

**ST. JOHN'S UNIVERSITY SCHOOL OF LAW and
The FINANCIAL INDUSTRY REGULATORY AUTHORITY**

***The 2010 Second Annual*
SECURITIES DISPUTE RESOLUTION TRIATHLON PROBLEM***

Smith vs. Morill aka Where Eagles Dare to Fly

BACKGROUND INFORMATION:

The numbers and types of investors who have been injured by the ongoing financial crisis know no bounds: the young and old; the poor and the rich; the unsophisticated and sophisticated. Are additional safeguards needed to forestall further casualties and promote responsible investing and investment advisement, or are these casualties just part of the inherent risks and vagaries of investing?

Meet Dr. Taylor Smith and Randy Morill, next-door neighbors living in the upscale community of Pleasantville, U.S.A. Pleasantville is a bedroom community where houses sit on two-acre lots, luxury cars adorn the three-car garage driveways, and the American dream appears to be realized. Morill, a forty-six year old securities broker at a small firm, Champion Investment Corp. (Champion), lives with (his)(her) second spouse, seventeen-year-old son, fifteen-year-old stepdaughter and a nine-year-old Airedale terrier. Dr. Smith, also forty-six, is a single parent who lives with (his)(her) three children: a daughter, age fifteen and twin sons, age seventeen. Smith is a dermatologist in a local medical practice. Although Smith and Morill are not social friends, they have been friendly neighbors for over thirteen years, offering cups of sugar, hammers and mail pick-up as needed. Their children share school and extracurricular activities.

Dr. Smith takes great pride in (his)(her) three children and wants to give them the best education money can buy. They are all fine students, and Dr. Smith intended to send them to top private colleges. This choice comes at a hefty price. By the time the Smith children graduate, their education could easily cost Dr. Smith \$750,000. Dr. Smith earns \$350,000 a year.

On January 1, 2005, Dr. Smith realized that the \$500,000 (s)he had saved would not fully cover the anticipated educational expenses for (his)(her) three children. At that time, the stock market was doing well, and Dr. Smith wanted to share in the profits. (S)he had the \$500,000 invested in U.S. Treasury Bonds earning about 3.5% interest each year. Dr. Smith made a New Year's resolution to make more money by investing in the stock market. Dr. Smith knew that Morill was a securities broker at a small investment firm, and appeared to be successful. Smith decided to consult with Morill about some investment strategies Smith should pursue.

Following up on (his)(her) New Year's resolution later that week, Dr. Smith explained (his)(her) financial situation to Morill while Dr. Smith and Morill were shoveling the snow

off their walks. Over the next couple of months, Dr. Smith and Morill continued to have several discussions about Dr. Smith's investment goals and how Morill might effectuate them. These discussions took place on their front lawns, at their children's sporting events and even over a Saturday lunch at the local diner. Finally, in March 2005, Dr. Smith agreed to open an account at Morill's firm.

To open the account, Dr. Smith had to complete a New Account Application. (See *Attachment A*) On the New Account Application, Dr. Smith listed (his)(her) income accurately, checked "moderate" for risk tolerance and "growth" for investment objective. Dr. Smith wrote in 0 years investment experience for stock, mutual funds and options, and 10 years experience for bonds. (S)he listed (his)(her) net worth at \$5.6 million, but as follows:

House-----	Net Equity of \$1.9 million ¹
Art and collectibles-----	\$0.95 million
Whole life insurance policy-----	\$0.5 million (cash surrender value)
Medical Practice-----	\$1.4 million (goodwill)
Cash-----	\$0.6 million (cash to be deposited in the account and savings)
Retirement Account-----	\$0.25 million

Initially, with Morill's advice, Dr. Smith invested the entire \$500,000 "college fund" into the account with a 50/50 mix of relatively stable stock mutual funds and well-established stocks in the energy, technology and manufacturing sectors. Smith was very proud of (his)(her) own choice of one stock in particular, a pharmaceutical stock, Novamerc. Dr. Smith paid a total of \$10,000 in commissions on these initial trades.

From March 2005 through April 2008, Dr. Smith's total investments grew forty per cent. Dr. Smith was excited and believed that Morill walked on water. During this time, Dr. Smith didn't really check the monthly statements; (s)he simply opened them and looked at the account value. Dr. Smith didn't think (s)he needed to look at anything else; (s)he would see Morill on a regular basis. Morill always smiled, a gesture interpreted by Dr. Smith as an assurance that everything was okay. During this time, Dr. Smith didn't deposit or withdraw any money from (his)(her) account.

By April 2008, Dr. Smith's investments were worth \$700,000. Dr. Smith saw Morill at a soccer game, and they made small talk. Morill remarked that the market was doing really well. Then, to Dr. Smith's horror, from mid-2008 until February 2009, Dr. Smith's investments tanked. Each month, (s)he saw the account go down a little more. By February 2009, the account dropped to \$350,000.

By this point, the twin boys were planning on attending very expensive colleges, and Dr. Smith's daughter had her eye on an Ivy League College. Dr. Smith knew that (his)(her) main other assets had declined in value, and (s)he did not want to surrender the life

¹ The appraisal value of the house at this time was \$2,878,000, and there was a newly refinanced fifteen year adjustable mortgage on the house of \$978,000.

insurance or give up the house in which the children had been raised. (S)he explained all this to Morill, telling Morill that (s)he was concerned about paying for schooling, and asked Morill to help find a solution.

Among the investment ideas Morill discussed with Smith were private placements. Also known as private financing or private investing, private placements are a method of raising capital for a business, particularly small firms. Morill told Dr. Smith about private placements, explaining that the companies did not register their securities because they were exempt from registration; and the securities were often sold to "accredited" investors, who were wealthier than the average investor. Dr. Smith told Morill (s)he was interested in learning more about this type of investment.

In early March 2009, Morill suggested that Dr. Smith might wish to invest in the private placement of securities of an exciting new company, Wings of Eagles, which was being offered pursuant to Rule 506 of Regulation D of the Securities Act of 1933. Wings of Eagles, as the name implies, manufactured private jets. Morill explained to Dr. Smith why this was such a unique opportunity. Since so few companies actually manufactured private jets, Wings of Eagles had very little competition. Wings of Eagles had already set up a factory and had begun manufacturing the jets. Although Wings of Eagles had not yet secured a strong market share in its three years of business, this promising company reported that it already had eager customers lined up including several, unnamed celebrities and real estate moguls.

Morill explained to Dr. Smith that because the market was down, Dr. Smith could buy low and have an opportunity to earn greater profits when the market rebounded. That was just what Dr. Smith wanted. Morill also told Dr. Smith that "there are no sure things, just exciting opportunities." Morill further advised Dr. Smith that Morill's firm was investing in Wings of Eagles. This particular investment was sold in lots of \$50,000 and required a minimum investment of \$500,000. Dr. Smith only had \$350,000 in (his)(her) account. Investors were also required to have a minimum net worth of \$5 million. Morill gave Dr. Smith a copy of the Private Placement Memorandum. Dr. Smith read the first page of the Memorandum, taking note of the following two clauses:

- There is no public market for the securities being offered, and no such market is expected to develop following this offering.
- The shares offered hereby are speculative and investment in stock involves a high degree of risk. Investors must be prepared to bear the economic risk of their investment for an indefinite period and be able to withstand a total loss of their investment.

