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2 Phoenix, Arizona 85004-4429  
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Jesse B. Simpson State Bar No. 011099  
Daniel A. Goldfried State Bar No. 018371

Attorneys for Respondent  
James T. M. Verbic

BEFORE THE ARIZONA CORPORATION COMMISSION

WILLIAM A. MUNDELL  
Chairman  
JIM IRVIN  
Commissioner  
MARC SPITZER  
Commissioner

No. S-03435A-01-0000

**RESPONDENT'S REQUEST FOR  
A HEARING AND RESPONSE TO  
NOTICE OF OPPORTUNITY FOR  
HEARING**

In the matter of:

JAMES T. M. VERBIC  
(CRD #2125770)  
7880 N. 71st Street  
Paradise Valley, Arizona 85253

Respondent.

Respondent James T. Verbic hereby requests a hearing in this matter pursuant to A.R.S. § 44-1972 and A.A.C. R14-4306. Mr. Verbic also responds to the numbered paragraphs of the Notice of Opportunity for Hearing Regarding Proposed Order of Revocation and for Other Affirmative Action as follows:

**I. JURISDICTION.**

1. Mr. Verbic acknowledges that because he is a former licensed salesperson, the Securities Division of the Arizona Corporation Commission has jurisdiction over this matter.

Arizona Corporation Commission

**DOCKETED**

DEC 31 2001

DOCKETED BY

1 **II. RESPONDENT**

2 2. Mr. Verbic acknowledges that he became a registered securities salesman in  
3 Arizona in or around 1991. He was associated with Merrill Lynch throughout his entire  
4 career as a registered representative until his termination on January 3, 2000. He worked  
5 in Merrill Lynch's Scottsdale office. Mr. Verbic contends that his termination by Merrill  
6 was wrongful. In that regard, he has filed a claim against Merrill Lynch with the National  
7 Association of Securities Dealers. His claim is attached as Exhibit 1 to this Request for  
8 Hearing.

9 3. Mr. Verbic has not been in the securities business since his termination by  
10 Merrill on January 3, 2000. Accordingly, this matter is moot. Mr. Verbic does not agree  
11 with the characterization in the Notice of Opportunity for Hearing that the Commission  
12 has the authority to bring this action to suspend or revoke a registered representative's  
13 license once registration has expired. Moreover, even if authority exists for this action, the  
14 taxpayers of Arizona should be concerned that their scarce resources are being squandered  
15 in an enforcement action that even if successful will achieve little, if any, benefit to the  
16 public.

17 **III. FACTS**

18 3. Brenda Jo Barger is Mr. Verbic's wife. Since their marriage, Ms. Barger has  
19 continued to use her maiden name.

20 4. Mrs. Verbic's actions have not been portrayed accurately in this Notice. At no  
21 time was she attempting to hide matters from Merrill Lynch. At the hearing, Mrs. Verbic  
22 will testify as to the correct nature of her actions.

23 5. Gary M. Paster was a customer of Merrill Lynch and his accounts were serviced  
24 by Mr. Verbic. Mr. Paster also became a close personal friend of the Verbics.

1           6. Gary and Cynthia Paster were not relatives of the Verbics. They were, however,  
2 very close family friends. Mr. Paster even babysat for Mr. Verbic's children from time to  
3 time.

4           7. Gary and Cynthia Paster were not operating a bank; however, throughout the  
5 relevant time frame they sought from Mr. Verbic recommendations on investments  
6 including investments not available through Merrill Lynch; such investments included a  
7 construction loan and an investment in Mr. Verbic's music management business. Mr.  
8 Verbic reported these contacts to Merrill management. Mr. Verbic never earned any  
9 compensation in connection with these investments, Mr. Paster was repaid in full – often  
10 with interest and the arrangements were disclosed by Mr. Verbic to his broker-dealer firm,  
11 Merrill Lynch.

12           8. The statement in paragraph 8 of the Notice is incorrect. Mr. Verbic did not  
13 solicit Mr. Paster to invest \$30,000 outside of Merrill. Mr. Verbic passed along an  
14 investment opportunity pursuant to Mr. Paster's request. Mr. Verbic did not broker the  
15 loan or earn any compensation in connection with the loan.

16           9. The statement in paragraph 9 of the Notice is incorrect. Mr. Verbic was asked  
17 by Mr. Paster to seek out this type of investment and he did so at Mr. Paster's request. As  
18 stated above, Mr. Verbic did not receive any compensation in connection with Mr. Paster's  
19 loan, the loan was repaid in full with interest and the arrangement was disclosed to Merrill  
20 Lynch.

21           10. Paragraph 10 of the Notice alleges matters pertaining to Mr. Paster's state of  
22 mind. On information and belief, Mr. Verbic denies that Paster's state of mind is  
23 accurately described in paragraph 10.

