

Award
FINRA Dispute Resolution

In the Matter of the Arbitration Between:

Claimants

Robert C. Kraynak
Robert C. Kraynak IRA
Leslie A. Kraynak
Leslie A. Kraynak IRA

Case Number: 13-02888

vs.

Respondent

Charles Schwab & Co., Inc.

Hearing Site: Los Angeles, California

Nature of the Dispute: Customers vs. Member

This case was decided by an all-public panel.

REPRESENTATION OF PARTIES

For Claimants Robert C. Kraynak, Robert C. Kraynak IRA, Leslie A. Kraynak and Leslie A. Kraynak IRA, hereinafter collectively referred to as "Claimants": T. John Kirk, Esq., Maddox, Hargett & Caruso, P.C., Fishers, Indiana.

For Respondent Charles Schwab & Co., Inc., hereinafter referred to as "Respondent" or "Schwab": Gordon C. Young, Esq., Barr & Young, Danville, Colorado.

CASE INFORMATION

Statement of Claim filed on or about: September 30, 2013.

Claimants signed the Submission Agreement: September 21, 2013.

Statement of Answer filed by Respondent on or about: December 13, 2013.

Respondent signed the Submission Agreement: December 12, 2013.

CASE SUMMARY

Claimants asserted the following causes of action: unsuitable investments; violation of the California Corporate Securities Act and Regulations; breach of contract; constructive fraud/breach of fiduciary duty; violation of the NASD and NYSE Conduct Rules;

respondeat superior; and negligence and negligent supervision. The causes of action relate to Claimants' investments in Fannie Mae and Freddie Mac preferred stock.

Unless specifically admitted in its Answer, Respondent denied the allegations made in the Statement of Claim and asserted various affirmative defenses.

RELIEF REQUESTED

In the Statement of Claim, Claimants requested:

1. Actual damages and/or rescission in the amount of \$271,593.90;
2. Pre and post judgment interest;
3. Costs of arbitration, including FINRA filing fees, expert witness fees, reasonable attorneys' fees, arbitrator fees and expenses; and
4. Punitive damages.

In its Statement of Answer, Respondent requested:

1. Dismissal of the Statement of Claim in its entirety;
2. Assessment of all FINRA costs and forum fees against Claimants;
3. Expungement of all references to this matter from the regulatory records of non-parties Patrick Bentivegna and Jeffrey Miner; and
4. Such other relief as provided by law.

At the close of the hearing, Claimants requested actual damages and/or rescission in the amount of \$113,640.00.

OTHER ISSUES CONSIDERED AND DECIDED

The Arbitrators acknowledge that they have each read the pleadings and other materials filed by the parties.

After the conclusion of Claimants' case-in-chief, Respondent made a Motion to Dismiss. Claimants opposed the motion. The Panel deferred its ruling.

At the close of the recorded hearing, Respondent renewed its request for expungement of non-parties Patrick Bentivegna and Jeffrey Miner's Central Registration Depository ("CRD") records. The Panel determined that Claimants opposed the request by virtue of putting on the case.

In recommending expungement for non-party Patrick Bentivegna, the Panel reviewed and relied upon the following:

- A current copy of non-party Patrick Bentivegna's BrokerCheck report;
- Claimants' Exhibit 10 – MARS and CS2 Notes;
- Respondent's Exhibit 3 – Summary of Kraynak's Fannie Mae and Freddie Mac Preferred Stock Activity;
- Respondent's Exhibit 4 – Trade Confirmations of the Kraynak's Buys and Sells of Fannie Mae and Freddie Mac;
- Respondent's Exhibit 5 – MARS Notes for Robert Kraynak;

- Respondent's Exhibit 9 – Kraynak Responses to Schwab Customer Service Questionnaire dated April 8, 2009;
- Respondent's Exhibit 20 – New Account Documents and Account Verifications for Robert Kraynak IRA Rollover;
- Respondent's Exhibit 21 – New Account Documents for Kraynak Trust Account; and
- Respondent's Exhibit 22 – New Account Documents and Account Verifications for Kraynak Family Trust Account;

In recommending expungement for non-party Jeffrey Miner, the Panel reviewed and relied upon the following:

- A current copy of non-party Jeffrey Miner's BrokerCheck report; and
- Claimant's Exhibit 10 – MARS and CS2 Notes.

