

N.A.S.D. AWARD

NATIONAL ASSOCIATION OF SECURITIES DEALERS

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In the Matter of the Arbitration Between

Name of Claimant(s)

Jerry Spiegel and Emily Spiegel Foundation, et. al.

94-01651

Name of Respondent(s)

Dean Witter Reynolds Inc.

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**REPRESENTATION**

For Claimants, Jerry Spiegel & Emily Spiegel Family Foundation; Emily Spiegel TTEE 63 Trust FBO Pamela Spiegel U/A/D 5/1/63; Lise Spiegel 1963 T 5/1/63; Emily Spiegel TTEE 63; Trust FBO Carrie Rosenblatt U/A/D 5/1/63; Emily Spiegel TTEE 63 Trust FBO; Jack Rosenblatt U/A/D 5/1/63; Jerry Spiegel; J.S. Realty; DDS Co.; Churchill Financial Company; Jesco Co., Dawson Holding Company and Arthur Sanders, collectively ("Claimants"), Robert Goodmann, Esq. of Burns, Handler & Burns, New York, New York.

For Respondent Dean Witter Reynolds Inc. ("Respondent"), James Yellen, Esq., in-house counsel, New York, New York.

**CASE INFORMATION**

Statement of Claim filed: May 3, 1994.

Claimants' Submission Agreement signed on: April 27, 1994.

Statement of Answer filed by Respondent on: September 9, 1994.

Respondent failed to sign a Submission Agreement pursuant to Section 25(b) of the NASD Code of Arbitration Procedure.

**HEARING INFORMATION**

Hearing Dates/Sessions:	October 25, 1995-	Two Sessions
	October 26, 1995-	Two Sessions
	January 4, 1996-	Two Sessions
	March 12, 1996-	Two Sessions
	March 13, 1996-	Two Sessions
	March 14, 1996-	Two Sessions

The hearings were held at the offices of the NASD, Inc. located in New York City, New York.

### **CASE SUMMARY**

Claimants alleged that in early 1990, Neil Rook ("Rook"), a representative of Respondent, induced Claimants to transfer their accounts from Shearson Lehman to Respondent by representing to Claimants that their accounts would not be subject to contingent deferred sales charges ("CDSC" charges) as well as various miscellaneous fees. Claimants further alleged that Respondent imposed CDSC charges on their account in violation of their agreement and its fiduciary duty to deal fairly and properly. Claimants contended that Respondent's confirmations to Claimants operated to confuse and mislead them into believing that no CDSC charges were imposed on the sale of their securities, when in fact Respondent was imposing such charges in violation of its agreement with Claimants.

Claimants alleged that Respondent improperly charged their account with miscellaneous charges contrary to its account executive's representations and their agreement. Claimants also alleged that after repeated demands, Respondent reversed a few of the charges but has failed to reverse the remaining charges totalling \$25,015.60.

Claimants alleged that Respondent made several unsuitable and unauthorized trades in their account which resulted in losses and needless commissions. Claimants further alleged that Respondent churned their account through a pattern of purchases and subsequent unauthorized sales of the same investments. Claimants contended that this pattern served only to provide Respondent with commission fees and served no bona fide investment purpose to them.

Respondent maintained that Claimants employed Frank Socci, Jr. ("Socci") and authorized him to conduct business on their behalf with Respondent. Respondent further maintained that Socci was advised that investments in DWR's mutual funds would entail a sales charge if the funds were sold within a certain time period and that he signed letters which specifically indicated that he was aware of these CDSC charges. Respondent denied misrepresenting facts concerning the CDSC charges and maintained that its confirmations are not deficient and meet applicable standards. Respondent next maintained that all transactions in the accounts were executed pursuant to instructions by Socci who was properly authorized and that the accounts were not excessively traded or churned. Further, Respondents maintained that the charges assessed against Claimants accounts were explained to Socci and that they received prospectuses which also fully disclosed the sales charges.

### **RELIEF REQUESTED**

Claimants requested the following;

1. an award in the sum of \$227,673.20, plus interest for wrongfully debited CDSC charges;
2. an award in the sum of \$25,015.60 plus interest for wrongfully charged miscellaneous charges;
3. an award in the sum of \$254,860.77 plus interest for churning the account; and
4. an award in the sum of \$549,695.26 plus interest for commissions generated by wrongful churning and unsuitable trades.

5. an award for attorney's fees and costs.

