Representing Customers in Securities Arbitration

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I. INTRODUCTION

The approach taken in a securities arbitration case generally differs from that taken in a federal or state court case in many respects. First, keep in mind that the procedures for arbitration are different than those for court cases. A set of procedural rules will apply and should be followed. Each forum has its own procedural rules which differ in certain respects. For example, both the New York Stock Exchange, Inc. and National Association of Securities Dealers have arbitration facilities available to the public and have codes of arbitration procedure to guide you through the arbitration process.

The evidence presented at hearings and the rules governing the use of evidence differ in arbitration. The Federal Rules of Evidence do not apply in arbitration. Thus, arbitrators are not shielded from "hearsay" or other "inadmissible" evidence. Objections to questions asked of witnesses and evidence to be introduced are made in arbitration hearings. However, arbitrators generally will admit all evidence with the qualification that they give it whatever weight they deem sufficient.

The triers of fact and law differ in an arbitration proceeding. Arbitrators are bound by different standards than juries or judges. Arbitration is essentially a "businessman's forum" which seeks to do equity. Thus, fairness is an overriding concern. In fact, the first page of the Arbitrator's Manual places emphasis on equity by quoting Aristotle: "[e]quity is justice in that it goes beyond the written law. And it is equitable to prefer arbitration to the law court, for the arbitrator keeps equity in view, whereas the judge looks only to the law, and the reason why arbitrators were appointed was that equity might prevail."

When trying an arbitration case, also keep in mind arbitration's stated advantages and objectives of speed, efficiency and lower costs. There are strong aversions to notice pleading, extensive discovery ("fishing expeditions") and lengthy hearings.

A premium is placed on pre-filing preparation and initial presentation. The arbitration claim filed by you on behalf of your client should be factually and legally well-researched. Multiple or lengthy amendments to your initial statement of claim should be avoided. In addition, the pre-hearing procedures for arbitration, although becoming more flexible especially regarding discovery, are still far more restrictive than in court.

Finally, once a claim is filed, a hearing is completed, and a decision is rendered by the arbitrators, the decision entered is virtually irreversible. A very narrow set of grounds for reversal of awards is outlined in more detail below.

II. PRELIMINARY FACT GATHERING AND INVESTIGATION

A. General

In arbitration, initial fact gathering and investigation is extremely important. An approach that is at least as extensive as employed in other types of litigation is suggested. When handling a securities arbitration case, you should always keep in mind that the securities business is extremely complex, and laypersons are often not familiar with proper versus improper activity on the part of broker/dealers or with the duties and standards imposed upon broker/dealers. Clients are often quick to blame themselves for the losses in their accounts and are embarrassed to admit that they did not understand market risks. Your client may have claims but may not realize it.

B. Dealings with the Client

After your initial contact with your client, ask him to prepare a written narrative of his dealings with his broker as a preliminary matter. Writing a narrative about what happened will force the client to organize his thoughts and focus on that which he believes is important.

In addition, gather and review the client's documents as a preliminary matter. If possible, you should review the client's documents prior to an in-depth interview with the client. In any type of securities arbitration case, the following documents should be reviewed, if possible, prior to filing a claim:

a) monthly account statements for the account at issue;
b) trade confirmations for the account at issue;
c) new account documents for the account at issue;
d) correspondence between your client and the broker/dealer;
e) offering literature;
f) monthly account statements and other account documents for other brokerage accounts of the client.

If you have the time and ability to do so, you should consider “scheduling” the client's account. Such scheduling often reveals problems in the account such as excessive trading and short holding periods, among others. (See Exhibit 1 for an example of an account that has been scheduled).

After reviewing available documentation, conduct an in-depth interview with your client. Gather background information about the client such as level of education, knowledge and sophistication, trading history, and financial condition and status. Also, determine the impression your client will likely make on a panel of arbitrators. Assess your client's credibility and honesty. Determine what type of impression your client generally makes.

C. Other Interviews/Contacts - Consider Obtaining Affidavits

Once you have reviewed the client's documents and conducted an in-depth interview with the client, determine what potential witnesses exist to the transactions at issue. For example, if your client is an elderly person and always took his daughter with him to his registered representative's office, ask the daughter what the broker said. Find out what your client was told. Ask your client if he regularly had contact with anyone else at the brokerage firm other than the broker. For example, the client may have routinely talked to the broker's sales assistant or may have talked to the branch manager on one or more occasions. Ask your client for names of people with whom

he dealt and what he was told.

Other customers of the broker/dealer and registered representative may warrant an inquiry. For example, if your client's next door neighbor also used the same registered representative, call the neighbor. He may be able to provide valuable insight into the registered representative's pattern and practice of dealing with customers.

Speak with other persons employed in the securities industry. They are most familiar with industry rules, regulations, customs and practices and can be a wealth of information.

D. Independent Investigation

Your pre-filing investigation should not end with a review of account documents and in-depth interviews with your client and potential witnesses. You should also investigate the background of the registered representative who handled your client's account. The Secretary of State's office in most states can provide you with some information about the registered representative if the registered representative is licensed in that state. For example, you may be able to find out where the registered representative is licensed to do business, what securities licenses he holds, and if he has a disciplinary record.

In addition, research the public information available about the securities at issue during the time your client purchased or sold the securities. Determine what SEC filings are available for the securities at issue. Check securities evaluation services and reference materials. Look for magazine and newspaper articles concerning the securities at issue. What was generally said about the product during the relevant period may contradict what your client was told by his registered representative.

E. Employing an Expert

Whether or not you decide to use an expert witness to evaluate your client's case or to testify at an arbitration hearing depends on the economics of the client's case. If the loss suffered by the client justifies the cost of an expert and if you are not familiar with the securities industry or if you are a novice at securities arbitration, retaining an expert provides several advantages.

First, an expert can help you identify and assess the merits of your client's potential claims. In addition, an expert can help you identify documents that are essential to proving your case or that will aid you in developing your case. A good securities expert will know what documents will be useful in formulating and supporting his opinion about your client's claims. The documents identified by your expert can be requested specifically in your discovery request. Once documents are obtained from your client and later in discovery, an expert can help you review and evaluate the documents. An expert may be able to discover irregularities in your client's account that may have previously gone unnoticed.

You may want your expert to have an opportunity to talk to your witnesses who will be testifying at the arbitration hearing. By doing so, your expert will know how the witness will testify at the hearing and can help you prepare the witness for the hearing. This is particularly helpful if your

expert cannot (or is not permitted to) sit through the entire arbitration hearing. Also, an expert may be particularly helpful in preparing your witness for cross-examination by opposing counsel.

An expert can often provide valuable insight into possible testimony from an expert hired by opposing counsel. An experienced securities expert may be able to predict how other expert witnesses will testify about certain matters such as industry standards, practices, rules, and regulations. This insight will enable you to tailor your case accordingly and to prepare a more effective cross-examination of the opposing party's expert.
Although you may hire an expert simply to help you evaluate your client's claims and prepare for the arbitration hearing, at times you may want your expert to testify at the arbitration hearing. While arbitrators may have basic knowledge of the securities industry, particularly in arbitrations sponsored by self-regulatory organizations (i.e. NYSE, NASD, AMEX) in which one arbitrator will be a representative of the securities industry, do not assume that the arbitrators are familiar with complex securities issues such as churning, suitability standards, supervisory standards, back-office procedures, and control.

