

NATIONAL ASSOCIATION OF SECURITIES DEALERS

In the Matter of the Arbitration Between

Name of Claimant

Park Nicollet Medical Foundation

95-00139

Names of Respondents

Piper Jaffray, Inc. and
Piper Capital Management, Inc.

REPRESENTATION

Claimant, Park Nicollet Medical Foundation was represented by Mark J. Briol, Esq. of Mark J. Briol & Associates, Minneapolis, Minnesota.

Respondents, Piper Jaffray, Inc. and Piper Capital Management, Inc. were represented by George F. McGunnigle, Esq. and Lawrence J. Field, Esq. of Leonard, Street & Deinard, Minneapolis, Minnesota.

CASE INFORMATION

The Statement of Claim filed was filed with the National Association of Securities Dealers, Inc. ("NASD") on January 10, 1995.

Claimant, Park Nicollet Medical Foundation's Submission Agreement was signed on January 6, 1995 by James Toscano, Executive Vice President of Park Nicollet Medical Foundation.

A Joint Statement of Answer was filed with the NASD by Respondents, Piper Jaffray, Inc. and Piper Capital Management, Inc. on February 17, 1995.

Respondent, Piper Jaffray, Inc's Submission Agreement was signed on January 31, 1995 by Mark S. Reed, Esq., Vice President and Assistant General Counsel of Piper Jaffray, Inc.

Respondent, Piper Capital Management, Inc. did not file an executed Submission Agreement with the NASD but Piper Capital Management, Inc. submitted to the jurisdiction of the NASD through the joint answer and counsel appeared at the hearing on its behalf. Accordingly, Piper Capital Management, Inc. will be bound by the panel's determination on all issues submitted for resolution.

HEARING INFORMATION

A Pre-Hearing Conference was held on: April 29, 1996 for one (1) hearing session.

The hearing took place on the following dates:

March 12, 1996 for one (1) hearing session;
March 13, 1996 for two (2) hearing sessions;
March 14, 1996 for two (2) hearing sessions;
March 15, 1996 for two (2) hearing sessions;
May 31, 1996 for two (2) hearing sessions;
June 3, 1996 for two (2) hearing sessions;
June 5, 1996 for two (2) hearing sessions;
June 6, 1996 for two (2) hearing sessions;
June 7, 1996 for one (1) hearing sessions; and,
June 11, 1996 for two (2) hearing sessions.

The hearing location was Minneapolis, Minnesota.

CASE SUMMARY

Claimant, Park Nicollet Medical Foundation ("Park Nicollet") alleged that it hired a professional investment adviser, Respondent, Piper Capital Management, Inc. ("Piper Capital") which has an affiliate broker-dealer, Respondent, Piper Jaffray, Inc. ("Piper Jaffray") to manage its Endowment Fund in the summer of 1991. Most of Park Nicollet's funds were invested at that time in certificates of deposit which were coming due in September of 1991. Park Nicollet alleged that its primary investment objective was the preservation of capital. Indeed, Park Nicollet sent Piper Capital a copy of its investment guidelines for the Endowment Fund. Piper Capital was given half of Park Nicollet's Endowment Fund and another investment advisory firm was given the other half. Each of the firms were given the same investment guidelines to follow. Piper Capital and Park Nicollet determined to split the Endowment Fund into two segments. The "fixed income" segment was to be the safest, most conservative and largest portion of the Endowment Fund. A smaller portion of the fund was to be devoted to equities and both segments were to be conservatively invested.

Park Nicollet alleged that Piper Capital advised it to invest all of the fixed income segment in the Piper Jaffray Institutional Government Income Portfolio ("the Fund"). Park Nicollet alleged that Piper Capital told it, orally and in writing, that the Fund was very safe and an investment that was entirely consistent with Park Nicollet's declared primary investment objective of preservation of capital. Park Nicollet alleged that Piper Capital claimed the Fund was structured so as to minimize price risk and that the Fund had a price volatility comparable

to that of a three year treasury security. Park Nicollet also alleged that Piper Capital further represented that the Fund's portfolio was structured to minimize the normal principal fluctuations that an investment in fixed-income securities has in response to changes in market conditions. Given these representations, Park Nicollet entrusted \$700,000.00 to Piper Capital in September of 1991 of which \$420,000.00 was invested in the Fund. The monies were deposited at Piper Jaffray, the affiliate broker-dealer of Piper Capital. Park Nicollet was advised that it would be kept informed of any developments which might directly affect its portfolio. In 1992, Park Nicollet invested an additional \$1,197,895.00 in the Fund and in 1993 Park Nicollet invested and additional \$700,000.00 in the Fund.

Park Nicollet alleged that Piper Capital, as an investment adviser to the Fund itself, embarked upon a highly risky, wildly speculative program which was entirely inconsistent with Park Nicollet's primary investment objective of preservation of capital. The Fund invested relatively little money in actual government securities. Instead, the Fund invested heavily in risky, exotic derivatives which were highly volatile and subject to great liquidity risks. Park Nicollet alleged that when the value of the Fund's shares dropped almost 36% in 1994, no one from Piper Capital advised Park Nicollet to get out of the Fund.