After some consideration, Dr. Smith thought this was such a great opportunity, (s)he decided to invest \$600,000 even though (s)he only had \$350,000 in (his)(her) account. Morill also informed Dr. Smith that (s)he had to pay an upfront commission on the Wings of Eagles investment of 3.5%, or \$21,000 for a \$600,000 investment.

To put together the total amount Dr. Smith needed for the investment and commissions, Dr. Smith liquidated (his)(her) entire remaining portfolio of \$350,000. (S)he then paid a total of \$9,000 in commissions for the sales, netting \$341,000. Smith then raised an additional \$280,000 by selling a large share of (his)(her) art collectibles. To complete (his)(her) investment in Wings of Eagles, Dr. Smith had to fill out a "Qualified Purchaser Questionnaire" which asked information about Dr. Smith's income and net worth. Dr. Smith told Morrill that although (his)(her) income was the same as when the account was opened, (his)(her) net worth had dropped to \$3.4 million. Dr. Smith explained to Morill that with the market decline, the values of (his)(her) house, (his)(her) art and collectibles and (his)(her) medical practice had also declined and were estimated to be valued as follows:

House-----	Net Equity of \$0.8 million
Art and collectibles-----	\$0.15 million
Whole life insurance policy-----	\$0.55 million (cash surrender value)
Medical Practice-----	\$0.9 million (goodwill)
Cash-----	\$0.7 million (cash in the account, including the proceeds from the liquidated collectibles and savings)
Retirement Account-----	\$0.3 million

When Dr. Smith asked Morill if he could use the financial information Smith had originally provided on Smith's original Account Application, Morill told Smith, "It's up to you." If Dr. Smith didn't complete the questionnaire, (s)he would not be able to invest in the private placement. By signing the Qualified Purchaser Questionnaire, Dr. Smith certified to the following (which was printed in 12-point font in bold immediately above the signature line):

- (a) I have read the Private Placement Memorandum of the Company (Wings of Eagles) and understand and accept the risks associated with an investment in the Securities;
- (b) I am aware that the offering of Securities involves securities for which no market exists, thereby requiring any investment to be maintained for an indefinite period of time;
- (c) I acknowledge that any delivery to me of the Private Placement Memorandum relating to the Securities prior to the determination by the Company of my suitability as an investor shall not constitute an offer of Securities until such determination of suitability shall be made; and
- (d) My answers to the foregoing questions are true and complete to the best of my information and belief, and I will promptly notify the Company of any changes in the information I have provided.

On March 30, 2009, Dr. Smith purchased 12,000 shares of Wings of Eagles at an initial purchase price of \$50 per share, for a total purchase of \$600,000. (S)he paid the \$21,000 commission on the purchase to Morill's firm. Morill's share of the commission

was \$10,000. Between April of 2009 and January of 2010, Dr. Smith's account statement showed that the investment was worth \$600,000.

In February of 2010, Wings of Eagles suddenly collapsed. Dr. Smith lost (his)(her) entire investment of \$600,000. To make matters worse, Champion, which had also invested in the deal, collapsed as well. What had happened? Searching for an explanation, Dr. Smith scoured the financial press and the web. Several articles stated that Wings of Eagles had had an increasingly difficult time collecting its account receivables, had lost its bank financing and had run out of funds to continue to operate.

In April, 2010, Dr. Taylor Smith filed a claim against (his)(her) broker, Randy Morill, with FINRA, asking for \$600,000 for the loss of the investment, \$21,000 in paid commissions and attorney's fees. (See *Attachments B (Statement of Claim) and C (Claimant's Submission Agreement)*) In (his)(her) answer, Morill denied all of the claims, and asked that the complaint be expunged from (his)(her) CRD (Central Registration Depository) record.² (See *Attachments D (Statement of Answer) and E (Respondent's Submission Agreement)*)

During prehearing discovery, it was learned that Champion had performed due diligence of Wings of Eagles; it had received a large fee for lining up investors and supervising the private placement; and had documents in its files indicating an awareness and some concerns about problems with Wings of Eagles' receivables. (See *Attachment F*)

Factual Context For Each Round

Negotiation: Facts as written.

Mediation: Parties are mediating because they have reached an impasse in negotiations. The impasse was caused, in part, by intense emotions and different risk assessments.

Arbitration: Parties are arbitrating because they have reached an impasse in mediation. The impasse was caused, in part, by disagreement about the issue of expungement.

The question to be addressed in arbitration is: *Whether Morill knowingly, recklessly or negligently made an unsuitable recommendation to Dr. Smith?*

* This problem was developed by the St. John's Law School/FINRA Triathlon Problem Committee: Kenneth L. Andrichik, Lisa Catalano, Elayne E. Greenberg, Paul F. Kirgis, Christine Lazaro and Nicholas R. Weiskopf

² See <http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p117540.pdf> for information about expungement.

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Private Facts for Randy Morill

How did you get yourself into this mess! You did almost everything according to the book. You have an impeccable CRD (Central Registration Depository) record. During the twenty five years you've been a broker, you've kept applying much of what you've learned in training. ABC...Always Be Closing. Family, friends and neighbors are all potential clients. Yes, Dr. Taylor Smith is your neighbor and client. And, you've been successful. You've managed to weather other downturns, several market crashes, and even your stormy first divorce that halved your net worth.

Somehow this seems different. Of course, all investors love you when the market makes them money, and hate you when they suffer the inevitable losses. The original mix of stocks and mutual funds were entirely appropriate for Dr. Smith. It's not like Dr. Smith was a novice - after all, wasn't Novamerc (his)(her) idea?

You wouldn't have recommended the private placement investment if Dr. Smith didn't ask for it. Even though Dr. Smith didn't have the \$5 million net worth, (s)he was still an accredited investor as defined by Regulation D. It is also true that you weren't familiar with all the particulars of the investment. However, you were familiar with other similar private placements.