24           11. Mr. Verbic denies the allegations in paragraph 11. Paster never made this loan  
25 to Verbic. The loan by Mr. Paster was to a homebuilder.  
26

1 12. As the Securities Division notes, Paster's loan to the homebuilder was repaid in  
2 full with interest. Mrs. Verbic will explain her actions at the hearing but there was never  
3 any intent to conceal anything.

4 13. Mr. Verbic denies that he recommended to Paster a second investment outside  
5 of Merrill.

6 14. Gary Paster was carefully following the developments at a public company  
7 called Nuko that was originally recommended by Mr. Verbic. Mr. Paster owned Nuko  
8 common stock. Mr. Paster had conversations directly with the senior management of  
9 Nuko. Based on those conversations, Mr. Paster learned that there was a possibility that  
10 Nuko senior management would spin out some of the assets of the company into a new  
11 company called "Internext." Based on the advice of Nuko senior management, not  
12 Mr. Verbic, Paster decided that he wished to invest in this new company which was  
13 identified under a working name "Internext." After making the decision that he wished to  
14 invest, Mr. Paster contacted Mr. Verbic and asked him how the investment could be  
15 structured. Mr. Verbic and Mr. Paster agreed on a planned structure which was never  
16 completed because Nuko never followed through on the deal and "Internext" was never  
17 created.

18 15. The allegations of paragraph 15 establish that this was an investment initiated  
19 by Mr. Paster with Robert Kondamoori. Mr. Kondamoori was not simply a promoter of  
20 Internext but was the president of Nuko. This allegation is totally inconsistent with the  
21 notion that Mr. Paster was proposing to make this investment based on Mr. Verbic's  
22 advice as opposed to his communication directly with the president of Nuko.

23 16. Although there was a signed "IOU," it was done in anticipation of a private  
24 offering of stock by the newly formed spin-off company. Mr. Verbic was actively seeking  
25 an underwriter for a private placement offering. Mr. Paster and Mr. Verbic planned to  
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1 subscribe to the offering if the offering went forward. The offering never occurred and no  
2 funds ever changed hands.

3 17. The Internext investment never occurred because senior management of Nuko  
4 never followed through on their plan to form the new company. There was never any  
5 borrowing by Mr. Verbic from Mr. Paster.

6 18. Merrill Lynch management was well aware of the proposal by senior  
7 management at Nuko to form a new company named Internext. They were also aware of  
8 Mr. Verbic's efforts to work on a private placement on behalf of Internext. There was no  
9 offer of common stock of Internext to Paster because Internext never existed. Thus, it was  
10 literally impossible for any order to buy \$50,000 worth of Internext common stock to exist  
11 since Internext itself did not exist. There was also no possibility of it being reflected on  
12 the books and records of Merrill since it never happened.

13 19. Mr. Verbic denies the allegations in paragraph 19.

14 20. Mr. Paster was a close family friend of the Verbics. He sometimes visited their  
15 home and babysat for the Verbics' children. In that context, Mr. Paster spoke to  
16 Mr. Verbic about many aspects of their respective lives over and above the account he  
17 maintained at Merrill Lynch. He learned that Mr. Verbic was starting a separate company  
18 devoted to the management of a rock and roll band. Mr. Paster had spent his career in the  
19 entertainment industry and wanted to help Mr. Verbic in his new endeavor. Both the  
20 music management business and Paster's involvement in it were disclosed to Merrill  
21 Lynch management. In that context, Mr. Paster offered to loan Mr. Verbic \$30,000.  
22 Mr. Paster's loan was paid back in full even though the music management business  
23 became defunct. Indeed, Mr. Verbic's signature on the promissory note was notarized in  
24 Merrill Lynch's offices.

25 21. Mr. Paster loaned the music management business \$30,000 in January 1999.  
26 This was not a personal loan to Mr. Verbic or his wife. It resulted from Mr. Paster's

1 strong desire to assist Mr. Verbic in getting his music management business off the  
2 ground. Mr. Paster told Mr. Verbic that he would also assist Mr. Verbic by employing his  
3 "contacts" in the entertainment field.

4 22. Mr. Verbic has no information regarding the source of funds except that  
5 Mr. Paster told him that the investments at Merrill should not be disrupted. Mr. Verbic  
6 never suggested that Paster withdraw monies from his IRA.

7 23. The Verbics repaid a portion of Mr. Paster's principal in April of 1999. Mrs.  
8 Verbic handled this aspect of the business for Mr. Verbic. Mrs. Verbic's use of her  
9 maiden name was not intended to hide anything from Merrill Lynch (she has never  
10 changed her name to "Verbic"); to the contrary, Mr. Verbic disclosed his music  
11 management business to Merrill Lynch and Mr. Paster's participation in it.

12 24. Once Mr. Paster became involved in litigation with Mr. Verbic and Merrill  
13 Lynch he refused to accept the tender of the remaining \$10,000 owed to him on the  
14 promissory note. He obviously did this in an effort to gain an advantage in his litigation  
15 against Mr. Verbic and Merrill Lynch.