Once you weigh the advantages and disadvantages of hiring an expert for your particular case, you must consider what type of expert best suits your client's needs. Experts can generally be divided into two categories: industry experts and financial experts.

1. Industry Experts:

Industry experts can include former employees of brokerage firms, self-regulatory organizations, and government agencies, academics, and practicing attorneys, among others. Industry experts can provide valuable testimony concerning industry customs, practices, standards, rules and regulations.

2. Financial Experts:

Financial experts can include accountants, economists, and academics, among others. Financial experts can provide useful assistance in calculating damages and evaluating your client's account to determine losses incurred. Such an expert can also assist you in scheduling the trades in your client's account. If needed, a financial expert can assist you in calculating turnover ratios, cost equity maintenance factors, “in-and-out” trading, holding periods, and other ratios that may be important to your particular case.

F. Other

In addition to reviewing the facts with your client, checking on the broker and securities involved in the dispute, and consulting an expert, you should consider contacting other attorneys who have handled similar cases or reviewing current literature available on the arbitration process. In 1990, the Public Investors Arbitration Bar Association (PIABA) was founded to facilitate the exchange of information helpful to the public investor. Several publications are currently available through PIABA including:

S. Goldberg, PIABA's 1991 Report on Punitive Damages in Securities Arbitration (1991); S. Goldberg, PIABA's 1991 Public Investor Recovery Guide and Arbitrator Source Book to Stockbroker Fraud and Securities Arbitration (1991).

PIABA is in the process of setting up an information exchange program on expert witnesses for securities arbitrations, among other things. In addition to PIABA publications, numerous other source books have been published in recent years concerning securities arbitration.

III. CASE EVALUATION

A. Legal Theories

Once you have talked with your client and reviewed the client's documents, you must analyze the legal theories that would support a cause of action. First, determine if there are any violations of the federal securities laws. Violations of federal securities laws can be broken down into two broad categories: registration violations and antifraud violations.

Determine if there are any violations of applicable state securities laws. Again, two broad categories of violations exist: registration violations and antifraud violations. An advantage to bringing a claim for a violation of state securities laws is that most state laws provide for the recovery of attorneys' fees and costs if a violation is found.

You should also determine if the facts of your client's case support a claim for a violation of the federal or state racketeer influenced and corrupt organizations ("RICO") statutes. RICO can justify broader discovery in an arbitration claim because you are permitted to introduce evidence to establish a pattern and practice of behavior in support of your RICO claim. In addition, RICO statutes permit the recovery of treble damages. However, arbitrators generally do not routinely find in favor of claimants on their claim for RICO violations. Arbitrators are hesitant to impose treble damages. Thus, bring RICO claims only in exceptional cases.

You should also explore claims for fraud under various state statutes. Fraudulent activity on the part of a broker/dealer will often support both a securities fraud claim and a common law fraud claim. Many states authorize recovery of attorneys' fees and punitive damages if the arbitrators find in favor of the claimant on his fraud claim.

Another common claim in securities cases is breach of fiduciary duty or breach of duty (negligence). Many states specifically hold that brokers owe their customers a fiduciary duty of utmost good faith and loyalty. For example, see Gochnauer v. A.G. Edwards & Sons, Inc., 810 F.2d 1042 (11th Cir. 1987) ("The law is clear that a broker owes a fiduciary duty of care and loyalty to a securities investor"); E.F. Hutton & Co. v. Weeks, 166 Ga.App. 443, 304 S.E.2d 420, 422 (1983) ("The broker's duty to account to its customer is fiduciary in nature, resulting in an obligation to exercise the utmost good faith"); contra Interstate Securities Corp. v. Hayes Corp., 920 F.2d 769 (11th Cir. 1991) (Eleventh Circuit interpreting Florida law. Court recognized that fiduciary duty between customer and broker existed, but held that any damages arise out of breach of contract between investor and broker). When bringing a claim for breach of fiduciary duty, in addition to case law, cite the rules, regulations, customs and practices of the industry in support of your

claims. These rules, regulations, customs, and practices establish standards that will support a cause of action for breach of fiduciary duty if violated and if the client incurs damages as a result of the breach.

Your client may have a cause of action for breach of contract. Most customer agreements and trade confirmations incorporate industry rules and regulations into a contract with the customer. Accordingly, violations of industry rules and regulations by the broker/dealer and registered representative give rise to a breach of contract claim if damage results.

Counsel for customers in securities arbitrations should give serious consideration to the pursuit of state law claims that may exist. Often, these state law claims will have longer statutes of limitation than those provided for federal or state securities law violations, and thus may permit a customer to pursue these claims even if the statute of limitations may have already run on his federal or state securities law claims.

Many other causes of action may exist. You may find violations of ERISA statutes or violations of various agency statutes. You may have a claim against the brokerage firm for negligent hiring or retention. Explore those areas of law you believe may give rise to a cause of action for your particular client.

B. Nature of Claim

In a customer/broker case, one or more of the following claims typically may exist:
1. Suitability - Determine if the investments recommended to your client were suitable for him in light of his investment objectives and circumstances. A securities broker/dealer has an obligation to “know his customer” and to recommend only investments to the customer which are suitable in light of the customer's investment objectives and circumstances. You may also argue that a broker/dealer has a duty to refrain from taking orders from a client if such orders are unsuitable for the client.
2. Churning - Determine if the broker/dealer has caused your client to buy and sell securities with excessive frequency for the primary purpose of generating commissions. You must show that the broker/dealer had actual or de facto control over the account. To determine if churning has occurred, you should calculate the turnover ratio, cost equity maintenance factor, and holding period for your client's account.
3. Unauthorized Trading - Determine if the broker/dealer has effected trades in your client's account without having either a written power of authority to do so or your client's specific prior approval to trade a specific quantity of a specific security.
4. Misrepresentation/Omissions - Your client may have a claim for misrepresentation or omission if the broker/dealer has misrepresented an investment or other material facts to him or omitted to advise him of material facts.
5. Failure to Supervise - Determine if the broker/dealer either failed to adopt or enforce adequate procedures to ensure compliance with industry rules, regulations and standards.
6. Illegal Markups/Markdowns - You may have a claim for illegal markups/markdowns if the broker/dealer sold securities to your client at too high a price or bought securities from your client at too low a price.
7. Trading on Material Non-Public Information (Insider Trading) - Determine if your client's

broker traded his account based on “tips.” You may have a claim for trading on insider information.
8. Margin Violations - Your client may have a claim for a margin violation if the broker/dealer improperly extended credit to a customer or improperly liquidated securities which secured the extension of credit.
9. Market Manipulation - Your client may have a claim if the broker/dealer has “rigged” the market.
10. Other Violations of Industry Standards of Conduct - Determine if your client may have claims for violations of “good business practices”, “just and equitable principles of trade”, and “fair dealing”.

C. Problems and Pitfalls

As with most litigation, you must be aware of problems and pitfalls that could prevent you from bringing a claim on behalf of your client. First, know what the statutes of limitation are on the potential claims your client may have. Second, be prepared for defenses such as waiver, ratification and estoppel. Although these defenses are often raised by opposing counsel in securities arbitration cases, they generally are not given as much weight by arbitrators as they are by courts. However, you should be prepared to show that these are not valid defenses. Also be prepared to show that your client mitigated his damages.

