

N.A.S.D. REGULATION AWARD

NATIONAL ASSOCIATION OF SECURITIES DEALERS REGULATION, INC.

In the Matter of the Arbitration Between

Name of Claimant

Richard F. Dawahare,
POA/Woodrow W. Dawahare

96-00965

Name of Respondents

Dean Witter Reynolds Inc.
Smith Barney, Inc.
Adam Spencer

REPRESENTATION

Claimant Woodrow W. Dawahare ("Claimant") was represented by William W. Allen, Esq. And Stephen P. Stolz, Gess Mattingly & Atchison, Lexington, KY.

Respondent, Dean Witter Reynolds ("DWR") was represented by William E. Johnson, Esq., Johnson, Judy, True & Guarnieri, Frankfort, KY.

Respondent Smith Barney, Inc. ("SBI") was represented by Linda R. Alpert, Esq., Smith Barney, Inc., New York, NY.

Respondent Adam S. Spencer ("Spencer") appeared *pro se*.

CASE INFORMATION

The Statement of Claim was filed March 4, 1996.

Claimant's Uniform Submission Agreement was signed March 7, 1996.

DWR's Statement of Answer and Crossclaims against Spencer and SBI was filed April 23, 1996.

DWR's Statement of Answer to SBI's Crossclaim was filed May 14, 1996.

DWR's Crossclaim against Spencer was withdrawn June 5, 1997.

DWR did not submit an executed agreement to arbitrate.

SBI's Statement of Answer and Crossclaims against Spencer and DWR was filed April 30, 1996.

SBI's Statement of Answer to DWR's Crossclaim was filed April 30, 1996.

SBI's Crossclaim against Spencer was withdrawn June 6, 1997.

SBI's Uniform Submission Agreement was signed April 30, 1996.

Spencer did not file a Statement of Answer nor an executed agreement to arbitrate.

HEARING INFORMATION

Hearing Dates/Sessions: June 11, 1997/two sessions
June 12, 1997/two sessions
June 13, 1997/two sessions
September 22, 1997/two sessions
September 23, 1997/two sessions
September 24, 1997/two sessions

Hearing Location: Seelbach Hotel
Louisville, KY

CASE SUMMARY

Claimant alleged, among other things, that while Spencer was employed by DWR and later, by SBI, Spencer asserted and exercised de facto control over the Claimant's securities account and thereby engaged in an unsuitable and high risk pattern of trading that exposed Claimant's account to an undue risk of loss and generated excessive commissions. Claimant alleged that at the time of the conduct complained of, Claimant was in his late seventies and had been diagnosed as suffering from Alzheimer's Disease. Claimant contended his failing memory and other health problems rendered him substantially unable to participate meaningfully in the management of his account, to recognize the mounting risk of loss arising from the increasingly speculative positions in his account, and to recognize the high commissions being generated by the excessive activity. The undue risk of loss arose, in part, from the very large speculative short positions in the stock of American on Line, Cascade Communications Corporation and Adtran, Inc. Rapidly rising share prices of those stocks during October, November and December 1994, resulted in a steep decline in the value of the account and actual losses in excess of \$500,000.00 within a period of sixty days.

Claimant alleged that commissions generated by the trading activity in his account at SBI and DWR comprised a large majority of Spencer's total business. Claimant asserted that when Spencer was hired by DWR in September 1994, he was paid substantial incentive compensation, one-half of which was withheld for one year and was payable to him only if, during the year, the Claimant's account had generated gross commissions in an amount equal to approximately 70% of the amount of gross commissions generated by the account when it was at SBI. Claimant contended that this hiring prerequisite gave Spencer a strong financial incentive to churn Claimant's account and that it materially increased the chances that the Claimant would be harmed and thus Claimant requested punitive damages against DWR. Claimant further alleged that in December 1994, Spencer gave Claimant a written guarantee against loss arising from the short position in America On Line in order to dissuade Claimant from bringing Spencer's conduct to the attention of DWR.

Respondent DWR denied the allegations of wrong-doing as asserted in the Statement of Claim. DWR maintained that excessive trading did not occur while the account was at DWR, as the account was at DWR only from October 3, 1994 to approximately February 4, 1995. DWR contended that the trading in the account was not heavy while it was at Dean Witter, and Spencer's total commissions were \$34,520.61 for October, \$15,756.06 for November, \$12,567 for December and \$5,377 for January, or total commissions from Claimant's transactions while at DWR of approximately \$44,000.00.

DWR defends against the unsuitability claim by contending that it had every right to rely upon the prior trading experiences of Claimant at SBI, as having established the suitability for the trading in the account.

In addition, DWR properly relied upon representation of Spencer, the concurrence by Claimant through the transfer of the account, his execution of the margin agreement, his congratulatory telephone conversation with Robert Berg, and his receipt without comment of records of trades, monthly account statements and letters from Robert Berg. DWR maintained that it had no knowledge of Claimant's dissatisfaction with the account until January 16, 1995.