16 25. Mr. Paster has released any claim with respect to the \$30,000 loan as part of the  
17 settlement of his NASD arbitration against Mr. Verbic and Merrill Lynch.

18 **IV. REVOCATION PURSUANT TO A.R.S. § 44-1962.**

19 Mr. Verbic denies that the Securities Division has shown grounds to revoke his  
20 registration as a securities salesman. Specifically, he denies that he is engaged in  
21 dishonest or unethical practices in the securities industry or that he is engaged in any effort  
22 to conceal from Merrill Lynch the transactions described herein:

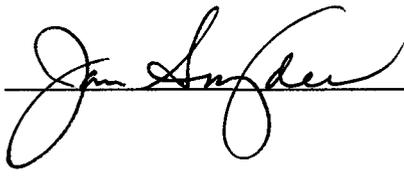
23 • Mr. Paster made a loan to a homebuilder that was completely repaid with  
24 interest. Mr. Verbic did not receive anything of value in connection with that loan. The  
25 arrangement was disclosed to Merrill Lynch.

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4 Tucson, Arizona 85701  
5 (520) 623-0341  
6 PCCN 50468/AZBN 003002  
7 Attorney for Claimant

BEFORE THE ARBITRATION TRIBUNAL.

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

8  
9 In the Matter of the Arbitration ) No. 00-04819  
10 of: )  
11 JAMES T. VERBIC, ) STATEMENT OF CLAIM FOR  
12 Claimant, ) WRONGFUL TERMINATION,  
13 and ) INTERFERENCE WITH  
14 MERRILL LYNCH, PIERCE, FENNER & ) PROSPECTIVE ECONOMIC  
15 SMITH, INC.; JOHN GEE and SUSAN ) ADVANTAGE, BREACH OF THE  
16 GEE, husband and wife, ) COVENANT OF GOOD FAITH AND  
17 Respondents. ) FAIR DEALING, INTENTIONAL AND  
18 ) NEGLIGENCE, INTENTIONAL AND  
19 ) CONTRACTUAL RELATIONS,  
20 ) INTENTIONAL INFLICTION OF  
21 ) EMOTIONAL DISTRESS AND FAILURE  
22 ) TO OBSERVE NASD RULES  
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INTRODUCTION

19 James T. Verbic was asked to lie to investigators from the American Stock Exchange by  
20 his manager, John Gee, to protect Mr. Gee and other management representatives from Merrill  
21 Lynch. He refused, told the truth and was fired. Merrill Lynch sought to protect itself and certain  
22 corrupt members of its management team by discharging Mr. Verbic, compromising a contrived  
23 claim made by a Phoenix lawyer without Verbic's approval, thereby covering up serious criminal  
24 conduct by its agents. At 32 years of age, Mr. Verbic's nine year career as a stockbroker is over.  
25 At this young age, he was earning a million dollars a year. Merrill Lynch has cost Mr. Verbic and  
26 his family millions of dollars in income. Merrill Lynch has cost James Verbic a career. All of  
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1 this was done to conceal criminal misconduct -- including forgery, obstruction of justice,  
2 conspiracy, submitting false documents to a Federal District Court, subornation of perjury and  
3 managerial incompetence within Merrill Lynch. Claimant therefore seeks compensation for his  
4 lost wages and benefits, past and future, and emotional harm in the sum \$20,000,000.00 and  
5 punitive damages in the sum of \$20,000,000.00 for a total award of \$40,000,000.00, plus  
6 attorneys fees.  
7