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.

FINDINGS

Claimant Robert C. Kraynak ("Kraynak") claims to have been a conservative investor with little or no investment experience at the time he and his wife opened their family trust and IRA accounts 1/ with Respondent Charles Schwab & Co., Inc. ("Schwab"). The Statement of Claim ("SOC") alleges that Kraynak's risk tolerance was "low" and that his investment objective was "capital preservation." However, according to the opening account documents that Kraynak signed between October 2000 and November 2001, he listed his investment knowledge and experience as extensive, with 35 years' experience in stocks, 15 years' experience in bonds and 15 years' experience in options. He listed his overall investment objectives as capital preservation, income and growth. In 2001, when Kraynak added an option/margin trading authorization to his accounts so he could sell covered calls, he listed his net worth at \$3 million with a liquid net worth of \$2 million. He also listed his option trading experience as good with 20 years of experience and an average of 5 trades per year. Moreover, later in Kraynak's relationship with Schwab he added "speculation" to his investment objectives because he wanted to be able to invest in IPOs.

The SOC goes on to allege that because of Kraynak's lack of investment experience, he relied upon Schwab to structure a "bond ladder" to provide income for him and his wife during their retirement—which formal retirement began in approximately mid-2001. 2/ More to the point, Kraynak claims that between late 2006 and 2008 he was induced to purchase Fannie Mae ("Fannie") and Freddie Mac ("Freddie") Preferred Stock based on representations that the investments were "safe" and were "implicitly backed" by the United States Government. He further alleges that representatives from Schwab on whom he relied for advice about his fixed income investing, Patrick Bentivegna

1. Claimants are Robert and Leslie Kraynak, husband and wife, who opened 4 accounts here relevant. Two accounts were IRAs and the other two were family trust accounts. Robert Kraynak managed all 4 accounts. Therefore, all references hereinafter to "Kraynak" are intended to refer to claimants and each of their accounts collectively.

2. Kraynak retired from Xerox after having worked there in various positions for approximately 36 years. Between 2001 and 2010 he worked for himself as a sales trainer.

("Bentivegna") and Jeffrey Miner ("Miner"), 3/ omitted to disclose the risks associated with the Fannie and Freddie Preferred, omitted to disclose Fannie and Freddie's solvency issues that "were widely known throughout the market . . . for a number of months," and failed to disclose that their compensation was based on the sale of fixed income products.

Kraynak made multiple purchases of Fannie and Freddie Preferred in all 4 accounts between 12/6/2007 and 7/14/2008 at prices ranging from 26.20 per share down to 16.91 per share. The par value of these securities was 25 per share and these preferred paid interest/dividends at the rate of 8.25% to 8.375%.

Based on these core allegations, Kraynak seeks damages, and/or rescission, on theories of Suitability, Violation of California Corporations Code's Anti-Fraud Provisions, Breach of Contract, Breach of Fiduciary Duty, Constructive Fraud, Violation of FINRA Conduct and NYSE Board Rules and Negligence. 4/

During the time Kraynak was a Schwab customer, he alone directed the activities in his various accounts. Schwab tried on multiple occasions to garner Kraynak as a "managed" client but Kraynak chose to conduct his transactions online at a much lower cost. Kraynak principally purchased debt instruments for his various accounts because he wanted to generate income in the 5% to 6% range. He apparently learned about preferred stocks in 2004 from his dealings with Bentivegna who told Kraynak that preferreds were riskier than straight bonds. Kraynak admitted that he bought preferreds because he wanted to achieve better returns.

In a recorded conversation between Kraynak and Bentivegna on November 30, 2006, Kraynak told Bentivegna that his (Kraynak's) "strategy" was to principally purchase short-term bonds, but was "spicing it up on the long end with some preferred stocks." In fact, Kraynak first learned about Fannie Preferreds from an IPO/New Issue he apparently heard about, and then Bentivegna later drew Kraynak's attention to them.