DWR further maintained that Claimant was happy with the account as long as it was profitable. He showed a profit by short trading with Spencer at SBI from April, 1993, through October 3, 1994, and it was only when the market turned, causing substantial losses by short trading, that he and his son Richard, began demanding guarantees against losses from Spencer.

Respondent SBI denied all allegations of wrongdoing and denied any liability for Claimant's alleged loss. SBI maintained that contrary to Claimant's allegations, Claimant's account was profitable at SBI, with a gain of over \$100,000.00 on a net basis. SBI further maintained that the investments were suitable for Claimant based on his risk-oriented objectives, extensive investment background and high net worth. SBI contended that Claimant admittedly had over 20 years experience in the market, maintained accounts with numerous firms, was one of the principals in a chain of department stores, had a substantial liquid and total net worth, and his investment goals included appreciation with risk. SBI asserted that Claimant made a generous profit on many trades at SBI, including short sales in American On-Line ("AOL"), and is merely making a hindsight attack on isolated short trades involving AOL which he expressly authorized and approved. SBI maintained that Claimant was aware of the risk of these trades, acknowledged the trading through written communications and oral discussions with the branch manager, and his account was always adequately supervised by SBI.

SBI denied that it had any knowledge of Claimant's alleged mental infirmities, and was never informed of any problems or complaints by either Claimant or any member of Claimant's family, including one member who had a power of attorney in favor of the Claimant, which power of attorney was never disclosed to SBI. SBI further maintained that any losses were due to market fluctuations over which SBI had no control, especially after the account left SBI in a transfer to DWR in September 1994.

RELIEF REQUESTED

Claimant requested an damages in the amount of \$604,463.06, plus pre-award interest from August 31, 1997 to the date of the award, against Spencer, DWR and SBI, allocated between DWR and SBI as the panel deems appropriate; punitive damages against DWR; the costs and expenses of the arbitration, including attorney's fees and that all forum fees be assessed to Respondents.

DWR requested that Claimant's claim be dismissed without any award to Claimant; and for DWR's recovery of attorneys' fees and assessments.

SBI requested that the Statement of Claim be dismissed and that the costs and fees of the arbitration be assessed to Claimant.

Spencer 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 considered that while DWR did not file a properly executed agreement to arbitrate but is required to submit to arbitration pursuant to Rule 10301 of the NASD Regulation Code of Arbitration Procedure ("Code"), DWR is bound by the decisions of the panel.

The panel granted Spencer's Request to participate in the hearing notwithstanding his did not file an executed agreement to arbitrate nor a Statement of Answer, the panel granted his request to participate in the hearing. Spencer did attend the hearing on June 11, 12 and 13, 1997 but chose not to attend on September 22, 23 and 24, 1997. The by-laws of the NASD and Rule 10301 of the Code require Spencer to submit to arbitration and his appearance waived any issue of notice pursuant to Rule 10315 of the Code, therefore, the panel determined that Spencer is bound by the determinations and rulings of the panel.

The panel considered SBI's renewed Motion to Dismiss at the conclusion of Claimant's case but deferred decision until the conclusion of the case in its entirety.

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 Respondent Adam Spencer is liable to and shall pay to Claimant \$1,000.00.
2. That Claimant's claims against Respondent Smith Barney, Inc. are denied.
3. That Respondent Dean Witter Reynolds, Inc. is liable to and shall pay to Claimant \$25,000.00 in compensatory damages.
4. That Respondent Dean Witter Reynolds, Inc. is liable to and shall pay to Claimant \$24,000.00 in punitive damages.
5. That Respondent Dean Witter Reynolds, Inc.'s Crossclaim against Respondent Smith Barney, Inc. is denied.
6. That Respondent Smith Barney, Inc.'s Crossclaim against Respondent Dean Witter Reynolds, Inc. is denied.

OTHER COSTS

Pursuant to Rule 10333 of the Code, DWR and SBI are each assessed a member surcharge of \$500.00. SBI shall receive credit for the surcharge deposit previously submitted to NASD Regulation, leaving no further member surcharge due from SBI. DWR has a member surcharge due of \$500.00.

FORUM FEES

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

12 sessions x \$1,000.00 = \$12,000.00

Forum Fees are assessed at \$4,000.00 to Claimant, \$4,000.00 to DWR and \$4,000.00 to SBI.

Claimant shall receive a credit for the \$1,000.00 hearing session deposit previously submitted to the NASD Regulation, leaving a net Forum Fee assessment due from Claimant of \$3,000.00.

DWR has a net Forum Fee assessment due of \$4,000.00.

SBI shall receive a credit for the \$1,500.00 hearing session deposit previously submitted to the NASD Regulation, leaving a net Forum Fees assessment due from SBI of \$2,500.00.

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

DATE

CONCURRING ARBITRATORS' SIGNATURES

10/6/97

Amelia F. Adams

Amelia F. Adams, Presiding
Public Arbitrator

Hugh C. Durbin
Public Arbitrator

Gerald B. Brenzel
Industry Arbitrator

Date Decision Served by NASD Regulation:

October 23, 1997

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Amelia F. Adams, Presiding
Public Arbitrator

6 October 1997

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