Your client can also prove to be a pitfall if he lacks credibility or does not appear to be honest. Stress to your client the importance of being honest, especially during cross-examination. If your client tries to dodge answering a question, he will appear to be hiding something when in fact a truthful response may not be damaging to his case. Your client's knowledge, level of sophistication, and prior brokerage experience could also be a problem in certain instances.

Accessibility to evidence can also be a problem. If you cannot get the documents you need to prove your case (because you did not ask for them in discovery or because the opposing party has refused to produce them or no longer has the documents) you may have difficulty supporting your claims. If opposing counsel claims his client no longer has certain documents, be advised that both the SEC and the SROs have record retention requirements that hold that broker/dealers must keep certain records for a specified period of time. See Securities Exchange Act of 1934, Section 17(a) (15 U.S.C. Section 78q) and rules promulgated thereunder.

D. Damage Considerations

Although there are a variety of legal approaches to damage awards, arbitrators generally do not appear to adhere strictly to such approaches and do not appear to worry about theoretical bases of damages. Instead, arbitrators appear to be governed by what they believe is a fair and equitable resolution to the matter. This approach often results in awards with damages split equally between the parties. In other words, if the client can show damage of $100,000.00 attributable to churning but failed to timely object to such activities over a long period of time, the arbitrators may give him $50,000.00 as a compromise.

Although arbitrators tend to do what they deem “fair”, you should clearly outline your damages

in your statement of claim. Under the 1934 Act, 15 U.S.C. Sec. 78bb(a), damages are limited to "actual damages." However, the term "actual damages" is not defined. In court cases, the following types of damages have been awarded:

a. Rescission - based on the concept of preventing a respondent from unjustly retaining the benefit from fraudulent transactions. Claimant returns the security in exchange for return of consideration paid. If the security is no longer available, claimant obtains recovery of the difference between the consideration paid for the security and any consideration received for it. See also Sec. 12(2) of the 1933 Act, 15 U.S.C. Sec. 771(2).

b. Out-of-Pocket Damages - most common measure of damages in Rule 10b-5 cases. Claimant gets the difference between the price he paid for a security and its actual value absent respondent's fraudulent conduct. Keep in mind that Claimant has a duty to mitigate his damages. If Claimant does not sell after he has notice of fraud, he may be limited to losses as of the date of discovery.

c. Consequential Damages - May recover subsequent expenditures required to maintain investment.

d. Churning Damages - older view just repaid commissions, but newer view is to give back commissions plus decline in portfolio due to account not being properly managed. Gives client the benefit of the bargain. See Miley v. Oppenheimer & Co., 637 F.2d 318, 326-29 (5th Cir. 1981). Based on Miley theory, evidence of increases or decreases due to general market conditions as shown by Dow Jones Industrial or S&P Index, etc. may be introduced. Brodsky, Measuring Damages in Churning and Unsuitability Cases, 6 Sec.Reg.L.J. 157, 165-66 (1978).

In addition to compensatory damages, other damages should be considered, including:

a. Interest: Under the 1934 Act, prejudgment interest is awarded in the discretion of the court. Arbitrators presumably have the same discretion. See Blau v. Lehman, 368 U.S. 403, 414 (1962); Wolf v. Frank, 477 F.2d 467, 479 (5th Cir.) cert. denied, 414 U.S. 975 (1973); Woods v. Barnett Bank of Ft. Lauderdale, 765 F.2d 1004, 1014 (11th Cir. 1985). Prejudgment interest may also be available for a breach of contract claim under state law.

b. Attorneys' Fees and Costs: Arbitrators may award attorneys' fees and costs if available under state or federal law. You must provide the arbitrators with evidence of their authority to award attorneys' fees and costs. For example, attorneys' fees are expressly available under federal RICO, 18 U.S.C. Sec 1964(c) (injured party "shall recover threefold the damages he sustains and the cost of suit, including a reasonable attorney's fee") and under Georgia RICO, O.C.G.A. 16-14-6 (remedy is three times actual damages, punitive damages, where appropriate, and attorneys' fees). See also Georgia Securities Act, O.C.G.A. 10-5-14 (a)(attorney's fees permitted for violation of antifraud provisions).

c. Punitive Damages: Although punitive damages are not available under the federal securities laws, they may be available under state law for fraud or breach of fiduciary duty. As with attorneys' fees and costs, you must provide the arbitrators with evidence of their authority to award

punitive damages. See Arceneaux v. Merrill Lynch, 767 F.2d 1498 (11th Cir. 1985) (affirming compensatory damages of $46,675 and punitive damages of $300,000); Hatrock v. Edward D. Jones & Co., 750 F.2d 767 (9th Cir. 1985)(Upheld award of compensatory damages of $36,880 and punitive damages of $200,000).

Presently, individual circuits have taken different positions regarding the availability of punitive damages in arbitration. For example, the Eleventh Circuit has held that arbitrators may award punitive damages. See Willoughby Roofing & Supply Co. v. Kajima International, Inc., 776 F.2d 269 (11th Cir. 1985) and Bonar v. Dean Witter Reynolds, Inc., 835 F.2d 1378 (11th Cir. 1988). The Second Circuit, however, in reliance on Garrity v. Lyle Stuart, Inc., 40 N.Y.2d 354, 353 N.E.2d 793, 386 N.Y.S.2d 831 (1976)(which held that arbitrators could not, as a matter of public policy, award punitive damages) has, on occasion, refused to uphold such awards. As this article is being written, two cases are on appeal before the Second Circuit regarding the issue of punitive damages in arbitration, and should be decided in the summer of 1991. See Fahnestock & Co. v. Waltman, 1990 U.S. Dist. LEXIS 11024 (S.D.N.Y. August 22, 1990), appeal docketed, C.A. Nos. 90-7867, 90-7869 (2nd Cir.) and Matter of Arbitration between Barbier and Shearson Lehman Hutton, Inc., 752 F.Supp. 151 (S.D.N.Y. 1990)(motion for reconsideration filed and pending as of 1/25/91). These decisions may clear up some of the confusion presently surrounding the punitive damage availability issues.

In arguing for punitive damages, it is important to note that the SROs have adopted rules prohibiting the inclusion of any conditions in pre-dispute arbitration agreements that would limit the ability of arbitrators to make any award. See Rule 636(d) of the NYSE Code of Arbitration Procedure ("No agreement shall include any condition which limits or contradicts the rules of any self-regulatory organization or limits the ability of a party to file any claim in arbitration or limits the ability of the arbitrators to make any award.") and NASD Rules of Fair Practice, Article III, Section 21(f)(4). Thus, brokerage firms cannot include language in their pre-dispute arbitration clauses that would prohibit arbitrators from making awards of punitive damages.

Typically, punitive damages are awarded only in exceptional cases. While you should include a request for punitive damages in your statement of claim if the facts warrant such damages, the chance of recovering punitive damages, while greater today than five years ago, is still fairly slim.

d. Treble Damages: Although treble damages are provided for under the federal RICO statutes and in some state RICO statutes, arbitrators are reluctant to award RICO damages.

e. Damages for Emotional Distress: Damages may be available for intentional infliction of emotional distress and breach of fiduciary duty. See Malandris v. Merrill Lynch, 447 F.Supp. 543 (D. Colo. 1977) modified, 703 F.2d 1152 (10th Cir. 1983) cert. denied, 464 U.S. 824 (1983) (upholding verdict of $1,030,000 for churning loss of $30,000 and severe emotional distress, reducing punitive damages award from $3 million to $1 million.) However, damages for mental and emotional distress are disfavored in arbitration.