After this point in August 2007, Kraynak and Bentivegna talked about Fannie in general because Kraynak was also looking at buying some Fannie Bonds. In this conversation, Bentivegna was clear that Fannie Bonds were not guaranteed by the United States Government and thus not as "safe" as bonds issued, for example, by the Federal Home Loan Bank. Bentivegna and the financial community in general talked about Fannie and Freddie debt having the "implicit backing" of the United States Government, but it was understood that this was not the same thing as a guarantee and Kraynak understood as much.

The first conversation between Bentivegna and Kraynak regarding Fannie Preferreds occurred on December 18, 2007 when Kraynak called in to find a place to reinvest the funds from a CD that was maturing. Bentivegna offered Kraynak the Fannie Preferred but Kraynak opted to purchase a government guaranteed Ginnie Mae issue.

Notably, Kraynak made his first purchase of 550 shares of Fannie Preferreds on December 6, 2007 at \$23.25 per share for a total investment of \$12,787.50, 12 days before Bentivegna even mentioned this particular security to Kraynak. Kraynak purchased the Ginnie Mae on that occasion instead of the Fannie Preferred because he

3. Bentivegna and Miner were Regional Bond Specialists who, at different times, serviced the office out of which Kraynak maintained his accounts. Kraynak's account representative was another individual by the name of Linda Speikerman.

4. There are other theories set forth in the SOC. However, they are largely duplicative of those set forth here.

wanted the government guarantee. The next day, Kraynak purchased 200 shares of Fannie 8.25% Preferred at a total cost of \$5,030.00.

On January 14, 2008, Kraynak talked to Bentivegna about purchasing a CD from Citizens Bank, which he did on that date. Three days later on January 17, Kraynak purchased 2435 shares of Fannie 8.25% Preferred at a total cost of \$62,507.00. Thereafter, between January 25 and March 6, 2008 Kraynak purchased online another 3775 shares of Fannie 8.25% Preferred at a total cost of approximately \$99,000.00. On February 28, 2008 Kraynak purchased 885 shares of Fannie 8.375% Preferred at a total cost of \$23,010.00.⁵ During the time that Kraynak made these purchases, Fannie Debt obligations were AA rated by S&P, Fitch and Moody, 7 steps above investment grade.

On March 10, 2008 Kraynak became concerned about what he perceived to be the volatility in the price of Fannie Preferreds. At this time, the price of the Fannie Preferreds had dropped by between 7%-8%. Acting on his concern Kraynak called Bentivegna. In their conversation Bentivegna referred Kraynak to an article published in Barron's—the issue for the week of March 10. That article was quite critical of Fannie and Freddie and warned in the event of a crisis that notwithstanding the “implied backing” of the United States Government, preferred and common shareholders would suffer grievously.

Kraynak looked online for the Barron's article because he did not have a subscription. He did not find the exact article to which Bentivegna referred him. Instead he found another article published on March 7 that discussed the markets' fear of mortgage backed securities, including Freddie and Fannie issues, notwithstanding their AAA ratings and “what is widely perceived to be the implicit backing of the federal government.”

Kraynak took no action in response to this article and candidly testified that even had he read the Barron's article to which Bentivegna referred him, he still would have held on to his Fannie Preferreds. On March 10, the closing price of Fannie Preferreds was \$23.34.⁶ Roughly 2 months later, on May 2, 2008, Fannie Preferreds closed at \$25.10.

It is significant that on April 24, 2008 Bentivegna transferred from the Regional Bond Desk to the Santa Rosa Branch Office where he became a straight Financial Consultant (“FC”), like Linda Speikerman who was, in fact, the FC with whom Kraynak met annually to discuss his portfolio at the Torrance Branch near where he and his wife resided. Therefore, it is less than likely that Bentivegna gave any advice or counsel to Kraynak after this point in spite of Kraynak's somewhat hazy recollection to the contrary.

