

NASD REGULATION AWARD

NATIONAL ASSOCIATION OF SECURITIES DEALERS REGULATION

In the Matter of the Arbitration Between

Name of Claimant

Jerry W. Carter

CASE NO.
96-00417

Name of Respondents

Gerald P. Hirsch
Churchill Securities, Inc.
Kevin M. Mahon

Name of Third Party Respondent

Avin E. Bakal

REPRESENTATION

Claimant Jerry W. Carter ("Claimant"): Howard B. Possick, Esq. of the law firm of Arent Fox Kintner & Kahn, Washington, DC

Respondent Gerald P. Hirsch ("Hirsch"): Jerome Kowalski, Esq. Of the Law Offices of Klepner & Cayea, L.L.P., New York, NY

Respondent Churchill Securities, Inc. ("Churchill") during the hearing was represented by Daryl J. Hudson, III, Esq., Washington, D.C. On March 27, 1997, Daryl J. Hudson, III, Esq. withdrew as counsel to Churchill and from that time forward Churchill was represented by Paul Syracuse, President of Churchill.

Kevin M. Mahon ("Mahon") was represented by himself.

Third Party Respondent Avin E. Bakal ("Bakal") was not represented.

CASE INFORMATION

Statement of Claim filed: January 26, 1996

Amended Statement of Claim filed: January 6, 1997

Claimant's Reply to Counterclaim filed: July 8, 1996

Claimant's Submission Agreement signed on: January 26, 1996
Claimant's Reply to Kevin M. Mahon's Amended Answer to the Statement of Claim containing Additional Counterclaim and Third-Party Claims filed: January 13, 1997
Claimant's Motion to Dismiss Respondents' Counterclaims filed: January 23, 1997

Joint Statement of Answer, Affirmative Defenses, and Cross Claim against Respondent Mahon filed by Respondents Hirsch and Churchill on: April 1, 1996
Respondents Hirsch and Churchill's Answer to Respondent Mahon's Cross-Claim filed on: July 23, 1996
Hirsch's Uniform Submission Agreement signed on: April 1, 1996
Churchill's Uniform Submission Agreement signed by Gerald P. Hirsch as President of Churchill Securities on: April 1, 1996

Respondent/Cross-Claimant Churchill's Statement of Cross-Claim against Gerald P. Hirsch filed: January 10, 1997
Respondent/Cross-Claimant Churchill's Memorandum in Opposition to Motion to Dismiss filed: February 3, 1997

Mahon's Answer to the Statement of Claim, and Cross-Claim; Counterclaim, Cross-Claim Against Hirsch and Churchill; and Third Party Claim Against Avin E. Bakal filed: June 25, 1996
Mahon' Amended Answer to the Statement of Claim Containing Additional Counterclaims and Third-Party Claims filed: January 9, 1997
Respondent Mahon's Answer to the Amended Statement of Claim filed: January 13, 1997
Mahon's Uniform Submission Agreement signed on: June 26, 1996

Avin E. Bakal neither filed an answer nor did he execute a uniform submission agreement.

HEARING INFORMATION

Preliminary Hearing with the Panel: October 9, 1996 - two sessions
December 13, 1996 - one session

Hearing Dates/Sessions: February 10, 1997 - two sessions
February 11, 1997 - two sessions
February 12, 1997 - two sessions

Hearing Location: NASD Executive Offices and NASD Regulation District 9
Washington, DC

CASE SUMMARY

Claimant, a self employed artist, opened accounts with Mahon at Churchill in August 1995. Claimant alleged, among other things, that Mahon took control of Claimant and his account.