Several alternative approaches to damage calculations exist. You may want to ask the arbitrators to approach the calculation of damages for your client on a more "equitable" type basis. For ex-

ample, you may argue that your client should be awarded damages to “make him whole” including the losses he incurred from his securities investment (or rescission of the purchase if he still holds the securities), his lost investment opportunities, attorneys' fees and costs, and any other damages the arbitrators “deem just and equitable.” This leaves more opportunity for the arbitrators to do what they believe is fair under the circumstances.

IV. FORUM FOR ARBITRATION HEARINGS

A. General

There are several alternative forums in which to conduct securities arbitrations. The following self-regulatory organizations (SROs) all have arbitration facilities available to the public:

American Stock Exchange (AMEX)
Boston Stock Exchange
Chicago Board Options Exchange (CBOE)
Cincinnati Stock Exchange
Midwest Stock Exchange
Municipal Securities Rulemaking Board
National Association of Securities Dealers, Inc. (NASD)
New York Stock Exchange, Inc. (NYSE)
Pacific Stock Exchange
Philadelphia Stock Exchange
National Future Association

In addition, the American Arbitration Association will arbitrate disputes involving securities issues.

Where you file a claim on behalf of your client often will depend upon the governing arbitration agreement between your client and his broker/dealer. Absent consent, the broker/dealer must be a member of any SRO forum selected. If the broker/dealer is a member of the SRO, the SRO forum acquires jurisdiction at the written request of the nonmember investor. If the broker/dealer is not a member of the SRO selected by the investor, the forum can acquire jurisdiction only with the broker/dealer's consent.
When selecting a forum, consider the costs involved in filing a claim in the forum, the expertise of a particular SRO, and the geographic location of the forum's facilities.

When filing a claim, you should request that a hearing be held in the particular location you and your client would prefer. However, the SRO's Director of Arbitration decides where the first hearing will be held. The location of any subsequent hearing will be decided by the arbitration panel chosen for your case. If you file a claim with the American Arbitration Association (AAA), the AAA will choose the location of the hearing unless all of the parties mutually agree on a location.

The major SROs (NASD and NYSE) conduct hearings in certain designated locations around the country. Check with the particular SRO to find out if it has a location convenient for you and

your client. SROs typically will give the investor's choice great weight in selecting where to hold the arbitration hearing.

In choosing the forum, consider the pool of arbitrators from which arbitrators will be chosen to hear your case, local biases that may exist, and the time involved in traveling to forums that are not conveniently located.

When you file a claim on behalf of your client, you generally will be required to pay a filing fees. Each SRO or the AAA will have its own filing fee schedule that you should consult to determine the appropriate filing fee. Usually the filing fee is dependent upon the amount in dispute. The AAA determines the amount based on the amount of claims and counterclaims and assesses additional charges where more than two parties are involved in the arbitration proceeding. SROs determine the filing fee based on the amount of the Claimant's claim.

In addition to the initial filing fee, SROs often impose additional fees if multiple sessions are required to resolve the dispute. However, filing fees are customarily assessed against the losing party. SRO arbitrators are paid a small stipend by the SRO for their participation in the hearing. In AAA arbitrations, the parties usually pay for all the sessions after the first session is held.

When determining whether to file a claim with an SRO or with the AAA, you need to consider the composition of the panel of arbitrators that will hear your dispute. In SRO arbitrations, at least one person on the arbitration panel will be from a member organization of the SRO. This panel member is considered an “industry arbitrator.” The Respondent brokerage firm and/or the registered representative will also be members of or affiliated with the SRO. An advantage to having a panel member with industry expertise is that he can often facilitate discovery and proof or appreciation of key issues (e.g. issues relating to customs, practices and standards of the industry). A disadvantage is that the arbitrator may possibly be biased or prejudiced toward the industry. For example, the arbitrator's firm may engage in the same types of practices on which your client's claims are based.

AAA has no affiliation with the securities industry, and its panelists are not typically from that industry. The advantage to AAA is total impartiality on the part of the arbitrators. The disadvantage is that the arbitrators may not have the requisite expertise.

The Securities and Exchange Commission (SEC) is responsible for oversight of SRO administered arbitration proceedings; however, the SEC has no such relationship with AAA arbitration proceedings. Nevertheless, the SEC has recommended that brokerage firms expand their arbitration clauses to include AAA arbitration.

B. The AMEX Window

Much has been written in the past few years concerning a provision contained in the American Stock Exchange (AMEX) Constitution known as the “AMEX Window.” The AMEX Window provision states:

> Sec. 2. Arbitration shall be conducted under the arbitration procedures of this Ex-

> change, except as follows:
> ...
> (c) if any of the parties to a controversy is a customer, the customer may elect to arbitrate before the American Arbitration Association in the City of New York, unless the customer has expressly agreed, in writing, to submit only to the arbitration procedure of the Exchange."

Thus, assuming that the brokerage firm is a member of the AMEX, a customer may be able to pursue his arbitration claim in the AAA forum if his customer agreement gives him a choice of two or more arbitration forums. The AMEX Constitution closes the Window only if the customer has agreed "to submit only to the arbitration procedure of the Exchange." AMEX Constitution, Article VIII Section 2(c). Much debate has occurred over whether the words "the Exchange" refer only to the American Stock Exchange or all exchanges.

In a recent decision in Florida, Joseph v. Prudential-Bache Securities, et al., No. CI90-72844-DIV 33 (9th Judicial Circuit, Orange County, May 1, 1991), the court entered a judgment ordering arbitration before the AAA pursuant to the AMEX window which the customer had elected to use. The court found that the words "the Exchange" referred only to the AMEX, thus giving the customer the option to pursue AAA arbitration through the AMEX Window. The court also found that the reference to arbitration before the AAA in the City of New York was not a venue provision requiring AAA arbitrations to be held in New York.

In selecting the arbitration forum for your client, give consideration to the AMEX Window if your client's customer agreements with the broker/dealer are broad enough to permit use of the Window.

V. POTENTIAL DEFENDANTS

A. General Considerations

The defendants that you may name in your client's arbitration claim are limited to parties subject to express or implied arbitration agreements. All registered personnel consent to NYSE and/or NASD arbitration by virtue of being registered. You should also consider who has the ability to pay an award should arbitrators find in favor of your client. This is the classic "deep pocket" consideration.

B. Theories of Liability

When bringing an arbitration claim on behalf of a customer, you should almost always name the brokerage firm in addition to (or in lieu of) the registered representative with whom your client dealt. The following theories can be used to name the brokerage firm:

1. Respondeat Superior
2. Control person liability
3. Aiding and Abetting/Conspiracy
4. Direct Liability

(a) Failure to Supervise
(b) Negligent Hiring/Retention

The registered representative should be named only after careful consideration. There are some advantages to naming the registered representative as a defendant. First, naming the registered representative virtually assures that he or she will be present at the hearing. Second, it subjects the registered representative to personal discovery (i.e. you may serve the registered representative individually with a request for documents). Also, naming the registered representative could provide an additional source of recovery should your client be awarded damages. Finally, naming the registered representative can be advantageous if he has a history of regulatory and/or legal problems.

