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HENRY RICHMOND, Complainant, v. SMITH BARNEY, INCORPORATED, Respondent.	CFTC Docket No. 98-R71

INITIAL DECISION

This dispute arises from erroneous price quotes provided by Smith Barney. Henry Richmond asserts that he is entitled to disavow the trade that he made in reliance on the erroneous quotes and to recover his entire $7,992 loss on the trade. Smith Barney admits that its price quote service had been plagued by "ongoing" problems affecting the reliability of its price quotes, that it in fact gave Richmond erroneous price quotes, but asserts that it is not liable for Richmond's loss because after it promptly reported the error to Richmond he chose to hold the position.

After carefully reviewing the parties' documentary submissions, it has been concluded that Richmond has established that Smith Barney recklessly violated Section 4b of the Commodity Exchange Act by failing to disclose the ongoing problems with its quote service, but that the damages proximately caused by this

violation are limited to Richmond's loss at the time that he learned of the erroneous quote: $1,700.

Factual Findings

Henry Richmond's Investment Experience

1. Henry Richmond, a resident of White Plains, New York, opened a commodity account with Smith Barney in July of 1994. [Exhibit B to answer.] Richmond was 76 years old at that time. Richmond represented on the account application that he had an estimated net worth of seven million dollars and an annual income of six-hundred thousand dollars; that he had been investing in stocks and bonds since 1983 and options since 1985, but that he had no commodities experience; that "growth" was his main investment objective; and that his risk tolerance was "aggressive." In contrast, Richmond claims that he should not be considered "an experienced and aggressive investor," because "I feel that I am psychic and I play numbers rather than economics." [Exhibit A to Smith-Barney's reply to *sua sponte* discovery order (filed August 10, 1998); and Richmond's reply to *sua sponte* discovery order (filed August 14, 1998).]

2. The monthly account statements establish that Richmond held large positions and experienced huge swings between significant profits and losses, and support the conclusion that Richmond had been an aggressive trader before the disputed trade. For example, the January 1995 statement reported 24 long bond futures contracts with an unrealized profit of $60,271; the February 1995 statement reported 36 long bond futures contracts with an unrealized profit of $129,393; and the December 1995 statement reported 75 long NYMEX platinum futures contracts

and a year-to-date cumulative realized and unrealized profit of $265,332. The monthly statements also show that Richmond could withstand significant losses. For example, the December 1996 monthly statement reported a year-to-date cumulative realized and unrealized loss of $150,773; the January 1997 statement reported an unrealized loss of $104,625 in bond futures; and the November 1997 monthly statement reported that Richmond had a year-to-date realized and unrealized loss of $261,921. [Exhibit B to Smith-Barney's reply to *sua sponte* discovery order.]

Both sides indicated that Richmond relied to some extent on the advice of Renee Gattullo, a Smith-Barney financial advisor. [See Richmond's reply to *sua sponte* discovery order; and page 2 of the Answer.]

3. According to Smith-Barney, in October of 1987, the aggressive trading in Richmond's account automatically triggered a supervisory review, and Dennis Schmidt, the branch office manager spoke to Richmond. Schmidt then sent a letter confirming the conversation:

> Thank you for taking my call concerning your account . . . and your daughter's account . . . where you have discretion.
>
> Both accounts have losses of $209,000 and $123,000, respectively.
>
> You mentioned that you are [an] experienced commodity speculator with over 20 years of experience. It is important for us at Smith-Barney to make sure we know that our clients can afford risk and have the knowledge/experience in trading aggressively.
>
> Please feel free to use me as a resource at [telephone number] or if you are ever in the branch, stop in and say hello.

[Letter dated October 8, 1997, exhibit C to Smith-Barney's reply to *sua sponte* discovery order.] Neither side has explained the discrepancy between Richmond's statement to Schmidt that he had 20 years experience with commodities and his earlier representation to Smith Barney, on an "account verification profile" dated May 9, 1996, that he had no commodities investment experience. [Exhibit C to Smith-Barney's reply to *sua sponte* discovery order.]

Smith Barney's Quote Service Problems

4. Paragraph 15 of the Commodity Client Agreement signed by Richmond states: "Commodity information, all price quotations or trade reports given to me are also subject to change and errors as well as delays in reporting and I acknowledge that reliance upon such information is at my own risk."

5. At the time of the disputed trade, in December of 1997, Smith Barney's White Plains branch office had been experiencing "ongoing problems" with its Bridge-Knight Ridder quote system that occasionally resulted in various problems, including delayed and/or inaccurate quotes. [¶¶4 and 5 of Gina Tong affidavit, exhibit D to Smith Barney's reply to *sua sponte* discovery order.] However, Richmond would not become aware of this problem until after he had made the disputed trade. [See transcript of recorded conversations on December 22, 1997, exhibit C to answer; and Richmond's reply to *sua sponte* discovery order.]

The Disputed Trade

6. On December 22, 1997, at 9:50 a.m., Richmond telephoned the White Plains branch office and asked where the Dow Jones Index (the "Dow") and New

York Futures Exchange Index ("NYFE") were trading. Smith Barney "matter-of-factly" gave quotes from the Bridge-Knight Ridder quote system that the Dow was down 22 points and the NYFE was up 2.25 points. Several minutes later, Richmond called to request the same two quotes. The Bridge-Knight Ridder system showed that the Dow was down 12 points and the NYFE was up 3.25 points. Unfortunately, while the Bridge-Knight Ridder quotes for the NYFE were correct, the quotes for the Dow were not correct. [Complaint.]