## 8 FACTUAL BACKGROUND

### 9 I. James T. Verbic's Background

10 James T. Verbic is 33 years of age. He attended the U.S. Military Academy at West Point  
11 for three years and was honorably discharged from the United States Army. He completed his  
12 college education at the Arizona State University in 1990 with a Bachelor's of Arts in History.  
13 Fresh out of college, Mr. Verbic was hired by Merrill Lynch as an Associate Financial Consultant  
14 in their Scottsdale office in January of 1991. He was then 23 years of age, without any prior  
15 sales or financial experience. On May 14, 1991 he took and passed his Series 7 examination.  
16 Although Mr. Verbic was issued a financial consultant number in January of 1993, he had been  
17 handling the \$40 million dollar book of the former Resident Manager of the office, William  
18 Bahney. In December of 1992 Mr. Bahney was promoted to Resident Vice-President and it was  
19 agreed that Mr. Verbic would take over his book and he eventually paid Mr. Bahney and then  
20 Merrill Lynch a total of \$50,000.00 for Mr. Bahney's book of business then worth approximately  
21 \$34,000,000.00.  
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24 Once Mr. Verbic was issued a financial consultant number in January of 1993 he became  
25 eligible for the \$100,000.00 performance based bonus known as the Merrill Lynch Certificate  
26 Program and also to participate in Merrill's Wealthbuilder and FCCAAP programs. During his  
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1 first year of production, Mr. Verbic did approximately \$610,000.00, making him the biggest  
2 producer in the Scottsdale office, as well as earning him recognition as a member of the Win  
3 Smith Fellow Club, a prestigious Merrill Lynch award. After Mr. Bahncy left the office as  
4 manager, Thomas Whalen replaced him and then was transferred out of the office and demoted.  
5 For approximately half of 1993 and all of 1994, the Scottsdale office was without an acting  
6 manager and received little supervision. In early 1995, Anthony Dechellis was appointed  
7 manager of the Scottsdale office. By this time, Mr. Verbic had a second year of production at  
8 \$850,000.00, and was on his way to a million dollar plus year in his third year, making him by far  
9 the biggest producer in the office, as well as one of the largest in the district. In 1996 Mr. Verbic  
10 produced \$1,500,000.00, in 1997 \$1,750,000.00, making him one of the top 500 producers in the  
11 firm. In 1998 he went on to produce \$2,000,000.00 and in 1999 he produced \$2,750,000.00,  
12 making him one of the top 100 producers at Merrill Lynch by the age of 32. At that time, his  
13 business was a combination of consults, new issues and stock trading. During his almost ten  
14 years at Merrill Lynch, he was never sent for any formal training of any kind by the Respondent.  
15 Indeed, except for some on the job training by his first manager, Mr. Bahney, he never received  
16 any training at all from the Respondent. At all times in his production career with Merrill Lynch  
17 from 1993 to January of 2000 Mr. Verbic was generally left to his own devices when making any  
18 decisions.  
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## 22 2. Factual Background of Dispute

23 The catalyst for Mr. Verbic's discharge was a Phoenix lawyer by the name of Wayne N.  
24 Howard, who became a client of Merrill Lynch and Mr. Verbic in April of 1997. Mr. Howard  
25 has practiced law for nearly three decades in Arizona and his wife, Lucia Howard, also a client of  
26 Mr. Verbic, is a Harvard law graduate and has practiced business law at Myers, Hendricks for  
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1 nearly 20 years . Aside from his law practice, Mr. Howard is an experienced business man. He  
2 owns and operates several nursing homes in the Tucson area and claimed to have contacts with  
3 the most successful and significant business figures in the Phoenix community. The Howards are  
4 a very sophisticated, knowledgeable couple, with significant net worth. Indeed, Mr. Howard  
5 represented to Mr. Verbic that he was worth nearly \$50,000,000.00. Mr. Howard proved to be a  
6 very aggressive, risk -taking investor, who, through deceit and fraud, sought to "set up" Mr.  
7 Verbic and Merrill Lynch when his investment strategies went bad. And, because of lack of  
8 competent management and supervisory oversight, and outright criminal behavior conducted by  
9 management in the Scottsdale offices, Merrill Lynch and ultimately Mr. Verbic, became  
10 vulnerable to Mr. Howard's tactics and strategies. Mr. Howard lost approximately \$5,000,000.00  
11 because of his investment decisions. He devised a scheme to get Merrill Lynch to make up his  
12 losses, which included suborning perjury of Mr. Verbic. Mr. Verbic refused, reported the bribe  
13 to Merrill Lynch management, but because of criminal misconduct by Merrill's own management  
14 team, Mr. Howard accomplished his goal. Merrill settled his claim and paid him \$5,000,000.00  
15 and then fired Mr. Verbic. All of this started when Mr. Howard wanted to take control of  
16 Unisource, the holding company that owned Tucson Electric Power.  
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### 20 3. Unisource Option Contracts

