

AWARD

NASD Regulation, Inc. Office of Dispute Resolution

In the Matter of the Arbitration Between

Alice Shotwell Gustafson,
as Trustee for the Alice Gustafson
Revocable Living Trust,

Claimant and Counter-Respondent,

v.

No. 94-00401

Shearson Lehman Brothers,
n/k/a Smith Barney, Inc., and
James F. Peters, Jr.,

Respondents and Counter-Claimants.

REPRESENTATION OF PARTIES

Claimant and Counter-Respondent Alice Shotwell Gustafson, as Trustee for the Alice Gustafson Revocable Living Trust ("Claimant") was represented by Joseph H. Spiegel, Esq. of Law Offices of Joseph H. Spiegel, P.C. located in Southfield, Michigan and J. Laevin Weiner, Esq. of Law Offices of J. Laevin Weiner located in Bloomfield Hills, Michigan.

Respondent and Counter-Claimant Shearson Lehman Brothers, n/k/a Smith Barney, Inc. ("Smith Barney") was represented by William A. Hohauser, Esq. of Salomon Smith Barney, Inc. located in New York, New York.

Respondent and Counter-Claimant James F. Peters, Jr. ("Peters") was represented by Andrew J. McGuinness, Esq. of Dykema Gossett, PLLC located in Ann Arbor, Michigan.

CASE INFORMATION

The Statement of Claim was filed on or about February 1, 1994.

Claimant's Amendment to Include Additional Exhibits to the Statement of Claim was filed on or about March 20, 1995.

The Amended Statement of Claim was filed on or about June 27, 1995.

Claimant's Submission Agreement was signed on March 15, 1994.

The Statement of Answer of Respondent Smith Barney was filed on or about June 24, 1994.

Smith Barney's Statement of Answer to the Amended Statement of Claim was filed on or about August 7, 1995.

The Submission Agreement of Respondent Smith Barney was signed on June 2, 1994.

The Statement of Answer of Respondent Peters was filed on or about June 24, 1994.

The Corrected Statement of Answer of Respondent Peters was filed on or about July 14, 1994.

Respondent Peters' Statement of Answer to the Amended Statement of Claim was filed on or about September 6, 1995.

Respondent Peters' Modified Submission Agreement was signed on June 27, 1994.

Claimant's Post-Hearing Submission was filed on or about June 17, 1998.

Respondent Smith Barney's Post-Hearing Submission was filed on or about June 22, 1998.

Respondent Peters' Post-Hearing Submission was filed on or about June 25, 1998.

Claimant's Reply to the Post-Hearing Submissions was filed on or about June 26, 1998.

HEARING INFORMATION

The telephonic pre-hearing conferences were held on:

May 26, 1995 for one (1) session; January 23, 1996 for one (1) session; February 7, 1996 for one (1) session; April 11, 1997 for one (1) session; June 9, 1997 for one (1) session; and September 22, 1997 for one (1) session.

The hearing was held on:

June 17, 1997 for two (2) sessions; June 18, 1997 for two (2) sessions; June 19, 1997 for two (2) sessions; July 8, 1997 for two (2) sessions; July 9, 1997 for two (2) sessions; July 10, 1997 for two (2) sessions; October 28, 1997 for two (2) sessions; October 29, 1997 for two (2) sessions; January 5, 1998 for two (2) sessions; January 6, 1998 for two (2) sessions; January 7, 1998 for three (3) sessions; June 12, 1998 for two (2) sessions; and June 13, 1998 for one (1) session.

CASE SUMMARY

Claimant is the trustee of the Alice Gustafson Revocable Living Trust (the "Trust"). Respondent Peters was a broker with Smith Barney.

Claimant alleged that she first came in to contact with Respondent Peters as a result of opening a business account for her company, Hubert Distributors, Inc. Claimant contended that Peters convinced her to entrust him with the running of an account for some of her personal funds. Claimant eventually opened an account on behalf of the Trust with Smith Barney and Peters (jointly referred to as "Respondents"). Claimant asserted that at this time most of Claimant's personal brokerage accounts were handled by professional money managers.

