[* 1]

SUPREME COURT OF THE STATE OF NEW YORK — NEW YORK COUNTY

PRESENT: Hon. _____ PART 36

Justice

MERRILL LYNCH, PIERCE,FENNER & SMITH,
RAYMOND MIRANDA

INDEX NO. 101660/05

MOTION DATE _____

- v -

MOTION SEQ. NO. 001

MARTHA PRISCILLA GRAEF

MOTION CAL. NO. _____

The following papers, numbered 1 to _____ were read on this motion to/for _____

	PAPERS NUMBERED
Notice of Motion/ Order to Show Cause — Affidavits — Exhibits ...	
Answering Affidavits — Exhibits	
Replying Affidavits	

Cross-Motion: ☐ Yes ☐ No

Upon the foregoing papers, it is ordered that this motion is decided as follows:

Dated: 9/12/05

[illegible]
J.S.C.

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE
DATED: _____ J.S.C.

Check one: ☒ FINAL DISPOSITION ☐ NON-FINAL DISPOSITION

Petitioners Merrill Lynch, Pierce, Fenner & Smith, Inc. (Merrill Lynch) and Raymond Miranda petition, pursuant to 9 USC § 10 (a), to vacate a December 22, 2004 award (Award) by a panel of National Association of Securities Dealers arbitrators (Panel). In their memorandum of law, petitioners request that, in the alternative, the Award be modified or remanded for explanation. The Award awarded respondent $148,000 against petitioners, jointly and severally. Respondent cross-moves, pursuant to 9 USC § 9, for an order confirming the Award, and pursuant to 22 NYCRR 130, for costs and attorney's fees.

Background

Respondent is the niece of the late Robert L. Graef, who died on November 30, 2002, and the executrix of his estate. Mr. Graef, who was 88 when he died, had suffered from glaucoma, cataracts, diabetes, and congestive heart failure. He had had a heart attack in August 2002, and then a second one shortly thereafter. Mr. Graef had been hospitalized eight times in the last six months of his life. A consulting doctor's report, dated August 27, 2002, noted that Mr. Graef suffered from senile dementia. A medical history taken in the emergency room of St. Francis Hospital on August 31, 2002, notes that, for some time, Mr. Graef had been chronically bed-ridden.

In or about September 1998, Mr. Graef, who had been an active securities trader and a moderate-aggressive investor, enlisted defendant Miranda, a licensed broker and financial advisor employed

by Merrill Lynch, to organize many of his diverse holdings. Shortly thereafter, Mr. Graef opened a Cash Managing Account (CMA) at Merrill Lynch, with a checking/margin facility. The latter allows the owner of a CMA to draw checks against the value of his or her securities portfolio when the account does not contain enough cash to cover the checks. Interest, charged against the portfolio, accrues on such checks as are drawn. All of Mr. Graef's accounts at Merrill Lynch were non-discretionary. Respondent made no claim to the Panel concerning any purchase or sale of a security. Rather, respondent's claim was based on checks that had been written against the CMA.

Respondent claimed that, in the last two years of Mr. Graef's life, non-party Neressa Lewis, who had been Mr. Graef's home health aid since June 5, 1999, converted a total of more than $350,000 from Mr. Graef through checks written against his CMA, and on an account that Mr. Graef had maintained at the Washington Mutual bank. Respondent claimed that Ms. Lewis "wrote checks ... to herself and to cash, including by forging Mr. Graef's signature and/or his indorsement, and/or kept for herself funds resulting as change from checks cashed by others (such as pharmacies) ... ." Amended Petition, Exh. A, at 3. On August 20, 2004, a Nassau County grand jury indicted Ms. Lewis on a charge of grand larceny in the third degree, but she has not been apprehended.

Respondent contended that no CMA checks had been drawn on Mr. Graef's Merrill Lynch accounts from 1997 through 1999, and that checks totalling only $960 were drawn in 2000. However, in 2001,

CMA checks totalling $59,104.58 were drawn, and in 2002 checks in the amount of $165,470 were drawn, resulting in a margin loan of $132,354 (an amount equal to almost 50% of the value of Mr. Graef's accounts at Merrill Lynch), plus accrued margin interest. Respondent argued that, although Miranda had been aware that checks on Mr. Graef's CMA account were being written with greater frequency and in larger amounts in 2002 than in the past, and although he had tried to call Mr. Graef several times because he was concerned about those checks, neither Miranda nor Merrill Lynch took any steps to secure Mr. Graef's accounts.