21 Sometime in April of 1998, Wayne Howard approached Mr. Verbic and told him that he  
22 wanted to take a "huge" position in Unisource, the holding company for Tucson Electric Power.  
23 Mr. Howard wanted to purchase a large amount of Unisource stock and 20,000 call options  
24 because he believed that the Arizona Corporation Commission<sup>1</sup> would be taking action which  
25 would allow Tucson Electric to recover significant "stranded costs" and Unisource, as a holding  
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27 <sup>1</sup>Mr. Howard is a former member of the Arizona Corporation Commission.  
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1 company, would benefit greatly. He believed, under the circumstances, that Unisource stock was  
2 significantly undervalued. The strategy was to amass a huge stock share in Unisource and  
3 become a controlling shareholder. Mr. Verbic had never been involved in a transaction of this  
4 nature or size previously. He sought the assistance of his administrative manager, Kerry Kleissle.  
5 Mr. Verbic did not believe the strategy Mr. Howard was suggesting was wise and that was  
6 confirmed when he discussed the matter with Mr. Kleissle. Both Mr. Kleissle and Mr. Verbic  
7 met with Mr. Howard to discuss his strategy and his reasons for it. Mr. Kleissle made it  
8 absolutely clear that the strategy was extremely risky and that purchasing so many option  
9 contracts could ultimately result in a complete loss since the contracts could expire worthless.  
10 Notwithstanding these admonitions, Mr. Howard insisted on proceeding with his strategy with  
11 respect to Unisource. Before Merrill Lynch would permit Mr. Howard to engage in this strategy  
12 they required him to sign a Hold Harmless letter which Mr. Verbic drafted using language  
13 suggested by Mr. Kleissle. Mr. Howard, the lawyer with almost 30 years experience, signed the  
14 Hold Harmless letter (See Exhibit 1 hereto).  
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16  
17 No one in the Scottsdale office had ever been engaged in option contract purchases of the  
18 size contemplated by Mr. Howard. None of the Merrill Lynch managers in the Scottsdale office  
19 were aware (nor did they investigate the rules) that purchasing option contracts in excess of 4500  
20 would violate NASD regulations (NASD Conduct Rule 2860) and that's exactly what happened.  
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22 Mr. Howard began purchasing the Unisource stock options in the Spring of 1998 and  
23 within a few months accumulated approximately 7,200 Unisource option contracts. At that time,  
24 NASD Conduct Rule 2860 had an option contract limit of 4,500. Mr. Howard's purchases  
25 reached this limit on September 17, 1998. The American Stock Exchange notified Merrill Lynch  
26 of the limit violation on the same date.  
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1 A month later, on or about October 8, 1998, while Mr. Verbic was in Reno on business,  
2 he received a telephone call from John Gee, his manager and Richard Pello, the compliance  
3 officer. For the first time, Verbic was informed of the Rule violation. Gee and Pello were very  
4 upset about the option contract limit violation and wanted Mr. Verbic to return and get Howard  
5 to start selling the options to get it below the 4,500 limit. At the same time, Howard was still  
6 placing buy orders, and Mr. Gee and Mr. Pello were still approving them. Mr. Verbic cut his trip  
7 short and came back to Scottsdale. From September 17, 1998 until after October, 18, 1998,  
8 Howard continued to purchase Unisource option contracts.  
9

10 Merrill Lynch and John Gee were aware of the contract limit violation in September of  
11 1998 and took no steps to stop Howard's buy orders for more Unisource options even after the  
12 American Stock Exchange demanded that the stock option overages be liquidated. At one point,  
13 however, John Gee became frantic, stating that his job, Rich Pello's and Verbic's job were on  
14 the line, that the reputation of Merrill Lynch was on the line and that Mr. Verbic had to handle  
15 the matter, it was his client. On John Gee's orders and over the objection of Howard, James  
16 Verbic began liquidating the Unisource contracts. Notwithstanding Howard's anger over having  
17 to have his Unisource contracts sold, he began a new investment strategy -- shorting Internet  
18 stocks -- in a big way.  
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21 He began with E-Bay stock, shorting approximately 7,000 shares. He then began to short  
22 sell 10,000 shares of Amazon.com and 35,000 shares of Yahoo stock on the assumption that  
23 these Internet stock were way overvalued. Unfortunately, Mr. Howard's strategy in short selling  
24 the Internet stock was a complete disaster. The stock continued to appreciate and Mr. Howard  
25 was receiving margin calls to cover his short position on the Internet stocks. The shorting of the  
26 Internet stocks was occurring the last few months of 1998. Mr. Howard, obviously concerned  
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1 about the losses he sustained on his stock strategies, devised a plan to recover his losses by trying  
2 to "set up" James Verbic and Merrill Lynch. Sometime in mid to late November of 1998, Mr.  
3 Howard began to selectively tape his telephone calls to Mr. Verbic. During the same time, upon  
4 orders of John Gee, Mr. Verbic was directed to sell stock in Mr. Howard's account to cover  
5 margin calls. Mr. Howard's losses began to mount. He had a plan which he hoped James Verbic  
6 would held him with.  
7

