

When a Broker's Advice Isn't, Exactly

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When Robert Kadar was searching for a brokerage firm in 2000 that could help him manage his large chunk of stock options, he said Banc of America Securities won him over by promising that a team of experts would carefully monitor and manage his account.

Three years later, the same firm had a different view of its role in Mr. Kadar's life: In arguments before a New York Stock Exchange arbitration panel, Banc of America Securities claimed that its only legal responsibility was to execute trades properly, with no duty to offer advice or warnings about investments.

"The reason I searched for a 'full-service' brokerage and eventually selected BofA Securities is that I knew I needed help managing the stock and stock options gained through my employment. If I had felt comfortable managing it myself I would have done so through my online account," said Mr. Kadar, a 47-year-old New Jersey resident.

Banc of America Securities' split approach on whether its brokers give advice isn't unusual on Wall Street. While advertisements and promotional brochures portray brokers dishing out advice that will lead to comfortable retirements and beachfront vacation homes, nearly every Wall Street firm sings a different tune in the private confines of mandatory arbitration, where customers must raise complaints far from the public eye.

Once inside such closed-door hearings, investors learn something that isn't contained in any ad or brochure: Their brokers claim that legally, they don't have to give advice, don't have to monitor accounts, and aren't responsible for anything beyond accepting and completing trade orders.

In Mr. Kadar's case, after being wooed to Banc of America based on promises that its brokers would analyze and manage his portfolio on an ongoing basis, he claimed the firm actually did little to help him diversify an account that was highly concentrated in the stock of his then employer, online advertising-services firm DoubleClick Inc.

Banc of America Securities, a unit of Banc of America Corp., advertises on its Web site that it matches all clients with "financial advisors" who provide personalized investment advice. The firm told arbitrators that it had no legal requirement to give him unsolicited advice about the particulars of when he should trade his DoubleClick stock.

During arbitration the company said it had repeatedly told Mr. Kadar to diversify his stock, but the requests he made to sell his stock at specific prices often couldn't be honored because he aimed too high. Kadar's portfolio declined because he held on to DoubleClick too long, convinced it would increase in price, Banc of America claimed.

"We don't have a duty to provide ad-

vice. However, we oftentimes do, and in

the Kadar case, we certainly did," said Banc of America Securities spokeswoman Shirley Norton. "But he's the one who has to sell the stock. We can't force him to sell the stock."

In a decision released in April 2004, the NYSE panel awarded Mr. Kadar—who had sought \$5.5 million—a total of \$625,000 plus interest against Banc of America Securities.

Mr. Kadar's case is hardly unique. All over Wall Street, major full-service firms, including UBS AG, Merrill Lynch & Co. and Morgan Stanley, promise their biggest and best brokerage clients that they will have a bevy of financial experts attending to their every need, but in arbitration they disavow any legal responsibility to give advice.

"In almost every case, especially every case with a New York connection, they throw that in," said Stuart D. Meissner, the New York attorney who represented Mr. Kadar, of the legal strategy firms use.

Wall Street's assertion that it isn't required to provide brokerage advice is dependent upon the type of account customers hold: discretionary or nondiscretionary.

Discretionary accounts allow brokers total control over investment decisions, and trades can be made without first obtaining a client's permission.

Nondiscretionary accounts, which are the majority of accounts held by individual investors, require brokers to obtain permission for each trade from their clients. It is with these latter accounts that brokerage firms can argue that they aren't responsible for giving bad advice or no advice at all. That argument has been bolstered since 2002, when a \$164.5 million jury verdict for Canadian investor Henryk de Kwiatkowski against Bear Stearns Cos. was overturned.

The U.S. Court of Appeals panel that overturned the de Kwiatkowski case ruled that the broker's duties on a nondiscretionary account "ordinarily end after each transaction is done, and thus do not include a duty to offer unsolicited information, advice, or warnings concerning the customer's investments."

In the two years since this ruling, brokerage firms have cited it in arguments against customers' claims that they received shoddy investment advice.

Take Virginia resident Michael Kalina's case this year against Citigroup Inc.'s Smith Barney unit. Smith Barney, which distributes brochures telling potential clients that its brokers specialize in stock-option advice ranging from exercise strategies to tax implications, opened an account for him that was quickly filled with WorldCom stock after he exercised options in 1999.

Mr. Kalina claimed he lost \$427,093 because Smith Barney didn't provide advice about hedging his concentrated position. Smith Barney countered that Kalina made his own investment decisions, opting to maintain a large position in WorldCom. During the hearing, it claimed it had no legal duty to either recommend

that he sell WorldCom or suggest a hedging strategy.

"I made a big stink about that at the hearing," said Mr. Kalina's attorney, Lawrence Klayman, of Klayman & Toskes in Boca Raton, Fla. "I asked, what's the difference between a discount brokerage firm and a full-service broker firm? A full-service firm is getting paid to make recommendations to clients, isn't it?"

Smith Barney lost and paid out \$200,000. Spokeswoman Kimberly Atwater said the firm was disappointed in the ruling, and felt that the evidence didn't support an award.

Like Messrs. Kadar and Kalina, Oklahoma swimming-pool contractor Michael J. Sanford was also attracted to the idea of a broker watching over his account when he signed up for one in 1999 at Merrill Lynch. He received brochures describing how the firm creates investment strategies for its clients, and he claims the Merrill broker who solicited his account promised to watch his portfolio and advise him. At the time the broker and his partner were also handling 400 other customer accounts, which Mr. Sanford told an NYSE arbitration panel left little time for any real advice or monitoring.

In arbitration, Merrill said it wasn't legally required to provide any advice to Mr. Sanford. The firm argued that Mr. Sanford's losses were the result of his own aggressive trading strategy combined with a bear market. Merrill settled the case for an undisclosed amount. Mr. Sanford had sought to recoup \$556,300.

"We provide the services to our clients that we promise to provide. Claimants' lawyers routinely mischaracterize our advertising to invent new legal theories to support cases of dubious or no merit. When they do this, we resist these baseless claims," said Merrill Lynch spokesman Mark Herr. "Each case is unique and in this case, the claimants sought to impose a duty on the firm that the law simply does not recognize."

Because securities-industry arbitration panels rarely explain their decisions, it is impossible to know how seriously they weigh Wall Street's stance on advice to nondiscretionary customers. Attorneys on both sides say that the argument is only one of many "kitchen sink" defenses lobbed by firms during a hearing, and often, the most important factors influencing decisions involve details unique to each case.

But investors and the attorneys that represent them say that if brokerage firms spend millions of dollars a year to tell the public that they will monitor accounts and give good advice, they shouldn't do an about-face in litigation.

"People rely on their brokers. You're hiring expertise from a licensed professional the way a lawyer or a doctor is a licensed professional," said William Federman, the Oklahoma attorney who represented Sanford. "I don't cop out after I'm hired and say, 'All I'm supposed to do for a client is show up at courthouse, I'm not supposed to come prepared to present a case.'"

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