There are, of course, some disadvantages to naming the registered representative. First, it may result in separate counsel becoming involved to represent the broker, thus giving the defense two sources from which to attack your client. Naming the registered representative may frustrate settlement because of the regulatory reporting requirements and implications of being named as a defendant in an arbitration claim. Third, it encourages a "unified" defense effort to defeat the claimant. Also, naming the broker forces him or her into an adversarial role. Finally, it may prevent the sequestration of the registered representative.

Naming supervisory personnel as defendants should also be given careful consideration. Many of the same advantages and disadvantages in naming a registered representative apply to naming supervisory personnel. The rules and regulations of the industry regarding supervisory responsibilities of branch office managers and compliance officers will generally support naming such persons. However, despite the technical exposure of branch office managers and compliance personnel, practical considerations demand that you carefully balance the advantages and disadvantages.

First, the reputation and standing of the branch office manager and/or compliance officer in the community may affect your decision to name him. Second, you should consider the extent of malfeasance or non-feasance attributable to the branch office manager or compliance officer.

VI. DRAFTING THE COMPLAINT

A. General

The Code of Arbitration Procedure used by SROs requires that the Complaint (Statement of Claim) set forth the relevant facts and documents which support the Claimant's allegations as well as the remedies requested by the Claimant. Remember that the pleadings become part of the evidence. The pleadings are considered the arbitrator's first exhibits.

B. Tips

The complaint is your first opportunity, and often the only pre-hearing opportunity, to make an impression with the arbitrators. Use this opportunity to your advantage. Adopt a letter format for your complaint and tell a story. (See Exhibit 2). Do not prepare the complaint in traditional court

format! Most arbitrators abhor this format. One good basic format to follow is the following:

1. Introduction
2. The Parties
3. Fact Sequence
4. Analysis
5. Demand for Relief

The complaint should be detailed and concise, but do not go overboard. Avoid overstating your case. Attach essential supporting documents or analysis to your complaint as exhibits. Consider citing or attaching relevant case law on key points only, but be careful not to go overboard. Remember that many arbitrators are not lawyers or trained in the law. At the end of your complaint letter, request the location where you desire the hearing to be held. If appropriate, request consecutive hearing dates.

In drafting your client's complaint, carefully consider all the claims, state and federal, that may exist. There seems to be a trend in arbitration today in which arbitrators may not permit a claimant to pursue certain claims before the panel if the claims were not specifically brought in the pleadings.

VII. OPEN ISSUES

A. Joinder of Claims

Both the NYSE and NASD will consider permitting parties to join their claims in certain circumstances. Rule 612(d) of the NYSE Code of Arbitration Procedure states that

> [a]ll persons may join in one action as claimants if they assert any right to relief jointly, severally, or arising out of the same transaction, occurrence or series of transactions or occurrences and if any questions of law or fact common to all these claimants will arise in the action. ...A claimant or respondent need not assert rights to or defend against all the relief demanded. Judgment may be given for one or more of the claimants according to their respective rights to relief, and against one or more respondents according to their respective liabilities.

Pursuant to the NYSE rule, the Director of Arbitration determines initially whether the parties should proceed in a joint hearing or in separate hearings. The Director makes this ruling subsequent to the filing of all the responsive pleadings. Any further determinations regarding joining or consolidation of claims are made by the arbitrators. See also Section 25(d) of the NASD Code of Arbitration Procedure.

While both the NYSE and NASD have provisions for joining claims, at the present, the NYSE seems somewhat more predisposed to permit joint claims. Typically, the NYSE will allow parties to file claims jointly, while the NASD prefers that claims be filed individually with subsequent motions for consolidation made to join the individually filed claims.

The Securities Industry Conference on Arbitration ("SICA") recently adopted proposals suggesting that the SROs implement rules similar to those set forth in the Federal Rules of Civil Procedure on joinder of claims and parties.

B. Class Actions

Whether or not the SROs should accept class action claims is presently a topic of much debate. To date, no securities class action suit has been conducted in the SRO arbitration forums. The SROs are not set up to accommodate class action law suits. However, SICA is exploring proposals to permit such claims in arbitration. The Securities Industry Association ("SIA") opposes such proposals.

Several questions or issues should be explored in considering permitting class action claims to proceed in arbitration. First, the quality of the arbitrators should be considered. Will the arbitrators be available to sit at length through multiple hearings? Second, should non-legal panel members be asked to make rulings on class action legal issues that are often very complex? Third, are the SROs equipped to accommodate the lengthy hearings generally required for a class action suit? Fourth, do the SROs have the procedural mechanisms to handle class action claims?

You should continue to monitor changes to the SROs' codes of arbitration procedure because class action arbitration claims may eventually be accepted by various SROs.

VIII. PRE-HEARING MATTERS

As mentioned earlier, the statement of claim should be a detailed pleading that tells your client's story, and should not be only notice pleading. See Section 25 of the NASD Code of Arbitration Procedure and Rule 612 of the NYSE Code of Arbitration Procedure ("The Statement of Claim shall specify the relevant facts and the remedies sought."). The claim will be served upon opposing parties by the Director of Arbitration for the forum chosen. All subsequent pleadings are served by the parties themselves.

Once the claim is filed, the parties have the right/option to conduct discovery as permitted by the SRO's rules.

A. Discovery

Once the claim is filed, you may serve a request for production of documents and information on any other party twenty business days or more after service of the claim by the Director of Arbitration on that party or after the answer has been filed. See Rule 619(b) of the NYSE Code of Arbitration Procedure. You should attempt to serve your discovery on opposing parties early in your case. In many instances, disputes will arise concerning discovery, and you will want plenty of time to attempt to resolve these disputes prior to the hearing.

In drafting your discovery requests, carefully consider what documents you really need to support your claims. Make your requests specific and concise, if possible, so that you are not accused by opposing counsel of going on a fishing expedition. Moreover, very broad and general

document requests will more often than not be responded to with an objection that the request if overbroad, ambiguous, and/or irrelevant to the matters at hand. Use your experts to help you determine what documents you need to request in discovery.

Pursuant to the discovery rules of the SROs, a party upon whom a document or information request is served has 30 calendar days to satisfy the requests or object to the requests. Any response to an objection to any document or information request must be served on all parties within ten calendar days of receipt of the objection. If the parties cannot resolve their discovery disputes among themselves, a pre-hearing conference may be requested to address discovery disputes.

B. Pre-Hearing Conferences

If disputes do arise concerning discovery, attempt to resolve them with opposing counsel. If your efforts fail, submit a written request to the SRO to schedule a pre-hearing conference. Pre-hearing conferences can be used effectively to confront discovery problems prior to the first hearing. Both the NASD and NYSE now charge a fee to conduct a pre-hearing conference, with costs ranging from $15.00 to $300.00. See Rule 629(h) of the NYSE Code of Arbitration Procedure and Section 43 of the NASD Code of Arbitration Procedure.

For a pre-hearing conference, the SRO will appoint an arbitrator, who may also be a member of the panel of arbitrators who ultimately will hear the case, to resolve the dispute among the parties. In a customer complaint, a public arbitrator will be selected. Pre-hearing conferences are usually held by telephone conference call with the arbitrator, opposing counsel, and an SRO representative on the line. Be prepared to support your requests for certain documents. Show the arbitrator that these documents are essential to your case and why. Be prepared to contradict your opposing counsel's arguments for withholding certain requested documents.

