

NATIONAL ASSOCIATION OF SECURITIES DEALERS REGULATION, INC.

In the Matter of the Arbitration Between

Name of Claimant

Hugh C. Montgomery

95-04415

Name of Respondents

\*Smith Barney Shearson, Inc.  
Mercer Securities Ltd.  
Stephen J. Schappell  
Mercer Securities, Inc.

REPRESENTATION

Claimant Hugh C. Montgomery ("Claimant") was represented by Merritt A. Cole, Esq. and Michael J. Taichman Robins, Esq., Dilworth, Paxson, Kalish & Kauffman, Philadelphia, PA.

Respondent Smith Barney, Inc. (formerly known as Smith Barney Shearson, Inc. "SBS") was represented by Sean J. Coughlin, Esq., Smith Barney, Inc., New York, NY.

Respondent Mercer Securities, Inc. and Mercer Securities, Ltd. ("Mercer") did not appear.

The Executor of the Estate of Respondent Stephen J. Schappell, deceased ("Schappell") did not appear.

CASE INFORMATION

The Statement of Claim was filed September 15, 1995.

Claimant's Uniform Submission Agreement was signed July 28, 1995.

Respondent SBS filed a Statement of Answer December 29, 1995.

Respondent SBS did not file an executed Agreement to arbitrate.

Respondent Mercer did not file a Statement of Answer or an agreement to arbitrate.

The Executor of the Estate of Respondent Schappell did not file a Statement of Answer or an agreement to arbitrate.

HEARING INFORMATION

Hearing Dates/Sessions: May 28, 1997/two sessions  
May 29, 1997/two sessions

Hearing Location: Vincent Varallo & Associates  
Philadelphia, PA

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Hearing Dates/Sessions: September 4, 1997/two sessions  
September 5, 1997/two sessions  
October 6, 1997/two sessions  
December 1, 1997/one session

Hearing Location: NASD Regulation District Office  
Philadelphia, PA

### CASE SUMMARY

Claimant alleged that Respondents SBS, Schappell, and Mercer (collectively "Respondents") induced Claimant, through fraudulent misrepresentations and omissions, to authorize unsuitable investments, with an over-concentration of such investments. Claimant further alleged that Respondents engaged in excessive trading in his account which resulted in a breach of contract as well as a breach of federal and state securities laws. Specifically, Claimant asserted that when he retired from his position as a Program Manager with General Electric Corporation in March 1992, he opened a non-discretionary IRA account with SBS, in which he deposited \$652,874, and Schappell was the Account Executive in charge of this account.

Claimant alleged that as a retiree, with no significant source of earnings other than from his investments, Claimant informed Schappell that the funds in his account had to be invested conservatively, which Schappell agreed to do. However, Claimant alleged that Schappell invested Claimant's IRA account to be invested in extremely speculative and volatile securities, such as Akers Laboratories which was and still is a non-publicly traded stock, for which there is no market and which pays no dividends.

Claimant further alleged that SBS failed to supervise Schappell and both SBS and Schappell failed to disclose the risks to which Claimant's account was being subjected. Claimant asserted that the failure of SBS and Schappell were the direct and proximate cause of the losses suffered at both SBS and later at Mercer. Moreover, even though the SBS IRA account was a non-discretionary account, Schappell generally made trades without Claimant's prior authorization, knowledge or consent.

Claimant alleged that in August 1993, when Schappell left SBS and became a broker at Mercer, he persuaded Claimant transfer his account to Mercer shortly thereafter. Claimant alleged that Schappell continued at Mercer to concentrate Claimant's retirement funds in extremely speculative securities.

Claimant alleged that the fraudulent, unlawful and improper conduct of the Respondents which resulted in Claimant's losses included, but are not limited to, unsuitable investments; over concentration of such investments; fraudulent misrepresentations and omissions; excessive trading; breach of contract; breach of fiduciary duty; negligence; violations of the anti-fraud provisions of federal and state securities laws; and violations of federal and state securities laws relating to supervisory duties.

Respondent SBS denied allegations of wrong-doing as asserted in the Statement of Claim and maintained that the Statement of Claim was an attempt to collect from SBS losses Claimant sustained at Mercer. SBS further contended that Claimant alleged damages against SBS because Mercer Securities ceased operations in February 1995 and Schappell died in December 1994.