Claimant maintained that, sometime in March 1992, after solicitation by Peters, Claimant agreed to entrust more of her moneys with Peters and allowed him to transfer outside accounts in the Trust account. According to Claimant, Peters liquidated these accounts' assets and repurchased them in the Trust account thereby generating a large amount of commissions. Claimant alleged that, also in March 1992, Claimant agreed to grant Peters discretion over the Trust account.

Claimant contended that, from the period of March 1992 through April 1993, Peters handling of the account changed. Claimant asserted that the amount of trading, commissions and costs went up markedly. Claimant also maintained that the focus of the account shifted to more risky investments. Claimant alleged that, particularly in the last several months of this period, there was a large amount of in-and-out trading and the commissions were about \$70,000. Claimant contended that the cost to equity ratio, commissions earned, and turnover rate increased significantly in March 1992, then again in late 1992 and once more time in early 1993. Claimant asserted that she did not advise Peters of any change in investment goals during this time period.

Claimant asserted that during this time Peters and his staff, known as The James Peters Group, were running their own form of mutual fund, picking stocks, then purchasing them (or selling them) for his various customer accounts en masse. Claimant maintained that several of his picks were directly against Smith Barney's recommendations for the stocks. Claimant alleged that Smith Barney was aware of the trading and large commissions in Claimant's account but did not

question it.

Claimant contended that Peters planned on leaving Smith Barney for Kidder Peabody and began soliciting his clients, including Claimant, to transfer their accounts. Claimant asserted that, after his departure in May 1993, the branch office manager and the new Smith Barney registered representative for the Trust account contacted Claimant to meet with her regarding her accounts. Claimant maintained that, in the meeting and on the printed portfolio review they provided to her, they pointed out large unrealized losses in the account and suggested a repair strategy, which consisted of putting most of her money back in accounts run by professional money managers, just as Claimant had done prior to entrusting the moneys to Peters in March 1992. Claimant alleged that during the meeting the branch office manager admitted he should have watched the account more carefully when it was under Peters' control.

Respondents denied all liability to Claimant in their respective Statements of Answer.

Respondents alleged that Claimant's account was handled in accord with her investment objectives, which included but were not limited to appreciation with risk. Respondents contended that the transactions were proper and were executed based upon a reasonable basis for their recommendation, as required by NASD regulations. Respondents asserted that Claimant maintained an active role in the management of her account and made suggestions for trades (including short sales) from time to time. Respondents maintained that they had numerous meetings (subsequent to granting discretion) with Claimant and her representatives and gave much information in order to keep Claimant fully apprised of the status of her account.

Respondents further alleged that Claimant, a woman of extensive wealth, invested in leading companies which in no fashion could be considered unsuitable. Respondents contended that the turnover rate in the account at issue, which was conceded to be two (2) at most, by law is not considered excessive under the governing case law. Respondents asserted that Claimant's account was profitable in the approximate amount of \$160,000 and that Claimant is merely attempting, through hindsight, to extract additional profits through this arbitration claim.

Respondents counterclaimed for fees and expenses they were obliged to pay during the course of this arbitration, on the grounds that this arbitration claim was frivolous and further that the proceedings were unduly lengthened by the conduct of Claimant's counsel.

RELIEF REQUESTED

Claimant sought repayment of commissions and fees in the amount of \$199,444, payment for lost opportunity in the amount of \$225,317, payment of attorneys fees in the amount of \$212,381 and payment for out-of-pocket costs incurred during this litigation in the amount of \$42,579.59, as a

result of the alleged excessive trading and inappropriate strategy conducted Respondents.

Respondents requested that the Statement of Claim be dismissed in its entirety with prejudice, plus an award of attorney fees and costs.

In its Counterclaim, Smith Barney sought recovery of \$100,000 in costs (including \$25,000 in court reporter and transcription charges), plus \$75,000 in attorney's fees, as sanctions, against either Claimant or her counsel.

At the conclusion of the hearing, Peters requested an award of \$62,500 against Claimant as partial compensation of attorney's fees incurred and an additional \$162,500 in partial compensation for Respondent Peters's lost time, for a total of \$225,000.

