective costs, including attorneys' fees.

FORUM FEES

Pursuant to Section 43c of the Code of Arbitration Procedure, the following Forum Fees are assessed:

5 sessions X \$500 = \$2,500 minus hearing session deposit of 500 = net \$2,000 due.

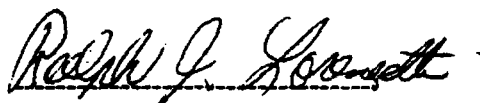
Respondents be and hereby are liable, jointly and severally, and shall pay to the NASD the sum of \$2,000.00 representing outstanding forum fees.

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

Concurring Arbitrators' Signatures
Name

Richard S. Wayne, Esq.
Chairperson - Public Arbitrator

Wallace E. Sarran, Jr.
Industry Arbitrator



Ralph J. Lorenzetti
Public Arbitrator

Executed on:
Date of Decision: ~~7/12/94~~ 7/27/94

Date of Decision: July 27, 1994

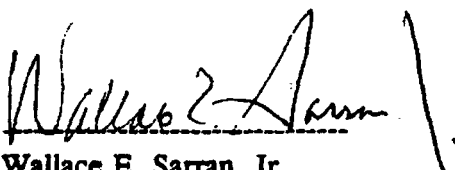
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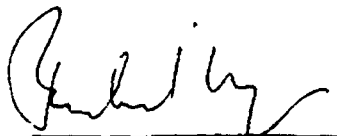
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