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Panel Finds Brokerage Defrauded Ga. Retiree

Augusta area man awarded $924,626 by NYSE arbiters

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In the first of at least 75 such cases, a panel of New York Stock Exchange arbitrators has found brokerage A.G. Edwards & Sons and two of its Augusta employees liable for fraud and breaches of fiduciary duty in managing a Georgia retiree's account.

The panel awarded Wendell A. Gresham of Harlem, Ga., $924,626, a figure that includes $400,000 in punitive damages—a rarity in such arbitrations, according to Gresham's attorneys—and $239,718 in attorney fees. The decision came July 8 after eight days of hearings.

Gresham's attorneys Edward J. Dovin, Brian N. Smiley and Sandra L. Malkin of Atlanta's Gard Smiley Bishop & Dovin represent about 75 former A.G. Edwards' clients who claim they lost a total of more than $25 million as a result of alleged mismanagement of accounts in the Augusta office. Unless they settle, all of the cases will go to mandatory arbitration over the next several years.

Should arbitration proceedings in the other cases produce a similar outcome, the 116-year-old brokerage based in St. Louis could feel the impact on its bottom line. For the 2003 fiscal year ending Feb. 28, 2003, Edwards reported net income of $118.8 million on revenue of $2.2 billion.

Gresham, 59, retired from Procter & Gamble's Augusta synthetic detergent plant in early 1999 after working 31 years and acquiring company stock in his Employee Stock Ownership Plan worth about $1.4 million. He claimed he left before the company's retirement age at the urging of A.G. Edwards' Augusta branch manager, William Gibbs, and Gibbs' assistant Susan Saccone, who allegedly promised to manage and make Gresham's money grow at least 10 percent and likely as much as 18 percent to 20 percent a year.

Gibbs and Saccone made similar promises to dozens of other P&G employees, many of whom, like Gresham, took early retirement, according to Gresham's attorneys.

Gresham's lawyers said Gibbs promised their client and other P&G workers that their money would be placed in safe, conservative investments, but instead it wound up in risky tech stocks that plummeted in value.

In a little more than two years, Gresham's retirement funds had dwindled drastically under Edwards' management, his lawyers said. By the time he pulled his money from the brokerage, he had a net out-of-pocket loss of about $265,000.

Other P&G retirees fared even worse. Some are in bankruptcy, and others lost their homes, said Gresham's lawyers, who represent about 75 former Edwards' clients, many of whom had worked for P&G.

"Economically, it's the kind of disaster for people in the Augusta area that you would associate with an act of nature," said Smiley.

Neither attorney who represented Edwards—in-house counsel James C. Browning Jr. and Richard H. Kuhlman of St. Louis' Blackwell Sanders Peper Martin—could be reached.

Gibbs and Saccone's attorney Peter J. Anderson of Sutherland Asbill & Brennan declined comment, deferring to Edwards' director of public relations, Margaret G. Welch.

Welch had a brief statement: "We strongly disagree with the panel's decision and are evaluating our options."

Edwards can file a motion to vacate the award.

Asked if Edwards had set aside any funds to pay claims arising out of the Augusta office, Welch said, "We do not comment on the status of our legal reserves as they relate to individual matters."

In a joint answer filed early in the case, Edwards, Gibbs and Saccone called it "certainly regrettable that Mr. Gresham and millions of other investors lost money as a result of declining stock markets."

But, they added, that didn't mean those losses were the fault of the brokers. They denied violating any state or federal securities laws and argued that Gresham was an informed and active investor who ratified their decisions and raised no questions about his account until the market declined.

Bait and Switch?

Gresham, a former Marine who served in Vietnam but did not complete high school, went to work for P&G in 1967. According to his statement of claim, he worked the third shift as part of the clean-up crew, then worked his way up the company structure, becoming a mechanic in his last eight years at P&G. In 1998, he made a salary of about $65,000.

He began considering early retirement in 1997, the statement said, since he could retain some company benefits by leaving at the age of 55. He was invited to attend a seminar conducted by Gibbs, who had been actively recruiting P&G and Lowe's workers as clients.

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Brian L. Smiley, Sandra L. Malkin, Edward J. Dovin represented Gresham and other Edwards ex-clients.

Gibbs, Gresham claimed, pitched what is known as the "Dow 10" or "Dow 5" strategy. That investment strategy involves choosing either five or 10 stocks from among the Dow 30 that provide the highest dividend yield, then weeding out underperformers at the end of each year and replacing them with other high-yield Dow stocks.

Gibbs allegedly called the strategy foolproof and told the P&G workers they could live comfortably off annual withdrawals of 9 percent of their account, while watching it grow.

Smiley said that, regardless of the merits of the Dow strategy, the retirees' funds should never have been put solely into five or 10 stocks.

However, despite promoting the Dow strategy, Gibbs never followed that investment approach, Dovin said.

While Gibbs' clients thought their funds were being invested in "a time-tested, mechanistic strategy," Dovin said, "little did they know, [Gibbs] never used it." Instead of the Dow stocks, he substituted technology stocks. By early 2000, Dovin said, "people had nothing [in their accounts] but a handful of tech stocks."

Gresham, according to pleadings, had no Dow stocks but had 47 percent of his retirement portfolio tied up in two nonconservative technology stocks.

Gibbs and Saccone then convinced Gresham and other investors to put in $100,000 each for some short-term trading—stocks the brokers would buy, keep for a week or 10 days and then sell.

They bought shares of Citrex on March 3, 2000, with Gresham's $100,000, then sold it three days later for a profit of $14,498.38. The next day, they invested $114,032.01 of his money in PSINet, an Internet service provider that had a history of losses, according to the case pleadings. By the end of March, PSINet had fallen from almost $58 a share to $34.

The Edwards brokers, however, did not trade the PSINet shares, but held them month after month as they continued to decline.

Dovin said Gibbs "rode [that stock] all the way down," while his clients lost $12 million.

Gresham filed his arbitration claim June 12, 2002, naming Edwards, Saccone and Gibbs as respondents. He claimed breach of fiduciary duty, negligence, breach of NYSE and NASD rules, breach of contract, fraud and violations of state securities laws.

Warning Went Unheeded

Dovin said Gresham's case was bolstered by a company document—notes written by an Edwards regional manager of a telephone conversation in which one of Gibbs' colleagues called his investment strategy "dangerous." The note was written the very day Gresham opened his account.

"Unfortunately," Dovin said, "nothing happened."

Smiley called the document a "red flag," but added that "you seldom see a red flag that has 'danger' written on it."

He said arbitration panels seldom make specific findings when issuing awards. Nor do they often award punitive damages, he added.

The $400,000 punitives in this case, Smiley said, "is the kind of award that ought to send a message."

Gresham, he added, saw both "the best and the worst the capitalist system had to offer." He watched his hard work and long tenure at P&G pay off with a retirement account of more than a million dollars, but he also saw how "somebody who works at a major brokerage firm ... could in effect pull a bait and switch," Smiley said. ❐

Gard Smiley Bishop & Dovin partner Steven J. Gard is the cousin of Daily Report *Editor and Publisher S. Richard Gard Jr.*