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## **NASDR AWARD**

NATIONAL ASSOCIATION OF SECURITIES DEALERS REGULATION, INC.

9/96

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**Names of Claimants:**

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Securities Dealers

Edward P. Hansen and Barbara L. Hansen

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NASDR Case Number 95-03291

**Name of Respondent:**

Smith Barney Inc.

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### **REPRESENTATION OF PARTIES**

Claimants, Edward P. Hansen and Barbara L. Hansen were represented by Timothy M. McDaniel, Esq. of McDaniel & Allen, P.C. located in Houston, Texas.

Respondent, Smith Barney, Inc. was represented by William Hohausser, Esq. of Smith Barney, Inc. located in New York, New York.

### **CASE INFORMATION**

Claimants, Edward P. Hansen and Barbara L. Hansen's Statement of Claim was filed on or about July 6, 1995.

Claimants, Edward P. Hansen and Barbara L. Hansen's Submission Agreement was signed on June 30, 1995.

Respondent, Smith Barney, Inc.'s Statement of Answer to was filed on or about September 29, 1995.

Respondent, Smith Barney, Inc.'s Submission Agreement was executed on September 29, 1995 by Pete S. Michaels, Esquire, Associate General Counsel and First Vice President of Smith Barney, Inc.

### **HEARING INFORMATION**

The hearing was held in Houston, Texas on the following dates:

- August 20, 1996 for two (2) sessions
- August 21, 1996 for two (2) sessions
- August 22, 1996 for two (2) sessions

### CASE SUMMARY

**Claimants' Allegations** In their Statement of Claim, Claimants, Edward P. Hansen and Barbara L. Hansen (the "Hansens") alleged various claims and causes of action against Respondent, Smith Barney, Inc. ("Smith Barney") for the acts and omissions of two Smith Barney brokers, Eldridge N. Bollich ("Bollich") and Bernard C. Hemmer ("Hemmer"). The Hansens alleged that at relevant times, Bollich and Hemmer were acting within the course and scope of their duties as employees of and brokers for Smith Barney, and that Smith Barney was liable for Bollich's and Hemmer's conduct under the doctrine of respondeat superior, principal/agent law, and applicable securities laws and regulations.

The Hansens alleged that Edward P. Hansen retired in 1986 from his 36 year career with the same company as an engineer. Prior to his retirement, and although he had previous experience involving primarily purchasing and holding stocks and bonds for long term appreciation, Edward P. Hansen allegedly felt he needed expert counsel on the handling and investment of funds which had been accumulated as a result of retirement for his and Barbara L. Hansen's retirement years. As a result, Edward P. Hansen consulted with Hemmer who was with Rotan Mosle at the time. Hemmer had been a golfing buddy of Edward P. Hansen's since approximately 1973, and the Hansens were good friends with both Hemmer and his wife.

As alleged, Hemmer suggested that the Hansens use a fund manager and suggested an individual named Phil Goldsmith ("Goldsmith") of Goldsmith & Harris in New York. Hemmer explained that he had known Goldsmith for many years and that Goldsmith at one time managed a department at Rotan Mosle, Inc. and that he did a very good job of it. Hemmer stated that other members of Rotan Mosle, Inc. allegedly knew Goldsmith and thought highly of him, and that Goldsmith was managing other accounts in Houston for which Rotan was the broker and these accounts were likewise doing well. On the strength of these recommendations, Edward P. Hansen met jointly with Hemmer and Goldsmith.

According to the Claimants, Goldsmith explained his concept of investing for an account such as the Hansens' account. The Hansens alleged that Goldsmith stated that he would invest only in equity stocks in which Goldsmith & Harris had done significant research. Goldsmith also allegedly indicated that his partner was a chemical engineer and

that they knew that industry very well. As alleged, in addition to being persuaded by the presentation, Edward P. Hansen explained his conservative investment objectives, which acknowledged the existence of reasonable business risks but which stressed a conservative, no margin buy and hold philosophy seeking primarily capital gains and preservation of capital. Edward P. Hansen's investment objectives allegedly never changed and never included a willingness to engage in speculative high risk investments. As alleged, since Edward P. Hansen was assured that his investment objectives could be met, the **Hansens** opened a stock account with Hemmer as the broker and Goldsmith & Harris as the investment adviser. In approximately 1987, the **Hansens** also opened a bond account in furtherance of their conservative investment objectives.

Sometime after the **Hansens** opened their initial stock account, Bollich and Hemmer began working together as a team, with Bollich taking the role as the chief spokesman. By approximately July, 1988, however, the **Bollich/Hemmer** team had allegedly generated approximately \$24,606 in commissions and net losses in the amount of approximately \$34,815. Goldsmith was also allegedly receiving a 1% management fee in addition to these sums. As a result of this disappointing performance, Edward P. Hansen met with Bollich and Hemmer to, as alleged, stress the importance of preserving and, hopefully, increasing his retirement savings and that he did not have the stock account for the benefit of **Rotan Mosle** or the **Bollich/Hemmer** team. As a result of this meeting, the **Bollich/Hemmer** team allegedly agreed to provide the **Hansens** with what they described as "a very special commission arrangement" which was either sixty percent of the normal rate or sixty percent off the normal rate. Since the **Hansens** did not have any basis to check, they did not know what the rate actually was. According to the Claim, subsequent to this meeting, however, and up until approximately September or October, 1990, the total commissions had been reduced to a total of approximately \$9,796, and the previous losses were reversed and a net gain in the approximate amount of \$81,185 was achieved. With limited exceptions, the bond account performed with the bond market.

