

Seeking Justice

When you arbitrate an investment dispute, brokers have the upper hand

BY JANE BRYANT QUINN

EVERY SOLUTION CREATES A NEW PROBLEM THAT THE solvers hadn't foreseen. Such is the story of securities arbitration. It began as a quicker way than a lawsuit for nailing stockbrokers who lie. But what used to be an informal process is turning into juridical hell.

Arbitration takes longer than it used to, costs much more and requires you to hire expert help. Brokerage-house lawyers paper you with motions and won't produce documents that are crucial to your case. They may force you, deliberately, to travel to a distant state. No wonder the process is widely perceived as stacked against the little guy.

Do pursue it anyway, if your broker deceived you and the firm won't right your wrong. You'll go to a hearing where you and your broker each tell your story to an arbitration panel. Evidence is offered and witnesses questioned. The panel's decision is usually final. Roughly half of the cases filed with the National Association of Securities Dealers (NASD) are settled before the hearing begins—so you may get some money just for entering a claim. Of the cases the panels hear, clients win about half the time.

Your fault: The injustice, to wronged investors, is that they rarely come out whole. For example, take a widow who lost \$100,000 in speculations her broker said were safe. The arbitrators might give her only \$50,000, saying she wasn't careful enough. She pays her attorney \$16,500 and expenses eat up \$5,500. Her net: only \$28,000—just 28 percent of her loss. And that's not bad. Outcomes can be even worse.

In truly egregious cases, you might get punitive damages in addition to an award for financial loss. But despite brokers' yelps about the occasional \$3.5 million case, punitives are both modest and rare. They're awarded in only 2 percent of the arbitrated complaints, reports Richard Ryder, publisher of the Securities Arbitration Commentator in Maplewood, N.J. Out of 221 cases, Ryder says, the median award came to \$40,000—about the same as the median award for financial loss.

Brokers think even that's too much. For a while they were slipping obscure language into your brokerage agreement, waiving your right to punitive awards. The Supreme Court scotched that ploy last March, but in some states investors still can't collect. The industry is lobbying Congress to wipe out punitives altogether. If that happens, fewer cases will settle, says San Francisco lawyer Cary Lapidus. The threat of punitive damages is what persuades many brokers to pay. Remove that threat, and they've little to lose by arbitrating everything.

People who serve as arbitrators say they harbor no bias against either side. But the brokers' own actions suggest that they think they can skew the odds. Take their attitude toward the two main arbitration forums: one run by the NASD, one run by the independent American Arbitration Association (AAA).

The NASD keeps tight control over who arbitrates each case. It normally won't hear problems more than six years old. It says that its arbitrators uniquely understand the industry. That's just what the brokers want. At big firms and many smaller ones, too,

your customer agreement now requires arbitration at the NASD or the New York Stock Exchange. The AAA is toast.

Given their druthers, however, investors' lawyers vote for the AAA. The forum feels more neutral, they say. There's a better choice of arbitrators. And the AAA takes older cases. If you have just learned that a real-estate deal you bought in the '80s was corrupt, the AAA is your best hope for getting money back.

No choice: In both of these forums, the outcomes of cases appear, on average, about the same, according to a 1992 study by the General Accounting Office. So if you feel better about the AAA, why should your broker deny you the choice?

The NASD is looking into this and other complaints, with findings expected in November. Here's a wish list of reforms:

- Freer choice of NASD arbitrators and access to the AAA.
- Selecting an arbitrator early. "That would save months of arguing over issues," Boston lawyer David Shellenberger says.

- Ending the six-year rule that's denying justice to victims of drawn-out scams.

- Getting decisions explained in writing. Arbitrators today don't have to say why you won or lost.

- Sideline arbitrators known to be biased.

- Creating a list of documents that the parties must provide. New York lawyer David Robbins says investors should get, among other things, the form the broker filled in when you opened your account (he may have exaggerated your wealth to justify selling you risky things); any missing monthly account statements and trade confirmations; the research reports on your investments (maybe your broker sold things the firm didn't recommend); any taped telephone conversations between you and your broker; your broker's disciplinary history, and the firm's compliance manual, which may show that your broker broke the firm's internal rules.

You'll need a lawyer for a successful arbitration.

You don't stand much chance when you try to represent yourself. Lawyers rarely appear for cases worth less than \$10,000 or \$20,000. But they'll help you prepare a smaller claim for hourly rates of \$150 to \$300, Robbins says.

Beyond arbitration lies a newer solution. It's called mediation, a version of the talking cure. The warring parties engage a professional peacemaker, who shuttles between them with proposals and ideas. If you parley enough, you may reach a reasonable compromise. If not, nothing's lost. You return to the arbitration track. New York City lawyer Jack Friedman believes that a settlement in mediation pretty much parallels what you'd get from arbitration. But you get it quicker and at a much lower cost.

Before entering mediation, ask a lawyer what your case is worth. Brokers tend to mediate when they think they're on the losing side, so you want to be sure not to leave any money on the table. For experienced mediation, call the American Arbitration Association (212-484-4000). The NASD began a similar program this month (212-858-4400). But mediation or arbitration, resign yourself to getting less money than you're owed. Your loss is the price of granting your broker too much trust.

Reported by: TEMMA EHRENFELD and LOUISE NAMETH



Even when you're proved right, you rarely get all your money back