Respondent requested that the Statement of Claim be dismissed in its entirety and that it be awarded costs.

#### **OTHER ISSUES CONSIDERED & DECIDED**

The arbitrators made the following rulings concerning Respondent who failed to sign a Submission Agreement:

1. Pursuant to Section 1 of the Code, the arbitrators found subject matter jurisdiction over this entire controversy.
2. The arbitrators found that the Respondent was a member of the NASD at the time the controversy arose. Consequently, the arbitrators found personal jurisdiction over the Respondent pursuant to Section 12 of the NASD Code of Arbitration Procedure.
3. In view of (2) above, the arbitrators found that the Respondent was required to file with the NASD a properly executed Submission Agreement pursuant to Section 25(b) of the NASD Code of Arbitration Procedure.

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 remains 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. Respondent be and hereby is liable and shall pay to the Claimant \$175,000.00 in actual damages.
2. Each party shall bear their respective costs, including attorney's fees.
3. Forum fees shall be split equally.
4. All other claims be and hereby are denied.

#### **FORUM FEES**

Pursuant to Section 43c of the Code of Arbitration Procedure, the arbitrators have determined that the NASD shall retain the \$250.00 non-refundable filing fee submitted by Claimants and have assessed the following fees:

12 hearing sessions x \$1000.00	= \$12,000.00
minus Claimants hearing session deposit	= \$ 1,000.00
Total fees outstanding	= \$11,000.00


1. Claimants be and hereby are liable for \$6,000.00 representing one-half of forum fees assessed. Claimants previously deposited \$1,000.00 with the NASD and, accordingly, shall pay \$5,000.00 to the NASD.
2. Respondents be and hereby are liable for \$6,000.00 representing one-half of forum fees assessed.

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

Arbitrator's Signature  
Name

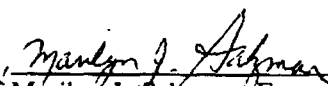
  
Matthew J. Tolan

I, Matthew J. Tolan, do hereby affirm that this is my decision in the above-captioned matter.

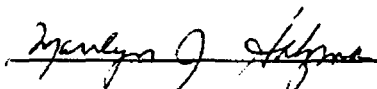
  
Matthew J. Tolan

Date of Decision: July 8, 1996

Arbitrator's Signature  
Name

  
Marilyn J. Salzman, Esq.

I, Marilyn J. Salzman, Esq., do hereby affirm that this is my decision in the above-captioned matter.



Date of Decision: July 8, 1996

## DISSENTING OPINION

Arbitrator Stephen A. Hochman does not join in this award and has filed the following dissenting opinion in connection therewith:

With all due respect to my co-arbitrators, I cannot join in this award because, in my opinion, it is inconsistent with the result that would have been obtained in a court of law. I realize that arbitrators are not required to follow the law, but I believe that, nevertheless, arbitrators should decide disputes in accordance with applicable law rather than on the basis of their own subjective notions of justice and equity.

I regret that I was unable to convince my co-arbitrators to explain their award. I believe that a reasoned award enhances respect for the arbitral process. The most often cited argument against a reasoned arbitral award is that the explanation may increase the risk of judicial reversal. However, it is well established that courts will not overturn arbitral awards merely because the arbitrators did not follow the law. In fact, the absence of an explanation can result in a case being sent back to the arbitrators for an explanation of the basis for their award.<sup>1</sup>

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<sup>1</sup> In Clemens v. Dean Witter Reynolds, Inc., 708 F. Supp. 62 (S.D.N.Y. 1989), the arbitrators awarded \$50,000 to the claimants but did not explain the basis for their award or the method by which they calculated damages. The claimants moved to vacate the award on the ground that the arbitrators manifestly disregarded the law by failing to award claimants the full amount of their damages. The claimants' theory was that, once the arbitrators made any award (thus implying a finding of fact that respondent's employee was not licensed as a broker), claimants were entitled to rescind all losing transactions made by the unlicensed broker, which would entitle claimants to over \$900,000 in damages. After holding that the arbitrators did not manifestly disregard applicable law in failing to award damages to claimants based on the rescission method of computing damages (since there was no legal support for claimants' argument that such method was the correct method of computing damages under the applicable Kentucky law), the court refused to confirm the \$50,000 award and remanded the case to the arbitrators for an explanation of the basis for their award and the method by which they calculated damages of \$50,000.

