

N.A.S.D. AWARD

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

In the matter of the Arbitration Between

Name of Claimant

Mark Peterson

NASD Arbitration
#95-00959

vs.

Name of Respondents

Murphey Favre Inc.
Washington Mutual Savings Bank
Johanna Steele

REPRESENTATION

Claimant represented himself.

For Respondents Murphey Favre and Washington Mutual: H. Richard Namba, Esq., Murphey Favre Inc., Seattle, Washington

Respondent Johanna Steele represented herself.

CASE INFORMATION

Statement of Claim filed: February 23, 1995

Claimants' Submission Agreement signed: February 23, 1995

Respondent Murphey Favre's Statement of Answer filed: April 21, 1995

Murphey Favre's Submission Agreement signed: April 20, 1995

Respondents Washington Mutual and Johanna Steele did not file separate answers or submission agreements; however, Johanna Steele appeared at hearing and acknowledged her submission to NASD jurisdiction, and Mr. Namba acknowledged that he represented Washington Mutual and submitted to NASD jurisdiction on its behalf.

HEARING INFORMATION

The hearing was held in Seattle, Washington, on September 11, 1995, and lasted one session.

CASE SUMMARY

Claimant alleged misrepresentation, fraud, failure to disclose and lack of suitability with respect to his investment in the Composite Tax Exempt Fund.

Respondents denied the allegations of the claim, and asserted that the investment was appropriate for Claimant and that full disclosure was provided.

RELIEF REQUESTED

Claimant requested damages of \$4995.

Respondents requested dismissal of the claim.

OTHER ISSUES CONSIDERED & DECIDED

The parties have agreed to receive 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 arbitrator has decided in full and final resolution of the issues submitted for determination as follows:

The NASD has jurisdiction in this arbitration over the questions (1) whether Respondents sold the \$40,00 total investments in Composite Tax Exempt Fund, in December 1993 and January 1994, to Claimant by means of fraud, and (2) whether these investments were suitable for purchase by Mr. Peterson. This Arbitrator has no jurisdiction to resolve any of the questions of improper or inappropriate corporate linkage between the Respondents Murphey Favre and Washington Mutual Savings Bank which Mr. Peterson alleges, or the corporate behavior of those two entities which he has challenged as unethical. Accordingly, I take no position on any of these charges which are appropriately the concern of governmental regulatory authorities.

By his own statement, Mr. Peterson had learned about tax-exempt bonds from co-workers at Boeing, was interested in purchasing tax-exempt bonds when he first met with Respondent Johanna Steele in late December 1993, and remained interested thereafter when he made a second

purchase in early January 1994. It was uncontested that Ms. Steele elicited information from Claimant and his wife Linda to verify the suitability of a tax-advantaged investment, and in point of fact Claimant has not disputed the suitability of his investing in tax-exempt bonds or bond fund.

With considerable detail, Ms. Steele describes the conversations she had with Claimant and his wife Linda. She describes Mr. Peterson's personal and family situation and testifies that Claimant's investment horizon, as he had explained to her the anticipated needs of his five-year old son, was a minimum of ten years. Ms. Steele and Richard Namba for Murphey Favre argue that Claimant's investments in the Composite Tax Exempt fund would have well served Claimant's objectives had he maintained the position over the long term, which he did not. On his own volition, in September 1994, Mr. Peterson sold his position in the fund at a loss in principal value.

Of course, it is a historical fact that indices of principal value and total return, across the spectrum of American domestic bonds and bond funds, fell dramatically during this same period from December 1993 into late 1994. With the general decline in the bond market in 1994, Mr. Peterson certainly would have lost principal value in individual bonds he might have purchased just as he did in the Composite Tax Exempt bond mutual fund. Significantly, Ms. Steele also points out that when Mr. Peterson's income-stream situation changed later in life after he had retired, there would have been no fee involved in transferring out of the Composite Tax Exempt fund into the Composite Income fund. There would, of course, have been significant selling commissions if and when he chose to move out of a portfolio of individual tax free bonds no greater than \$40,000 and into taxable income investments. And of course, there is the classic advantage of a mutual fund -- diversification. For all of these reasons, I have no difficulty in concluding that the aggregate \$40,000 purchase of the Composite Tax Exempt mutual fund shares was a suitable investment for Mr. Peterson.

The crux of the charge that Mr. Peterson does assert against the Respondents is that, (1) Ms. Steele fraudulently assured him that his investment in the Composite Tax Exempt mutual fund would be as safe as putting money into a savings account and (2) she further fraudulently assured him that he would recoup the 3.5% front-end sales commission he was to be charged within a matter of months. Under the law, it is the Claimant who carries the burden of proving fraud by clear and convincing evidence.

Ms. Steele denies making either of the statements that Mr. Peterson charges. Both parties point to a graph Ms. Steele prepared for Mr. Peterson demonstrating that with historical returns, the fund performed with solid positive returns. Ms. Steele testifies that she explained it as such. Mr. Peterson may have misunderstood this graph to be a future projection, but it was plainly marked as a historical analysis and there was no credible evidence presented that Ms. Steele made any assurance that the fund would continue to perform *in futuro* as it had in the past. Indeed, to the contrary, Respondents presented evidence that Mr. Peterson acknowledged and understood that the value of his fund shares could fluctuate over time.

Questioning of Ms. Steele and Mr. Namba revealed no material economic self-interest motivation that convincingly demonstrated to this Arbitrator that fraud has occurred. While the sales

commissions on the mutual fund were approximately a percentage point greater than that which would have been paid on only the purchase of individual bonds, considering the normal markups and markdowns that he would have encountered on the combined purchase and sale, Mr. Peterson most likely would have ended up paying more in sales commissions to Murphey Favre if he had actually purchased and then sold individual tax-exempt bonds. There was no redemption charge on the mutual fund, and as noted above there would have been no transfer fee within the Composite Group of Funds.

As described, the testimony and evidence on these two points are sharply contested. On balance, however, I found Ms. Steele's overall testimony, throughout the entirety of the hearing, on a number of different issues including specifically these two charges, to generally be more credible and convincing than that of Claimant and his supporting witnesses. Accordingly, I have determined to credit Ms. Steele's testimony on these two issues that charge fraud.


1. I thus find that Claimant has not carried his burden of proof and shown by clear and convincing evidence that he was induced to purchase this mutual fund by means of fraud. As noted above, I also hold that purchases of this mutual fund were suitable investments for Mr. Peterson. Accordingly, I have awarded in favor of the Respondents.

2. The parties shall each bear their respective costs of arbitration.

FORUM FEE

Pursuant to Section 43 (c) of the Code of Arbitration Procedure, the NASD shall retain the \$50 non-refundable filing fee, and the \$100 hearing session deposit shall be retained as an assessment of forum fees for one session.

ARBITRATOR


Harry E. Jennings, Jr.

Date of Decision: September 21, 1995.

Date Served: 09/25/95