Claimant alleged that he had trust and confidence in Mahon who knowingly took advantage of Claimant's trust. Claimant alleged that Mahon persuaded Claimant to invest large amounts of his funds in Auxer Industries, Inc. ("Auxer"). Claimant alleged that numerous others customers of Respondents were induced to buy and bought Auxer stock. Claimant alleged that Mahon misled Claimant and failed to provide him material information concerning Auxer stock including, but not limited to, (a) the financial condition and financial performance of Auxer stock; (b) the business of Auxer; (c) the market in which Auxer stock is traded; (d) the background of Auxer's two directors and officers; and, (e) the risks of investing in Auxer stock. Claimant alleged that Mahon knew that it was risky, speculative and highly inappropriate, and contrary to Claimant's best interest for Claimant to invest large amounts of his funds in Auxer. Claimant alleged that Mahon not only induce Claimant to concentrate his funds in Auxer stock, but also engaged in unauthorized purchases for Claimant's account. Claimant alleged that Mahon deliberately refused and failed to sell at the target price, ignoring Claimant's request to sell the Auxer stock. Claimant alleged that, without obtaining Claimant's prior approval, Mahon purchased substantial additional shares of Auxer for Claimant's account. Claimant alleged that he complained to Hirsch about this matter, and informed Hirsch that he was transferring his account at Churchill to another brokerage firm. Claimant alleged that Hirsch made promises, material misrepresentations and omissions to prevent Claimant from transferring his account. Claimant alleged that because of Hirsch's assurances, Claimant did not transfer his Auxer stock to another brokerage firm. Claimant alleged that Hirsch failed to liquidate Claimant's vast majority of Auxer stock as promised. Claimant alleged that Respondents Hirsch, Churchill and Mahons' misconduct makes them liable for: fraud, violations of the Maryland Securities Act, negligence, breach of contract, breaches of fiduciary duties and other duties owed by brokers, brokerage firms and their principal, unsuitability, unauthorized trading, negligent supervision and violating the doctrine respondeat superior.

In their initial pleading, Respondents Hirsch and Churchill denied all allegations of wrongdoing asserted by Claimant. Hirsch and Churchill maintained that Claimant was both a sophisticated and experienced investor. Hirsch and Churchill maintained that Claimant, against Hirsch's advice, insisted on engaging in option trading, among other speculative investment/trading practices. Respondents Hirsch and Churchill maintained that Hirsch contacted Claimant in November of 1995 to advise him that he was over concentrated in Auxer stock. Hirsch and Churchill maintained that in this conversation Hirsch immediately informed Claimant that Mahon was a "rogue" broker, unauthorized to represent Churchill. Churchill and Hirsch maintained that within a day or two of Hirsch's initial conversation with Claimant, Hirsch again called Claimant, urging that the Auxer stock be liquidated in a consistent and orderly fashion. Hirsch and Churchill maintained that, contrary to Hirsch's recommendation, in the interim, Claimant had not sought to liquidate his shares, and had placed orders to purchase additional shares of Auxer. Hirsch and Churchill maintained that Claimant did agree with Hirsch that he was unduly concentrated in Auxer stock and Hirsch immediately began to liquidate the Auxer shares in an orderly fashion. Hirsch and Churchill maintained that in or about the third week of November 1995, Claimant called Hirsch and directed him to stop selling further Auxer shares. Respondents Hirsch and Churchill maintained that after a significant "window of opportunity" had closed as a consequence of Claimant's own conduct, Claimant then sought to have the Auxer stock liquidated and have Churchill guarantee payment of the difference.

Respondents Hirsch and Churchill asserted a cross claim against Mahon and alleged that while they deny liability for any putative damages sustained, Hirsch and Churchill assert that if they are found liable, said liability is secondary, passive, vicarious, constructive, technical or imputed and that Claimants alleged damages arose through the primary, active and direct conduct of Mahon. Hirsch and Churchill asserted that, in the event that Claimant recovers judgment against Respondents Hirsch and Churchill, Mahon will be liable to indemnify them for the amount of any such judgment which may be recovered against them and by Claimant, together with attorneys' fees and costs.

Mahon denied all allegations of wrongdoing against him asserted by Claimant and Respondents Hirsch and Churchill. Mahon maintained that he was employed by Churchill until July 19, 1995 and that his registration was voluntarily terminated. Mahon maintained that he terminated his employment with Churchill prior to Claimant's forming a relationship with Hirsch and Churchill. Mahon further maintained, during Claimant's association with Churchill, that he was never compensated in any manner.