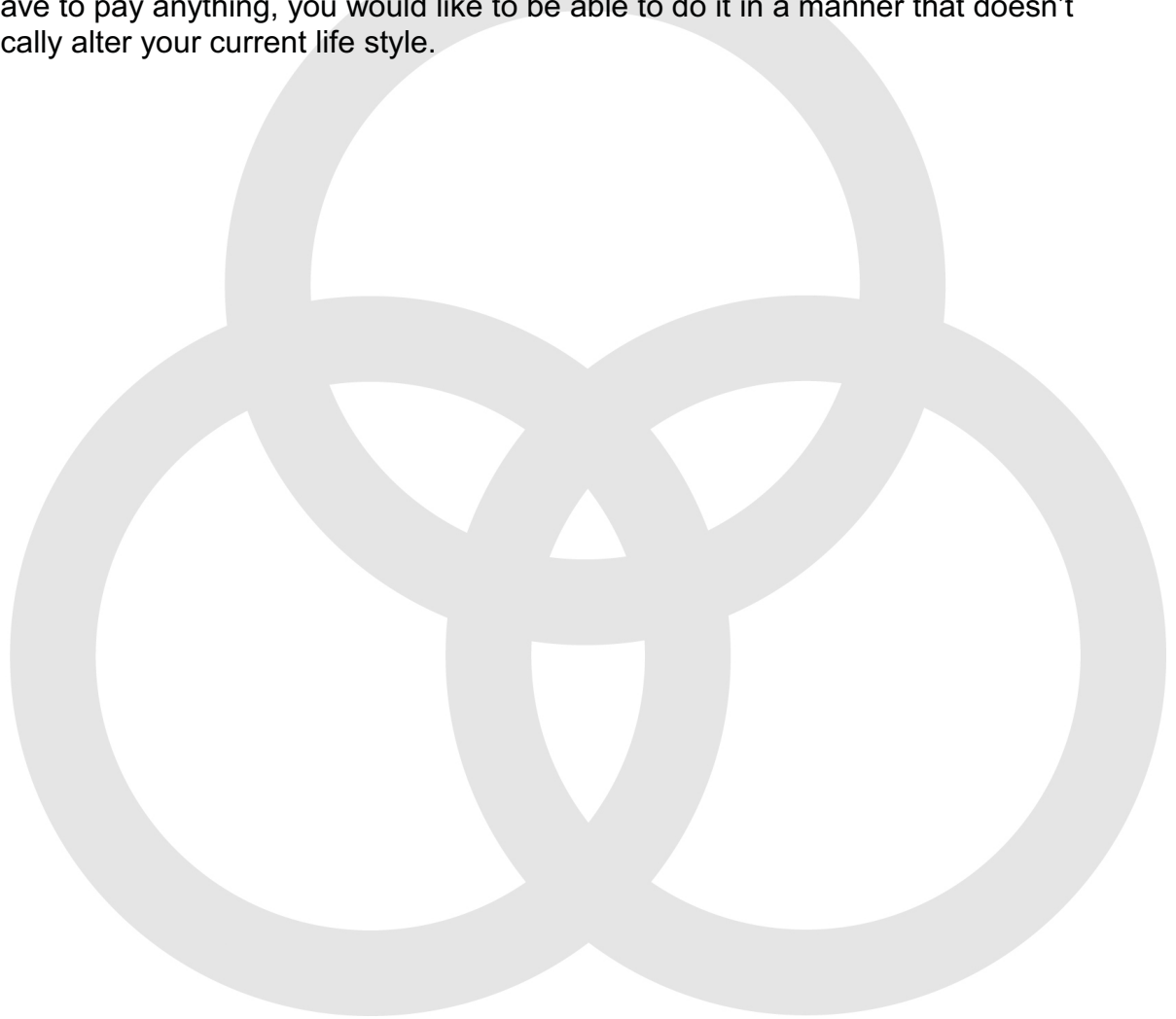
Besides, Dr. Smith was given the private placement memorandum to read, and Dr. Smith signed the Qualified Purchaser Questionnaire. The private placement memorandum informed about the volatility of the investment and specifically warned that an investor can lose their entire investment. It was right there in black and white! Your firm even invested its own money in Wings of Eagles. Surely, it was reasonable for you to believe that Champion performed its own due diligence about this investment as it was required to do.

You knew nothing about the receivables problem when Dr. Smith made (his)(her) investment in Wings of Eagles. It wasn't until Champion collapsed and you read the news that you learned that Champion knew that Wings of Eagles may not have properly reported its receivables.

You understand doctors like Dr. Smith. Some doctors view themselves like God and absolve themselves of all responsibility. It's so much easier to blame others than to take any responsibility. But are you really to blame for a game of risk?

You now are working with a new brokerage firm and are earning an income of about \$140,000 per year, way below what you used to make. Definitely, you are not making enough to pay your maintenance obligations to your first spouse, your financial obligations to your current family and the upcoming college tuition obligations for your seventeen year old son. How fortunate that you still have your house and a nest egg of \$1,400,000. Better times and a family inheritance created this buffer.

At the time of the incident in question, you had no insurance that would cover claims brought against you by your clients such as Dr. Smith, and you still do not have such insurance. Ideally, you would like to pay out nothing and preserve your pristine record. If you have to pay anything, you would like to be able to do it in a manner that doesn't drastically alter your current life style.



NEW ACCOUNT APPLICATION



Account Type:

Individual Account

Joint Account (more than one account holder)

Applicant Information

Mr. Mrs. Ms. Dr. **Suffix** Sr. Jr.

Taylor _____ Middle Name _____ Smith _____
First Name Middle Name Last Name

225 Pleasantville Road _____
Permanent Address

Pleasantville _____ USA _____ 11111 _____
City State ZIP Code

555-555-5555 _____ 555-999-9999 _____
Work Phone Home Phone

Are you:

Single Married Domestic Partner Divorced Widowed Number of Dependents: 3

Are you currently:

Employed Self-Employed Not Employed Retired Student

Dermatologist _____
Occupation

Household Financial Background

ANNUAL INCOME (from all sources)	NET WORTH	NET WORTH DETAILS
<input type="checkbox"/> \$25,000 and under	<input type="checkbox"/> \$25,000 and under	House - \$1.9 Million
<input type="checkbox"/> \$25,001-50,000	<input type="checkbox"/> \$25,001-50,000	Art & Collectibles - \$0.95 Million
<input type="checkbox"/> \$50,001-100,000	<input type="checkbox"/> \$50,001-200,000	Whole Life Insurance Policy - \$0.5 Million
<input type="checkbox"/> \$100,001-250,000	<input type="checkbox"/> \$200,001-500,000	Medical Practice (Good Will) - \$1.4 Million
<input checked="" type="checkbox"/> \$250,001-500,000	<input type="checkbox"/> \$500,001-1,000,000	Cash (including savings) - \$0.6 Million
<input type="checkbox"/> Over \$500,000	<input type="checkbox"/> \$1,000,001-3,000,000	Retirement Account - \$0.25 Million
	<input checked="" type="checkbox"/> Over \$3,000,000	

Risk Tolerance

- Conservative.** I want to preserve my initial principal in this account, with minimal risk, even if that means this account does not generate significant income or returns and may not keep pace with inflation.
- Moderately Conservative.** I am willing to accept low risk to my initial principal, including low volatility, to seek a modest level of portfolio returns.
- Moderate.** I am willing to accept some risk to my initial principal and tolerate some volatility to seek higher returns, and understand I could lose a portion of the money invested.
- Moderately Aggressive.** I am willing to accept high risk to my initial principal, including high volatility, to seek high returns over time, and understand I could lose a substantial amount of the money invested.
- Significant Risk.** I am willing to accept maximum risk to my initial principal to aggressively seek maximum returns, and understand I could lose most, or all, of the money invested.



Investment Objective

- Income
- Growth
- Aggressive Growth
- Tax Deferral
- Speculation

Financial Investment Experience

Investment	Years experience
Mutual Funds	_____ 0 _____
Individual Stocks	_____ 0 _____
Options	_____ 0 _____
Bonds	_____ 10 _____

Agreement to Arbitrate

You agree to submit to arbitration any dispute between you and CIC and/or any of its officers, directors, employees or agents relating to your brokerage account(s). Any arbitration under this agreement will be conducted under the arbitration rules of FINRA Dispute Resolution. Arbitration may be initiated by either of us serving written notice on the other. The arbitrators' ruling will be final and judgment on it may be entered in any court of competent jurisdiction.

