

N.A.S.D. REGULATION AWARD

NATIONAL ASSOCIATION OF SECURITIES DEALERS REGULATION

In the Matter of the Arbitration Between

Name of Claimant

Charles P. Deegan, Executor of the
Estate of Zelda T. Westlake

95-00059

Name of Respondents

Shearson Lehman Brothers, Inc.
PaineWebber, Inc.
Henry James Faragalli

REPRESENTATION

Claimant Charles P. Deegan, Executor of the Estate of Zelda T. Westlake ("Claimant") was represented by Marcy C. Panzer, Esq., Cozen & O'Connor, Philadelphia, PA

Respondent Henry J. Faragalli, Jr. ("Faragalli") was represented by Thomas Loder, Esq. Rubin & Associates, Paoli, PA

Respondent Shearson Lehman Brothers, Inc. (n/k/a Smith Barney Inc.) was represented by Victor Machcinski, Jr., Esq., New York, NY

Respondent PaineWebber, Inc. ("PaineWebber") was represented by John Linsenmeyer, Esq. and Ben A. Indek, Esq. Morgan, Lewis & Bockius, New York, NY

CASE INFORMATION

Statement of Claim filed on: January 4, 1995

Claimant's Submission Agreement signed on: December 29, 1994

Statement of Answer filed by Respondent Faragalli on: March 16, 1995

Respondent Faragalli did not file an executed agreement to arbitrate.

Statement of Answer and Motion to Stay filed by Respondent Shearson Lehman Brothers, Inc. ("Shearson") on: March 3, 1995

Respondent Shearson's Submission Agreement signed on: November 14, 1995

Statement of Answer filed by Respondent PaineWebber on: August 21, 1995

Respondent PaineWebber's Submission Agreement signed on: August 21, 1995

HEARING INFORMATION

Prehearing Date/Sessions: March 22, 1996/one session
April 8, 1996/one session

Hearing Date/Sessions: April 19, 1996/two sessions

Hearing Location: Holiday Inn
Philadelphia, PA

Hearing Dates/Sessions: July 15, 1996/two sessions
July 18, 1996/two sessions
July 19, 1996/two sessions
September 30, 1996/two sessions
October 2, 1996/two sessions

Hearing Location: Vincent Varallo Associates, Inc.
Philadelphia, Pennsylvania

CASE SUMMARY

Claimant, the authorized representative of the Estate of Zelda T. Westlake ("Mrs. Westlake") alleged, among other things, that Faragalli, PaineWebber, and Shearson (collectively "Respondents") converted Westlake's portfolio into one consisting of speculative equity investments and unit investment trusts that were unsuitable to Mrs. Westlake's expressed investment objectives and objective needs. Claimant alleged that at the time of Mrs. Westlake's husband's death in 1985, Mrs. Westlake held a portfolio of conservative investments consisting almost exclusively of tax-free municipal bonds. Claimant alleged that Faragalli earned significant commissions during this process for PaineWebber. Claimant alleged that in particular, Faragalli, who exercised great influence with the elderly Mrs. Westlake, invested her heavily in EECO and caused her to have an improper concentration in that issue. Claimant alleged that substantial sums were lost due to Faragalli's actions. Claimant alleged that although, while he was employed at each, PaineWebber and Shearson restricted Faragalli's dealings in EECO to protect their own interests, nothing was done by either PaineWebber or Smith Barney to protect Mrs. Westlake. Claimant alleged that PaineWebber and Shearson breached their fiduciary duties and supervisory responsibilities by not doing at least as much as they did for their own account to protect Mrs. Westlake from Mr. Faragalli's actions. Claimant alleged that PaineWebber and Shearson failed to act in accordance with standard NASD guidelines for supervision, as had been represented to Mrs. Westlake was their practice and procedure. Claimant alleged that proper supervision would have uncovered Faragalli's improper activity regarding her account. Claimant alleged that Respondents' fraudulent actions resulted in damages to the Estate of Mrs. Westlake.

