

N.A.S.D. REGULATION AWARD

NATIONAL ASSOCIATION OF SECURITIES DEALERS REGULATION

In the Matter of the Arbitration Between

Name of Claimants

Fred L. & Lillian M. Swann

95-01984

Name of Respondents

Merrill Lynch, Pierce, Fenner & Smith, Inc.
Gene Randall Rhoades

REPRESENTATION

Claimants Fred L. and Lillian M. Swann ("Claimants") were represented by Geoffrey P. Damon, Esq., Cincinnati, OH.

Respondents Merrill Lynch, Pierce, Fenner & Smith, Inc. ("MLPFS") and Gene Randall Rhoades ("Rhoades") were represented by Jonathan A. Schorr, Esq., Merrill Lynch, Pierce, Fenner & Smith, Inc., New York, NY.

CASE INFORMATION

The Statement of Claim was filed on April 24, 1995.

Claimants' Submission Agreement was signed on March 30, 1995.

The Joint Statement of Answer submitted by Respondents MLPFS and Rhoades was filed on June 23, 1995.

Respondent MLPFS's Submission Agreement was signed on June 23, 1995.

Respondent Rhoades did not submit an executed agreement to arbitrate.

HEARING INFORMATION

Hearing Dates/Sessions:

June 12, 1996/two sessions
June 13, 1996/two sessions
June 14, 1996/two sessions
October 9, 1996/two sessions
October 10, 1996/three sessions
October 11, 1996/three sessions
December 16, 1996/two sessions
December 17, 1996/two sessions

Hearing Location:

American Arbitration Association
Cincinnati, OH

CASE SUMMARY

Claimants, alleged among other things, that MLPFS and Rhoades (collectively "Respondents") engaged in unauthorized trading in Claimants' account, failed to follow Claimants' instructions, recommended unsuitable transactions, and failed to adequately diversify Claimants' portfolio. Claimants alleged that Respondents induced Claimants to authorize transactions in unsuitable securities and to purchase on margin in amounts which exceeded Claimants' net worth. Claimants alleged that on June 23, 1994, Claimants were pressured to place a sell order to sell 22,000 shares of Unisys Corporation ("Unisys") at \$9.00 to meet a \$31,000.00 margin call. Claimants alleged that later the same day, Claimants informed Respondents that they did not wish to sell the Unisys shares and that Claimants would come to the Respondents' office to arrange to pay the margin call. Claimants alleged that when they arrived at Respondents' office, Rhoades informed them that 10,000 shares of Unisys had, in fact, been sold but that the remaining 12,000 were still owned by Claimants. Claimants alleged that Rhoades called first thing the next morning and informed Claimants, in disregard to repeated instructions to cancel the sell order, that all 22,000 shares of Unisys had been sold during the business day of June 23, 1994. Claimants alleged that MLPFS failed to properly supervise Rhoades throughout this incident. Claimants alleged that Respondents misrepresented the nature of the risk involved when recommending specific investment transactions, inducing Claimants to authorize transaction which were not only unsuitable for Claimants but led to an under-diversified portfolio, persuaded Claimants to purchase excessively on margin and disregarded Claimants' stated investment objective of safety of principal. Claimants alleged that Claimants reasonably relied upon Respondents' knowledge and expertise to their detriment. Claimants alleged violations of the Kentucky securities laws and regulations promulgated thereunder, as well as federal securities laws and regulations; common law fraud; breach of implied and/or express contract; breach of fiduciary duty; a violation of state laws governing negligent and intentional infliction of emotional distress; negligence and gross negligence; failure to supervise; liability based upon theories of agency and respondeat superior; intentional, willful and/or reckless disregard of Claimants' rights based on the malicious and/or fraudulent misconduct of Respondents. Claimants alleged that the actions of Respondents directly and proximately resulted in financial loss, irreparable emotional and psychiatric harm, depression and other damages to Claimants.