Although, in my view, all arbitral awards should be supported by reasons, I believe it is most important for an arbitrator who disagrees with the majority to explain the reasons for his or her dissent. In most cases an award can be supported by a simple explanation limited to the extent necessary to support the award, and it need not cover all of the issues raised by the parties or involve lengthy findings of fact and conclusion of law. Such an explanation of the basis for an arbitral award is not only helpful to the parties, but the process of writing it serves as a useful discipline for the arbitrators in their attempt to make a correct and rational decision. The more understandable the award, the more likely it is to be perceived as rational. I believe that the losing party is entitled at least to an explanation which will demonstrate that the award was rendered impartially and is supported by logical reasoning. Without such an explanation, the arbitration process may appear to be an arbitrary process, where the arbitrators are free to "split the baby" or decide disputes on the basis of their own personal values and prejudices. Such a subjective process is inconsistent with the reasonable expectation of most parties that their conduct will be judged on the basis of objective and predictable rules of law.

In addition to the fact that reasoned awards are the norm in labor, maritime and international arbitrations, there is much support for requiring arbitrators in other fields to explain their awards. After a two-year review of the arbitration programs administered by the securities industry, the General Accounting Office found widespread support, both from representatives within the brokerage industry and investor groups, for federal legislation to require arbitrators to explain the reasons for their decisions.<sup>2</sup> In contrast to the NASD Rules, Rule 13.2 of the Center for Public Resources' Non-Administered Arbitration Rules and Commentary provides that awards "shall state the reasoning on which the award rests unless the parties agree otherwise." The Commentary to this Rule states:

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2     Securities Arbitration - How Investors Fare, United States General Accounting Office Report (May 1992), p.53.



Most parties engaging in arbitration want to know the basis on which the arbitrator(s) reached their decision. Our Committee, moreover, considers it good discipline for arbitrators to require them to spell out their reasoning. Sometimes this process gives rise to second thoughts as to the soundness of the result. The Rule 13.2 mandate gives the arbitrator(s) greater leeway than would a requirement to state "conclusions of law and findings of fact."

Some parties hesitate to arbitrate out of a concern that arbitrators are prone to "split the baby", i.e., to make compromise awards. Any tendency on the part of arbitrators to reach compromise awards should be restrained by the requirement of a reasoned award.

Certain administering organizations and practitioners favor "bare" awards without explanation of any sort, in the belief that such awards are the least likely to be challenged and overturned by a court. In the Committee's view, the risk that a reasoned award will be successfully challenged normally is small and is outweighed by the other considerations mentioned above.<sup>3</sup>

Since my co-arbitrators have chosen not to reveal the reasons or the rationale upon which their award is based, I cannot focus my dissent on the areas of disagreement. Thus, the best way for me to explain the reasons for my dissent is to set forth what I believe to be the correct findings of fact and conclusions of law with respect to each of the claims set forth in the Statement of Claim.

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3 CPR Institute For Dispute Resolution (CPR) Non-Administered Arbitration Rules and Commentary.

A. The following are my findings and conclusions with respect to the claim that the Respondent wrongfully debited to Claimants' accounts CDSC charges (commonly referred to as back-end sales charges) in the amount of \$227,673.20:

1. Spiegel Associates ("Spiegel") was the duly authorized agent of the Claimants with full and complete authority to act for Claimants in connection with their accounts with Respondent (which aggregated approximately \$8,000,000).

2. Prior to February 1990, the Claimants' accounts were handled by Neil Rook ("Rook"), who was then an account executive at Shearson Lehman ("Shearson").

3. During the period that Claimants' accounts were handled by Rook at Shearson, Shearson permitted Claimants to trade in the firm's proprietary fixed-income mutual funds without being charged the usual CDSC charges when Claimants sold their shares of such funds. (This finding is based on the testimony of both Rook and Arthur Sanders ("Sanders"), the President of Spiegel, which was not disputed by Respondent.)

4. In or about February 1990, Rook left Shearson and became an account executive with Respondent and induced Claimants to transfer their various brokerage accounts to Respondent by promising and representing to Claimants that, if they transferred their accounts to Respondent, Respondent would similarly waive its usual CDSC charges so as to permit Claimants to trade in Respondent's proprietary fixed-income mutual funds without incurring CDSC charges when it sold its shares of such funds. (This finding is based on the testimony of both Rook and Sanders.)