#### 8 4. The Phoenician Breakfast.

9 On December 23, 1998, at Mr. Howard's request, Mr. Verbic met with him for breakfast  
10 at the Phoenician hotel. At that meeting, Mr. Howard told Mr. Verbic that he would take care of  
11 him financially if he would quit Merrill Lynch and "help" him in a lawsuit he planned to bring  
12 against Merrill Lynch to cover his losses. Mr. Howard told Mr. Verbic if he quit and testified on  
13 his behalf about the poor supervision and management at Merrill Lynch he could come up with  
14 as much as a million dollars to tide him over until he got back on his feet. Mr. Verbic was  
15 shocked by this proposal, and told Mr. Howard that he couldn't respond to it, that he needed to  
16 talk to his wife, and left the Phoenician. Mr. Verbic immediately called his attorney Jay Simpson  
17 of Lewis and Roca, went to his office and relayed to Mr. Simpson what he had been told by Mr.  
18 Howard. Mr. Simpson advised him to inform Merrill Lynch of Mr. Howard's "proposal". The  
19 proposal was clearly an attempt to "buy" Mr. Verbic's cooperation and testimony in Mr.  
20 Howard's scheme to recoup his losses. James Verbic went to his office and told his manager,  
21 John Gee, of Mr. Howard's proposal. Mr. Verbic told Mr. Gee that he was extremely concerned  
22 about Mr. Howard, he did not want to quit Merrill Lynch and he did not want his job to be  
23 jeopardized because of the problems Mr. Howard was having. John Gee assured Mr. Verbic that  
24 he and the District Manager, Herschell Parent, would protect him and for him not to worry. Mr.  
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LAW OFFICES OF  
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1 Gee informed Mr. Verbic that he had talked with Mr. Parent, everything was going to be fine and  
2 for him not to worry about it. However, Mr. Howard continued to surreptitiously tape telephone  
3 conversations, both with John Gee and Mr. Verbic after the meeting at the Phoenician through  
4 January 7, 1999. On January 11, 1999, Mr. Howard's attorney sent Merrill Lynch a letter to  
5 cease all activity in Wayne Howard's account. On April 28, 1999 Wayne Howard filed a  
6 Statement of Claim with the NASD against Merrill Lynch, James Verbic and his wife Brenda  
7 Verbic, Richard Pello and his wife Lee Pello, and Kerry Kleissle and his wife Mary Kleissle,  
8 claiming damages in excess of \$5,000,000.00. Merrill Lynch hired Janet Lord of the law firm of  
9 Fennemore Craig to defend itself and the Verbics, Pellos and Kleissles in the Howard claim.  
10 Although James Verbic had asked Gee to have Merrill hire Jesse B. Simpson of the law firm of  
11 Lewis and Roca to represent him and his wife, Merrill refused. Mr. Simpson had represented Mr.  
12 Verbic before the NASD in another arbitrations and was trusted by the Verbics. Until late in  
13 1999, Ms. Lord confided in both James Verbic and Jay Simpson not to worry about the Howard  
14 claim, it was defensible.

##### 17 5. The Gary and Cynthia Paster Claims

18 In July of 1999, Gary and Cynthia Paster filed a statement of claim with the NASD  
19 against Merrill Lynch and James Verbic. One of their claims was that Mr. Verbic conducted  
20 business with them outside of Merrill Lynch. In Merrill Lynch's response to the claim, it denied  
21 that it was improper for its financial consultants to engage in business with clients "outside" of  
22 Merrill Lynch. Moreover, Mr. Verbic was questioned at length about the allegations in the Paster  
23 Statement of Claim with Merrill management and traveled to New York and discussed the case  
24 with Merrill's lawyers (and top management) and was assured by his manager, respondent Gee  
25 not to worry about the claim. However, after he refused to lie for Mr. Gee, as described below,  
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1 Merrill Lynch cites claims made in the Paster matter as a basis for his termination.

2 **6. November 1999: The Forging of Stephen Callahan's Signature by Merrill Lynch**  
3 **and Submitting Forged and False Documents to Federal District Court.**

4 In November of 1999, the Howard's NASD claim against Merrill, Pello, Verbic and  
5 Kleissle had been pending approximately seven months. On November 5, 1999, another broker  
6 in the Scottsdale office, Stephen A. Callahan, quit and went to work for Paine Webber. Mr.  
7 Callahan had worked for Merrill Lynch since October of 1992. One day in March of 1999, when  
8 Mr. Callahan came to work, he found a Financial Consultant Employment Agreement and  
9 Restrictive Covenant on his chair for his signature. The agreement prohibits a broker from  
10 taking his "book", his clients, if he leaves the firm. He told both John Gee and Richard Pello  
11 that he would not sign the document. He also informed Mr. Gee's secretary, Laurie Lopez, who  
12 had previously informed Mr. Callahan that she had gone through all the files to see who had not  
13 signed the agreement and was requesting that everyone who had not previously signed do so. On  
14 Friday, November, 5, 1999, Mr. Callahan quit Merrill Lynch. On Monday, November 8, 1999,  
15 Merrill Lynch filed a Complaint against Mr. Callahan in the United States District Court in  
16 Phoenix obtaining a Temporary Restraining Order prohibiting him from contacting his clients  
17 from Merrill Lynch. Attached to the Complaint was a copy of a Financial Consultant  
18 Employment Agreement and Restrictive Covenant signed by Mr. Callahan. Also attached was an  
19 Affidavit signed, under oath, by Richard Pello ostensibly attesting to the authenticity of the  
20 Agreement. That must have been a busy weekend for Mr. Gee and Mr. Pello. Mr. Callahan's  
21 signature was forged on the Agreement by using a computer and scanner.