During the summer of 2008, specifically on July 14, 2008, Kraynak engaged in a series of tax-motivated transactions to avoid the “wash sale” rules. He claims that Bentivegna directed him in this respect; however, this does not seem credible in light of the fact that Bentivegna had stopped working as a Regional Bond Specialist 3-months earlier. Regardless, on July 14, 2008 Kraynak sold all of the Fannie Preferreds in his taxable accounts at prices ranging from \$21 to \$16 a share and recorded the losses. He then turned around and purchased equivalent amounts of Freddie Preferred at prices ranging \$16.91 to \$17.00 a share.

5. Kraynak's online trades cost him \$9.00 per transaction and Bentivegna received no commission on any of the purchases of Fannie and Freddie Preferreds. The total fees charged on the purchases of Fannie and Freddie Preferreds, according to the undisputed testimony, was \$178.00.

6. Kraynak's purchases by this point ranged from 26.30 to 23.25 per share.

Thereafter, Fannie and Freddie Preferreds ran a steady course downward until ultimately they were placed in conservatorship on September 8, 2008, at which point the stock prices dropped to around \$3.00, closing as low as \$0.83 on December 31, 2008. 7/ Schwab issued a press release on September 8, 2008 advising its customers about the effect of the government takeover and giving investors limited advice in light of the crisis. Kraynak chose to hold on to his shares.

Prior to the takeover of Fannie and Freddie, Kraynak's statements revealed the risk involved in the Preferreds. The yields, based on the "coupon rate," were well above 10% and were in line with the yields of some of Kraynak's other risky investments including a leveraged high yield bond fund. Kraynak claimed not to understand the significance, from a risk standpoint, of these yields—claiming that all he was interested in was receiving his interest and dividend payments to support himself and his wife. However, we do not believe Kraynak was as naïve as he made himself out to be, given the length of time he bought and sold debt instruments through Schwab (2001 on), coupled with his 35-year career in business with Xerox, a liberal arts degree from Columbia University, and a free subscription to the Wall Street Journal that Schwab provided to him at his request.

It was not until July 2008 that Miner joined the Regional Bond Desk, where Bentivegna had previously worked and interacted with Kraynak. Kraynak testified that he first spoke with Miner in August of 2008 but had no specific recollection of the alleged conversation. Miner testified he never spoke with Kraynak until after the government placed Fannie and Freddie into conservatorship.

Interestingly, Kraynak completed a survey about his experiences at Schwab in April 2009. In that survey, he gave a 7 on a scale of 1-10 to his level of satisfaction with Schwab and the likelihood that he would recommend Schwab as an investing source to others. In his written comments about areas for improvement he complained that there was no reliable information publicly available about the quality of debt offerings, other than the ratings agencies that had proved less than reliable. He made no mention whatsoever about anything relating to the matters about which he now complains nearly 7 years later.

Kraynak transferred his accounts from Schwab to Fidelity and ultimately sold all of his Fannie and Freddie Preferreds at prices in the \$6-\$11 range. After taking account of dividends and proceeds of the sales, Kraynak suffered a net loss on all of his Fannie and Freddie Preferred purchases of \$113,640.46.

Kraynak filed the SOC in this action on September 30, 2013, more than 5-years after Fannie and Freddie were placed in conservatorship.

CONCLUSIONS

Based on the findings above, we conclude that neither Respondent nor its agents, Bentivegna and Miner, was guilty of any act(s) of wrongdoing with respect to the Fannie and Freddie Preferreds about which Kraynak complains in this action. Kraynak himself decided to purchase Fannie Preferred in his account before Bentivegna even mentioned the security in their conversations. Kraynak knew and understood that preferred stocks were "riskier" than bonds or other more secure debt instruments from his years of investing in fixed income obligations.

7. The government did in fact back the bonds, including interest payments, issued by Fannie and Freddie, some of which Kraynak held along with the Preferreds.