5. Claimants relied on the representation and agreement which Rook made on behalf of Respondent that Respondent would not charge Claimants its usual CDSC charges when Claimant sold such fixed-income mutual funds (the "Waiver Agreement"), and Claimants would not have traded in such fixed-income mutual funds and incurred CDSC charges upon the sales thereof (which were as high as 4 - 5% of the gross sales proceeds) if it were not for the Waiver Agreement.

6. Although Rook testified that he believed that Respondent's branch manager authorized him to enter into the Waiver Agreement on behalf of Respondent, based on the credible testimony of Respondent's branch manager and the other evidence submitted by Respondent, I find that Rook did not have the actual authority from Respondent to enter into the Waiver Agreement on behalf of Respondent.

7. Notwithstanding Rook's lack of actual authority to waive CDSC charges on behalf of Respondent, Respondent is nevertheless legally bound by the Waiver Agreement since Rook had the apparent authority to make such agreement on behalf of Respondent.

8. Each confirmation notice sent to Claimants from Respondent's branch office covering each of the 11 sales transactions imposing CDSC charges was misleading in that it failed to adequately disclose the existence of the CDSC charge by understating the gross amount of the sales price of the mutual fund shares sold by stating that such gross amount was equal to the stated amount of the net sales proceeds, giving the impression that there was no CDSC charge (even though, if one were to multiply the stated number of shares sold by the stated price per share, the resulting amount would equal the correct gross sales proceeds, which exceeded the incorrectly stated gross sales proceeds by an amount equal to the unstated CDSC charge).

9. Although I have no basis to find that Spiegel had actual knowledge of the fact that Claimants were incurring CDSC charges upon their sales of shares of Respondent's mutual funds, Respondent argued that employees or representatives of Spiegel knew or should have known that the Waiver Agreement was not being complied with by Respondent because the existence and amount of such CDSC charges were plainly disclosed (a) in duplicate confirmations covering each of such 11 sales transactions, which were sent by Respondent's trust company to Claimants on or about the sametime that each of the misleading confirmations were sent to Claimants from Respondent's branch office, and (b) in subsequent summary statements which Respondent sent to Spiegel.

10. Even if Claimants were chargeable with knowledge of the fact that Respondent was not complying with the Waiver Agreement, such knowledge would not legally excuse Respondent from liability for its breaches of the Waiver Agreement or estop Claimants from recovering damages suffered by reason of such breaches.

11. The Waiver Agreement was breached by Respondent in connection with 11 separate sales by Claimants of fixed-income mutual funds during the period from July 10, 1992 through December 20, 1993 by reason of Respondent debiting Claimants' accounts for a total of \$227,673.20 in CDSC charges as a result of such 11 sales transactions, the dates and details of which are specified on Exhibit B to Claimant's Statement of Claim. (Respondent did not dispute the claim that Exhibit B contained an accurate summary of the dates and amounts of the CDSC charges debited to Claimants' accounts.)

12. Pursuant to a letter dated November 10, 1992, Spiegel confirmed that Frank Socci, Jr. ("Socci"), who was the Comptroller of Spiegel, was authorized to "journal funds between the Spiegel accounts" and "to place orders in the accounts."

13. After Rook was requested by his branch manager to get a letter from Spiegel acknowledging its awareness of the CDSC charges, Rook prepared a letter, dated August 10, 1992, addressed to Respondent on a sheet of paper containing a typed letterhead of Spiegel and a space for a signature by Socci, which letter stated that Spiegel was "aware of the structure of the Dean Witter back-end funds such as USGVT" and that "if money is taken out it may be subject to a sales charge" (the "Awareness Letter").

14. Although Socci testified that he did not remember signing the Awareness Letter and that he often signed batches of confirmation letters which were typed and submitted to him by Rook, he acknowledged that his signature on the Awareness Letter was genuine.

15. Although Socci had the authority to place orders in (and journal funds between) the Claimants' accounts, he did not have the authority from Spiegel to terminate the Waiver Agreement which was procured by Sanders on behalf of Claimants.