Respondents denied all allegations of wrong doing as asserted in the Statement of Claim. Respondents maintained that the sale of Unisys stock to meet the margin call was authorized by Claimants. Respondents maintained that while Claimants' stated investment objective was for "safety of principal with only moderate risk", Claimants were, in fact, sophisticated investors with a history as high risk, large position traders. Respondents maintained that any recommendations made to Claimants were suitable for Claimants and that any under-diversification of Claimants' portfolio was the result of Claimants' own decisions. Respondents maintained that Claimants were experienced in the use of margin and have a trading history of taking large, usually unsolicited positions, in equity securities in order to achieve trading gains. Respondents maintained that in July 1993, Claimants placed an unsolicited order for 20,000 shares of Unisys priced at \$11 3/4 for a total face value, including commissions, of \$237,269.00. Respondents maintained that at this time Claimants had an existing margin debit of over \$139,000.00. Respondents maintained that they questioned whether Claimants really wanted to invest such a large sum in one stock. Respondents maintained that Claimants repeatedly assured Respondents that they knew the potential risks and rewards and wanted to hold these positions. Respondents maintained that at several points Claimants were urged to consider selling some of the Unisys shares and realize a profit, but Claimants wished to hold out for a higher price and larger profit. Respondents maintained that when Unisys began to decline, Claimants faced margin maintenance calls in the account and on June 23, 1994, Claimants issued a sell order for 22,000 shares of Unisys. Respondents maintained that subsequent to the sell order, Claimants did attempt to cancel the sell order, but Respondents informed Claimants that

the order had already been executed. Therefore, Respondents maintained that the sell orders were not unauthorized nor did Respondents fail to follow Claimants' instructions. Respondents maintained that as Claimants had an unsatisfied margin call, Respondents would have had the right to sell these or any other securities in Claimants' account at Respondents' discretion to satisfy the margin call, as Claimants did not timely indicate that they could or would meet the margin maintenance call through the deposit of necessary funds. Respondents maintained that Claimants did not even make a verbal complaint until months after the trades in Unisys, and during most of those months, Unisys had been near or below the price at which it was sold and Claimants could have reestablished their position if they had so desired. Respondents raised the affirmative defenses of failure to state a claim for which relief may be granted; Claimants directed, approved and authorized each and every transaction; Claimants ratified every transaction; estoppel; claims are barred by applicable statutes of limitations; failure to mitigate damages; and waiver. Respondents maintained that any alleged losses suffered by Claimants were the result of Claimants' own decision and market fluctuations.

RELIEF REQUESTED

Claimants requested damages in the amount of \$1,500,000.00; punitive damages in the amount of \$2,500,000.00; pre-award interest at 10%; and the costs of this arbitration including reasonable attorney's fees.

Respondents requested that the Statement of Claim be dismissed in its entirety and that Claimants be assessed the costs of the arbitration including reasonable attorney's fees.

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.

Pursuant to the by-laws of the NASD, the panel determined that Rhoades was required to submit to this arbitration, notwithstanding his failure to submit an executed agreement to arbitrate. Therefore, Rhoades is bound the panel's rulings and determinations.

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. That Claimants' Statement of Claim is dismissed with the exception of the request for the assessment of forum fees.
2. That Claimants' request for punitive damages is denied.
3. That each party shall bear its own costs and expenses, including attorney's fees, with the exception of forum fees as discussed below.
4. That any and all relief not specifically addressed herein is denied.

FORUM FEES

Pursuant to Rule 10332(c) of the Code of Arbitration Procedure, the following Forum Fee(s) are assessed:

18 sessions x \$1,000.00 = \$18,000.00

Forum Fees are assessed against Respondent Merrill Lynch, Pierce, Fenner & Smith, Inc. Claimants will be refunded the \$1,000.00 hearing session deposit previously submitted to the NASD Regulation. Therefore, Respondent Merrill Lynch, Pierce, Fenner & Smith, Inc. has a net assessment due of \$18,000.00.

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

DATE

Dec. 21, 1996

CONCURRING ARBITRATORS' SIGNATURES

Dennis E. Minni

Dennis E. Minni, Chairman
Public Arbitrator

Amelia F. Adams
Public Arbitrator

Robert Shiffra
Industry Arbitrator

Date Decision Served by NASD Regulation: December 130, 1996

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DATE

CONCURRING ARBITRATORS' SIGNATURES

Dennis E. Minni, Chairman
Public Arbitrator

12/20/96

Amelia F. Adams
Amelia F. Adams
Public Arbitrator

Robert Shiffra
Industry Arbitrator

Date Decision Served by NASD Regulation: December 30, 1996

FORUM FEES

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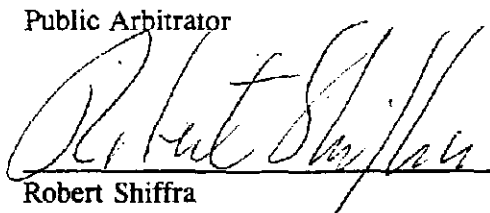
DATE

CONCURRING ARBITRATORS' SIGNATURES

Dennis E. Minni, Chairman
Public Arbitrator

Amelia F. Adams
Public Arbitrator

12-21-96



Robert Shiffra
Industry Arbitrator

Date Decision Served by NASD Regulation: December 30, 1996