Mr. Miranda acknowledged at the arbitration that he had no communication with Mr. Graef after June 2002, and that although he had promised to visit Mr. Graef, who could not readily understand conversations on the telephone, he failed to do so. He also acknowledged that, except for the two conversations discussed below, whenever he called Mr. Graef in 2001 or later, he reached an answering machine and never received a return call. Respondent suggests that it was not in Merrill Lynch's interest to stop the margin loans from increasing, by either stopping Mr. Graef's check-writing privilege or putting a hold on his accounts, inasmuch as Miranda and Merrill Lynch were profiting from the margin loans and the accruing margin interest. Respondent sought compensatory damages of $150,000 for the losses to Mr. Graef's accounts, as well as refunds of margin interest, and of any commissions and management fees that had been charged for the accounts. Respondent also sought punitive damages.

Petitioner contends that the Award should be vacated, because the Panel disregarded applicable law when it issued the Award, because the Award is irrational and violates public policy, and because the Panel was biased.

Standard of Review

Under the Federal Arbitration Act ("FAA"), 9 USC § 1, et seq., the court has an "extremely limited" power of review. Wall St. Assocs., L.P. v Becker Paribas Inc., 27 F3d 845, 849 (2d Cir 1994), quoting Fahnenstock & Co. v Waltman, 935 F2d 512, 516 (2d Cir), cert denied 502 US 942 (1991). Section 9 of the FAA provides that, upon timely application of any party, a court must confirm the award unless the award is vacated, modified, or corrected, pursuant to sections 10 and 11. Section 10 (a) provides, in relevant part, that a court may vacate the award:

> (1) where the award was procured by corruption, fraud, or undue means;
> (2) where there was evident partiality or corruption in the arbitrators, or either of them;
> (3) where the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence pertinent and material to the controversy; or of any other misbehavior by which the rights of any party have been prejudiced;
> (4) where the arbitrators exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.

In addition, the Federal courts have held that an arbitral award may be vacated on one of the following three non-statutory grounds: if the arbitrators "manifest[ly] disregard[ed] ... the law" in reaching their decision (First Options of Chicago, Inc. v Kaplan, 514 US 938, 942 [1995]), if the award is "completely

irrational" (I/S Stavborg (O.H. Meling, Manager) v National Metal Converters, Inc., 500 F2d 424, 430 [2d Cir 1974]), or if implementation of the award would violate a public policy. An award is made in manifest disregard of the law only if "(1) the 'arbitrators knew of a governing legal principle yet refused to apply it or ignored it altogether,' and (2) 'the law ignored by the arbitrators was well defined, explicit, and clearly applicable to the case.'" [citations omitted] DiRussa v Dean Witter Reynolds Inc., 121 F3d 818, 821 (2d Cir 1997), cert denied 522 US 1049 (1998); see also Halligan v Piper Jaffray, Inc., 148 F3d 197 (2d Cir 1998), cert denied 526 US 1034 (1999). An award may not be vacated merely because of an error of law. International Telepassport Corp. v USFI, Inc., 89 F3d 82 (2d Cir 1996). Indeed, an award should be confirmed, "'despite a court's disagreement with it on the merits, if there is a barely colorable justification for the outcome reached.'" Wallace v Buttar, 378 F3d 182, 190 (2d Cir 2004) (emphasis in original) quoting Banco de Seguros del Estado v Mutual Marine Office, Inc., 344 F3d 255, 260 (2d Cir 2003). An award is "completely irrational" where the reviewing court is "'unable to infer a ground for the arbitrators' decision from the facts of the case' such that the award 'can only represent "evident partiality" on the part of the arbitrators.'" Matter of Arbitration Between Red Apple Supermarkets/Supermarkets Acquisitions and Local 338 RWDSU, 1999 WL 596273, *8 (SD NY 1999), quoting Tinaway v Merrill Lynch & Co., 658 F Supp 576, 579 (SD NY 1987). Arbitrators need not give any explanation of their award.