Park Nicollet alleged that the conduct of Piper Capital and Piper Jaffray violated the Minnesota State Securities Laws, Section 10(b) and Rule 10b-5 of the Securities and Exchange Act of 1934, The Federal Investment Advisers Act of 1940 and the Investment Company Act of 1940. In addition, common law claims for negligence, common law fraud, breach of fiduciary duty and violations of various self regulatory organization rules were asserted.

In their joint answer to the statement of claim, Piper Jaffray and Piper Capital alleged that the claim was without merit because it was an attempt to turn the bond market collapse of 1994 into a litigation windfall. Piper Jaffray and Piper Capital asserted that Park Nicollet invested heavily in the Fund which performed extremely well until 1994 when the Federal Reserve Board took the unprecedented action of raising interest rates six times in a single year. These serial interest rate hikes triggered the bond market's most precipitous drop in decades. The interest rate hikes particularly affected the market for mortgage backed securities, so-called derivatives, in which the Fund heavily invested. The derivatives of the type the fund invested in consisted of Collateralized Mortgage Obligations ("CMOs") such as "Interest Only" ("IOs"), Principal Only ("POs") and Inverse Floating Rate ("inverse floaters") mortgage securities. Piper Jaffray and Piper Capital alleged that Park Nicollet which is part of HealthSystem Minnesota employed experienced financial managers. Park Nicollet had an Investment Committee comprised of especially seasoned investors including an attorney and an accountant.

From the outset of the relationship with Piper Capital, Park Nicollet recognized and admitted in writing that Piper Capital and Piper Jaffray were not promising any of Park Nicollet's investment objectives would be met. Park Nicollet was repeatedly informed that the Fund would experience price volatility especially if interest rates rose. Park Nicollet received

the prospectus as well as a letter to shareholders dated November 15, 1993, included in the Fund's 1993 annual Report which stated:

The fund will experience moderate price volatility and is designed for investors with long-term investment objectives. As such, it should be viewed in the context of your entire investment portfolio.

Piper Capital and Piper Jaffray also asserted that the Fund's prospectus dated January 28, 1992 specifically warned that "inverse or reverse floating CMOs are typically more volatile than fixed or floating rates types of CMOs" and that "if the underlying mortgage assets experience slower than anticipated prepayments of principal, the yield on a PO class will be affected more severely than would be the case with a traditional mortgage-backed security. Piper Capital and Piper Jaffray asserted that they acted in the best interests of Park Nicollet and that Park Nicollet had not suffered any lost capital or damages whatsoever. Piper Capital and Piper Jaffray asserted that Park Nicollet's capital was completely preserved and that Park Nicollet was entitled to no money damages.

RELIEF REQUESTED

Park Nicollet requested actual damages in the approximate amount of \$746,347.00, the exact amount to be determined at trial, attorney's fees in the amount of \$401,879.10, punitive damages of \$3,444,678.30, costs, disbursements and expenses incurred in pursuing the arbitration, for such other damages as may be established at hearing and for such other relief as the arbitrators deemed just and equitable.

Piper Jaffray and Piper Capital requested dismissal of the statement of claim in its entirety.

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. Piper Jaffray, Inc. and Piper Capital Management, Inc. shall pay to Claimant,

Park Nicollet Medical Foundation, the sum of One Hundred Five Thousand One Hundred Forty One Dollars and No Cents (\$105,141.00);

2. Simple interest is assessed at the statutory rate pursuant to the Minnesota Securities Law from and inclusive of June 11, 1996 to an inclusive of the date the award is satisfied;

3. Park Nicollet Medical Foundation's claim for punitive and/or treble damages is denied and dismissed in its entirety; and,

4. Other than forum fees which are addressed below, the parties shall each bear their respective costs, expenses and attorney's fees incurred in this matter.

FORUM FEES

Pursuant to Section 43c of the Code of Arbitration Procedure, the following Forum Fees are assessed. The NASD shall retain the \$250.00 non-refundable claim filing fee and the \$1000.00 hearing session deposit previously deposited with the NASD by Park Nicollet Medical Foundation. Piper Jaffray, Inc. shall directly reimburse Park Nicollet Medical Foundation in the amount of \$1250.00 for these filing fees. The NASD shall also retain the \$500.00 member surcharge assessed to Piper Jaffray, Inc. according to Section 45 of the Code of Arbitration Procedure.

Piper Jaffray, Inc. is assessed and shall pay to the NASD additional forum fees in the amount of \$17,300.00. Forum fees were calculated at the rate of \$1000.00 per hearing session for eighteen hearing sessions and \$300.00 for the single session pre-hearing conference.

Additional forum fees assessed to Piper Jaffray, Inc. by the arbitrators are payable to the National Association of Securities Dealers, Inc.

Concurring Arbitrators' Signatures
Name

<u>/s/ D. Randall Blohm</u>	<u>July 5, 1996</u>
D. Randall Blohm, Esq.	Dated
Presiding Chairperson/Public Arbitrator	

<u>/s/ John C. DeMoss</u>	<u>July 8, 1996</u>
John C. DeMoss, Esq.	Dated
Panelist/Public Arbitrator	

<u>/s/ James Nyquist</u>	<u>July 5, 1996</u>
James Nyquist	Dated
Panelist/Industry Arbitrator	

Date Award Served on the Parties by the NASD: July 8, 1996