After the pre-hearing conference, ask for a written order from the panel or confirm in a letter to opposing counsel what was and was not ordered to be produced. Generally, the arbitrator will give a date by which documents ordered to be produced must be produced by opposing parties. Confirm this date in your letter.

C. Pre-Hearing Exchange

At least 10 calendar days prior to the first scheduled hearing date, you must serve upon opposing counsel the documents you intend to present at the hearing and the names of all witnesses you intend to call or may call in your case-in-chief. See Rule 619(c) of the NYSE Code of Arbitration Procedure and Section 32(c) of the NASD Code of Arbitration Procedure. This rule does not require that you serve copies of documents or a list of witnesses you intend to use or may use for purposes of cross-examination or rebuttal. However, be careful to reserve the right to use documents and witnesses for purposes of cross-examination or rebuttal.

If many of the documents you intend to use have already been exchanged among parties in discovery, often you can reach an agreement with opposing counsel that these documents need not be copied and produced again pursuant to the 10-day rule. Simply state in your 10-day letter that

in your case-in-chief, you may use any documents previously produced by any parties.

D. Appointment of Arbitrators

Prior to your first scheduled hearing date, arbitrators will be selected to preside at the hearing. The rules governing the selection of arbitrators can be found at Section 19 of the NASD Code of Arbitration Procedure and Rule 607 of the NYSE Code of Arbitration Procedure. Generally, the Director of Arbitration selects one public arbitrator in a customer case if the amount in controversy does not exceed $30,000, but the customer can request three arbitrators. For amounts exceeding $30,000.00, the Director of Arbitration selects at least three, but no more than five, arbitrators, the majority of whom are not industry arbitrators. The customer can request that a majority of arbitrators be from the industry. The Director of Arbitration appoints one arbitrator to act as chairman of the panel.

Once the Director of Arbitration selects a panel of arbitrators, notice will be given to all parties of the identity of the arbitrators. Background history for each arbitrator will be provided. A party may make a further inquiry with the Director of Arbitration concerning an arbitrator if he so desires. See Rule 608 of the NYSE Code of Arbitration Procedure. Both the NASD and NYSE provide that each party has one peremptory challenge to remove an arbitrator from a panel within five days of notification of the composition of the panel. See Rule 609 of the NYSE Code of Arbitration Procedure and Section 22 of the NASD Code of Arbitration Procedure. Each party has unlimited challenges for cause to remove arbitrators.

In addition to the background information provided on each arbitrator, Section 41(f) of the NASD Code of Arbitration Procedure permits a party to get copies of all awards by an arbitrator with the SRO if requested from the Director of Arbitration within three business days of notification of the arbitrator's identity. Previous awards rendered by a panel member may give you some insight into the type of claims the arbitrator has previously heard, the awards rendered on those claims, and the damages requested by the parties and ultimately awarded by the panels. This information may assist you in making a decision whether to exercise your peremptory right to remove a certain panel member.

In addition, investigate each panel member's past affiliations. Check with other attorneys who have had experience with the arbitrators to gather insight into how these persons generally conduct themselves at hearings. For example, some arbitrators tend to ask witnesses a good number of questions, while other arbitrators may never ask questions. Also, some arbitrators may favor legal arguments as opposed to equitable arguments. If you believe that a particular panel member will likely rule against your client, you should consider challenging the member for cause (if good cause exists) or using your peremptory challenge to remove him.

Always remember than the panel selected for the hearing will decide whether your client wins or loses his case. The panel members ultimately control the outcome of your case. Avoid arbitrators who believe that all customers are greedy or gamblers, or those arbitrators who have not adhered to industry standards and rules themselves. Avoid arbitrators who are unduly legalistic.

For a discussion of the disclosures required of arbitrators and disqualification of arbitrators, see

Sections 23 and 24 of the NASD Code of Arbitration Procedure and Rules 610 and 611 of the NYSE Code of Arbitration Procedure.

IX. THE HEARING

A. Hearing Procedure

An arbitration hearing has a format that is similar to a non-jury trial. The claimant makes an opening statement, and then the respondent makes an opening statement. Opening statements are optional, but you should almost never elect not to make one. The claimant then presents his case by calling witnesses and introducing documents. Each respondent has the right to cross-examine each witness called by the claimant. The respondent presents his case next in the same fashion. Closing arguments are made, parties and counsel then leave the room, and the arbitrators usually decide the case. An award is then sent to the parties in approximately 30 days after the last hearing date.

B. Hearing Tactics

Because the Federal Rules of Evidence do not apply in an arbitration proceeding, hearsay, if relevant and material, will usually be admissible, for what it is worth. Objections to evidence are frowned upon by arbitrators. Arbitrators usually admit evidence and state that they will give it whatever weight they deem necessary. Affidavits usually can be admitted. Motions are unlikely to succeed.

Although witnesses are asked questions on direct and cross examination, testimony can often be in narrative form. Thus, if a witness wants to “explain” an answer, he usually will be permitted to do so. You should pay close attention to arbitrator's questions. Arbitrators can, and often do, ask the witnesses questions. These questions will often indicate what the arbitrators have focused on in the hearing.

Documents are often critical to proving your case, especially in cross-examination. You must know what documents to request in discovery and how to evaluate the documents so that you can effectively use them in the hearing.

X. THE AWARD

A. General

Pursuant to Rule 636(a)(4) of the NYSE Code of Arbitration Procedure and the NASD Rules of Fair Practice, Article III, Section 21(f)(1)(iv), arbitrators are not required to give factual findings or legal reasoning in their awards. Arbitrators need only give a summary of the issues in controversy, the damages or relief sought, and the damages or other relief awarded. See Rule 627 of the NYSE Code of Arbitration Procedure.

B. Vacating, Modifying, and Confirming Awards

A decision entered by a panel of arbitrators or by a single arbitrator is virtually irreversible. A very narrow set of grounds for reversal of awards is outlined in 9 U.S.C. Section 10 which states:

> In any of the following cases the United States court in and for the district wherein the award was made may make an order vacating the award upon the application of any party to the arbitration - (a) Where the award was procured by corruption, fraud, or undue means. (b) Where there was evident partiality or corruption in the arbitrators, or either of them. (c) Where the arbitrators were guilty of misconduct in refusing to postpone the hearing...or in refusing to hear evidence pertinent and material to the controversy.... (d) Where the arbitrators exceeded their powers.... (e) Where an award is vacated and the time within which the agreement required the award to be made has not expired, the court may...direct a rehearing by the arbitrators.

Thus, awards can be reversed for fraud, evident partiality, corruption, or unreasonable refusal to grant a postponement or to hear evidence. See Wilko v. Swan, 346 U.S. 427, 436-37 (1953) (dictum)("[T]he interpretations of the law by the arbitrators in contrast to manifest disregard are not subject, in the federal courts, to judicial review for error in interpretation.") and O.R. Securities, Inc. v. Professional Planning Assoc., Inc., 857 F.2d 742 (11th Cir. 1988)(Assuming arbitration awards could be set aside for manifest disregard of law, more than error or misunderstanding of law must be shown. To set aside, one would have to show that the arbitrators understood the law, properly stated it, but then disregarded it.)