Mahon counterclaimed that at no time relevant to any of the events described in the Statement of Claim was he officially or unofficially associated with Hirsch and Churchill. Mahon alleged that Claimant is fully aware that Mahon was not involved or connected to Claimant's securities account at Churchill. Mahon alleged that Claimant is aware that he did not commit or participate in any of the actions and/or events ascribed to him in Claimant's claim. Mahon asserted that notwithstanding Claimant's complete knowledge that Mahon could not have committed or participated in any of the actions and/or events ascribed to and alleged of Mahon, Claimant falsely accused Mahon of such conduct. Mahon alleged that Claimant has defamed and libeled him and committed the torts of abuse of process and/or malicious prosecution; and, that Claimant, Hirsch and Churchill are guilty of civil conspiracy to abuse process, or to prosecute maliciously.

Mahon asserted a cross claim against Hirsch and Churchill and a third party claim against Bakal. Mahon alleged that after he voluntarily terminated his association with Churchill, the Churchill agent or agents who solicited Claimant, under the supervision and direction of Bakal and/or Hirsch, falsely and fraudulently identified himself or themselves to Claimant as Mahon. Mahon maintained that such agent(s) falsely and fraudulently identified himself or themselves to Claimant as Mahon in making further telephone calls to Claimant. Mahon alleged that as a result, third party respondent Bakal, and cross-respondent Churchill and Hirsch breached and violated 15 U.S.C. §§ 6102 and 57a C.F.R. § 310.4(d), Section 10(b) and Rule 10b-5 thereunder of the Securities Exchange Act of 1934, and Article III, Sections 1, 18, 27 and 35(d) of the NASD's Rules of Fair Practice. Mahon asserted an additional counterclaim against Claimant for illegally tape recording telephone calls from Claimant's residence in violation of Maryland's Wiretapping and Electronic Surveillance Act.

Claimant replied to Mahon's counterclaim stating that Mahon's counterclaim is meritless, frivolous, malicious and asserted in bad faith and for improper purposes including harassment. Hirsch and Churchill categorically denied all allegations of wrongdoing asserted by Mahon in his cross claim.

Respondent Cross-Claimant Churchill asserted a cross-claim against Hirsch. On August 26, 1996 the common stock of Churchill was acquired by Paul C. Syracuse ("Syracuse") and Eric Krygier ("Krygier") from Hirsch. Respondent Churchill maintained that it holds a complete right of indemnification against Hirsch. Respondent Churchill maintained that if Hirsch is proven to have wilfully or with gross negligence perpetrated harm on Claimant as alleged by Claimant, then Hirsch should indemnify Churchill, as the assignee of Syracuse and Krygier, for any damages assessed against Churchill arising from the conduct of Hirsch. Churchill maintained that Hirsch has engaged in a systematic pattern of conveying assets with the apparent purpose of defrauding creditors and potential judgment creditors. Churchill maintained that Hirsch has continued this pattern of fraudulent conveyance even after providing a personal guarantee of indemnity to Syracuse and Krygier with the apparent motive of evading the consequences of a judgment against Hirsch and/or Churchill.

RELIEF REQUESTED

Claimant requested, in his pleading, that Respondents be jointly and severally liable for out of pocket losses in the amount of at least \$115,000, plus other damages including lost income, attorneys' fees, arbitration costs, punitive damages, prejudgment interest and expenses. Claimant requested that Mahon's counterclaim be dismissed with prejudice and that Claimant be awarded attorneys' fees and expenses related to the defense of the counterclaim.

Hirsch and Churchill requested that an award be entered in their favor dismissing the Statement of Claim against them together with attorneys' fees and costs.

Hirsch and Churchill cross claimed requesting indemnification, or in the alternative, contribution from Mahon in the amount of any judgment which may be recovered against them in favor of Claimant, together with attorneys' fees and costs of suit.

Hirsch and Churchill requested that Mahon's cross claim be dismissed with prejudice and that Hirsch and Churchill be awarded attorneys' fees and expenses relating to the defense of the cross-claim.

Mahon requested that Claimant's claim be dismissed in its entirety.

Mahon requested that Hirsch and Churchills' cross claim be dismissed with prejudice and that he be awarded costs, expenses, and attorney's fees.

