

AWARD

NASD Regulation, Inc. Office of Dispute Resolution

In the Matter of Arbitration Between

James Sexton and Maureen Sexton,

Claimants,

and

No. 96-01198

Gruntal & Co., Inc., and Timothy L. Johnson,

Respondents.

REPRESENTATION OF PARTIES

James Sexton and Maureen Sexton were represented by Mark J. Briol, Esquire of Briol & Associates, located in Minneapolis, Minnesota and Terrence J. Fleming of Linquist & Vennum, P.L.L.P. of Minneapolis, Minnesota.

Gruntal & Co., Inc. was represented by Lionel Hest, Esquire of Fulbright & Jaworski, L.L.P., located in New York, New York.

Timothy L. Johnson was not represented by counsel.

CASE INFORMATION

James Sexton and Maureen Sexton's Statement of Claim was filed on or about March 13, 1996.

James Sexton and Maureen Sexton's Submission Agreement was signed on March 13, 1996.

Gruntal & Co., Inc.'s Statement of Answer was filed on or about May 9, 1996.

Gruntal & Co., Inc.'s Submission Agreement was signed on April 4, 1996 by John Girrito, Executive Vice President of Gruntal & Co., Inc.

Timothy L. Johnson's Statement of Answer was filed on or about May 10, 1996.

Timothy L. Johnson's Submission Agreement was signed on May 10, 1996.

HEARING INFORMATION

The hearing was held on: July 9, 1997 for two (2) session; July 10, 1997 for two (2) sessions; July 11, 1997 for two (2) sessions.

The hearing was held in Dallas, Texas.

CASE SUMMARY

Claimants, James Sexton ("Mr. Sexton") and Maureen Sexton (hereinafter collectively referred to as "Claimants"), brought this action to recover losses in their portfolio allegedly resulting from the high pressure tactics and unsuitable trading, and by misrepresentations and omissions of material facts by Timothy L. Johnson ("Mr. Johnson"), a registered representative of Gruntal & Co., Inc. ("Gruntal") at all times relevant herein.

According to Claimants, Mr. Johnson and Gruntal relentlessly pursued a course of action that resulted in Mr. Sexton investing virtually all of his savings into two highly speculative stocks, both of which were totally unsuitable to Mr. Sexton given that he is an unsophisticated and inexperienced investor. Claimants stated that Mr. Johnson advised Mr. Sexton to open a margin account without ever explaining the disadvantages or risks of margin, or the mechanics or strategies of margin trading. Claimants reported that, from March 1993 to December 1993, Mr. Johnson and Gruntal made the following transactions in their account:

<u>Date</u>	<u>Investment</u>	<u>Activity</u>	<u>Quantit</u> <u>y</u>	<u>Price</u>	<u>Total</u>
2/11/9 3	Clothestime, Inc.	Buy	2,000	14 1/8	\$28,250.00
2/28/9 3	Clothestime, Inc.	Buy	2,000	12	24,000.00
3/18/9 3	Clothestime, Inc.	Buy	1,000	13 3/8	13,375.00
3/18/9 3	Clothestime, Inc.	Buy	1,000	13 3/8	13,375.00
3/25/9 3	Clothestime, Inc.	Sell	6,000	13 5/8	81,750.00
3/29/9 3	Clothestime, Inc.	Buy	5,000	13 1/8	65,625.00
4/2/93	Clothestime, Inc.	Sell	5,000	13 5/16	68,562.50

4/7/93	Clothestime, Inc.	Buy	5,000	13 1/8	65,825.00
5/17/93	Clothestime, Inc.	Buy	5,000	12 1/2	62,500.00
5/28/93	Clothestime, Inc.	Buy	5,000	11 11/16	58,437.50
12/2/93	Clothestime, Inc.	Buy	7,000	8 1/4	57,753.75
3/25/93	Cambridge Biotech Corp.	Buy	5,000	6 1/8	30,625.00
4/6/93	Cambridge Biotech Corp.	Buy	4,000	6 1/8	24,500.00
4/28/93	Cambridge Biotech Corp.	Buy	6,000	5 7/16	32,625.00
12/7/93	Cambridge Biotech Corp.	Sell	2,000	2 7/8	5,750.00
12/9/93	Cambridge Biotech Corp.	Buy	2,000	3 1/8	6,250.00

Claimants asserted that Mr. Johnson recommended and directed Mr. Sexton to maintain these highly concentrated positions, for which Gruntal was a market maker, and never advised Mr. Sexton to diversify his portfolio. Claimants averred that Mr. Johnson and Gruntal made these investments on Mr. Sexton's behalf without regard to market conditions, mounting bad news to which they had access concerning both companies or the price of the stock. Claimants further asserted that despite their knowledge of and access to a considerable body of material information concerning the risks of Clothestime, Inc. and Cambridge Biotech Corp., Mr. Johnson and Gruntal, through their representations and their silence, concealed that information from Mr. Sexton. Claimants stated that the Clothestime, Inc. stock is virtually worthless and that the Cambridge Biotech Corp. stock was sold for about \$53,000.