Notwithstanding the narrow set of grounds for reversal, those against whom awards are entered are filing motions to vacate or modify awards in district court with more frequency. While vacating or modifying an award is still an uphill battle, some of these motions have been successful. Research indicates that of approximately 21 reported challenges made in 1990, seven were successful. In a recent Alabama decision, Robbins, et al. v. Painewebber Inc., et al., [Current Transfer Binder] Fed. Sec. L. Rep. (CCH) Para. 95,885 (N.D. Ala. April 19, 1991) an arbitration award was challenged for the arbitrators' refusal to admit evidence and for their manifest disregard of the law. The award was vacated. The district court's decision is presently on appeal before the Eleventh Circuit. The Robbins case represents a more detailed judicial review and scrutiny of the factual and legal findings of the arbitrators than most awards were subjected to in the past when challenged. Close attention should be given to the Eleventh Circuit's ultimate decision in the Robbins case as it could have an impact on future challenges to arbitration awards.
Serious consideration should be given prior to filing a motion to vacate or modify an award. By filing such a motion, one opens himself up to possible Rule 11 sanctions.

C. Other

Presently, awards from the SROs are made publicly available. Future awards purportedly will report the names of the attorneys involved in the arbitration. This should help facilitate the gathering of information from the customer's perspective from other attorneys who have pursued similar claims.

XI. MISCELLANEOUS

A. Preparation Tactics

Be prepared for “Attila the Hun” litigation tactics. Many brokerage firms will threaten sanctions or counterclaims for attorneys' fees even when your claim is meritorious. Some stonewall discovery and occasionally resort to tactics such as threatening your witnesses who are still working in the brokerage industry.
With documents, pay close attention to details. Be on the lookout for forged, backdated or missing documents.
Preparation is of paramount importance. Do not treat an arbitration case any less seriously than a trial. Finally, make sure that if you do not understand the industry, you have consulted someone who does. Educate yourself prior to the hearing if necessary.

B. Representation at Hearings

More and more non-attorneys are becoming involved in the representation of customers in securities arbitrations. Presently, neither the NYSE or the NASD require that a person be represented by an attorney at an arbitration hearing. Some customers have opted to represent themselves at hearings. Others have opted to be represented by persons other than attorneys who have knowledge of and an understanding of the mechanics of the securities industry and arbitration process.

The SIA recently made a motion that attorneys be required to represent individuals at arbitrations unless the person representing the customer had close family ties to that customer. Both the SEC and the SROs opposed the SIA's motion. SICA tabled the motion.

While qualified individuals who have knowledge of the securities industry and arbitration process may be a great help in pursuing a claim, serious problems may exist in a customer being represented by an non-attorney. First, these persons often have little or no legal training and may fail to recognize sensitive legal issues which could be important to pursuit of the customer's claims. Second, arguably the customer would not be able to maintain confidences with his or her non-attorney representative. No attorney-client privilege would exist between the client and his representative, and thus, the client could be compelled to disclose confidential information discussed with the non-attorney representative.

These and other factors should be carefully considered by the customer in electing to be represented by a non-attorney.

EXHIBIT 1

THE WIDOW SMITH

VS. CHURNEM & BURNEM BROS.

RATIOS

‘TOTAL TURNOVER’

AVERAGE EQUITY		1,778,102.00 / 16 months=		111,131.38
TOTAL PURCHASES/AVERAGE EQUITY	2,104,760.14/111,131.38	=	18.94	TURNOVER
MONTHLY TURNOVER	18.94/ 16 mos.	=	1.184	PER MONTH
ANNUAL TURNOVER			1.184 x 12 months =	14.21

'MAINTENANCE COSTS'	
TOTAL COMMISSIONS	19,005.86
MARKUP/MARKDOWN	75,666.08
MARGIN INTEREST	11,195.09
FEES/CHARGES	45.45
TOTAL COSTS	105,912.48

TOTAL COSTS/AVERAGE EQUITY	105,912.48/111,131.38	=	95.30%	
MONTHLY AVERAGE	95.30% / 16 mons	=	5.9565	
ANNUAL PERCENTAGE	5.9565 x 12 mos	=	71.48%	ANNUAL COSTS

TRADING ANALYSIS OF THE WIDOW SMITH ACCOUNT

AT CHURNEM & BURNEM BROTHERS

USING DOW AVERAGES FORM JUNE 30, 1986 THROUGH OCTOBER 20, 1987

DATE	BEGINNING BALANCE	OPENING DOW	CLOSING DOW	PERCENT CHANGE	DOW ADJUSTED PRICE	DEPOSITS OR (WITHDRAWALS)	NET ENDING BALANCE
6/30/86 - 7/8/86	34,607.00	1,892.72	1,820.73	-3.804%	33,290.72	10,641.56	45,248.56
7/8/86 - 9/25/86	45,248.56	1,820.73	1,768.56	-2.865%	43,952.04	59,000.00	104,248.56
9/25/86 - 10/17/86	104,248.56	1,768.56	1,837.04	3.872%	108,285.14	90,000.00	194,248.56
10/17/86 - 8/6/87	194,248.56	1,837.04	2,594.23	41.218%	274,313.81	100,000.00	294,248.56
8/6/87 - 10/20/87	294,248.56	2,594.23	1,841.01	-29.034%	208,815.16		
DOW JONES ADJUSTED VALUE	208,815.16						
LESS: ACTUAL	0.00						

MARKET VALUE

TRADING LOSSES TOTAL 208,815.16

THE WIDOW SMITH VS. CHURNEM & BURNEM BROTHERS

[Note: The following table/form is too wide to be printed on a single page. For meaningful review of its contents the table must be assembled with part numbers in ascending order from left to right. Row numbers, which are not part of the original data, have been added in the margins and can be used to align rows across the parts.]

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	AMOUNT	SECURITY	PURCHASE DATE	NET COST		SALE DATE	NET PROCEEDS	NET PROFIT OR LOSS	BUY PRICE	SELL PRICE
4	1,200	SURE THING	06/25/86	10,641.56		12/05/86	6,509.69	(4,131.87)	8.625	5.625
5	5,000	ZIMBABWE MOTORS pfd.	09/01/86	125,000.00		09/29/86	128,019.55	3,019.55	25.00	25.875
6	10,000	TRUST ME GROUP	09/25/86	100,000.00	5,000	10/10/86	49,107.58}	COMBINED	10.00	10.00
7			-	-	5,000	10/23/86	49,552.95}	(1,339.47)	-	10.00
8	10,000	VICTORIO WINE	09/29/86	107,500.00		10/29/86	100,000.00	(7,500.00)	10.75	10.00
9	4,000	SORE U.S. CORP	10/10/86	58,000.00		11/24/86	47,000.00	(11,000.00)	14.50	11.75
10	2,000	NATL BANK	10/22/86	43,250.00		11/07/86	44,878.50	1,628.50	21.625	22.50
11	3,000	DEFICIT CREDIT	10/29/86	61,500.00		11/03/86	66,270.68	4,770.68	20.50	22.375
12	10,000	HPSC INC wts.	11/06/86	67,500.00		05/25/87	40,000.00	(27,500.00)	6.75	4.00
13	7,000	PROSPECT GROUP-NEW	11/07/86	66,500.00	1,000	12/05/86	8,248.70}	COMBINED	9.50	8.50
14			-	-	5,000	02/24/87	46,875.00}	-	-	9.375
15			-	-	1,000	03/24/87	10,562.50}	(813.80)	-	10.5625
16	2,000	SLUDGE BOTTLING	11/21/86	33,000.00		-	- }	COMBINED	16.50	-
17	3,000	SLUDGE BOTTLING	11/21/86	49,500.00	5,000	12/22/86	70,854.97}	(11,645.03)	16.50	14.375

