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Information for Potential Clients of FINRA Arbitration

Examples of Financial Advisor Abuses Warranting FINRA Arbitration to Recover Money:

Breach of contract: breaching terms of the customer agreement designed to protect the customer.

Negligence: Failure to comply with industry standards for duty of care.

Unsuitability: recommendations to buy, sell or hold, in violation of client's level of risk tolerance or investment objective.

Misrepresentation: false facts to induce a client's investment decision.

Failure to disclose risks: omitting known facts to induce a client's investment decision.

Unauthorized trading: failing to obtain a client's written consent before discretionary trading of client's account.

Breach of fiduciary duty: financial advisor uses discretion to violate duty of due care, duty of loyalty, or prohibition on self-dealing.

Churning: encouraging excessive or unnecessary trades to generate fees or commissions.

Failure to properly supervise: brokerage firm negligently supervises its brokers, advisors or representatives who commit misconduct.

Elder Abuse: Financial abuse of an elderly person.

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The FINRA Arbitration Process

Investor claims against broker-dealers employing financial advisors, and sometimes investment advisors, are filed with FINRA, the Financial Industry Regulatory Authority. If jurisdiction with FINRA is not available, the AAA (American Arbitration Assn) or other forum may be used.

In contrast to litigation in court, FINRA arbitrations are considered less formal, less costly, and with quicker resolution (often 12-18 months if a hearing is required). Depositions are usually not allowed. Decisions are binding and final except in rare basis for appeals.

The following series of steps should be expected:

1. Formal Retention and Review of Facts and Documents

2. Preparing and Filing the Statement of Claim with details of the complaint.

The Respondent brokerage firm or investment advisor has 45 days to file an answer to the Statement of Claim.

3. Arbitrator Selection. Both parties rank potential arbitrators after reviewing background information. If the dispute involves over \$100,000 in damages, three arbitrators will be selected for the panel. For claims under \$100,000 one arbitrator is appointed, and cases under \$50,000 are adjudicated with one arbitrator without a hearing.

4. Initial Pre-Hearing Conference. A few months after filing, the parties' attorneys and the Panel hold a telephonic conference call to schedule the final hearings and related matters.

5. Discovery. The parties exchange documents, mostly from the FINRA Discovery Guide Lists. Customers are usually expected to exchange, for example, tax returns, other brokerage statements, emails and correspondence. If documents are not handed over, motions to compel are filed with the arbitrators who can issue sanctions.

6. Hearing. If the case cannot be settled, a hearing is held before the panel of FINRA arbitrators, usually in a conference room at FINRA or a downtown hotel. The clients attend all such final hearings. The parties engage in opening statements, evidence presentation, witness questioning, witness cross-examination, and closing statements. No decisions are made at the final hearings. The FINRA arbitration panel will then issue a decision within 30 days.

7. Appeal of Arbitration Award (Rare). The law permits a District Court to vacate or overturn an arbitration award if it finds that the arbitrators abused their powers, which is rarely found. Other than by making such a motion to vacate, the investment firm must pay an Award or may have its license suspended by FINRA.

Costs and Reimbursements for Clients in Contingency Cases

Under a contingency arrangement, clients do not pay any hourly legal fees to the firm. Instead, clients pay an attorney fee based on the agreed percentage of net monies recovered after the *client is reimbursed off-the-top for out of pocket costs.*

The client's out of pocket costs include:

- (1) Filing fees (e.g., \$1,575 for a three-arbitrator case with unspecified damages);
- (2) Arbitrator fees (\$1,125 per hearing session with three arbitrators, with number of hearing sessions depending on the case, often ranging from three to twelve);
- (3) Copying costs (20 cents per page);
- (4) Investigative and subpoena fees (if any);
- (5) Expert report and testimony at hearing (if any), which could cost often from \$2,000-\$10,000;
- (6) Accounting service fees (if any) to tabulate statements (varies, depending on how many years);
- (7) Travel or other expenses (if any); and
- (8) Attorney fees or expenses or sanctions ordered by any arbitrators or courts (if any, very rare).

Illustrative Example of Full Final Hearings, Without Settlement

Assuming a case is filed on a 40% contingency for an "unspecified" amount (but damages estimated at around \$500,000); the FINRA filing fee would be \$1,575. Assume the case does not settle, and goes all the way through final hearings, with a claimant's expert retained at a cost of \$4,000 including testimony. Assume that the hearing lasts three full days (six sessions), and had two pre-hearing conferences, so the number of hearing sessions might total eight, for an arbitrators' hearing fee payable to FINRA of \$9,000. Assume copying costs and other expenses of \$500.

Assume client loses at final hearing: The total client out-of-pocket obligation is \$15,075, and client owes no legal fees.

Assume client wins an Award of \$500,000 which is paid by the investment firm into the IOTA Attorney Trust Account. Off-the-top, **client receives back the \$15,075 expenses paid.** From the net recovery of \$484,925, the client also receives \$290,955 (60% of net recovery), so the client receives a **total check for \$306,030** (\$15,075 + \$290,955).

Illustrative Example of Settlement Before Final Hearings

Assuming a case is filed on a 40% contingency fee for an "unspecified" amount (but damages estimated at around \$500,000); the filing fee would be \$1,575. Assume

settlement occurs after two pre-hearing conferences (\$2,250) and costs and other expenses were \$300. Assume a settlement for \$300,000 cash is accepted by the client.

From the \$300,000 settlement deposited into the IOTA Attorney Trust Account, the client receives off-the-top their return of the \$4,125 ($\$1,575 + \$2,250 + \300) paid to the attorney for expenses to date. The client also receives \$177,525, which is 60% of the remaining balance ($\$300,000 - \$4,125$). The client would receive one check from the firm for both items, **totaling \$181,650** ($\$4,125 + \$177,525$).