Claimants made the following legal claims: (1) violations of § 10 of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder; (2) violations of The Securities Act, Tex. Civ. Code § 581-1 *et seq.* and regulations promulgated thereunder; (3) violations of the Texas Deceptive Trade Practices Act, Tex. Bus. & Com. Code Ann. § 17.01 *et seq.*; (4) breach of express and implied contracts; (5) fraud, negligent misrepresentation, breach of fiduciary duty, and negligence; (6) liability of Gruntal for the activities of its agent and employee, Mr. Johnson,

pursuant to control person liability under § 20(a) of the Securities Act of 1934, and § 581-33(F) of Texas Securities Act, and common law principles of agent and respondeat superior; (7) violation of § 27, Art. III of the NASD Rules of Fair Practice; and (8) because Mr. Johnson and Gruntal acted intentionally, willfully, wantonly, wrongfully, unlawfully, maliciously with willful indifference and reckless disregard of Claimants' rights, Claimants are entitled to treble damages under Tex. Bus. & Com. Code § 17.05(b)(1) and/or punitive damages under federal common law and state law.

Gruntal denied the allegations set forth in the Statement of Claim as they relate to any wrongdoing on its part. Gruntal stated that each of Mr. Johnson's purchase recommendations pertaining to the two stocks at issue were consistent with the recommendations issued by Gruntal's Research Department. Gruntal further contended that, in light of Mr. Sexton's investment objectives, his investment experience, and his net worth, Mr. Johnson's recommendations to buy these two growth stocks were eminently suitable at the time they were made, and the amount of money invested by Mr. Sexton was not at all inappropriate. Gruntal made the following affirmative defenses: (1) to the extent the Statement of Claim purports to base liability on § 10 of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, such claims should be dismissed pursuant to the statute of limitations; (2) all other claims should be dismissed pursuant to the applicable statutes of limitations under state law; (3) the Statement of Claim should be dismissed in its entirety pursuant to the doctrine of laches, that is, because Claimants failed to assert their claims, take action, or commence this suit within a reasonable period of time; (4) the Statement of Claim should be dismissed in its entirety due to Claimants' failure to take reasonable steps to mitigate their damages; (5) the Statement of Claim should be dismissed to the extent it seeks recovery pursuant to the NASD Rules of Fair Procedure inasmuch as there is no private right of action under NASD rules; and (6) the Statement of Claim should be dismissed for failure to state a claim upon which relief can be granted to the extent it seeks recovery for breach of contract, inasmuch as no contract was identified nor was any contractual provision that was purportedly breached identified.

Mr. Johnson denied the allegations set forth in the Statement of Claim as they relate to any wrongdoing on his part. Mr. Johnson adopted the factual and legal arguments set forth in Gruntal's Statement of Answer, as well as each and every affirmative defense set forth therein. According to Mr. Johnson, he and Mr. Sexton spoke frequently, during the time that Mr. Johnson serviced Mr. Sexton's account, and always explained the basis of his recommendations and ensured that he understood the risks and potential rewards of each investment and of investing on margin. Mr. Johnson further contended that Mr. Sexton never suggested in any way that he was disappointed with how the account was being handled.

RELIEF REQUESTED

James Sexton and Maureen Sexton requested an award for: actual damages in the amount of \$280,000; attorneys fees and costs; and punitive damages in an amount equal to three times

Claimants' actual damages.

Gruntal & Co., Inc. requested that the Statement of Claim be dismissed in its entirety and that it be awarded its costs and disbursements of this action, including attorneys' fees.

Timothy L. Johnson requested that the Statement of Claim be dismissed in its entirety.

OTHER ISSUES CONSIDERED AND 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 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 the Statement of Claim is hereby denied in its entirety with prejudice;
2. 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 \$1,000 per hearing session and \$300 for each pre-hearing conference, if any. There were six (6) hearing sessions x \$1,000 = \$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 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 NASD Regulation, Inc. Office of Dispute Resolution by James Sexton and Maureen Sexton.

Pursuant to § 10333 of the Code, the NASD Regulation, Inc. Office of Dispute Resolution shall retain the non-refundable member surcharge in the amount of \$500 previously deposited with the NASD Regulation, Inc. Office of Dispute Resolution by Gruntal & Co., Inc.

The NASD Regulation, Inc. Office of Dispute Resolution shall **retain** postponement fees in the amount of \$2,000 previously deposited with the NASD Regulation, Inc. Office of Dispute Resolution by Gruntal & Co., Inc.

The remaining forum fees in the amount of \$5,000 shall be born equally by the Respondents Gruntal & Co., Inc. and Timothy L. Johnson and the Claimants James Sexton and Maureen Sexton. Therefore Claimants James Sexton and Maureen Sexton shall pay \$2,000 (\$6,000 for six hearing sessions divided by two less the \$1,000 hearing deposit previously paid by Claimants James Sexton and Maureen Sexton) and Respondent Gruntal & Co., Inc. and Timothy L. Johnson shall pay \$3,000 (\$6,000 for six hearing sessions divided by two.)

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

Concurring Arbitrators' Signatures

/s/ Charles P. Aberg
Charles P. Aberg, Esquire
Chairperson
Public Arbitrator

July 18, 1997
Dated:

/s/ Melinda G. Jayson
Melinda G. Jayson, P.C.
Panelist
Public Arbitrator

July 28, 1997
Dated:

/s/ Bruce W. Collins
Bruce W. Collins
Panelist
Industry Arbitrator

July 18, 1997
Dates:

For NASD use only:
Date Award was served on the parties: July 31, 1997