Moreover, Bentivegna did not misrepresent or omit to state any matter with respect to the Fannie or Freddie Preferreds. He simply provided Kraynak with precisely the same information that the overall financial markets knew and understood about Fannie and Freddie. To this extent, he could not have breached any duty Schwab may have owed to Kraynak, regardless of Kraynak's admitted status as a self-directed investor. Neither did Bentivegna's conduct run afoul of any identifiable FINRA Conduct or NYSE Board Rule. And neither, in light of Kraynak's stated knowledge, experience, investment goals and portfolio make up, was his investment in Fannie and Freddie Preferreds unsuitable. In short, Kraynak was a victim of a market that very few people ever anticipated.

AWARD

After considering the pleadings, the testimony and evidence presented at the hearing, and the post-hearing submissions, the Panel has decided in full and final resolution of the issues submitted for determination as follows:

1. Respondent's Motion to Dismiss is denied.
2. Claimants' claims are denied in their entirety.
3. The Panel recommends the expungement of all references to the above-captioned arbitration from non-parties Patrick Bentivegna (CRD # 2477112) and Jeffrey Miner's (CRD # 4478731) registration records maintained by the CRD, with the understanding that pursuant to Notice to Members 04-16, non-parties Patrick Bentivegna and Jeffrey Miner must obtain confirmation from a court of competent jurisdiction before the CRD will execute the expungement directive.

Unless specifically waived in writing by FINRA, parties seeking judicial confirmation of an arbitration award containing expungement relief must name FINRA as an additional party and serve FINRA with all appropriate documents.

Pursuant to Rule 12805 of the Code of Arbitration Procedure (the "Code"), the Panel has made the following Rule 2080 affirmative findings of fact for non-party Patrick Bentivegna:

The claim, allegation, or information is factually impossible or clearly erroneous; and

The claim, allegation, or information is false.

Pursuant to Rule 12805 of the Code, the Panel has made the following Rule 2080 affirmative finding of fact for non-party Jeffrey Miner:

The registered person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation or conversion of funds.

The Panel has made the above Rule 2080 findings based on the following reasons:

At the outset it is important to observe that this panel has an important role in determining whether to order a claim expunged from a registered representative's CRD. According to the most current version of FINRA's Arbitrator Guide:

FINRA rules provide a framework for arbitrators to follow when considering requests to expunge customer dispute information. The *framework* (below) is intended to ensure that arbitrators recommend expungement *only* when the information is found to have no meaningful investor protection or regulatory value. (Emphasis added)

Rule 2080 establishes procedures to ensure that expungement occurs **only** when the arbitrators find and document one of its narrow grounds:

1. The claim, allegation or information is factually impossible or clearly erroneous;
2. The registered person was not involved in the alleged investment-related sales practice violation, forgery, theft, misappropriation or conversion of funds; or
3. The claim, allegation or information is false.

Arbitrator's Guide (Oct. 2014 Ed.)(Emphasis Added)

In this case, based on our findings in the case in chief, we find the evidence clear and convincing in favor of ordering expungement of the CRD's of both moving parties, Bentivegna and Miner. In particular, we conclude the allegations in this case against Bentivegna are clearly erroneous and false. In addition, we find that Miner was not involved in the alleged investment-related sales practice violations.

Also, importantly, in consideration of whether to expunge the records of Miner and Bentivegna, we have carefully reviewed their CRD Reports, with particular attention to the Disclosure Events section of the reports. With the exception of the instant case, Miner's CRD Report does not contain any disclosure events, and therefore the report does not enter into our decision based on the above findings that expungement is appropriate.

Bentivegna's CRD Report contains five disclosure events, which we have carefully reviewed. Of the five disclosure events, one event listed relates to the instant case.

A second disclosure event was settled. In the Comment Section, it is noted that Bentivegna was not named in the complaint, that he only took the trade from the client, and that he did not contribute to the settlement amount.

A third disclosure event indicates that this complaint resulted in no action and was closed.

A fourth disclosure event was settled. Bentivegna did not contribute to the settlement amount.

A fifth disclosure event indicated in the record that the security was a AAA rated insured municipal bond that has been "pre-refunded, called and the client made whole", and that the alleged compensatory damages have been denied.

Based on our review of the disclosure events listed in the CRD Report of Bentivegna, we do not find that there is anything which impacts our decision in this case, based on the above findings, that expungement is appropriate.