Based on the erroneous quotes, Richmond believed that he had discovered a significant discrepancy that indicated that the NYFE was going to continue to rise.[1] According to Richmond, the Smith-Barney support employee declined to comment on Richmond's opinion that an anomaly appeared to exist between the indices. Also, Richmond "could not reach" his advisor, Gattullo. Nonetheless, he then placed an unsolicited order to purchase four NYFE contracts at the market, eventually paying $508.25.[2] [See order tickets for the purchase and the sale of the contracts, exhibit A to Smith-Barney's reply to *sua sponte* discovery order.]

[1]Richmond did not articulate the basis of his hunch, and merely asserted that he uses "psychic" powers in picking trades. In contrast, according to Smith Barney, no direct relationship exists between the two indices, and any relationship that exists is necessarily "intricate and subtle" because the Dow Jones Index is comprised of 30 large companies while the New York Stock Exchange Composite Index, which underlies the NYFE, includes every stock on New York Stock Exchange. Also, aberrations between the indices are "not unusual in today's market." [Richmond's and Smith-Barney's reply to *sua sponte* discovery order.]

[2] Mr. Richmond actually bought five contracts, four for his own account and one for his daughter's account over which he had power of attorney. The losses claimed represent only the four contracts in his account.

7. At about 10:00 a.m., a friend of Richmond informed him that the Dow quotes he received were incorrect.

Tape recordings of conversations contradict Richmond's allegation that he then "immediately" complained to Smith Barney that he had been misinformed and demanded that he "wanted out of the purchase." [Exhibit C to the Answer.] The recordings establish that at 10:01 a.m., when a Smith Barney employee confirmed that the Dow quotes had been wrong, Richmond chose to hold the position and replied: "Ha, I paid $508.25. That's not so bad. It looks pretty strong then?"[3] During a second call at 10:22 a.m., Richmond asked if the problems with the quote service had been corrected, and again chose to hold the position.[4] [See exhibit C to answer.] Later that morning,[5] the market turned against Richmond, and Richmond liquidated his position, resulting in a loss of $7,995.32, including commissions and fees.[6]

Conclusions

Richmond has established that Smith Barney recklessly violated Section 4b of the Act by failing to disclose the ongoing reliability problems with its quote system. Notwithstanding the fact that the customer contract contained a general

[3] If Richmond had sold the contracts at 10:01 A.M., his loss would have been about $1,700.00. [Exhibit C, to Smith-Barney's reply to *sua sponte* discovery order.]
[4] If Richmond had sold the contracts at 10:22 A.M. his loss would have been about $3,700.00.
[5] The order ticket for the sale of the contracts is time-stamped 11:47 a.m. [Exhibit C, to Smith-Barney's reply to *sua sponte* discovery order.]

acknowledgement that quote systems were not totally reliable, the fact that Smith-Barney's quote system was in fact quite unreliable was patently material to any reasonable investor, and Smith Barney's failure to disclose the persistent problem was reckless, especially where Richmond had pointed out to the Smith Barney employee that the two quotes indicated an apparent aberration between the two indices.

Richmond's reliance on Smith Barney's omission is presumed. *Maloley v. R.J. O'Brien & Associates, Inc.*, [1987-1990 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 24,162 (CFTC 1988). Moreover, Richmond has amply demonstrated that his decision to initiate the trade was based on the apparent aberration indicated by the erroneous quotes. In these circumstances, the mere fact that Richmond chose to hold the position after being informed of the erroneous quotes simply cannot be stretched to establish that Richmond would have initiated the trade had he known that the quotes were erroneous.

However, Richmond's decision to hold the position does limit his damages. The recordings of the conversations on December 22, 1997 contradict Richmond's assertion that when he learned the Dow quotes were wrong he "immediately" called the Smith-Barney and said that he "wanted out of the purchase." Rather the recordings show that Richmond did not initially complain, and then made an informed decision to maintain his position for another ninety-plus minutes. In these circumstances, Smith Barney's liability must be limited to $1,700,00, the loss Mr.

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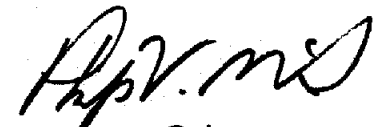
[6] Smith Barney stated that it "does not have any tape recordings" of the conversation when Richmond placed the order to sell the NYFE contracts. [Page 3 of the Answer.]

Richmond would have incurred had he actually sold the contracts immediately when the error was discovered. Any additional losses are directly attributable to Richmond's own decisions and actions.

ORDER

Henry Richmond has established that Smith-Barney, Incorporated violated Section 4b of the Commodity Exchange Act, causing $1,700 in damages. Accordingly, Smith-Barney, Incorporated, is ORDERED to pay to Henry Richmond reparations of $1,700, plus interest on that amount at 4.242% compounded annually from December 22, 1997 to the date of payment, plus $125 in costs for the filing fee.

Dated October 21, 1998.



Philip V. McGuire,
Judgment Officer