Also, during this time frame, but prior to 1990, Bollich and Hemmer left **Rotan Mosle** and joined Smith Barney. As alleged, they continued to work as a team similar to their arrangement at **Rotan Mosle**, and requested the **Hansens** to move their accounts to Smith Barney, which they did.

In their Claim, the **Hansens** pointed to two points of particular significance regarding the background of the relationship between the **Hansens** and the Bollich/Hemmer team. First, the **Hansens** allegedly had a close personal relationship with Hemmer trusting him implicitly as a friend and as a fiduciary. Second, the **Hansens** allegedly trusted the investment advice generated by the Bollich/Hemmer team with the assistance of Goldsmith as a result of the improved performance in their stock account. The **Hansens** alleged that they were therefore very open and vulnerable to a new opportunity recommended by the Bollich/Hemmer team in 1990, an opportunity in Dartmoor Partners, L.P.

During the Spring of 1990, Bollich and Hemmer allegedly told Edward P. Hansen that Goldsmith was starting a new fund that they thought the **Hansens** would be interested in. This fund was Dartmoor Partners, L.P. As part of their efforts to convince the **Hansens** to shift their retirement savings to this new fund, Bollich and Hemmer allegedly asked the **Hansens** to meet with Goldsmith. Sometime thereafter, the **Hansens** in fact met with Goldsmith and Bollich in Smith Barney's offices.

During this meeting, Goldsmith and Bollich allegedly told the **Hansens** about plans for a new fund suggesting that the **Hansens** shift funds from both their stock and bond accounts into this new fund. As alleged, Goldsmith and Bollich later furnished the **Hansens** with a private placement memorandum, and stressed that much legal work had gone into the venture and that it would be sound. The **Hansens** claimed that Goldsmith and Bollich represented that the fund would be similar to what the **Hansens** had been doing but that it would have some distinct advantages. In this regard, it was allegedly represented that Goldsmith would have much more leverage to make deals since he would have more money to work with, that he would be able to purchase in larger quantities, and that the commissions would be lower. It was also allegedly represented that the fund would have the opportunity to take advantage of stock trends, including possibly short and long trades on a limited basis, and would be able to buy or sell if market conditions warranted. As alleged, it was specifically represented that in no case would the **Hansens'** investment be in jeopardy because specific efforts would be limited to less than ten percent of the fund value. It was also allegedly represented that fund costs were expected to be less than one percent, which was better than the **Hansens'** stock fund in the past, and that the mode of operating the fund would be similar to the management of the **Hansens'** stock account. With the positive advantages described. According to the **Hansens**, Goldsmith and Bollich finally claimed that the **Hansens** could be confidently

assured of a minimum of a 20% per annum return, and that they could fully expect their returns to be greater.

Later, Bollich and Hemmer both allegedly recommended and urged the **Hansens** to make this investment. Claimants contended that Bollich in particular represented that this would be a great opportunity for the **Hansens** and that if they wanted to increase their retirement funds **substantially**, this was the way to do it. As alleged, he specifically represented that "this is the way the 'Big Boys' do it." He also allegedly pressured the **Hansens** to change their investments to **Dartmoor** by representing that Goldsmith would be concentrating on **Dartmoor** and might not give their stock account the attention it had been receiving in the past.

The **Hansens** alleged that, relying on these representations and strong recommendations, and yielding to Bollich's pressure tactics, they called Bollich and told him to proceed to dissipate both accounts and invest in **Dartmoor**. In this regard, \$250,000 was contributed in April 1990, and an additional \$205,000 was contributed in October 1990, resulting in a total investment of \$455,000.

The **Hansens** alleged that Smith Barney, through Bollich and Hemmer, specifically represented that **Dartmoor** was a safe investment, that the **Hansens'** funds would not be in jeopardy, that it was what the **Hansens** should be doing, i.e., that it was consistent with their investment objectives, and that the fund would be operated similar to the **Hansens'** stock and bond accounts, with the primary exception that **Dartmoor** would have significant advantages both in terms of returns and safety. Claimants further alleged that Smith Barney, through Bollich and Hemmer, also failed to disclose the true nature of the high risk trading to be done in the fund (and such risks were not made clear in the private placement memorandum), and that **Dartmoor** involved a very high degree of risk, was speculative, was unsuitable, and was completely inconsistent with the **Hansens'** previously stated investment objectives.

Over the following months, there were indications from Goldsmith that **Dartmoor** was not performing as well as previously hoped. Any negative connotations, however, were allegedly obfuscated by glowing expectations and predictions regarding specific transactions which would generate desired partnership performance.

