

12/97

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AWARD

NASD Regulation, Inc. Office of Dispute Resolution

In the Matter of Arbitration Between

Juan Manuel Pasalagua
and Maria Pasalagua,
Claimants,

and

No. 96-00949

D.E. Frey & Company, Inc., Peter
Sperling and Kenneth Sperling,
Respondents.

REPRESENTATION OF PARTIES

Claimants, Juan Manuel and Maria Pasalagua, were represented by William R. Burke, Jr., Esquire of Garcia & Burke, located in Houston, Texas.

Respondent, D.E. Frey & Company, Inc., were represented by Charles F. Brega, Esquire of Brega and Winters, P.C., located in Denver, Colorado.

Respondents, Kenneth and Peter Sperling were represented by J. Eugene Clements, Esquire of Clements, O'Neill, Pierce & Nickens, located in Houston, Texas.

CASE INFORMATION

Claimants, Juan Manuel and Maria Pasalagua's, Statement of Claim was filed on or about April 10, 1996. Claimants, Juan Manuel and Maria Pasalagua's Submission Agreement was signed on March 26, 1996.

Respondent, D.E. Frey & Company, Incorporated's, Statement of Answer was filed on or about May 15, 1996.

Respondents, Kenneth I. Sperling and Peter Sperling's Statement of Answer was filed on or about April 23, 1996.

Respondent, D.E. Frey & Co., Incorporated's, Submission Agreement was signed on May 15, 1996 by Mark Appleton, Esquire, General Counsel and Senior Vice President.

Respondents, Kenneth I. Sperling and Peter Sperling's Submission Agreement was signed on

HEARING INFORMATION

The hearing was held in Houston, Texas on: November 3, 1997 for two (2) sessions;
November 4, 1997 for two (2) sessions;
November 5, 1997 for two (2) sessions; and
November 6, 1997 for two (2) sessions.

CASE SUMMARY

Juan Manuel Pasalagua and Maria Pasalagua ("Claimants.") alleged that their losses were the result of the actions of D.E. Frey & Company, Incorporated ("D.E. Frey,") and Kenneth I. Sperling and Peter Sperling (together, "the Sperlings,") in failing to monitor their account and in failing to properly keep Claimants advised of developments in their D.E. Frey account. Claimants asserted that after being customers of the Sperlings for several years at other broker-dealers, on December 18, 1993, the Sperlings requested Claimants to execute the paperwork necessary to transfer their accounts to Correspondent Services Corporation, a firm that apparently handled the accounts for the new brokerage firm, D.E. Frey & Co, and that the transfer did occur on January 14, 1994 when securities valued at \$3,526,676.50 were transferred into an account with a margin balance of \$3,220,000. Claimants asserted that the net value of their account on January 31, 1994 was \$349,082.66 and that as of February 28, 1994 due to various transactions and the decline in the value of the securities, the net value of Claimants' account was \$276,496.34. Claimants said that in March of 1994, Kenneth Sperling telephoned Juan Manuel Pasalagua in Mexico City to advise him that the securities account required a \$30,000.00 deposit for a margin call, at which point Mr. Pasalagua requested the sale of a sufficient amount of securities to make the margin call. Claimants stated that based on the checks written and net margin interest (income minus loan interest,) the account had a net cash outflow of about \$50,000 during the remainder of 1994, and so, the account net value at the end of 1994 should have been almost \$200,000 if there had been a \$246,000 net value following the \$30,000 margin call.

Claimants asserted that in late 1994, Juan Manuel Pasalagua wrote a check for \$5,000 on the account and found that the account did not have sufficient funds to cover the check, and in fact the account had been "wiped out." Claimants pointed to the account statements which indicated that the net value of the account was reduced by about fifty-six percent (56%) during March of 1994 and that the net value of the account dropped from \$276,000 to \$119,456.08. Claimants asserted that they did not receive their monthly statements, (which failed to be forwarded by the defunct San Diego based mail-box company from whom they were receiving mail prior to 1994.) However, Claimants stated that they did have telephone conversations from Mexico City with the Sperlings in 1994 and that the Sperlings played golf with Mr. Pasalagua in mid-1994, yet despite always knowing how to reach Claimants, the Sperlings never advised the Pasalaguas of the status of their account. Claimants asserted that the Sperlings actually made a trip in January of 1995 to Mexico City to reassure Claimants regarding the handling of their account, and that

the Sperlings assured Juan Manuel Pasalagua that they would take care of him, possibly even giving him some override on commissions that they were earning on the account of another Mexican investor to whom he had introduced the Sperlings. Claimants contended that nothing was ever done to assist them, and alleged that had they known of the status of the account from the Sterlings or D.E. Frey & Co., through proper monitoring of their account, something could have been done to correct the losses with respect to their account. Juan Manuel and Maria Pasalagua alleged that Peter and Kenneth Sperlings' actions in failing to monitor Claimants' account at D.E. Frey & Co., and failure to advise Claimants of the developments with their account constituted fraud, negligent misrepresentation, violations of the Texas Deceptive Trade Practices Act, Texas Securities Act, and violations of NASD rules.

