

AWARD

NASD Regulation, Inc.

In the Matter of the Arbitration Between

Name of Claimant

S. Robert Kovac

and

96-02454

Name of Respondents

A. G. Edwards & Sons, Inc.,
Pauli & Company, and
Schneider Securities, Inc.

and

Third Party Claimants

A. G. Edwards & Sons, Inc.,
Pauli & Company, and
Schneider Securities, Inc.

and

Third Party Respondent

Stephen Kovac

REPRESENTATION OF PARTIES

S. Robert Kovac ("Claimant") was represented by Joseph J. Dehner, Esq., of Frost & Jacobs, Cincinnati, Ohio.

A. G. Edwards & Sons, Inc. ("AGE") was represented by Hope Johnson, Esq. And Jeff Jameson, Esq., of A. G. Edwards & Sons, Inc., St. Louis, Missouri.

Schneider Securities, Inc. ("SSI") was represented by Margaret Pepper, Esq., and Gary Cerani, Esq., of Davis & Cerani, P.C., Denver, Colorado.

Pauli & Company ("PC") was represented by Charles A. Seigel, III, Esq., of Seigel & Wolff, St. Louis, Missouri. PC settled with Claimant between the 1997 and 1999 hearing settings. PC did not participate in the 1999 hearing sessions.

Stephen Kovac ("Kovac") was not represented, and failed to appear at the hearings.

CASE INFORMATION

Claimant filed the Statement of Claim on or about May 15, 1996. Claimant signed the Submission Agreement on May 16, 1996. Claimant filed a notice of voluntary dismissal with prejudice of claim against PCIA, Inc., fka Pauli & Company, Inc. on or about January 19, 1998.

Respondent AGE filed a Statement of Answer on or about July 30, 1996. Respondent AGE filed a Third Party Claim against Kovac on or about July 30, 1996. AGE signed the Submission Agreement on July 11, 1996.

Respondent PC filed a Statement of Answer on or about August 12, 1996. Respondent PC filed a Third Party Claim against Kovac on or about August 12, 1996. PC signed the Submission Agreement on August 1, 1996.

Respondent SSI filed a Statement of Answer on or about August 15, 1996. SSI signed the Submission Agreement on August 15, 1996.

NASD Regulation, Inc. does not have a record of Kovac's Answer or Submission Agreement on file.

HEARING INFORMATION

Pre-hearing conferences were held on April 29, 1997 for one (1) session, May 15, 1998 for one (1) session, July 17, 1998 for one (1) session, and August 5, 1998 for one (1) session. All pre-hearing sessions were held with the majority of the panel in attendance.

The Arbitration Panel held hearings on December 2, 1997 for two (2) sessions, December 3, 1997, for two (2) sessions, December 4, 1997, for two (2) sessions, January 6, 1999, for two (2) sessions, January 7, 1999, for three (3) sessions, and January 8, 1999, for two (2) sessions in St. Louis, Missouri for a total of 13 sessions.

CASE SUMMARY

Claimant alleged that AGE, PC, and SSI (jointly referred to as "Respondents"): Approved and allowed Kovac to make unsuitable transactions in his IRA accounts; failed to supervise the activity of Kovac while he was a registered representative at each respective firm; breached their fiduciary relationship with Claimant; allowed unauthorized withdrawal of assets from Claimant's accounts based on forged signatures; at no time did Kovac have power of attorney for Claimant, nor was Kovac authorized to make withdrawals from Claimant's IRA accounts; approved and allowed Claimant's IRA accounts to be churned; approved and allowed unauthorized transactions in Claimant's IRA accounts; and failed to communicate with Claimant about the impropriety of what had occurred in Claimant's IRA account. The claim arose out of

withdrawals of assets and transactions in securities more fully presented during the hearing of this case.

