

N.A.S.D. REGULATION AWARD

NATIONAL ASSOCIATION OF SECURITIES DEALERS

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In the Matter of the Arbitration Between

Name of Claimants

Roman and Eleanor Mager

96-04254

Name of Respondents

Smith Barney Harris Upham & Co., Inc.  
Barry Whalen

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**CASE SUMMARY**

In a case filed with National Association of Securities Dealers Regulation, Inc. on September 24, 1996, claimants Roman and Eleanor Mager ("claimants") through their representative and counsel Mitchell Perlstein, Esq., of the law firm Investors Law Center, P.A. located in Boca Raton, Florida, alleged that respondents Smith Barney Harris Upham & Co., Inc. ("Smith Barney") and Barry Whalen ("Whalen") induced them to liquidate their existing annuity policy for the express purpose of purchasing inferior policies based upon material misrepresentations and omissions. Claimants further alleged that they were solicited to attend a seminar to learn more about investments and estate planning sponsored by respondents. Claimants also alleged that after the seminar, Whalen scheduled a meeting with them on or about August 17, 1995. Claimants asserted that at this meeting they disclosed their current portfolio, which consisted primarily of an annuity contract with Nationwide-Best of America ("existing policy") and a small conservative account with Fidelity investments. Claimants further asserted that Whalen convinced them that they could be getting more income, under another annuity plan, with no additional risk.

Claimants also asserted that based on respondents recommendation and reliance, they sold their positions in the Fidelity Short Term Bond Portfolio and the Fidelity Ginnie Mae Portfolio. Claimants contended that the Portfolio's were yielding in excess of 6%, but respondents had them place these funds in a money market account, which was paying only 5.28%. Claimants further contended that Whalen also recommended two annuity contracts, AIM/Cigna Heritage Variable Annuity ("AIM") and Smith Barney Vintage Variable Annuity ("Vintage"). Claimants also contended that AIM and Vintage were discussed together and were referred to as the replacement policies. Claimants alleged that they were told that the replacement policies were much better than the existing policy currently held at Nationwide. Claimants further alleged that Whalen promised that they would earn a higher monthly income and still allow their principal to grow. Claimants also alleged that based upon respondents recommendation and representations, they agreed to purchase the replacement policies.

Claimants asserted that respondents willfully concealed the fact that the recommended purchases of AIM and Vintage were replacing an existing annuity policy. Claimants further asserted that respondents failed to accurately complete the applications and did not disclose claimant's existing policy. Claimants also asserted that the Vintage application form has a section which required a response to whether the contract applied for will replace any existing annuity contract or life insurance policy. Claimants contended that

this was not a mere oversight, but rather an attempt by Whalen to deliberately conceal the existence of claimant's Nationwide policy, in an effort to avoid disclosure requirements. Claimants further contended that Whalen falsely certified the AIM application.

Claimants also contended that Whalen failed to complete and submit the form entitled "Absolute Assignment to Effect a 1035 Exchange (the "form"). Claimants alleged that this form was to effect a tax free exchange of policies subject to the Internal Revenue Tax Code provisions in Section 1035. Claimants further alleged that respondents negligence and deliberate omission of this form from the application package resulted in significant tax repercussions to them. Claimants asserted that Whalen did not provide them with a comparison of the policies, which is mandated by Florida Statute sec. 626. Claimants further asserted that respondents failed to advise them of the sales charge upon the surrender of the Existing policy. Claimants also asserted that respondents misrepresented the earnings and returns they could expect from the replacement policy. Claimants contended that respondents misrepresented the withdrawals and cashflow for the replacement policies. Claimants further contended that Smith Barney failed to reasonable supervise Whalen in connection with this dealings with claimant, thereby breaching their contractual and legal duties to them.

Respondents Smith Barney and Whalen (collectively referred to as "respondents") through their representative and in-house counsel Ellen Slipp, Esq., maintained that claimants omitted two essential facts which directly caused them damage. Respondents further maintained that claimants failed to disclose that they intended to use the proceeds of the sale of the Nationwide to purchase two annuities and that they swapped the investments for others without Whalen's advice. Respondents further maintained that when claimants and Whalen meet a week after the seminar, they discussed how claimants were happy with the Nationwide annuity. Respondents contended that they also discussed a variety of things, including the benefits of an annuity, and the claimant's overall investment objectives and goals. Respondents further contended that Whalen reviewed some of the aspects of Vintage with claimants, and gave them a prospectus and a brochure. Respondents also contended that a few days later claimants called Whalen and requested another meeting. Respondents maintained that during this meeting, claimants indicated that they were extremely interested in Vintage and even highlighted portions of the prospectus.