No person shall bring a putative or certified class action to arbitration, nor seek to enforce any predispute arbitration agreement against any person who has initiated in court a putative class action; or who is a member of a putative class action who has not opted out of the class with respect to any claims encompassed by the putative class action until: (i) the class certification is denied; or (ii) the class is decertified, or (iii) the customer is excluded from the class by the court. Such forbearance to enforce an agreement to arbitrate shall not constitute a waiver of any rights under this agreement except to the extent stated herein.

This agreement contains a predispute arbitration clause. By signing an arbitration agreement the parties agree as follows:

- (A) All parties to this agreement are giving up the right to sue each other in court, including the right to a trial by jury, except as provided by the rules of the arbitration forum in which a claim is filed.**
- (B) Arbitration awards are generally final and binding; a party's ability to have a court reverse or modify an arbitration award is very limited.**
- (C) The ability of the parties to obtain documents, witness statements and other discovery is generally more limited in arbitration than in court proceedings.**
- (D) The arbitrators do not have to explain the reason(s) for their award.**
- (E) The panel of arbitrators will typically include a minority of arbitrators who were or are affiliated with the securities industry.**
- (F) The rules of some arbitration forums may impose time limits for bringing a claim in arbitration. In some cases, a claim that is ineligible for arbitration may be brought in court.**
- (G) The rules of the arbitration forum in which the claim is filed, and any amendments thereto, shall be incorporated into this agreement.**

Signatures

Dr. Taylor Smith
Primary Applicant Name (please print)

Taylor Smith

Primary Applicant Signature

3/15/05

Date

of \$5 million. When Dr. Smith first opened (his) (her) account with Champion, (s) he had a net worth of \$5.6 million which was reflected on the New Account Application completed in March 2005; however, with the losses in the account, and the tough housing market, Dr. Smith's net worth had declined to \$3.4 million by February 2009. With Morill's acquiescence, Dr. Smith completed the questionnaire with the information that Dr. Smith had provided to Champion in 2005.

Between March 2009 and February 2010, everything seemed to be going fine. The account held steady at \$600,000. However, out of the blue in February 2010, Wings of Eagles went out of business. It seems that Wings of Eagles was having an increasingly difficult time collecting its accounts receivables, had lost its bank financing and had run out of funds. Overnight, Dr. Smith's account went from \$600,000 to \$0. Shortly thereafter, Champion went out of business as well.

Pursuant to FINRA Rule 2310, Morill was required to have reasonable grounds for believing that Wings of Eagles was a suitable investment for Dr. Smith. Pursuant to FINRA Regulatory Notice 10-22, Morill was obligated to conduct a reasonable investigation in connection with the Reg D offering.

In this case, Morill did not have reasonable grounds to believe that it was suitable to invest Dr. Smith's entire account, which represented a substantial portion of Dr. Smith's net worth, in a private placement of a single company. Moreover, Dr. Smith had indicated that (s)he had a moderate risk tolerance. As a relatively new company, Wings of Eagles was not appropriate for an investor seeking moderate risk.

Additionally, Morill knew that an investor was required to have a minimum net worth of \$5 million to qualify for the private placement, and that Dr. Smith had a net worth at the time of the purchase of only \$3.4 million. This should have been a clear sign for Morill that this was not an appropriate investment for Dr. Smith according to Wings of Eagles' own requirements.

Morill also failed to tell Dr. Smith that an investment in a private placement involved more risk than investing in stocks that are publicly traded or in stock mutual funds because there is no public market for the private placement.

RELIEF REQUESTED

Based upon the foregoing, Dr. Smith requests an award against Respondent Morill for compensatory damages in the amount of \$621,000 and all fees and costs including attorneys' fees for Morill's intentionally, recklessly and/or negligently unsuitable recommendation of a private placement offering.

FINRA ARBITRATION Submission Agreement

Claimant(s)

In the Matter of the Arbitration Between

Name(s) of Claimant(s)

Dr. Taylor Smith

and

Name(s) of Respondent(s)

Randy Morill

1. The undersigned parties ("parties") hereby submit the present matter in controversy, as set forth in the attached statement of claim, answers, and all related cross claims, counterclaims and/or third-party claims which may be asserted, to arbitration in accordance with the FINRA By-Laws, Rules, and Code of Arbitration Procedure.
2. The parties hereby state that they or their representative(s) have read the procedures and rules of FINRA relating to arbitration, and the parties agree to be bound by these procedures and rules.
3. The parties agree that in the event a hearing is necessary, such hearing shall be held at a time and place as may be designated by the Director of Arbitration or the arbitrator(s). The parties further agree and understand that the arbitration will be conducted in accordance with the FINRA Code of Arbitration Procedure.
4. The parties agree to abide by and perform any award(s) rendered pursuant to this Submission Agreement. The parties further agree that a judgment and any interest due thereon, may be entered upon such award(s) and, for these purposes, the parties hereby voluntarily consent to submit to the jurisdiction of any court of competent jurisdiction which may properly enter such judgment.
5. The parties hereto have signed and acknowledged the foregoing Submission Agreement.

Dr. Taylor Smith

Claimant Name (please print)

Taylor Smith

Claimant's Signature

April 15, 2010

Date

State capacity if other than individual (e.g., executor, trustee or corporate officer)

FINRA DISPUTE RESOLUTION, INC.

-----X
In the Matter of the Arbitration Between: :
: :
DR. TAYLOR SMITH, : FINRA Case No. 10-654321
Claimant, : :
: :
vs. : Statement of Answer
: :
RANDY MORILL, :
Respondent. :
: :
-----X

This Statement of Answer is filed on behalf of Respondent, Randy Morill, by Morill's attorneys, in response to the Statement of Claim filed on behalf of Dr. Taylor Smith.

Morill denies all liability to Claimant for the claims alleged. Dr. Smith is not the naïve, trusting investor the Statement of Claim implies. After Dr. Smith's accounts declined due to market conditions, (s) he requested that Morill find an investment that would allow Dr. Smith to recover the \$150,000 that had been lost in the account, and also make additional money. At the time, Morill's employer, Champion Investment Corp. (Champion), was working on the private placement for Wings of Eagles. Satisfied that Champion had done the requisite due diligence about the investment, Morill told Dr. Smith about the company.

In addition, Morill provided Dr. Smith with the "Qualified Purchaser Questionnaire", as well as the Private Placement Memorandum. Both documents made it clear that there was the risk that an investor could lose their entire investment. The documents also emphasized that there was no public market available for the securities, which presented additional risk to an investor. The questionnaire was also explicit in that it required an investor to have a minimum net worth of \$5 million. Dr. Smith knowingly filled out the questionnaire with stale information. Dr. Smith then signed the questionnaire, certifying that the information was correct, and also certifying that (s) he received and read the Private Placement Memorandum and understood the accompanying risks.

At the time Dr. Smith purchased the Wings of Eagles investment, Morill had no reason to believe that Wings of Eagles was in danger of collapsing. It had been in existence for three years, and was establishing a new market in private jet manufacturing. Until the company collapsed, virtually overnight, there was never any indication that the company was in danger.