In his counterclaim, Mahon requested damages against Claimant in the amount of \$250,000; plus costs and attorney's fees; in addition, Mahon requested liquidated damages of \$1,000 for each occasion on which the Maryland Wiretapping and Electronic Surveillance Act was breached, statutory punitive damages, costs and attorney's fees.

Mahon requested compensatory damages from third-party respondent Bakal and cross respondent Churchill and Hirsch, jointly and severally, for any and all sums for which he may be adjudged liable to Claimant, as well as for such other actual damages as may be proved at the hearing, plus punitive damages, costs, and attorney's fees.

Churchill in its cross claim against Hirsch requested a finding of fact and conclusion of law stating that damages assessed against Churchill are done so purely as an operation of law and solely as a result of Hirsch's conduct toward Carter; a declaratory judgment setting forth Churchill's right to a full and

complete indemnification from Hirsch for all damages and costs; an award for Churchill against Hirsch for the same amount that the Panel would award Claimant against Churchill; an award for Churchill for attorneys' fees; and a 1-year stay against the enforceability of any judgment to allow Churchill to indemnify the judgment amount from Hirsch.

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 Regulation.

That at the commencement of the hearing on the merits, Churchill dismissed its counterclaim against Respondent Hirsch.

Third Party Respondent Avin E. Bakal was sent hearing information by both first class mail and certified mail. The certified mail was signed for with the "green" card returned to the NASD Regulation and the first class mail is presumed to have been received as it was not returned. The panel exercised its jurisdiction pursuant to Rule 10301 of the Code of Arbitration Procedure and Bakal is bound by the rulings and determinations of this panel as set forth in its award.

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 Respondents Hirsch, Churchill and Mahon are jointly and severally liable to Claimant and shall pay the Claimant the sum of \$114,491.65 in compensatory damages; plus 10% simple interest from November 22, 1995 until the date the award is paid.
2. Respondents Hirsch, Churchill and Mahon are jointly and severally liable to Claimant for attorneys' fees in the amount of \$75,843.31
3. The amount due from Respondents Hirsch, Churchill and Mahon to Claimant as compensatory damages and attorneys' fees at this time, excluding interest, is \$190,334.97 (\$114,491.65 + \$75,843.31 = \$190,334.97.) The Panel sets forth the following payout schedule:

Respondents Hirsch, Churchill and Mahon, jointly and severally, shall pay to Claimant \$30,000 within 30 days from receipt of this award. After the first lump sum payment of \$30,000, Respondents Hirsch, Churchill and Mahon jointly and severally shall pay to Claimant the sum of \$10,000 in monthly installments until the award is paid. If

Respondents Hirsch, Churchill and Mahon default on any installment then the entire sum becomes due and owing.

4. Respondents Hirsch and Mahon are jointly and severally liable to Claimant for punitive damages in the amount of \$343,474.95. The Panel cites as its authority to award punitive damages the following cases; Mastrobuono v. Shearson Lehman Hutton, Inc., 115 S. Ct. 1212 (1995); R. C. Layne Construction, Inc. v. Stratton Oakmont, Inc., 651 N.Y.S.2d (N.Y. App. Dec. 24, 1996); Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Adler, 651 N.Y.S.2d 38 (N.Y. App. Dec. 17, 1996). The Panel finds that punitive damages should be awarded against Respondents Hirsch and Mahon based on their egregious fraudulent conduct. The Panel finds that Hirsch and Mahon are liable for common law fraud and for violations of the antifraud provisions of the federal securities laws and that the damages awarded in this arbitration to Claimant against Respondents Hirsch and Mahon are not dischargeable in bankruptcy.

5. That Mahon's counterclaim is denied in its entirety.
6. That Mahon's Third Party Claim against Avin E. Bakal is denied in its entirety.
7. That other than the attorneys' fees and forum fees addressed herein, the parties shall bear their respective costs.
8. Any and all claims for relief not specifically addressed herein are denied in their entirety.

OTHER COSTS

Churchill's postponement fees shall be retained by the NASD Regulation, Inc.

Mahon filed a counterclaim, cross claim and third party claim. Mahon deposited one non refundable filing fee, however, two additional non refundable filing fees remain due and owing to the NASD Regulation for a negative balance due to the NASD Regulation in the amount of \$1,000.00.