Respondents further maintained that claimants asked Whalen about the possibility of investing in two annuities through Smith Barney. Respondents also maintained that in reviewing the material given to claimants regarding Vintage, claimants noted that one of the stock portfolios, which comprised this annuity was AIM. Respondents contended that of their own volition, claimants expressed an interest in AIM and Whalen discussed this annuity with them. Respondents further contended that a few days later, claimants requested another meeting with Whalen. Respondents also contended that at this meeting, Whalen explained that most of his clients utilize the AIM and Vintage annuities as growth vehicles, whereby their principal grows on a long term, tax-deferred basis. Respondents maintained that claimants understood the benefits of this approach, but nevertheless insisted that they needed income.

Respondents further maintained that claimants reminded Whalen that, according to the prospectuses, each of the annuities allowed for systematic withdrawals of 15% per year without penalty, and informed Whalen that this was the amount which they wished to withdraw. Respondents also maintained that Whalen agreed with the claimants that this was a feature, however he disagreed with the advisability of withdrawing that much money from their annuities. Respondents contended that in order to support withdrawals of 15%, the account would have to outperform 15% without invading principal. Respondents further contended that Whalen was not comfortable with that amount and suggested to claimants that they act more conservatively by withdrawing 5% per - 7% per year. Respondents also contended that claimants were steadfast in their intent to withdraw that amount from their account, and

Whalen proposed that they wait and see how the money managers were performing. Respondents maintained that despite Whalen's continued advice to the contrary, claimants insisted on a withdrawal of 15%.

Respondents further maintained that on September 19, 1995, claimants purchased \$30,000.00 of AIM and \$40,000.00 of Vintage. Respondents also maintained that Whalen did not discover that the claimants had sold their Nationwide annuity until October 16, 1995 or thereabouts. Respondents contended that Whalen received a letter from Nationwide, that the annuity could not be transferred, as it has already been surrendered. Respondents further contended that Whalen then spoke to claimants and told them how disappointed he was that he was not able to represent them with Nationwide or include Nationwide in their Smith Barney account. Respondents also contended that claimants informed Whalen that they decided on their own to fund their purchases with the proceeds from the Nationwide annuity.

Respondents maintained the claimants never informed Whalen that these policies were to serve as replacement policies for the Nationwide annuity. Respondents further maintained Whalen did not indicated replacement policies on the AIM and Vintage applications since, he did not know that these new policies were designed as replacement policies. Respondents also maintained that when Whalen asked the claimants why they had never informed him about the transfer, they replied that they wanted the check to come directly to them, so that they could decide what they wanted to do with the money. Respondents contended that Whalen never advised claimants of the sales charge associated with the surrender of the Nationwide annuity, because claimants purposely chose not to tell Whalen of their intent to surrender the Nationwide annuity.

#### **RELIEF REQUESTED**

Claimants Roman and Eleanor Mager requested (1) \$10,000 in damages, representing their surrender loss, tax loss and policy loss; (2) 12% per annum in accordance with Section 517 of the Florida Statutes; (3) a refund of all commissions; (4) costs and fees of this action; (5) reasonable attorneys' fees; and (6) such other relief as the arbitrator finds appropriate.

Respondents Smith Barney and Whalen requested that the claims of claimant be dismissed in their entirety.

#### **AWARD**

Pursuant to Rule 10302 of the Code of Arbitration Procedure, a single Public Arbitrator, Arie Leo Douer, was selected to review the matter in controversy between the parties set forth in Submissions to Arbitration signed by claimants Roman and Eleanor Mager on June 7, 1996 and by respondents Smith Barney on December 17, 1996 and by Whalen on December 12, 1996 as required by Rules 10301 and 10302 of the Code of Arbitration Procedure.

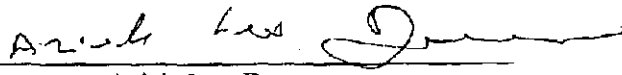
And, the Arbitrator, having considered the proof of the parties, has decided and determined in full and final resolution of the issues submitted for determination as follows:

1. Respondents Smith Barney and Whalen be and hereby are jointly and severally liable and shall pay claimant the sum of \$10,000.00.

2. All other relief request are denied.
3. The \$150.00 filing fee previously deposited by claimant shall be retained by NASD Regulation, Inc. Respondents Smith Barney and Whalen be and hereby are jointly and severally liable and shall pay claimant the sum of \$150.00 as reimbursement of the filing fee.

**AFFIRMATION**

I, **Arieh Leo Douer**, do hereby affirm upon my oath as arbitrator that I am the individual described herein who executed this instrument, which is my oath and award.

  
Arieh Leo Douer

Date of Decision: April 30, 1997