Wallace v Buttar, 378 F3d at 190. Finally, although a court may refuse to confirm an arbitral award on the ground of public policy (see UBS Warburg LLC v Auerbach, Pollack & Richardson, Inc. Sup Ct, NY County 2001, Index No. 119163/01), it may do so only "when enforcement of the award would be directly at odds with a well defined and dominant public policy resting on clear law and legal precedent." St Mary Home, Inc. v Service Empls. Intl. Union, District 1199, 116 F3d 41, 46 (2d Cir 1997); see also Greenberg v Bear, Stearns & Co., 220 F3d 22, 27 (2d Cir 2000).

Discussion

Although the petition alleges that the Award violates public policy, petitioners have failed to specify any public policy that the Award may implicate. With regard to bias on the part of the Panel, petitioners principally argue that arbitrator Grant failed to disclose that, approximately one year before the arbitration that is at issue here, he had represented certain individuals in an arbitration against Merrill Lynch, that had been dismissed. However, even where an arbitrator has previously served as an expert witness for a party, much less than where, as here, he has served merely as an attorney, an award should not be overturned on the ground of partiality. Lucent Technologies, Inc. v Tatung Co., 379 F3d 24 (2d Cir 2004). Petitioners have not alleged that Arbitrator Grant had a financial interest in the arbitration that is at issue here, or that he had a contemporaneous relationship of any kind with any of the parties thereto.

The Panel heard testimony that more than $142,000 of the money

that respondent claimed to have been stolen by Ms. Lewis was in the form of cash withdrawn from Mr. Graef's account at Washington Mutual. That money was transferred to Washington Mutual by checks drawn on Mr. Graef's CMA. Citing Lund v Chemical Bank (797 F Supp 259 [SD NY 1992]) and other cases, petitioners argue that they cannot be liable for those checks, because Mr. Graef was not injured, inasmuch as the checks merely transferred money to another account in his name, and because Merrill Lynch had no control over the funds once they were transferred to Washington Mutual. To be sure, the law is clear that, where the proceeds of a forged check reach the check's intended payee, there is no cause of action on the forgery. See Hillsley v State Bank of Albany, 24 AD2d 28 (1st Dept 1965). In Lund, as in Trans-American Steel Corp. v Federal Ins. Co. (535 F Supp 1185 (ND Ga 1982), which is cited in Lund, the plaintiff had been compensated by the alleged malefactor. Here, however, that principle of law is inapplicable. Respondent's claim was that Ms. Lewis arranged to have sums transferred from Mr. Graef's CMA to his account at Washington Mutual so that she could withdraw the funds from the latter account, and that petitioners' fault lay in their failure adequately to protect Mr. Graef's account, given their knowledge that an ever increasing number of checks were being written against that account in large, and often round amounts. Petitioners' handwriting expert testified to the Panel that the signatures on the checks at issue had all been written by one person, and that the signatures were consistent with what would be expected of an elderly and very sick person.

Respondent's case, however, did not depend on proving that the signatures on the checks had been forged. The gravamen of her claim was that petitioners had allowed Miss Lewis to misappropriate funds from Mr. Graef. It is evident, from the most cursory examination, that, on almost all of the checks at issue, the specification of the amounts of the check and of the payee was written by a hand different from that of the signer. See Gatswirth Affirm., Exh. 4.

Mr. Miranda's notes showed that, while on January 19, 2001, Mr. Graef had told him that he would notify him if he was going to write checks for more than his cash could cover, such checks continued to be written, without any notice to Mr. Miranda. Although Mr. Miranda noted, almost a full year later, that Mr. Graef "is running up significant margin," he did nothing for another six months. On June 18, 2002, Mr. Miranda called Mr. Graef to tell him that checks were continuing to be written. At this time, Mr. Miranda realized that, as he noted, Mr. Graef was having trouble hearing him. It is perhaps for this reason that Mr. Miranda failed to give Mr. Graef any details as to the sums involved, the fact that large sums were being drawn to the order of Ms. Lewis, or the extent of Mr. Graef's margin balance. As noted above, however, although Mr. Miranda promised, in this conversation, to visit Mr. Graef to discuss his account in person, and although his notes show that he intended to do so two days later, he never did.