Dr. Smith has failed to establish any actionable conduct on the part of Morill. The true parties to this action should be Champion and Wings of Eagles. Accordingly, Morill requests that the arbitration panel dismiss all claims, assess all fees against Claimant, and issue a recommendation for expungement pursuant to FINRA Rule 2080.

FINRA ARBITRATION Submission Agreement

Respondent(s)

In the Matter of the Arbitration Between

Name(s) of Claimant(s)

Dr. Taylor Smith

and

Name(s) of Respondent(s)

Randy Morill

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5. The parties hereto have signed and acknowledged the foregoing Submission Agreement.

Randy Morill

Respondent Name (please print)

Randy Morill

May 30, 2010

Respondent's Signature

Date

State capacity if other than individual (e.g., executor, trustee or corporate officer)

Memo to Files (2/05/09)

On the Wings of Eagles deal, I spoke to Wes, their CFO, and he admitted that the economy is hurting collections. He says over half of \$4,500,000 outstanding is "past due." I will follow up.

Ekg

Memo to BR, RR (2/24/09)

I have been tracking receivable collections in connection with the Wings placement. My up to date feed is the collections are very "soft," and that over seventy-five percent of receivables are past due—the average aging on past due is 140 days, and Wes tells me that initial down payments, and payments prior to delivery, are being increased to cover more of the total purchase price. Still, we must be careful about our position in the placement.

Ekg

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On January 1, 2005, Dr. Smith realized that the \$500,000 (s)he had saved would not fully cover the anticipated educational expenses for (his)(her) three children. At that time, the stock market was doing well, and Dr. Smith wanted to share in the profits. (S)he had the \$500,000 invested in U.S. Treasury Bonds earning about 3.5% interest each year. Dr. Smith made a New Year's resolution to make more money by investing in the stock market. Dr. Smith knew that Morill was a securities broker at a small investment firm, and appeared to be successful. Smith decided to consult with Morill about some investment strategies Smith should pursue.

Following up on (his)(her) New Year's resolution later that week, Dr. Smith explained (his)(her) financial situation to Morill while Dr. Smith and Morill were shoveling the snow

off their walks. Over the next couple of months, Dr. Smith and Morill continued to have several discussions about Dr. Smith's investment goals and how Morill might effectuate them. These discussions took place on their front lawns, at their children's sporting events and even over a Saturday lunch at the local diner. Finally, in March 2005, Dr. Smith agreed to open an account at Morill's firm.

To open the account, Dr. Smith had to complete a New Account Application. (See *Attachment A*) On the New Account Application, Dr. Smith listed (his)(her) income accurately, checked "moderate" for risk tolerance and "growth" for investment objective. Dr. Smith wrote in 0 years investment experience for stock, mutual funds and options, and 10 years experience for bonds. (S)he listed (his)(her) net worth at \$5.6 million, but as follows:

House-----	Net Equity of \$1.9 million ¹
Art and collectibles-----	\$0.95 million
Whole life insurance policy-----	\$0.5 million (cash surrender value)
Medical Practice-----	\$1.4 million (goodwill)
Cash-----	\$0.6 million (cash to be deposited in the account and savings)
Retirement Account-----	\$0.25 million

Initially, with Morill's advice, Dr. Smith invested the entire \$500,000 "college fund" into the account with a 50/50 mix of relatively stable stock mutual funds and well-established stocks in the energy, technology and manufacturing sectors. Smith was very proud of (his)(her) own choice of one stock in particular, a pharmaceutical stock, Novamerc. Dr. Smith paid a total of \$10,000 in commissions on these initial trades.

From March 2005 through April 2008, Dr. Smith's total investments grew forty per cent. Dr. Smith was excited and believed that Morill walked on water. During this time, Dr. Smith didn't really check the monthly statements; (s)he simply opened them and looked at the account value. Dr. Smith didn't think (s)he needed to look at anything else; (s)he would see Morill on a regular basis. Morill always smiled, a gesture interpreted by Dr. Smith as an assurance that everything was okay. During this time, Dr. Smith didn't deposit or withdraw any money from (his)(her) account.

By April 2008, Dr. Smith's investments were worth \$700,000. Dr. Smith saw Morill at a soccer game, and they made small talk. Morill remarked that the market was doing really well. Then, to Dr. Smith's horror, from mid-2008 until February 2009, Dr. Smith's investments tanked. Each month, (s)he saw the account go down a little more. By February 2009, the account dropped to \$350,000.

By this point, the twin boys were planning on attending very expensive colleges, and Dr. Smith's daughter had her eye on an Ivy League College. Dr. Smith knew that (his)(her) main other assets had declined in value, and (s)he did not want to surrender the life

¹ The appraisal value of the house at this time was \$2,878,000, and there was a newly refinanced fifteen year adjustable mortgage on the house of \$978,000.

insurance or give up the house in which the children had been raised. (S)he explained all this to Morill, telling Morill that (s)he was concerned about paying for schooling, and asked Morill to help find a solution.

Among the investment ideas Morill discussed with Smith were private placements. Also known as private financing or private investing, private placements are a method of raising capital for a business, particularly small firms. Morill told Dr. Smith about private placements, explaining that the companies did not register their securities because they were exempt from registration; and the securities were often sold to "accredited" investors, who were wealthier than the average investor. Dr. Smith told Morill (s)he was interested in learning more about this type of investment.

In early March 2009, Morill suggested that Dr. Smith might wish to invest in the private placement of securities of an exciting new company, Wings of Eagles, which was being offered pursuant to Rule 506 of Regulation D of the Securities Act of 1933. Wings of Eagles, as the name implies, manufactured private jets. Morill explained to Dr. Smith why this was such a unique opportunity. Since so few companies actually manufactured private jets, Wings of Eagles had very little competition. Wings of Eagles had already set up a factory and had begun manufacturing the jets. Although Wings of Eagles had not yet secured a strong market share in its three years of business, this promising company reported that it already had eager customers lined up including several, unnamed celebrities and real estate moguls.

Morill explained to Dr. Smith that because the market was down, Dr. Smith could buy low and have an opportunity to earn greater profits when the market rebounded. That was just what Dr. Smith wanted. Morill also told Dr. Smith that "there are no sure things, just exciting opportunities." Morill further advised Dr. Smith that Morill's firm was investing in Wings of Eagles. This particular investment was sold in lots of \$50,000 and required a minimum investment of \$500,000. Dr. Smith only had \$350,000 in (his)(her) account. Investors were also required to have a minimum net worth of \$5 million. Morill gave Dr. Smith a copy of the Private Placement Memorandum. Dr. Smith read the first page of the Memorandum, taking note of the following two clauses:

- There is no public market for the securities being offered, and no such market is expected to develop following this offering.
- The shares offered hereby are speculative and investment in stock involves a high degree of risk. Investors must be prepared to bear the economic risk of their investment for an indefinite period and be able to withstand a total loss of their investment.

After some consideration, Dr. Smith thought this was such a great opportunity, (s)he decided to invest \$600,000 even though (s)he only had \$350,000 in (his)(her) account. Morill also informed Dr. Smith that (s)he had to pay an upfront commission on the Wings of Eagles investment of 3.5%, or \$21,000 for a \$600,000 investment.