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25 Attorneys for Mr. Callahan hired a questioned document examiner, William J. Flynn, to  
26 analyze the "Agreement" and Mr. Callahan's signature. Mr. Flynn concluded that Mr. Callahan's  
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1 signature on the Employment Agreement was "lifted" or "scanned" from another document that  
2 Callahan had signed years before. The "Agreement" Merrill Lynch had submitted to Federal  
3 Court was a forgery; the Affidavit submitted to the Court was also false (see Exhibit 2 hereto,  
4 Defendant's Motion for Forfeiture, etc.). On November 15, 1999, after their fraud was exposed,  
5 Merrill Lynch dismissed the Federal suit against Stephen Callahan and thereafter paid him a  
6 substantial sum of money to settle his claim against Merrill Lynch for the fraud/forgery. The FBI  
7 began an investigation of the forgery. To add to Gee, Pello and Merrill's problems, the  
8 American Stock Exchange lawyers wanted to interview James Verbic regarding the Unisource  
9 stock option limit violation.  
10

11  
12 **7. The American Stock Exchange Investigation of the Unisource Stock  
Option Limit Violation.**

13 On November 15, 1999, the same day the *Callahan* suit was dismissed by Merrill Lynch,  
14 Mr. Verbic was informed by Richard Pello that the American Stock Exchange lawyers wanted to  
15 interview him regarding the Unisource option contract limit violation. John Gee was worried  
16 about this investigation. Neither he nor Pello had done anything to correct the situation when  
17 they were first notified of the limit violation. Gee began to meet with Mr. Verbic regarding the  
18 Unisource matter and his impending interview with the American Stock Exchange investigators.  
19

20  
21 **8. John Gee and James Verbic: What Happens When You Won't Lie For  
Your Boss.**

22 When John Gee became manager of the Scottsdale office, he became Mr. Verbic's  
23 mentor and Verbic his profit center. Mr. Verbic was the Scottsdale office's biggest producer. He  
24 had record years in both 1998 and 1999. Indeed in November 1999, he had a record month.  
25 John Gee was, for the entire period of time, effusive with his praise for Mr. Verbic. Almost on a  
26 daily basis he would send Mr. Verbic little notes telling him what a great day he had or that he  
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28

1 was "the man". There were constant celebrations, trips to Las Vegas, dinners, the  
2 congratulations were continuous. Indeed, not only was John Gee positive about how the *Howard*  
3 matter would turn out, so was Merrill's lawyer, Janet Lord who was representing the Verbics,  
4 Merrill Lynch, the Pellos, and the Kleissles. However, in December of 1999 things started to  
5 change. The American Stock Exchange interview had been scheduled and John Gee wanted to  
6 make sure Mr. Verbic would be a "team" player and protect him, Richard Pello, and Merrill  
7 Lynch.  
8

9 Mr. Gee had several meetings with Mr. Verbic regarding how he should testify during the  
10 AMEX interview. Mr. Gee wanted Mr. Verbic to lie about Mr. Gee and Mr. Pello's involvement  
11 in resolving the Unisource stock option limit violation. He wanted Mr. Verbic to falsely testify  
12 that Mr. Gee and Mr. Pello were instrumental in resolving the problem once they became aware  
13 of it, that they acted promptly and provided adequate supervision and oversight. The truth was  
14 altogether different. Neither Mr. Gee nor Mr. Pello provided any supervision or help to Mr.  
15 Verbic in dealing with Mr. Howard and the Unisource violation. Mr. Gee told Mr. Verbic to  
16 handle the problem, it was his client, it was his problem, get it solved. He failed to provide any  
17 supervision. Indeed, after Merrill was notified of the contract limit violation, Mr. Howard was  
18 still allowed to purchase an additional two thousand(2000) contracts.  
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21 During these meetings, Mr. Gee made it very clear that he had protected Mr. Verbic, that  
22 it was he that was responsible for Mr. Verbic having his job there, protecting him in the *Howard*  
23 and other cases and that he would continue to protect him and his job if he remained a "team"  
24 player. Mr. Gee's parting words to Mr. Verbic at each of these meetings was always "you protect  
25 me and Merrill and I'll protect you".  
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1                   **9. The AMEX Interview - December 8, 1999.**

2                   Mr. Verbic and his wife Brenda had gone to Chicago Thanksgiving and were to have  
3 returned several days before the scheduled interview. Mrs. Verbic got sick with the flu, was  
4 hospitalized and didn't return until December 2, 1999. On December 7, 1999, Mr. Verbic  
5 received a fax late in the day with questions that he would likely be asked by the AMEX  
6 investigators. The fax was sent by Merrill's attorney, Janet Lord.. The next day, December 8,  
7 1999, Mr. Verbic went to Ms. Lord's office where the telephonic interview by the AMEX  
8 lawyers took place. Participants in the interview included Janet Lord and Nicholas Piccinini,  
9 house counsel for Merrill Lynch, James Verbic and American Stock Exchange lawyers William  
10 Janis and Stephen Patti. The interview lasted over an hour and Mr. Verbic answered truthfully  
11 all the questions put to him. He did not provide the testimony Mr. Gee wanted. When Mr.  
12 Verbic was asked what management had done to resolve the Unisource problem, he testified  
13 truthfully. He did not lie for Gee or Merrill Lynch. Mr. Verbic answered the questions honestly  
14 and truthfully and to the best of his ability. When the interview was concluded, Mr. Verbic went  
15 back to his office, worked for a few hours and then left. The next morning Verbic wasn't at work  
16 ten minutes, when Janet Lord arrived at his office, shut the door, and began to berate him as "not  
17 a team player" a terrible witness and that he had done his staunchest supporter, John Gee, a very  
18 big disservice as well as Merrill Lynch. She went on like that for a good hour, left his office,  
19 went to John Gee's office and spent several hours in his office. From that date forward until  
20 January 3, 2000, Mr. Gee never spoke another word to Mr. Verbic. Mr. Verbic called Mr. Gee  
21 repeatedly, invited him to his Christmas party, nothing. On January 3, 2000, less than a month  
22 after he testified for the American Stock Exchange, Mr. Verbic was called into Mr. Gee's office  
23 and fired.  
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1 discharge was in breach of his employment contract with Respondent Merrill Lynch. The  
2 discharge was wrongful and in violation of the implied covenant of good faith and fair dealing  
3 and furthermore was done intentionally and in bad faith.