Except as expressly admitted in its Answer, AGE denied all allegations set forth in the Statement of Claim. AGE also asserted the following additional defenses: Claimant is barred from recovering from AGE under his agreements with AGE and under the Uniform Commercial Code as enacted in the State of Missouri; Claimant's failure to timely object to the transactions at issue, is deemed to be a ratification, waiver and estoppel of Claimant's right to recovery; all of the transactions in Claimant's AGE account were executed with the authorization of Claimant; Claimant had regular contact with his investment broker concerning the activity in his account, the securities therein, and the prices of those securities and the undertaking of orders; Claimant's failure to mitigate his damages bars him from recovery; Claimant is barred by his own contributory negligence and/or comparative fault from recovering any damages; Claimant's knowing and voluntary assumption of risk was the sole and proximate cause of his alleged damages; the damages allegedly suffered by Claimant were caused, if at all, by unforeseeable market factors and conditions affecting the value of securities in Claimant's account for which AGE is not liable or responsible; Claimant's claims are barred by applicable statutes of limitations; Claimant's requests for attorney's fees and interest fail to state a claim upon which relief may be granted, as there is no legal basis for recovery of same; and this cause of action fails to state a claim for which relief may be granted. AGE also asserted a Third Party Claim against Kovac.

AGE stated that it has been named as a Respondent in this arbitration which arises out of transactions in an account maintained by Kovac's father, the Claimant, during the time Kovac was the investment broker for such account. AGE asserted hypothetically, or in the alternative, in the event that the panel determines that AGE is liable to Claimant for any sum, then AGE is entitled to full contribution and indemnification from Kovac, as all allegations in the Statement of Claim arise out of Kovac's conduct during the time he was the investment broker for his father's account. AGE also asserted that, in connection with his employment at AGE, Kovac executed an agreement. Under the terms of the agreement, Kovac is liable to AGE for all damages, costs or expenses incurred in connection with this arbitration. AGE stated that it had performed all conditions precedent to the agreement.

Unless specifically admitted in its Answer, PC denied the allegations made in the Statement of Claim. PC asserted the following additional defenses: Claimant's failure to timely object to any of the transactions of which he complains constitutes a ratification of these transactions and a waiver or estoppel of Claimant's right to any recovery sought in the Statement of Claim; and Claimant's claims are barred by all applicable statutes of limitations. PC asserted a Third Party Claim against Kovac.

PC stated that it has been named in this arbitration, which arises out of transactions in accounts maintained by Kovac's father, during the time in which Kovac was the registered

representative for Claimant. PC asserted that in the event that it is entitled to indemnification and contribution from Kovac because all allegations of misfeasance in the Statement of Claim arise out of Kovac's conduct during the time in which he was the registered representative for Claimant's accounts at PC.

Unless otherwise admitted in its Answer, SSI each and every allegation contained in the Statement of Claim and specifically denied that it engaged, or allowed any of its' agents to engage, in any conduct which violates any laws or statutes. In addition, SSI asserted the following affirmative defenses: Claimant was an extremely knowledgeable and sophisticated investor who had represented to SSI that he had significant net income, net worth, and liquid net worth, and desired "Growth" and "Speculation" as his stated investment objectives; Claimant was at all times made aware of each and every transaction and withdrawal of funds from his account maintained by SSI; Claimant was provided with confirmations of all transactions, monthly statements of activity which clearly revealed all purchases, sells, withdrawals and interest which occurred in his account, and also received his year end tax information detailing each and every proceeds transaction, interest charged and received, and distributions from the IRA account, and never objected to the activity which was taking place; Claimant maintained control over his securities account at SSI; Claimant failed to provide any notification to SSI as required in account agreements signed by Claimant and any losses regarding the transactions are therefore borne by Claimant; Claimant's failure to timely object to the transactions is deemed to be a ratification, waiver, and estoppel of Claimant's right to recovery; Claimant's claims for damages are grossly inaccurate, and are substantially less than the amount claimed, and are the direct result of Claimant's own actions; Claimant failed to mitigate his damages; SSI, at all times relevant hereto, had in place a supervisory system which was reasonably designed to supervise the activities of its agents, and implemented such a system in a manner which would reasonably prevent and detect unlawful activities of its' agents; and contributory negligence, assumption of risk, and lack of reliance upon any action or inaction of SSI and that some or all of the claims of Claimant are barred by the applicable statutes of limitation.