To put together the total amount Dr. Smith needed for the investment and commissions, Dr. Smith liquidated (his)(her) entire remaining portfolio of \$350,000. (S)he then paid a total of \$9,000 in commissions for the sales, netting \$341,000. Smith then raised an additional \$280,000 by selling a large share of (his)(her) art collectibles. To complete (his)(her) investment in Wings of Eagles, Dr. Smith had to fill out a "Qualified Purchaser Questionnaire" which asked information about Dr. Smith's income and net worth. Dr. Smith told Morrill that although (his)(her) income was the same as when the account was opened, (his)(her) net worth had dropped to \$3.4 million. Dr. Smith explained to Morill that with the market decline, the values of (his)(her) house, (his)(her) art and collectibles and (his)(her) medical practice had also declined and were estimated to be valued as follows:

House-----	Net Equity of \$0.8 million
Art and collectibles-----	\$0.15 million
Whole life insurance policy-----	\$0.55 million (cash surrender value)
Medical Practice-----	\$0.9 million (goodwill)
Cash-----	\$0.7 million (cash in the account, including the proceeds from the liquidated collectibles and savings)
Retirement Account-----	\$0.3 million

When Dr. Smith asked Morill if he could use the financial information Smith had originally provided on Smith's original Account Application, Morill told Smith, "It's up to you." If Dr. Smith didn't complete the questionnaire, (s)he would not be able to invest in the private placement. By signing the Qualified Purchaser Questionnaire, Dr. Smith certified to the following (which was printed in 12-point font in bold immediately above the signature line):

- (a) I have read the Private Placement Memorandum of the Company (Wings of Eagles) and understand and accept the risks associated with an investment in the Securities;
- (b) I am aware that the offering of Securities involves securities for which no market exists, thereby requiring any investment to be maintained for an indefinite period of time;
- (c) I acknowledge that any delivery to me of the Private Placement Memorandum relating to the Securities prior to the determination by the Company of my suitability as an investor shall not constitute an offer of Securities until such determination of suitability shall be made; and
- (d) My answers to the foregoing questions are true and complete to the best of my information and belief, and I will promptly notify the Company of any changes in the information I have provided.

On March 30, 2009, Dr. Smith purchased 12,000 shares of Wings of Eagles at an initial purchase price of \$50 per share, for a total purchase of \$600,000. (S)he paid the \$21,000 commission on the purchase to Morill's firm. Morill's share of the commission

was \$10,000. Between April of 2009 and January of 2010, Dr. Smith's account statement showed that the investment was worth \$600,000.

In February of 2010, Wings of Eagles suddenly collapsed. Dr. Smith lost (his)(her) entire investment of \$600,000. To make matters worse, Champion, which had also invested in the deal, collapsed as well. What had happened? Searching for an explanation, Dr. Smith scoured the financial press and the web. Several articles stated that Wings of Eagles had had an increasingly difficult time collecting its account receivables, had lost its bank financing and had run out of funds to continue to operate.

In April, 2010, Dr. Taylor Smith filed a claim against (his)(her) broker, Randy Morill, with FINRA, asking for \$600,000 for the loss of the investment, \$21,000 in paid commissions and attorney's fees. (See *Attachments B (Statement of Claim) and C (Claimant's Submission Agreement)*) In (his)(her) answer, Morill denied all of the claims, and asked that the complaint be expunged from (his)(her) CRD (Central Registration Depository) record.² (See *Attachments D (Statement of Answer) and E (Respondent's Submission Agreement)*)

During prehearing discovery, it was learned that Champion had performed due diligence of Wings of Eagles; it had received a large fee for lining up investors and supervising the private placement; and had documents in its files indicating an awareness and some concerns about problems with Wings of Eagles' receivables. (See *Attachment F*)

Factual Context For Each Round

Negotiation: Facts as written.

Mediation: Parties are mediating because they have reached an impasse in negotiations. The impasse was caused, in part, by intense emotions and different risk assessments.

Arbitration: Parties are arbitrating because they have reached an impasse in mediation. The impasse was caused, in part, by disagreement about the issue of expungement.

The question to be addressed in arbitration is: *Whether Morill knowingly, recklessly or negligently made an unsuitable recommendation to Dr. Smith?*

* This problem was developed by the St. John's Law School/FINRA Triathlon Problem Committee: Kenneth L. Andrichik, Lisa Catalano, Elayne E. Greenberg, Paul F. Kirgis, Christine Lazaro and Nicholas R. Weiskopf

² See <http://www.finra.org/web/groups/industry/@ip/@reg/@notice/documents/notices/p117540.pdf> for information about expungement.

**ST. JOHN'S UNIVERSITY SCHOOL OF LAW and
The FINANCIAL INDUSTRY REGULATORY AUTHORITY**

***The 2010 Second Annual*
SECURITIES DISPUTE RESOLUTION TRIATHLON PROBLEM**

Private Facts for Dr. Taylor Smith

Morill has no morals. What a snake oil salesperson! Losing the \$600,000 will make it harder to pay the cost of college. True one of the seventeen year olds just won a full scholarship to Premier Elite College. So what! You were scammed, and that sleaze ball should pay you back every cent. You want to make sure that others aren't scammed too.

You know how those sleaze balls work. First, they're nice to you, let you make some money. And you did. Then, they move in for the kill. You paid Morill a lot of money over the years in commissions; you calculated that it was a total of \$19,000 before the private placement. You didn't mind so much when you were making money, but Morill charged you the same commission on Novamerc as the other securities. That's outrageous! Novamerc was your idea. You knew the pharmaceutical business; you prescribed their drugs all the time; and you knew that they had just released a new super drug for acne. Even though you heard rumblings that the FDA was going to recall this new super drug, you still wanted to invest in Novamerc. You should have known Morill wasn't very good when (s)he didn't even mention the recall.