FORUM FEES

Pursuant to Rule 10332 of the Code of Arbitration Procedure, the following Forum Fees are assessed.

9 hearing sessions x \$1,000 = \$9,000 - \$750 hearing session deposit of Claimant = \$8,250

Forum Fees Assessed Against: Respondents Hirsch, Churchill and Mahon are equally assessed forum fees so that each shall bear 1/3.

Hirsch is assessed forum fees in the amount of \$2,750, however Hirsch is entitled to offset this

amount with his hearing session deposit of \$750 previously filed so that the amount due as a forum fee from Hirsch is \$2,000.

Churchill is assessed forum fees in the amount of \$2,750, however Churchill is entitled to offset this amount with its hearing session deposit of \$750 previously filed so that the amount due as a forum fee from Churchill is \$2,000.

Mahon is assessed forum fees in the amount of \$2,750 plus Mahon owes non refundable filing fees in the amount of \$1,000. Mahon may offset these outstanding fees with his hearing session deposit of \$750 so that the fees due from Mahon (both for forum fees and non refundable filing fees) is \$3,000.

The panel directs that the \$750 hearing session fee previously deposited by Claimant shall be borne by Respondents Hirsch, Churchill and Mahon, jointly and severally, so that they are directed to refund directly to Claimant his hearing session deposited.

Fees are payable to NASD Regulation, Inc.

DATE

Concurring Arbitrators' Signatures

5/30/97

Robert O. Harris

Robert O. Harris, Esq. - Chairman
Public Arbitrator

Leonard E. Benade - Panelist
Public Arbitrator

James M. Metcalf - Panelist
Industry Arbitrator

Date Award served by NASD Regulation:

June 3, 1997

amount with his hearing session deposit of \$750 previously filed so that the amount due as a forum fee from Hirsch is \$2,000.

Churchill is assessed forum fees in the amount of \$2,750, however Churchill is entitled to offset this amount with its hearing session deposit of \$750 previously filed so that the amount due as a forum fee from Churchill is \$2,000.

Mahon is assessed forum fees in the amount of \$2,750 plus Mahon owes non refundable filing fees in the amount of \$1,000. Mahon may offset these outstanding fees with his hearing session deposit of \$750 so that the fees due from Mahon (both for forum fees and non refundable filing fees) is \$3,000.

The panel directs that the \$750 hearing session fee previously deposited by Claimant shall be borne by Respondents Hirsch, Churchill and Mahon, jointly and severally, so that they are directed to refund directly to Claimant his hearing session deposited.

Fees are payable to NASD Regulation, Inc.

DATE

Concurring Arbitrators' Signatures

May 29, 1997

Robert O. Harris, Esq. - Chairman
Public Arbitrator

Leonard E. Benade
Leonard E. Benade - Panelist
Public Arbitrator

James M. Metcalf - Panelist
Industry Arbitrator

Date Award served by NASD Regulation:

June 3, 1997

amount with his hearing session deposit of \$750 previously filed so that the amount due as a forum fee from Hirsch is \$2,000.

Churchill is assessed forum fees in the amount of \$2,750, however Churchill is entitled to offset this amount with its hearing session deposit of \$750 previously filed so that the amount due as a forum fee from Churchill is \$2,000.

Mahon is assessed forum fees in the amount of \$2,750 plus Mahon owes non refundable filing fees in the amount of \$1,000. Mahon may offset these outstanding fees with his hearing session deposit of \$750 so that the fees due from Mahon (both for forum fees and non refundable filing fees) is \$3,000.

The panel directs that the \$750 hearing session fee previously deposited by Claimant shall be borne by Respondents Hirsch, Churchill and Mahon, jointly and severally, so that they are directed to refund directly to Claimant his hearing session deposited.

Fees are payable to NASD Regulation, Inc.

DATE

Concurring Arbitrators' Signatures

Robert O. Harris, Esq. - Chairman
Public Arbitrator

Leonard E. Benade - Panelist
Public Arbitrator

June 2, 1997

James M. Metcalf
James M. Metcalf - Panelist
Industry Arbitrator

Date Award served by NASD Regulation: *June 3, 1997*