16. The Awareness Letter of August 10, 1992 did not contain any reference to the prior Waiver Agreement or the four separate breaches thereof which occurred on July 10, 1992. Accordingly, notwithstanding the fact that Socci signed the Awareness Letter which acknowledged his awareness that the withdrawal of cash from Respondent's fixed-income mutual funds "may be subject to a sales charge," and even if such awareness by Socci is imputed to Spiegel (and thus to Claimants), I find that the Awareness Letter did not constitute either (a) a waiver of the breaches of the Waiver Agreement which occurred one month prior to the date of the Awareness Letter or (b) a termination of the Waiver Agreement which would operate to excuse either such prior breaches or the breaches of the Waiver Agreement which took place subsequent to the date of the Awareness Letter.

17. Rook confirmed the existence of the Waiver Agreement between Respondent and Claimants and the fact that such agreement remained in full force and effect (and was not terminated by Socci's signature on the August 10, 1992 Awareness Letter) in a subsequent letter, dated April 28, 1993, which was typed on Respondent's printed letterhead and signed by Rook on behalf of Respondent and addressed to Sanders (the President of Spiegel), and Rook had the apparent authority to so confirm the existence of the Waiver Agreement on behalf of Respondent.

18. Although Respondent (a) did not violate any of its fiduciary or other duties to Claimants, (b) did not authorize Rook to enter into the Waiver Agreement, (c) did not have actual knowledge of the existence of the Waiver Agreement and (d) was not aware that each imposition by Respondent of CDSC charges to Claimants constituted a breach of the Waiver Agreement, Respondent is nevertheless liable to Claimants for the damages caused to Claimants by the unauthorized acts of Rook based on the legal doctrine of respondent superior and Rook's apparent authority to enter into the Waiver Agreement on behalf of Respondent.

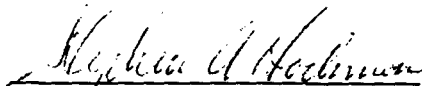
19. Based on the foregoing, Claimants should be awarded to sum of (a) \$227,673.20 to reimburse them for the CDSC charges which were charged to their accounts in violation of the Waiver Agreement and (b) interest on the amount of each such CDSC charge computed at the rate of 9% per annum from the date of each such improper charge (as set forth on Exhibit B to the Statement of Claim) to the date of the repayment thereof by Respondent (Claimants being entitled to such interest pursuant to the provisions of Sections 5001 and 5004 of the New York CPLR since the 11 separate impositions of CDSC charges by Respondent constituted breaches of a contract between Respondent and Claimants).

B. The following are my finding and conclusions with Respect to Claimants other claims as set forth in its Statement of Claim:

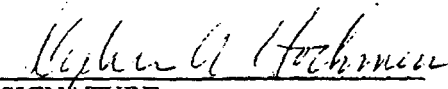
1. Claimants claim for the wrongful debiting of miscellaneous charges in the amount of \$25,015.60, as enumerated in Schedule H of its Statement of Claim, is denied in all respects because Claimant has failed to establish by a preponderance of the evidence that there was an agreement by Respondent or anyone having actual or apparent authority to act on its behalf that such miscellaneous charges would be waived.

2. Claimants claims for (i) losses caused by wrongful churning and unsuitable trades in the amount of \$254,860.77 and (ii) the repayment of commissions charged by Respondent on such trades in the amount of \$452,792.57 and \$96,902.69, which are enumerated in Schedules I and J of its Statement of Claim, are denied in all respects because: (a) Claimants were sophisticated investors who knowingly engaged in a pattern of aggressively trading in fixed-income securities and mutual funds and were aware of the risks inherent in trading in fixed-income securities of varying maturities, yields and durations (and the extent to which such trading could result in gains or losses, depending on future movements in interest rates); (b) Claimants failed to establish that Rook rather than Spiegel controlled the investment decisions relating to the purchases and sales made in Claimants' trading account; (c) all of the fixed-income securities and mutual funds which Claimants purchased in its accounts were suitable for purchase in accordance with Claimants' objectives of trading in fixed-income securities of issuers having a minimal credit risk; (d) Claimants traded in such fixed-income securities in the hope that such trading would produce a greater rate of return than merely buying and holding such fixed-income securities to maturity; and (e) the Commissions charged by Respondent in connection with such trading (which were deeply discounted from Respondent's normal commission rates) were not excessive, and there is no basis for a finding of churning or excessive or unsuitable trading in Claimants' accounts.

For the reasons stated above, I respectfully dissent from the award in this case.

  
Stephen A. Hochman, Esq. Arbitrator

I, Stephen A. Hochman, Esq., do hereby affirm that this is my decision in the above captioned matter.

  
SIGNATURE

Date of Decision: July 8, 1996