OTHER ISSUES CONSIDERED & DECIDED

Respondent Peters did not file with NASD Regulation, Inc. Office of Dispute Resolution a properly executed NASD Submission Agreement but is required to submit to arbitration pursuant to §10301 of the NASD Code of Arbitration Procedure (the "Code"), and having answered the claim, appeared and testified at the hearing, is bound by the determination of the arbitration panel on all issues submitted.

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 original(s) remain on file with NASD Regulation, Inc. Office of Dispute Resolution.

AWARD

After considering the pleadings, the testimony, and the evidence presented at the hearing, as well as the post-hearing submissions, and having deliberated over a period of three days (June 13, 1998, July 1, 1998, and July 6, 1998), the undersigned arbitrators have decided in full and final resolution of the issues submitted for determination as follows:

- (1) That Smith Barney, Inc. (n/k/a Solomon Smith Barney, Inc.) and James F. Peters, Jr. are jointly and severally liable for and shall pay to Alice Shotwell Gustafson, as Trustee for the Alice Gustafson Revocable Living Trust, the sum of Two Hundred Fifty Nine Thousand Five Hundred Dollars and No Cents (\$259,500.00);
- (2) The panel concluded that while there was no proven evidence of churning, there was clear evidence of: excessive trading; mismanagement of the account, in particular, after the account became subject to the discretionary power of Respondent Peters; and that there was a failure of supervision on the part of Smith Barney;
- (3) That the panel also concluded that Claimant did not appropriately monitor or supervise the account as to effectively mitigate her damages;
- (4) That the Counterclaims of Respondents Smith Barney, Inc. and James F. Peters, Jr. are hereby dismissed in their entirety with prejudice;
- (5) That other than forum fees, the parties shall each bear their own costs, expenses, and attorneys' fees incurred in this matter; and
- (6) That to the extent not specifically awarded or otherwise provided for above, all other claims and requests for relief by any party hereto are denied with prejudice.

FORUM FEES

Forum fees are calculated at the rate of \$1,000 per hearing session and \$300 for each pre-hearing conference, if any. There were twenty-six (26) hearing sessions x \$1,000 = \$26,000 in forum fees. There were six (6) pre-hearing sessions x \$300 = \$1,800. Total forum fees = \$27,800. Pursuant to §10332(b) of the Code, a hearing session is any meeting between the parties and the arbitrator(s), including a pre-hearing conference with an arbitrator, which lasts four (4) hours or

less.

Pursuant to §10332(c) of the Code, NASD Regulation, Inc. Office of Dispute Resolution shall retain the non-refundable filing fee in the amount of \$200 and shall retain as forum fees the hearing session deposit in the amount of \$750 previously deposited by the Claimant.

Pursuant to §10332(c) of the Code, Claimant is liable for and shall pay forum fees in the amount of \$13,150 (1/2 forum fees - hearing session deposit). Pursuant to §10332(c) of the Code, Respondents are jointly and severally liable for and shall pay forum fees in the amount of \$13,900 (1/2 forum fees).

Pursuant to §10332(c) of the Code, Respondent Smith Barney is liable for and shall pay the filing fee in the amount of \$500 associated with the filing of its Counterclaim. Pursuant to §10332(c) of the Code, Respondent Peters is liable for and shall pay the filing fee in the amount of \$500 associated with the filing of his Counterclaim. Pursuant to §10319 of the Code, Respondent Smith Barney is liable for and shall pay postponement fees in the amount of \$1,000.

Fees are payable to NASD Regulation, Inc. Office of Dispute Resolution.

Concurring Arbitrators' Signatures:

\s\ Michael B. Laikin, Esq.
Michael B. Laikin, Esq.
Chairperson
Public Arbitrator

July 13, 1998
Dated:

\s\ Irving Lopatin
Irving Lopatin
Panelist
Public Arbitrator

July 14, 1998
Dated:

\s\ S. Peter Bayekian
S. Peter Bayekian
Panelist
Industry Arbitrator

July 15, 1998
Dated:

For NASD Regulation use only:
Date award served on parties:

July 21, 1998