4  
5 2. Respondent's discharge of the Claimant was wrongful and in contravention of the  
6 public policy and laws of the State of Arizona. Respondent Merrill Lynch's acts as set forth  
7 above were motivated by bad faith, malice, greed and were outrageous in their execution and  
8 effect.

9  
10 3. Respondent John Gee was, at all times relevant, in a supervisory position relative to  
11 Claimant and able to cause and/or influence the terms and conditions of his employment with  
12 Respondent Merrill Lynch and was able to cause/and or influence Claimant's continued  
13 employment with Respondent Merrill Lynch. He had been given the discretion by Respondent  
14 Merrill Lynch to fire or not fire other brokers.

15  
16 4. Respondent John Gee interfered in the contractual and business relationship between  
17 Claimant and Respondent Merrill Lynch and with Claimant's prospective economic interest and  
18 advantage, and induced and caused Claimant to be discharged for improper and illegal reasons as  
19 aforesated.

20  
21 5. Claimant alleges that if Respondent John Gee had not caused and induced Respondent  
22 Merrill Lynch to discharge Claimant, that Claimant would have remained with and advanced  
23 within Merrill Lynch.

24  
25 6. The acts of Respondent John Gee were intentional and malicious and in bad faith,  
26 against public policy and in retaliation for Claimant refusing to testify falsely in an official  
27 proceeding, for truthfully cooperating in the investigation by the American Stock Exchange, and  
28 out of fear of exposure for his and other management employees of Respondent Merrill Lynch's

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1 participation in the illegal submission of a forged document and false Affidavit to the Federal  
2 District Court in the matter of *Merrill Lynch, Pierce, Fenner & Smith Inc., v. Stephen A.*  
3 *Callahan*, CIV 99-1989 PHX- RCB.

4  
5 7. As a member of the NASD and the New York Stock Exchange, Respondents are  
6 subject to the NASD's rules of fair practice and rules of the New York Stock Exchange and are  
7 obligated to abide by those industry rules, regulations, customs, and practices. By its conduct, as  
8 alleged above, Respondents violated many of these rules, including: (a) Rule 401 of the NYSE  
9 (good business practice); (b) Rule 1 of the NASD (high standards of commercial honor/equitable  
10 principles of trade); (c) Rule 18 of the NASD (manipulative, deceptive or fraudulent devices or  
11 contrivances); and (d) Rule 2110.

12  
13 8. Respondents' violation of the duties imposed by these rules damaged Claimant,  
14 causing his past and future monetary loss, injury to his reputation and mental anguish.

## 15 2. CAUSES OF ACTION

16 The foregoing facts give rise to the following causes of action:

- 17 1. Failure to conduct business observing high standards of commercial honor and just  
18 and equitable principles of trade.
- 19 2. Wrongful discharge in violation of public policy and the laws of the State of Arizona.
- 20 3. Breach of contract both implied and written.
- 21 4. Breach of the implied covenant of good faith and fair dealing.
- 22 5. Outrage.
- 23 6. Intentional interference with contractual relations.
- 24 7. Intentional interference with prospective economic advantage.
- 25 8. Intentional infliction of emotional distress.
- 26
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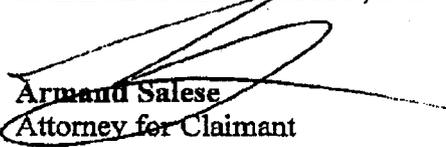
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**3. DAMAGES**

1. Compensatory damages of at least \$20,000,000.00.
2. Pre-judgement interest.
3. Costs of this arbitration.
4. Reasonable attorney's fees.
5. Punitive damages for no less than \$20,000,000.00 or in a greater amount as determined by the evidence at the arbitration of this matter.
6. Such other and further relief as the Arbitration Panel may deem just and equitable.

DATED this 25 day of October, 2000.

SALESE & McCARTHY, P.C.  
  
Armand Salese  
Attorney for Claimant