Kenneth I. Sperling and Peter Sperling ("Respondents,") asserted that when the Claimants transferred their account from Smith Barney Shearson to Correspondent Services Corporation, the Claimant's new account documents included, among other things, a standard margin agreement which notifies of and secures the customers' agreement to liquidation with or without notice to meet margin calls. Respondents said that the new account documents also included a Form W-8, in which the Claimants specifically designated the mail-box company's address as the Claimants' mailing address, the address to which they had been mailing correspondence to the Claimants for five years and continued to do so until Claimants gave notice that the mailing address changed on July 27, 1995, when the bulk of the equity was already exhausted. Respondents also alleged that in contradiction to Claimants' statements regarding Respondents' notice regarding their account, the Sperlings remained in touch with their customers and discussed their deteriorating account status with them both by telephone and in person. As evidence of such, the Sperlings were invited to play golf with Claimant as his guest at the Club de Golf Chapultepec in Mexico City, where at Mr. Pasalagua's invitation, they did discuss with Claimant problems with his account. Furthermore, the Sperlings said that in June of 1995, Mr. Pasalagua instructed them to liquidate the bonds collateralizing a loan at Texas Commerce Bank and to deposit available funds from the proceeds in Mr. Pasalagua's money market account to provide liquidity. The Sperlings stated that at no time, during any of their communications with Claimants, did Claimants complain about the diminution of their margin account nor urge the sort of claims of unknown and/or unauthorized sale of bonds to meet margin calls. The Sperlings asserted that Peter Sperling made a visit to the Claimants' home in January of 1995, but denied that there was any discussion of mishandling the account or of "taking care" of the Pasalaguas.

Respondents, the Sperlings finally stated that as late as December of 1995, at Mrs. Pasalagua's earnest request, the Sperlings personally authorized D.E. Frey to honor an excessive Master Card debit to the Pasalaguas' account (and thus, became *de facto* personal guarantors,) thereby leaving a debt remaining in the amount of \$1,069 to the Sperlings. Respondents alleged that the claim against them should be dismissed as they carried out the instructions of Claimants to the letter and because Claimants losses centered around mere market forces.

D.E. Frey & Co., Inc. ("Respondent") concurred with Respondents, the Sperlings, and denied any wrongdoing with respect to the handling of Claimants' account. Furthermore, D.E. Frey & Co. renewed the Sperlings' statements to the effect that the Sperlings merely followed Claimants' instructions as to meeting margin calls and mailing notice and that their losses were the result of

prevailing market conditions. Furthermore, Respondent, D.E. Frey & Co. cited to the Claimants' ratification of the account activity by continuing to do business with the Sperlings and D.E. Frey & Co., as well as transferring a substantial amount of funds back into his account. D.E. Frey & Co. stated that the Claimants assumed the risk of their investments, ratified all activity in their account and based on the doctrine of estoppel, could not challenge the transactions in question.

RELIEF REQUESTED

Claimants, Juan Manuel Pasalagua and Maria Pasalagua, requested an award for \$200,000 in actual damages as well as exemplary damages and reasonable attorney's fees and costs.

Respondents, D.E. Frey & Company, Incorporated, requested that the claims asserted against them be dismissed in their entirety and that they be awarded their costs and attorneys' fees.

Respondents, Kenneth Sperling and Peter Sperling, requested that Claimants repay the \$1,069.00 owed to them, that the claims asserted against them be dismissed in their entirety and that they be awarded their costs and attorneys' fees.

OTHER ISSUES CONSIDERED AND DECIDED

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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 original(s) remain on file with the NASD Regulation, Inc. Office of Dispute Resolution.

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, Juan Manuel and Maria Pasalagua's Statement of Claim is denied in its entirety and dismissed with prejudice.
2. Claimants, Juan Manuel and Maria Pasalagua are liable for and shall pay to Respondents, Kenneth I. and Peter Sperling, actual damages in the amount of \$1,107.
3. That other than forum fees, which are addressed below, all other claims and requests for relief not specifically awarded here are, and each of them, hereby denied with prejudice.

FORUM FEES

Forum fees are calculated at the rate of \$750 per hearing session and \$300.00 for each pre-hearing conference, if any. There were no pre-hearing conferences and there were eight (8) hearing sessions x \$750 = \$6,000 in forum fees. Pursuant to § 10332(b) of the NASD 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 § 10332(c) of the Code, the NASD Regulation, Inc., Office of Dispute Resolution shall retain the non-refundable filing fee of \$200 and shall retain as forum fees the hearing session deposit of \$750 previously deposited with the NASD Regulation, Inc., Office of Dispute Resolution by Claimants, Juan Manuel Pasalagua and Maria Pasalagua. Respondents, D.E. Frey & Company, Incorporated, and Kenneth Sperling and Peter Sperling, are jointly and severally liable^{1/2} for and shall pay to the NASD Regulation, Inc. Office of Dispute Resolution the sum of \$5,250 in forum fees.

Pursuant to § 10333 of the Code, the NASD Regulation, Inc., Office of Dispute Resolution shall retain the non-refundable member surcharge of \$350 previously deposited with the NASD Regulation, Inc., Office of Dispute Resolution by Respondent, D.E. Frey & Company, Incorporated.

The NASD Regulation, Inc. Office of Dispute resolution shall retain the postponement fees paid by D.E. Frey & Co., Inc. in the amount of \$750 and by Kenneth and Peter Sperling in the amount of \$750.

Fees are payable to the NASD Regulation, Inc., Office of Dispute Resolution.

Concurring Arbitrators' Signatures:

A. Bentley Nettles, Esquire
A. Bentley Nettles, Esquire
Chairperson, Public Arbitrator

December 16, 1997
Date

John J. King, Esquire
John J. King, Esquire
Panelist, Public Arbitrator

December 15, 1997
Date

Steve R. Newman
Steve R. Newman
Panelist, Industry Arbitrator

December 15, 1997
Date

For NASD use only:

Date Award was served on the parties: December 17, 1997