

N.A.S.D. AWARD

NATIONAL ASSOCIATION OF SECURITIES DEALERS

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In the Matter of the Arbitration Between

Name of Claimants

Bruce Babula and Sandra L. Babula

96-03302

Name of Respondents

Janney Montgomery Scott Inc.  
William J. Pearce

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CASE SUMMARY

In a case filed with the National Association of Securities Dealers Regulation, Inc. on August 1, 1996, claimants Bruce and Sandra Babula ("claimants"), who appeared Pro Se, alleged that respondents Janney Montgomery Scott, Inc. ("JMS") and William Pearce ("Pearce") fraudulently sold them products. Claimants further alleged that in July 1993, Pearce was well aware of their financial objectives and risk tolerance. Claimants also alleged that Pearce called with unprecedented urgency and strongly advised Mr. Babula to sell Eaton Vance National Municipals Fund ("EVNMF"). Claimants asserted that they sold the stock and purchased mortgage backed securities based on Pearce's recommendation and assurance that they were safe and would timely return the principal. Claimants further asserted that they noticed the principal return rate was at marked variance with what they had been promised. Claimants also asserted that in January 1996, after fruitless telephone conversations with Pearce, he admitted that JMS monthly statements overvalued the true market value of the securities. Claimants contended that in a letter they received on March 12, 1996 from JMS's Compliance Officer Edward Moody ("Moody") stated that at the time these securities were stated to have a three to five year average life and that two of the three were immediate pay bonds. Claimants further contended that after consulting with another investment firm they found out that the bonds were high-risk tranches and were projected as eight to twelve year bonds as of 1996. Claimant also contended that in another letter from JMS's Compliance Director Frank Salerna ("Salerna"), JMS indicated that they would remain unmoved by the facts and that they were not inclined to voluntarily correct their mistake.

Respondents Janney Montgomery Scott, Inc. and William J. Pearce through their representative and counsel Paula D. Shaffner of the law firm Saul, Ewing, Remick & Saul located in Philadelphia, Pennsylvania, maintained that the claim relates to Collateralized Mortgage Obligations ("CMO's"), which claimant Bruce Babula purchased for his own account and for four custodial accounts. Respondents further maintained that because of the 20-25 year maturities on the EVNMF and Mr. Babula's concern about the effect of interest rates on those portions, Pearce discussed liquidating EVNMF. Respondents also maintained that the decision to sell EVNMF evolved slowly and Pearce never made any such urgent telephone call to Mr. Babula. Respondents contended that Mr. Babula was instrumental in all decisions regarding the sale and purchase of securities. Respondents further contended that the funds from the sale were put into a money market account.

Respondents also contended that at the time the CMO's were recommended they were stated to have a three to five year life average, two of which were immediate paying bonds. Respondents maintained that Pearce thoroughly explained the CMOs and the risks and rewards of CMOs to Mr. Babula. Respondents further maintained that Pearce specifically discussed the pricing assumptions, the interest rate and the effect of prepayment of the mortgage loan in detail. Respondents also maintained that since some of the CMOs were paying both principal and interest on a monthly basis and given the information available about the average life, there is no doubt that they were appropriate investments for claimants.

Respondents contended that the investments paid interest on a monthly basis and that two of the CMOs paid principal for almost two years. Respondents further contended that the CMO's stopped paying principal and the average life of the bonds were extended due to a decrease in the Public Securities Association standard prepayment model ("PSA"), which changed the maturities on the CMOs. Respondents also contended that these risks were fully disclosed to claimants.

#### **RELIEF REQUESTED**

Claimants Bruce and Sandra Babula requested: (1) that JMS purchase without fee enough bonds at par value to reduce the factor outstanding to .67 on December 31, 1996; (2) that JMS purchase enough bonds at par to reduce the factor outstanding to .33 on December 31, 1997; (3) that JMS purchase all outstanding bonds at par on December 31, 1998; and (4) filing costs plus \$1,500.00 as compensation for their expenditure of time and lost financial opportunity.

Respondents Janney Montgomery Scott, Inc. and William Pearce requested that the claims of claimant be dismissed in their entirety.

#### **AWARD**

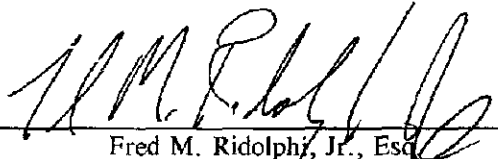
Pursuant to Section 10302 of the Code of Arbitration Procedure, a single Public Arbitrator Fred M. Ridolphi, Jr. was selected to review the matter in controversy between the parties set forth in submissions to Arbitration signed by claimants Bruce and Sandra Babula on July 30, 1996, by respondent William Pearce on August 8, 1996 and by respondent Janney Montgomery Scott, Inc. on August 8, 1996.

And, the Arbitrator, having considered the proof of the parties, has decided and determined in full and final resolution of the issues submitted for determination as follows:

1. The claims of claimants Bruce and Sandra Babula against respondents Janney Montgomery Scott, Inc. and William Pearce are dismissed in their entirety.
2. All other relief requests are denied.
3. The \$125.00 filing fee previously deposited with the National Association of Securities Dealers Regulation, Inc. by claimants Bruce and Sandra Babula shall be retained by the NASD Regulation, Inc.

**AFFIRMATION**

I, **Fred M. Ridolphi, Jr., Esq.**, do hereby affirm upon my oath as arbitrator that I am the individual described herein and who executed this instrument, which is my oath and award.

  
Fred M. Ridolphi, Jr., Esq.

Date of Decision: February 20, 1997