SBS maintained that while Claimant seeks recompense from SBS for \$376,571.00 in losses, Claimant's account, in fact, had a positive total return of over \$139,000.00 which the account was at SBS. SBS further contended that by the fall of 1992, Claimant's IRA account had a well-diversified mix of bond and bond funds and stocks. For example, Respondent maintained that Claimant's account, in October

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1992, had approximately \$150,000.00 in stocks (excluding closed-end bond funds and fixed-rate preferred stocks) in a portfolio of \$636,952.00. SBS further maintained that the stocks included such household names as Apple Computer, Exxon, IBM, National Semiconductor and Texas Instruments, and during that period the percentage of stocks (excluding closed-end bond funds and fixed-rate preferred stocks) in the portfolio was approximately 25%. In addition, SBS asserted that while the percentage of stocks in Claimant's account did increase during 1993, it increased not so much because Claimant was buying more stock, but because the stocks that he already owned increased sharply in value. SBS maintained that Claimant did not sustain any losses until after he left SBS. And, SBS asserted that while Claimant complains of losses on \$150,000.00 of Akers Research, he in fact only purchased \$52,500 worth of Akers Research while he was a SBS customer and SBS did not sell, trade in, or underwrite any stock in Akers Research.

SBS maintained that it is not responsible for losses incurred at Mercer, whether or not on positions transferred from SBS, as once Schappell and Claimant left SBS, they severed their ties with SBS completely and SBS could no longer review the account for activity or profitability. Therefore, while Claimant held an account at SBS, Claimant's exposure to stocks was appropriate and suitable, the trading was reasonable and the account was highly profitable.

The Estate of Schappell did not submit an Answer.

Mercer did not submit an Answer.

**RELIEF REQUESTED**

Claimant requested damages in the amount of \$450,625.60; interest of \$134,500.00; punitive damages; and reimbursement of all Claimant's costs and expenses, including reasonable attorneys' fees and expert witness fees incurred in pursuing this arbitration. SBS requested that the Statement of Claim be dismissed in its entirety.

The Estate of Schappell and Mercer did not request relief.

**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.

The panel determined that Respondents Mercer and the Estate of Schappell were served the Statement of Claim pursuant to Rule 10314 of the Code of Arbitration Procedure ("Code") and the notice of the hearing pursuant to Rule 10315 of the Code by reason of receipts for certified mail signed by representatives of both Respondents and provided an opportunity to submit a Statement of Answer to the allegations contained in the Statement of Claim.

Pursuant to the by-laws of the NASD and Rule 10301 of the Code, the panel further determined that Respondents SBS, Mercer Securities, Inc., Mercer Securities Ltd. and the Estate of Stephen Schappell, deceased, were required to submit to arbitration notwithstanding their failure to submit an executed agreement to arbitrate. Therefore, Respondents SBS, Mercer and Schappell are bound by the panel's rulings and determinations.

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### 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 the claims for compensatory damages and interest are denied; and
2. That the claim for punitive damages is denied; and
3. That Respondents SBS, The Estate of Schappell and Mercer are jointly and severally liable to and shall reimburse directly to Claimant the hearing session deposit of \$750.00 which Claimant submitted to NASD Regulation; and
4. That Respondents SBS, The Estate of Schappell and Mercer are jointly and severally liable to and shall pay to Claimant \$25,000.00 in expert witness fees and attorneys' fees; and
5. That except as specifically addressed herein and in the forum fees section below, each party will bear its own costs and expenses; and
6. That any and all relief not specifically addressed herein, is denied.

### OTHER COSTS

Pursuant to Rule 10333 of the Code, SBS is assessed a member surcharge of \$350.00. Respondent SBS shall receive credit for the \$350.00 deposit previously submitted and no further surcharge is due.

### FORUM FEES

Pursuant to Rule 10332(c) of the Code, the following Forum Fees are assessed:

11 sessions x \$750.00 = \$8,250.00

Forum Fees are assessed to Respondents SBS, The Estate of Schappell and Mercer jointly and severally. Respondents SBS, The Estate of Schappell and Mercer shall receive credit for the \$750.00 hearing session deposit which was reimbursed directly to Claimant, leaving a net assessment due from Respondents of \$7,500.00.

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

9/7/2031

DATE

CONCURRING ARBITRATORS' SIGNATURES

12/17/97

Sheldon Seligsohn

Sheldon Seligsohn, Presiding  
Public Arbitrator

Roy B. Steenhoff  
Public Arbitrator

Linda Checchio  
Industry Arbitrator

OTHER COSTS

OTHER COSTS

Date Decision Served by NASD Regulation:

December 29, 1997

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DATE

CONCURRING ARBITRATORS' SIGNATURES

Dec. 18, 1997

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Sheldon Seligsohn, Presiding  
Public Arbitrator

Roy B. Steenhoff  
Roy B. Steenhoff  
Public Arbitrator

\_\_\_\_\_  
Linda Checchio  
Industry Arbitrator

ASD Date Decision Served by NASD Regulation:

December 29, 1997

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DATE

CONCURRING ARBITRATORS' SIGNATURES

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Sheldon Seligsohn, Presiding  
Public Arbitrator

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Roy B. Steenhoff  
Public Arbitrator

12/26/97

  
Linda Checchio  
Industry Arbitrator

Date Decision Served by NASD Regulation:

December 29, 1997