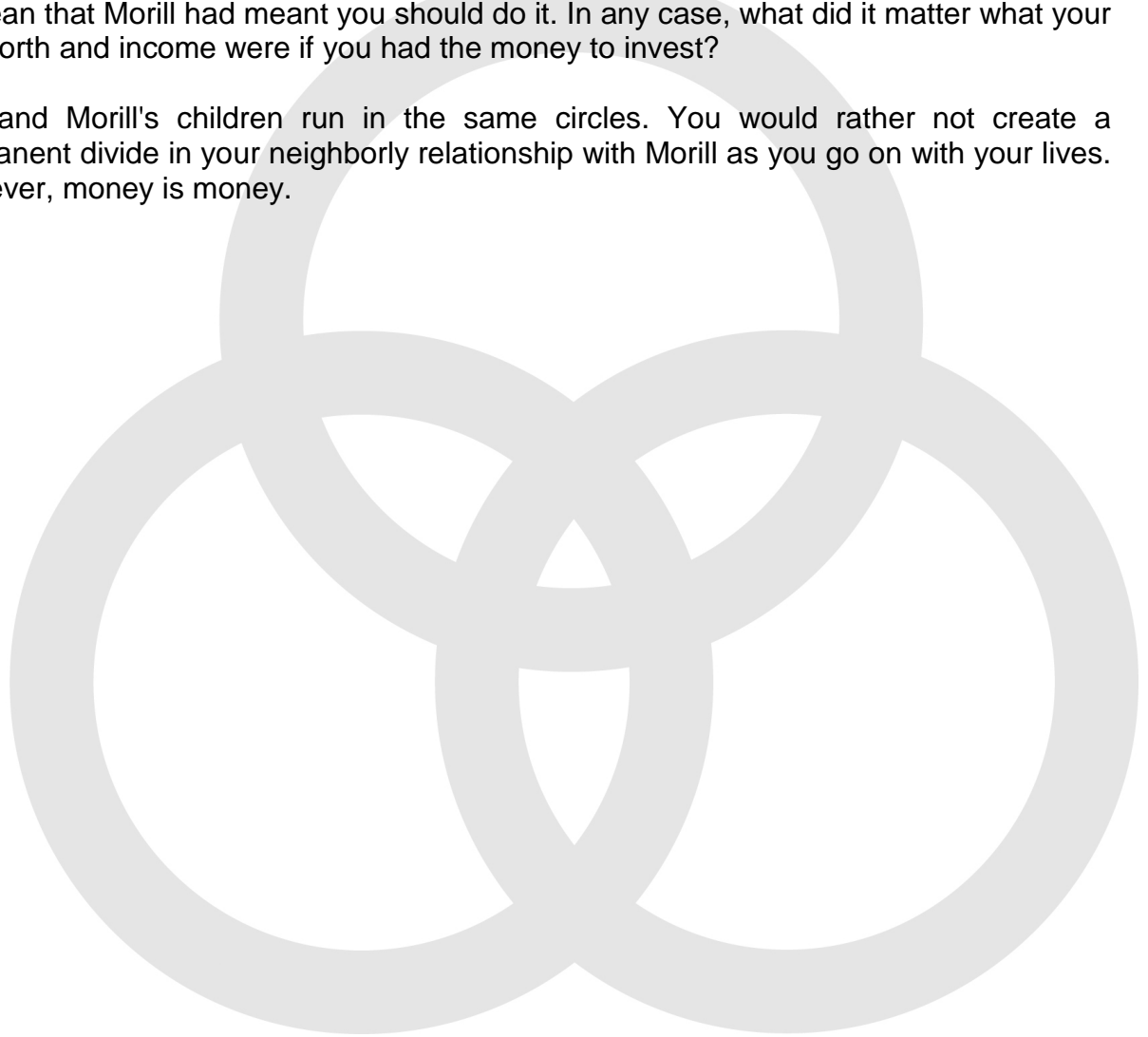
Wasn't Morill supposed to be watching the account? True, you didn't look at the account statements beyond a cursory review. Instead, you opened up the envelopes, sometimes glanced at the balance, and just put them in your desk every month. Anyhow, you saw Morill at least once a week at the kids' sporting events and in the backyard. In fact, in April 2008, you specifically remember Morill telling you everything was great. Why didn't (s)he say anything when the account started to tank? Just think of all those times you and the kids passed through Morill's yard to get to the lake, throughout the summer to go swimming and throughout the winter to go ice-skating. All those times, (s)he never said anything about improving your return or changing anything to protect your account. Why did you have to call (him)(her) and ask for help? That was humiliating.

No wonder Morill sold you the Wings of Eagles securities! Morill earned a 3.5% commission, and you lost everything. Why weren't you warned of all the risks? True, you got the private placement memorandum, but you really didn't read it. Shouldn't Morill have alerted you if there was anything important in the private placement memorandum? Wasn't that why Morill earned a commission as your broker? Wasn't Morill supposed to clarify the details? True, Morill did tell you something about private placements, but you didn't really follow what Morill was saying because (s)he liked to talk a lot and used a lot of financial jargon. Of course you didn't want to ask any

questions, because you didn't want to look stupid. Morill told you (his)(her) firm had also invested the firm's own money in Wings of Eagles. That gave you the reassurance to believe that Wings of Eagles was the way to recoup your previous failed investments and make more money.

Yes, you filled out the questionnaire, stating that you had a \$5 million net worth even though you didn't. However, your recollection is that Morill told you that you would only be able to invest in the company if you completed the paperwork and met the requisite qualifications. Although the actual words Morill used were, "It's up to you," you took that to mean that Morill had meant you should do it. In any case, what did it matter what your net worth and income were if you had the money to invest?

You and Morill's children run in the same circles. You would rather not create a permanent divide in your neighborly relationship with Morill as you go on with your lives. However, money is money.



Investment Objective

- Income
- Growth
- Aggressive Growth
- Tax Deferral
- Speculation

Financial Investment Experience

Investment	Years experience
Mutual Funds	_____ 0 _____
Individual Stocks	_____ 0 _____
Options	_____ 0 _____
Bonds	_____ 10 _____

Agreement to Arbitrate

You agree to submit to arbitration any dispute between you and CIC and/or any of its officers, directors, employees or agents relating to your brokerage account(s). Any arbitration under this agreement will be conducted under the arbitration rules of FINRA Dispute Resolution. Arbitration may be initiated by either of us serving written notice on the other. The arbitrators' ruling will be final and judgment on it may be entered in any court of competent jurisdiction.

No person shall bring a putative or certified class action to arbitration, nor seek to enforce any predispute arbitration agreement against any person who has initiated in court a putative class action; or who is a member of a putative class action who has not opted out of the class with respect to any claims encompassed by the putative class action until: (i) the class certification is denied; or (ii) the class is decertified, or (iii) the customer is excluded from the class by the court. Such forbearance to enforce an agreement to arbitrate shall not constitute a waiver of any rights under this agreement except to the extent stated herein.

This agreement contains a predispute arbitration clause. By signing an arbitration agreement the parties agree as follows:

- (A) All parties to this agreement are giving up the right to sue each other in court, including the right to a trial by jury, except as provided by the rules of the arbitration forum in which a claim is filed.**
- (B) Arbitration awards are generally final and binding; a party's ability to have a court reverse or modify an arbitration award is very limited.**
- (C) The ability of the parties to obtain documents, witness statements and other discovery is generally more limited in arbitration than in court proceedings.**
- (D) The arbitrators do not have to explain the reason(s) for their award.**
- (E) The panel of arbitrators will typically include a minority of arbitrators who were or are affiliated with the securities industry.**
- (F) The rules of some arbitration forums may impose time limits for bringing a claim in arbitration. In some cases, a claim that is ineligible for arbitration may be brought in court.**
- (G) The rules of the arbitration forum in which the claim is filed, and any amendments thereto, shall be incorporated into this agreement.**

Signatures

Dr. Taylor Smith
Primary Applicant Name (please print)

Taylor Smith

Primary Applicant Signature

3/15/05

Date

of \$5 million. When Dr. Smith first opened (his) (her) account with Champion, (s) he had a net worth of \$5.6 million which was reflected on the New Account Application completed in March 2005; however, with the losses in the account, and the tough housing market, Dr. Smith's net worth had declined to \$3.4 million by February 2009. With Morill's acquiescence, Dr. Smith completed the questionnaire with the information that Dr. Smith had provided to Champion in 2005.

Between March 2009 and February 2010, everything seemed to be going fine. The account held steady at \$600,000. However, out of the blue in February 2010, Wings of Eagles went out of business. It seems that Wings of Eagles was having an increasingly difficult time collecting its accounts receivables, had lost its bank financing and had run out of funds. Overnight, Dr. Smith's account went from \$600,000 to \$0. Shortly thereafter, Champion went out of business as well.