Respondents denied all allegations of wrongdoing and maintained, among other defenses, that Claimant had failed to establish (i) that Mrs. Westlake's investment desires were not followed, (ii) her account had been churned, and (iii) her investments were unsuitable. Respondents also maintained that, in any event, because she had made a charitable donation of all of her EECO prior to her death in 1990, Claimant lacked standing to assert any claim for EECO related losses. In addition, Shearson asserted that, since no EECO shares were purchased at the firm, Claimant lacked any factual or legal basis for alleged suitability claims against it. Moreover, PaineWebber and Shearson asserted that all of Faragalli's activities were knowingly ratified by Mrs. Westlake, that Faragalli was adequately supervised, and that

all compliance requirements were followed. Finally, Respondents asserted that all of Claimant's claims were barred by the applicable statutes of limitations. Respondents maintained that as a result of federal court litigation involving these claims, an order was entered by Judge Harvey Bartle in the United States District Court for the Eastern District of Pennsylvania (Civ. Action No. 91- 4270) on March 6, 1992, dismissing all claims under the federal securities laws as barred by the applicable statutes of limitations.

RELIEF REQUESTED

Claimant requested damages of \$381,529 against PaineWebber, \$58,849 against Shearson, and \$440,378 against Faragalli; equal amounts of punitive damages and pre-award interest for a total, respectively, of \$556,897 \$85,899 and \$642,796, plus attorneys fees, and the costs of this arbitration

Respondents requested that the Claimant's claim be denied in its entirety and sought reimbursements for the costs of this arbitration and that forum fees be assessed to 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.

Respondents each filed Motions to Dismiss prior to the commencement of the hearings. The Motions asserted that Claimant's claims were time-barred pursuant to applicable federal and Pennsylvania statutes of limitation. The Motions also asserted that on the face of the documents produced by the Claimant, he would be unable to prove any entitlement to damages because all the stock upon which Claimant's claim was based had been given away by the decedent, Zelda T. Westlake, prior to her death by contribution to a scholarship fund established in her late husband's name, for which a tax benefit was claimed. Shearson moved separately for dismissal of Claimant's suitability claims on the ground that they failed to state a claim for relief as a matter of law. On March 25, 1996, after full consideration, the Panel reserved decision on all Respondents' motions, which were renewed at the close of Claimant's case. As part of Respondents' Motions to Dismiss and for Summary Judgment and Directed Award, the Panel reserved decision on all Respondents' Motions to Dismiss and for Summary Judgment and Directed Award. Pursuant to Rule 10301(a) (formerly Section 12) of the NASD Code of Arbitration Procedure and the laws of the NASD, the Panel exercised its jurisdiction over Respondent Faragalli (notwithstanding his failure to submit an executed Submission Agreement) to which Faragalli asserted on the record on April 19, 1996. Therefore, Faragalli is bound by the rulings and the determination of this Panel.

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. That Claimant's claims are denied in their entirety and the Respondents' Motions to Dismiss this case and direct an award in their favor is granted.
2. That the claim for punitive damages is denied.
3. That each parties shall bear its own costs and expenses, including attorney's fees, except as specifically stated below.
4. That any relief not specifically addressed herein is denied.

FORUM FEES

Pursuant to Rule 10332(c) (formerly Section 43) of the Code of Arbitration Procedure, the following Forum Fees are assessed:

2 Prehearing Sessions x \$300.00 = \$600.00
12 hearing sessions x \$1,000.00 = \$12,000.00
Total forum fees = \$12,600.00
The Panel has determined that forum fees shall be assessed as follows:
Claimant is assessed forum fees in the amount of \$6,300.00. Claimant is to receive credit for the hearing fees assessed for the session deposits previously submitted to the NASD Regulation in the amount of \$1,000.00, leaving a net amount of \$5,300.00 assessment due from Claimant of \$5,300.00.
Respondent Faragalli is assessed forum fees in the amount of \$2,100.00.
Respondent Shearson is assessed forum fees in the amount of \$2,100.00.
Respondent PaineWebber is assessed forum fees in the amount of \$2,100.00.
Fees are payable to the National Association of Securities Dealers Regulation, Inc.

DATE

CONCURRING ARBITRATORS' SIGNATURES

11/21/96

Barbara A. Ash

Barbara A. Ash, Chairperson
Public Arbitrator

Albert Mancini, Jr.
Public Arbitrator

Jerry Brown
Industry Arbitrator

Date Decision Served by NASD Regulation: November 18, 1996

DATE

CONCURRING ARBITRATORS' SIGNATURES

Barbara A. Ash, Chairperson
Public Arbitrator

NOVEMBER 4, 1996

Albert Mancini, Jr.
Albert Mancini, Jr.
Public Arbitrator

Jerry Brown
Industry Arbitrator

Date Decision Served by NASD Regulation: November 18, 1996

DATE

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Barbara A. Ash, Chairperson
Public Arbitrator

Albert Mancini, Jr.
Public Arbitrator

H-4-96

Jerry Brown
Jerry Brown
Industry Arbitrator

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