RELIEF REQUESTED

Claimant requested an award of the following: An award against AGE, PC, and SSI restoring to his accounts all amounts that were taken without his authorization, with interest from the date of each withdrawal until repaid; an award against AGE, PC, and SSI for the losses suffered in his accounts, plus an amount in damages representing what his accounts would have been worth at the time of the hearing had they been invested reasonably; an award against AGE, PC, and SSI for all costs, penalties, interest, accountant and attorney fees and other expenses associated with analyzing the correct approach to dealing with the Internal Revenue Service and resolving all issues with it; disgorgement of income earned by each firm from Claimant's accounts; an award of attorneys' fees, expert witness fees, forum fees, and other costs associated with this proceeding; an award of punitive damages in an amount deemed just and equitable by the panel; and such other relief as the panel deems just and equitable.

AGE denied the claims asserted against it.

In its Third Party Claim, AGE requested in Count I, that in the event that AGE is liable to Claimant for any damages, then AGE seeks an award against Kovac for the full amount of such damages, all costs and expenses, including attorneys' fees, incurred by AGE in connection with this arbitration, and for such other and further relief as the arbitration panel deems just and proper. In Count II of its Third Party Claim, AGE requested an award for all damages, costs and/or expenses incurred by AGE in connection with this arbitration, and for such other and further relief as the arbitration panel deems just and proper.

PC requested that the panel dismiss this case and award it its costs and expenses, including attorneys' fees, incurred in connection with this case.

PC, in its Third Party Claim, requested an award against Kovac for the full amount of damages awarded to the Claimant, plus all costs and expenses, including attorneys' fees, incurred by PC in connection with this arbitration.

SSI denied the claims asserted against it, and asserted a Third Party Claim against Kovac for indemnification.

OTHER ISSUES CONSIDERED & DECIDED

Upon review of the file and the representations made by/on behalf of the Claimant, the undersigned arbitrators have determined that Third Party Respondent Kovac has been properly served with the Third Party Claims pursuant to Rules 10302 and 10314 of the NASD Code of Arbitration Procedure (the "Code"). The undersigned arbitrators have also determined that Third Party Respondent Kovac had received due notice of the hearing as required under Rule 10315 of the Code and that arbitration of the matter would proceed pursuant to Rule 10318 of the Code.

Both AGE and SSI moved for a dismissal at the close of Claimant's case. After hearing argument from the parties, and deliberation, the arbitrators denied the motions.

AGE moved for a partial dismissal on statute of limitations grounds. After hearing argument from the parties, and deliberation, the motion was denied.

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 NASD Regulation, Inc. Office of Dispute Resolution.

AWARD

After considering the pleadings, the testimony, and the evidence presented at the, the undersigned arbitrators have decided in full and final resolution of the issues submitted for determination as follows:

Respondent AGE is liable for and shall pay to the Claimant the sum of \$40,000 for compensatory damages, plus interest at the rate of nine percent (9%) per annum until paid. Interest begins to accrue 30 days after the receipt of the Award by AGE. Further, Respondent SSI is liable for and shall pay to the Claimant the sum of \$20,000 for compensatory damages, plus interest at the rate of nine percent (9%) per annum until paid. Interest begins to accrue 30 days after the receipt of the Award by SSI.

Third Party Respondent Kovac is liable for and shall pay to Third Party Claimant, AGE, the sum of \$40,000 for its claims made herein, plus interest at the rate of nine percent (9%) per annum until paid. Interest begins to accrue 30 days after the receipt of the Award by Kovac.

Third Party Respondent Kovac is liable for and shall pay to Third Party Claimant, SSI, the sum of \$20,000 for its claims made herein, plus interest at the rate of nine percent (9%) per annum until paid. Interest begins to accrue 30 days after the receipt of the Award by Kovac.