Pursuant to FINRA Rule 2310, Morill was required to have reasonable grounds for believing that Wings of Eagles was a suitable investment for Dr. Smith. Pursuant to FINRA Regulatory Notice 10-22, Morill was obligated to conduct a reasonable investigation in connection with the Reg D offering.

In this case, Morill did not have reasonable grounds to believe that it was suitable to invest Dr. Smith's entire account, which represented a substantial portion of Dr. Smith's net worth, in a private placement of a single company. Moreover, Dr. Smith had indicated that (s)he had a moderate risk tolerance. As a relatively new company, Wings of Eagles was not appropriate for an investor seeking moderate risk.

Additionally, Morill knew that an investor was required to have a minimum net worth of \$5 million to qualify for the private placement, and that Dr. Smith had a net worth at the time of the purchase of only \$3.4 million. This should have been a clear sign for Morill that this was not an appropriate investment for Dr. Smith according to Wings of Eagles' own requirements.

Morill also failed to tell Dr. Smith that an investment in a private placement involved more risk than investing in stocks that are publicly traded or in stock mutual funds because there is no public market for the private placement.

RELIEF REQUESTED

Based upon the foregoing, Dr. Smith requests an award against Respondent Morill for compensatory damages in the amount of \$621,000 and all fees and costs including attorneys' fees for Morill's intentionally, recklessly and/or negligently unsuitable recommendation of a private placement offering.

FINRA ARBITRATION Submission Agreement

Claimant(s)

In the Matter of the Arbitration Between

Name(s) of Claimant(s)

Dr. Taylor Smith

and

Name(s) of Respondent(s)

Randy Morill

1. The undersigned parties ("parties") hereby submit the present matter in controversy, as set forth in the attached statement of claim, answers, and all related cross claims, counterclaims and/or third-party claims which may be asserted, to arbitration in accordance with the FINRA By-Laws, Rules, and Code of Arbitration Procedure.
2. The parties hereby state that they or their representative(s) have read the procedures and rules of FINRA relating to arbitration, and the parties agree to be bound by these procedures and rules.
3. The parties agree that in the event a hearing is necessary, such hearing shall be held at a time and place as may be designated by the Director of Arbitration or the arbitrator(s). The parties further agree and understand that the arbitration will be conducted in accordance with the FINRA Code of Arbitration Procedure.
4. The parties agree to abide by and perform any award(s) rendered pursuant to this Submission Agreement. The parties further agree that a judgment and any interest due thereon, may be entered upon such award(s) and, for these purposes, the parties hereby voluntarily consent to submit to the jurisdiction of any court of competent jurisdiction which may properly enter such judgment.
5. The parties hereto have signed and acknowledged the foregoing Submission Agreement.

Dr. Taylor Smith

Claimant Name (please print)

Taylor Smith

Claimant's Signature

April 15, 2010

Date

State capacity if other than individual (e.g., executor, trustee or corporate officer)

FINRA DISPUTE RESOLUTION, INC.

-----X
In the Matter of the Arbitration Between: :
: :
DR. TAYLOR SMITH, : FINRA Case No. 10-654321
Claimant, : :
: :
vs. : Statement of Answer
: :
RANDY MORILL, :
Respondent. :
: :
-----X

This Statement of Answer is filed on behalf of Respondent, Randy Morill, by Morill's attorneys, in response to the Statement of Claim filed on behalf of Dr. Taylor Smith.

Morill denies all liability to Claimant for the claims alleged. Dr. Smith is not the naïve, trusting investor the Statement of Claim implies. After Dr. Smith's accounts declined due to market conditions, (s) he requested that Morill find an investment that would allow Dr. Smith to recover the \$150,000 that had been lost in the account, and also make additional money. At the time, Morill's employer, Champion Investment Corp. (Champion), was working on the private placement for Wings of Eagles. Satisfied that Champion had done the requisite due diligence about the investment, Morill told Dr. Smith about the company.

In addition, Morill provided Dr. Smith with the "Qualified Purchaser Questionnaire", as well as the Private Placement Memorandum. Both documents made it clear that there was the risk that an investor could lose their entire investment. The documents also emphasized that there was no public market available for the securities, which presented additional risk to an investor. The questionnaire was also explicit in that it required an investor to have a minimum net worth of \$5 million. Dr. Smith knowingly filled out the questionnaire with stale information. Dr. Smith then signed the questionnaire, certifying that the information was correct, and also certifying that (s) he received and read the Private Placement Memorandum and understood the accompanying risks.

At the time Dr. Smith purchased the Wings of Eagles investment, Morill had no reason to believe that Wings of Eagles was in danger of collapsing. It had been in existence for three years, and was establishing a new market in private jet manufacturing. Until the company collapsed, virtually overnight, there was never any indication that the company was in danger.

Dr. Smith has failed to establish any actionable conduct on the part of Morill. The true parties to this action should be Champion and Wings of Eagles. Accordingly, Morill requests that the arbitration panel dismiss all claims, assess all fees against Claimant, and issue a recommendation for expungement pursuant to FINRA Rule 2080.

FINRA ARBITRATION Submission Agreement

Respondent(s)

In the Matter of the Arbitration Between

Name(s) of Claimant(s)

Dr. Taylor Smith

and

Name(s) of Respondent(s)

Randy Morill

1. The undersigned parties ("parties") hereby submit the present matter in controversy, as set forth in the attached statement of claim, answers, and all related cross claims, counterclaims and/or third-party claims which may be asserted, to arbitration in accordance with the FINRA By-Laws, Rules, and Code of Arbitration Procedure.
2. The parties hereby state that they or their representative(s) have read the procedures and rules of FINRA relating to arbitration, and the parties agree to be bound by these procedures and rules.
3. The parties agree that in the event a hearing is necessary, such hearing shall be held at a time and place as may be designated by the Director of Arbitration or the arbitrator(s). The parties further agree and understand that the arbitration will be conducted in accordance with the FINRA Code of Arbitration Procedure.
4. The parties agree to abide by and perform any award(s) rendered pursuant to this Submission Agreement. The parties further agree that a judgment and any interest due thereon, may be entered upon such award(s) and, for these purposes, the parties hereby voluntarily consent to submit to the jurisdiction of any court of competent jurisdiction which may properly enter such judgment.
5. The parties hereto have signed and acknowledged the foregoing Submission Agreement.

Randy Morill

Respondent Name (please print)

Randy Morill

May 30, 2010

Respondent's Signature

Date

State capacity if other than individual (e.g., executor, trustee or corporate officer)

Memo to Files (2/05/09)

On the Wings of Eagles deal, I spoke to Wes, their CFO, and he admitted that the economy is hurting collections. He says over half of \$4,500,000 outstanding is "past due." I will follow up.

Ekg

Memo to BR, RR (2/24/09)

I have been tracking receivable collections in connection with the Wings placement. My up to date feed is the collections are very "soft," and that over seventy-five percent of receivables are past due—the average aging on past due is 140 days, and Wes tells me that initial down payments, and payments prior to delivery, are being increased to cover more of the total purchase price. Still, we must be careful about our position in the placement.

Ekg