4. Any and all relief not specifically addressed herein, including punitive damages, is denied.
5. The Panel has provided an explanation of their decision in this Award. The explanation is for the information of the parties only and is not precedential in nature.

FEES

Pursuant to the Code, the following fees are assessed:

Filing Fees

FINRA Dispute Resolution assessed a filing fee* for each claim:

Initial Claim Filing Fee	= \$ 1,425.00
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**The filing fee is made up of a non-refundable and a refundable portion.*

Member Fees

Member fees are assessed to each member firm that is a party in these proceedings or to the member firm(s) that employed the associated person(s) at the time of the event(s) giving rise to the dispute. Accordingly, as a party, Charles Schwab & Co., Inc. is assessed the following:

Member Surcharge	= \$ 1,700.00
Pre-Hearing Processing Fee	= \$ 750.00
Hearing Processing Fee	= \$ 2,750.00

Hearing Session Fees and Assessments

The Panel has assessed hearing session fees for each session conducted. A session is any meeting between the parties and the arbitrator(s), including a pre-hearing conference with the arbitrator(s), that lasts four (4) hours or less. Fees associated with these proceedings are:

One (1) Pre-hearing session with the Panel @ \$1,125.00/session	= \$1,125.00
Pre-hearing conference: April 29, 2014 1 session	

Six (6) Hearing sessions @ \$1,125.00/session	= \$6,750.00
Hearing Dates: February 17, 2015 2 sessions	
February 18, 2015 2 sessions	
February 19, 2015 2 sessions	

Total Hearing Session Fees	= \$7,875.00
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The Panel has assessed \$7,875.00 of the hearing session fees to Respondent.


All balances are payable to FINRA Dispute Resolution and are due upon receipt.

ARBITRATION PANEL

Steven A. Wawra	-	Public Arbitrator, Presiding Chairperson
Mark S. Priver	-	Public Arbitrator
Anita Rae Shapiro	-	Public Arbitrator

I, the undersigned Arbitrator, do hereby affirm that I am the individual described herein and who executed this instrument which is my award.

Concurring Arbitrators' Signatures



Steven A. Wawra
Public Arbitrator, Presiding Chairperson

3.24.15

Signature Date

Mark S. Priver
Public Arbitrator

Signature Date

Anita Rae Shapiro
Public Arbitrator

Signature Date

March 25, 2015

Date of Service (For FINRA Dispute Resolution office use only)

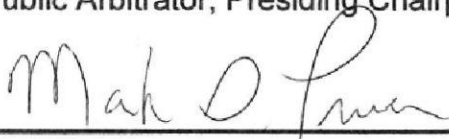
ARBITRATION PANEL

Steven A. Wawra	-	Public Arbitrator, Presiding Chairperson
Mark S. Priver	-	Public Arbitrator
Anita Rae Shapiro	-	Public Arbitrator

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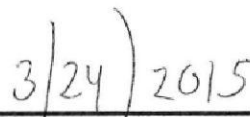
Concurring Arbitrators' Signatures

Steven A. Wawra
Public Arbitrator, Presiding Chairperson



Mark S. Priver
Public Arbitrator

Signature Date



Signature Date

Anita Rae Shapiro
Public Arbitrator

Signature Date

March 25, 2015
Date of Service (For FINRA Dispute Resolution office use only)

ARBITRATION PANEL

Steven A. Wawra	-	Public Arbitrator, Presiding Chairperson
Mark S. Priver	-	Public Arbitrator
Anita Rae Shapiro	-	Public Arbitrator

I, the undersigned Arbitrator, do hereby affirm that I am the individual described herein and who executed this instrument which is my award.

Concurring Arbitrators' Signatures

Steven A. Wawra
Public Arbitrator, Presiding Chairperson

Signature Date

Mark S. Priver
Public Arbitrator

Signature Date



Anita Rae Shapiro
Public Arbitrator

March 24, 2015

Signature Date

March 25, 2015

Date of Service (For FINRA Dispute Resolution office use only)