Any requests for relief/claims for damages not specifically set forth herein are, and each of them, denied with prejudice.

OTHER COSTS

Forum fees shall be assessed as follows: 50% to Claimant; 40% to AGE; and 10% to SSI.

Third Party Respondent Kovac is liable for, and shall pay to AGE, the sum of \$4,080 as an award of costs.

Third Party Respondent Kovac is liable for, and shall pay to SSI, the sum of \$1,020 as an award of costs.

FORUM FEES

Forum fees are calculated at the rate of \$600 per hearing session and \$300 for each prehearing conference with a single arbitrator, and \$600 for a pre-hearing conference with more than a single arbitrator in attendance. There were four pre-hearing sessions with two (2)

arbitrators @ \$600 per session and 13 hearing sessions @ \$600 = \$10,200 in forum fees. Pursuant to Rule 10332(b) of the NASD Regulation 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 Rule 10332(c) of the NASD Code of Arbitration Procedure, NASD Regulation, Inc. 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 \$600 previously deposited with NASD Regulation, Inc. by the Claimant.

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Pursuant to Rule 10332(c) of the NASD Code of Arbitration Procedure, PC is liable for, and shall pay to NASD Regulation, Inc. the non-refundable Third Party filing fee in the amount of \$500.

Pursuant to Rule 10332(c) of the NASD Code of Arbitration Procedure, NASD Regulation, Inc. 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 \$600 previously deposited with NASD Regulation, Inc. Office of Dispute Resolution by the Claimant.

Additional forum fees in the amount of \$4,500 (\$5,100 - \$600) are assessed by the arbitrators against the Claimant.

Additional forum fees in the amount of \$3,480 (\$4,080 - \$600) are assessed by the arbitrators against AGE.

Additional forum fees in the amount of \$1,020 are assessed by the arbitrators against SSI.

OTHER FEES

Pursuant to Rule 10333 of the Code, Respondent AGE has paid to NASD Regulation, Inc. the \$350.00 member surcharge previously invoiced.

Pursuant to Rule 10333 of the Code, Respondent SSI shall pay to NASD Regulation, Inc. the \$350.00 past due member surcharge previously invoiced.

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NASD REGULATION

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NASD Regulation, Inc. Office of Dispute Resolution
Arbitration No. 96-02454
Referral Page 2 of 2

all of which the funds went into Kovac's own account or some other account controlled by him:

- Kovac forged withdrawal signatures from IRA accounts;
- Kovac signed his own name on withdrawal documents on others' accounts;
- Kovac deceived others into signing withdrawal documents;
- Kovac forged documents to withdraw moneys from an annuity and then forged his father's name on the annuity check;
- Kovac withdrew more than authorized amounts from an account and then embezzled the remainder; and
- Kovac opened an account for his father with a forged signature, opened a joint bank account in Kovac's and his father's name and then funneled moneys from the brokerage account into the joint bank where he used his own signature to withdraw moneys.

On April 1, 1996, Kovac resigned from Schneider Securities, Inc. from its address at 2525 South Shore Blvd., League City, TX 77573 and probably has not been employed in the securities industry since. The panel does not know of Kovac's present whereabouts. His last known home address is 1803 Enterprise, League City, TX 77573. It is the panel's recommendation that the NASD take all steps necessary to bar Kovac from re-entering the securities industry.

Concurring Arbitrators' Signatures

Dated:

Keith E. Mattern
Public Arbitrator, Presiding Chair

Lawrence M. Raskin
Public Arbitrator



Stanley F. Van Sant
Industry Arbitrator
Arbitrator

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NASD REGULATION

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NASD Regulation, Inc. Office of Dispute Resolution
Arbitration No. 96-02454
Referral Page 2 of 2

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Arbitration No. 96-02454
Referral Page 2 of 2

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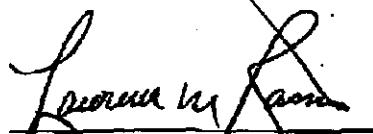
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