Citing De Kwiatkowski v Bear, Stearns & Co., Inc. (306 F3d

1293 [2d Cir 2002]) and other cases, petitioners argue that they cannot have been held to have a fiduciary duty to Mr. Graef, because his securities account was non-discretionary. These cases hold that, generally, where a securities account is non-discretionary, a broker has no fiduciary duty to offer information or advice between transactions. That principle is completely inapplicable here, where respondents' claim is not based on any trading decision. In Conway v Icahn & Co. (16 F3d 504 [2d Cir 1994]), the Court affirmed a judgment for plaintiff that was based on a claim that defendant's sellout, without notice to plaintiff, of certain stock in plaintiff's account, in order to meet a margin call, violated defendant's fiduciary duty to plaintiff. Mr. Miranda was not simply a broker. He was a "Wealth Asset Management Advisor." Mr. Graef had opened his CMA as an annual fee-based (rather than a commission per transaction) account, and he was to be provided with Financial Foundation Reports. Mr. Miranda acknowledged to the Panel that he had failed to follow Merrill Lynch's printed policy requiring a review of monthly statements so as to identify "long standing problems that should be brought to a Branch Manager's attention." Although the Panel failed to give any explanation of its Award, there would have been more than a colorable justification for the Award to be premised on a breach on the part of petitioners of their fiduciary duty to Mr. Graef.

Petitioners urge that the Award be vacated on the ground that Mr. Graef ratified payment on the checks drawn on his CMA. That argument is based on Mr. Graef's statement to Mr. Miranda, in

January 2001, that he knew that such checks were being written, and that he wished to continue his checking facility. However, respondent testified that when she looked through Mr. Graef's papers after his death she could find no statements from Merrill Lynch prior to one dated March 1, 2002. Almost $141,000 in checks were written on the CMA after that date, and Mr. Miranda acknowledged, as noted above, that his last meaningful contact with Mr. Graef had occurred more than a year earlier. While this court might have come to a different conclusion on the issue of ratification, this court cannot say that it was entirely irrational for the Panel to have rejected petitioners' argument.

Petitioners' arguments for modification appear to based upon incorrect premises. Petitioners calculate that Ms. Lewis's salary for the time that she worked for Mr. Graef amounted to $200,200. In addition, petitioners note that Mr. Graef must have had expenses, such as taxes, utility bills, and medications. Accordingly, petitioners argue that it was illogical for the Panel to award an amount that appears to approximate the difference between $350,000 and $200,200. The $350,000 amount, however, is the amount of checks written on all of Mr. Graef's accounts in 2002. From January 2000 to November 30, 2002, a total of $611,021 was written on those accounts, and in the approximately two and a half years that Ms. Lewis was employed by Mr. Graef, checks totalling $324,944 were made payable to her, that is, approximately $100,000 more than she should have received, by petitioners' own calculation. The total amounts of checks written against Mr.

Graef's CMA was more than $225,500, with more than $165,500 written in 2002. Of the latter amount, checks made payable for taxes, utility service, and medications, in 2002, totalled less than $15,000. There is no evidence that the Award was based on a mathematical error. Consequently, there is no basis for the court to modify the Award.

While petitioner's arguments have not prevailed, they are by no means frivolous. Accordingly, that branch of respondent's cross motion that seeks sanctions will be denied.

Accordingly, it is hereby

ORDERED that the petition is denied; and it is further

ORDERED that that branch of the cross motion that seeks sanctions is denied; and it is further

ORDERED that that branch of the cross petition that seeks confirmation of the Award is granted and the Award rendered in favor of respondent and against petitioners is confirmed; and it is further

ORDERED and ADJUDGED that respondent have judgment and recover against petitioners the amount of $148,000, plus interest at the rate of 9% per annum from the date of December 22, 2004, as computed by the Clerk in the amount of $____, together with costs and disbursements in the amount of $_____ as taxed by the Clerk, for the total amount of $_____, and that the respondent have execution therefor.

Dated: 4/14/05

ENTER:

MARILYN SHAFER
J.S.C.

UNFILED JUDGMENT
This judgment has not been entered by the County Clerk and notice of entry cannot be served based hereon. To obtain entry, counsel or authorized representative must appear in person at the Judgment Clerk's Desk (Room 141B).