During 1992, however, it became increasingly apparent that the partnership was in serious trouble. By late 1992, performance had allegedly deteriorated so drastically that the partnership apparently had to be liquidated, and it was in fact liquidated on or about October 9, 1992. According to the **Hansens**, out of their original \$455,000 investment, they received only \$14 1,117, resulting in a loss of principal in the amount of \$313,883.

Claimants contended that although Bollich and Hemmer were fiduciaries to the **Hansens** and in spite of Hemmer's close personal relationship with the **Hansens**, neither Bollich nor Hemmer ever hinted at their own culpability and responsibility, and simply chalked up the **Hansens'** losses as the risk of investing. Claimants further contended that their conduct, particularly in the face of their fiduciary duties of disclosure, amounted to nothing short of fraudulent concealment. As a result of the close relationship with Hemmer, the **Hansens** were allegedly not emotionally prepared to place blame where it belonged. The **Hansens** therefore continued to use and rely upon the Bollich\Hemmer team as their brokers and, as alleged, they remained unaware until shortly before their filed their Statement of Claim of their legal rights and that there might be remedies available to recover their significant losses in the **Dartmoor** investment.

The **Hansens** claimed entitlement to recover damages, punitive damages, and other relief pursuant to numerous legal theories, including negligence and unsuitability, misrepresentation and omission liability, Securities Act of 1933 and Texas Blue Sky Law violations, violations of the Texas Consumer Protection - Deceptive Trade Practices Act, breach of contract and of warranty, and breach of fiduciary duty.

**Smith Barney's Defenses.** Smith Barney, Inc. denied any liability to the **Hansens** and asserted various **affirmative** defenses, including failure to state a claim upon which relief may be granted, waiver, estoppel, that the investments were purchased outside of Claimants' accounts with Respondent, limitations, ratification and affirmance, that Respondent acted in compliance with all applicable rules and regulations, that Respondent acted in good faith, that Respondent exercised no discretion or de facto control over Claimants' accounts, that Claimants did not "purchase" an investment from Respondent nor did Respondent provide a "service" regarding the investment, that Claimants have not met a standard appropriate for an award of punitive damages, that Respondent owed no fiduciary duty to Claimants, **insufficiency** of pleadings, that there was no private cause of action for alleged, violations of the NASDR Rules of Fair Practice, that any damages

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suffered by Claimants were caused by third parties, failure to mitigate, and failure to prove loss causation.

### **RELIEF REQUESTED**

Claimants requested an award in the amount of **\$467,984** in actual damages and \$941,650 in punitive damages plus mental anguish damages in an undisclosed amount and attorneys' fees.

Respondent requested that the statement of Claim be dismissed in its entirety and that it be awarded costs and attorneys' fees.

### **OTHER ISSUES CONSIDERED AND DECIDED**

The parties have agreed that a signed handwritten or typed Award may be entered. The parties have also agreed to receive conformed copies of the award while the original remains on file with the NASDR.

### **AWARD**

After considering the pleadings, the testimony, and ~~the evidence~~ presented at the hearing, the undersigned arbitrators have decided in full and final the issues submitted for determination as follows:

1. The Statement of Claim submitted by Edward P. Hansen and Barbara L. Hansen is hereby dismissed with prejudice and denied in its entirety;
2. All requests for relief not specifically granted herein are hereby denied in their entirety; and
3. The parties shall bear their own costs including attorneys' fees except for those specifically enumerated herein.

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### **FORUM FEES**

Forum fees are calculated at the rate of \$1,000.00 per hearing session and \$300.00 for each pre-hearing conference. There were six (6) sessions x \$1,000.00, for a total of \$6,000.00 in forum fees. Pursuant to Section 43(b) of the Code of Arbitration Procedure (the "Code"), a hearing session is any meeting between the parties and the arbitrator(s), including a pre-hearing conference with an arbitrator, which lasts four (4) hours or less.

Pursuant to Section 43(c) of the Code, the National Association of Securities Dealers Regulation, Inc. ("NASDR") shall retain the non-refundable filing fee in the amount of \$250 and shall retain as forum fees the hearing session deposit in the amount of \$1,000 previously deposited with the NASDR by Claimants, Edward P. Hansen and Barbara L. Hansen. In accordance with Sections 43 and 45 of the Code, the NASDR shall retain the non-refundable member surcharge in the amount of \$350 previously submitted by Respondent, Smith Barney, Inc.

Claimants, Edward P. Hansen and Barbara L. Hansen are hereby, jointly and severally, liable for and shall pay to the NASDR the sum of \$5,000 in additional forum fees.

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



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Arbitrators' Signatures:

Dated:

Donald H. Fidler, Esq.  
Donald H. Fidler, Esq.  
Public Arbitrator, Chairperson

September 13, 1996

Felix L. Nigh, CPL  
Felix L. Nigh, CPL  
Public Arbitrator, Panelist

September 13, 1996

Robert E. Otto  
Robert E. Otto  
Industry Arbitrator, Panelist

September 17, 1996

Date served by NASDR: September 23, 1996

Dated served by the NASDR: \_\_\_\_\_

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