18	10,000	INSIDE TIP	11/24/86	52,500.00		11/27/86	51,248.00	(1,252.00)	5.25	5.25
19	15,000	STAR INT'L	12/21/86	71,250.00	10,000	01/13/87	57,547.04}	COM-BINED	4.75	5.875
20			-	-	5,000	01/13/87	28,773.14}	15,070.18	-	5.87
21	4,000	MO-JO HAND INDS	01/19/87	29,500.00		03/11/87	28,500.00	(1,000.00)	7.375	7.125
22	7,000	SNJHRNS CHFGRX INDS	01/19/87	108,107.90		01/20/87	107,747.70	(360.20)	15.25	15.589
23	15,000	VMX INC	01/21/87	52,500.00		01/23/87	49,687.50	(2,812.50)	3.50	3.3125
24	1,000	WEST-ERN STAGE-COACH	01/21/87	13,000.00		01/29/87	13,750.00	750.00	13.00	13.75
25	14,000	PRO-SPECT GROUP	01/29/87	138,250.00		03/24/87	147,875.00	9,625.00	9.875	10,5625
26	2,000	LEPER COLONY	02/20/87	47,625.00		05/06/87	40,500.00	(7,125.00)	23,8125	20.25
27	3,000	BIG GAIN GUARAN-TEE	03/19/87	33,375.00		-	- }	COM-BINED	11.375	-
28	5,000	BIG GAIN GUARAN-TEE	03/24/87	55,312.50	8,000	07/20/87	67,000.00}	(21,687.50)	11.0625	8.375
29	20,000	ANTARC-TIC MIN-ING	03/26/87	104,730.25	700	04/22/87	3,509.68}	COM-BINED	5.125	5.125
30			-	-	12,300	04/22/87	60,132.65}	-	-	5.00

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1	COMMISSION	
2	MARKUP/MARK-DOWN *	
3	BUY	SELL
4	291.56	240.31
5	1,500.00 *	1,355.45
6	2,500.00 *	892.42
7	-	447.05
8	5,119.05	5,263.16
9	2,761.90	2,473.68
10	250.00 *	120.00
11	1,000.00 *	854.32

12	1,500.00 *	1,250.00
13	1,750.00	251.30
14	-	625.00
15	-	187.50
16	1,000.00 *	-
17	1,250.00 *	1,020.03
18	1,500.00 *	1,252.00
19	1,500.00 *	1,202.96
20	-	601.86
21	1,000.00	500.00
22	1,357.90	1,375.30
23	1,875.00	937.50
24	365.00 *	125.00
25	3,500.00	2,625.00
26	625.00	500.00
27	750.00	-
28	937.50	1,000.00
29	2,230.25	87.50
30	-	1,537.50

THE WIDOW SMITH VS. CHURNEM & BURNEM BROTHERS

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1											
2			PUR-CHASE	NET		SALE	NET	NET PROFIT	BUY	SELL	
3	AMOUNT	SECUR-ITY	DATE	COST		DATE	PRO-CEEDS	OR LOSS	PRICE	PRICE	
4			-	-	7,000	04/22/87	35,095.47}	(5,992.45)	-	5.125	
5	4,000	STAR TECHNO-LOGIES	04/21/87	18,500.00		-	- }	COM-BINED	4.625	-	
6	4,000	STAR TECHNO-LOGIES	04/21/87	18,500.00	8,000	05/26/87	29,000.00}	(8,000.00)	4.625	3.625	
7	2,000	CATO	04/22/87	24,000.00		10/15/87	12,122.50	(11,877.50)	12.00	6.25	

		CORP-NEW 'A'									
8	7,000	CATO CORP-NEW 'A'	04/22/87	84,000.00		05/27/87	74,812.50	(9,187.50)	12.00	10.6875
9	7,000	WEST-ERN STAGE-COACH	05/06/87	84,000.00	1,000	06/04/87	10,500.00}	COM-BINED	12.00	10.50
10			-	-	2,000	06/08/87	20,000.00}	-	-	10.00
11			-	-	2,000	06/19/87	20,000.00}	-	-	10.00
12			-	-	2,000	09/04/87	25,000.00}	(8,500.00)	-	12.50
13	7,000	WEST-ERN STAGE-COACH	05/20/87	75,250.00		07/10/87	72,187.50	(3,062.50)	10.75	10.3125
14	11,000	VIC-TORIO WINE	07/10/87	79,750.00	3,000	07/24/87	20,625.00}	COM-BINED	7.25	6.875
15			-	-	8,000	08/06/87	58,000.00}	(1,125.00)	-	7.25
16	7,000	VIC-TORIO WINE	07/20/87	56,875.00		08/12/87	53,375.00	(3,500.00)	8.125	7.625
17	1,000	HIDDEN PAYOUT L.P.	08/06/87	50,000.00		09/18/87	23,798.16	(26,201.84)	50.00	24.25
18	1,000	HIDDEN PAYOUT L.P.	08/06/87	50,000.00		10/12/87	18,474.71	(31,525.29)	50.00	18.875
19	1,000	COLGATE PAL-MOLIVE	08/12/87	52,249.18	400	10/12/87	18,610.29}	COM-BINED	51.625	47.125
20			-	-	600	10/12/87	27,840.50}	(5,798.39)	-	47.00
21	2,500	CATO CORP-NEW 'A'	09/18/87	23,593.75		10/15/87	15,156.25	(8,437.50)	9.4375	6.063
22	2,000	MONEY-MAKER LTD	10/12/87	14,875.00		-	- }	COM-BINED	7,4375	-
23	2,000	MONEY-MAKER LTD	10/12/87	14,875.00	4,000	10/20/87	25,000.00}	(4,750.00)	7.4375	6.25
24	2,000	MONEY-MAKER LTD	10/12/87	14,875.00		-	- }	COM-BINED	7.4375	-
25	2,000	MONEY-MAKER LTD	10/12/87	14,875.00	4,000	10/20/87	20,250.00}	(9,500.00)	7.4375	5.0625
26		TOTALS		2,104,760.14			1,903,998.71	(200,761.43)		

****

********** This is piece: 2

****

1	COMMISSION	
2	MARKUP/MARK-DOWN *	
3	BUY	SELL
4	-	875.00
5	1,250.00 *	-
6	1,250.00 *	1,000.00
7	500.00 *	377.50
8	4,000.00 *	3,937.50
9	3,375.00 *	552.63
10	-	500.00
11	-	500.00
12	-	1,315.79
13	750.00 *	1,312.50
14	500.00 *	375.00
15	-	0.00
16	875.00	875.00
17	1,750.00 *	451.84
18	1,750.00 *	400.29
19	624.18	239.71
20	-	359.50
21	468.75	468.75
22	375.00	-
23	375.00	500.00
24	375.00	-
25	375.00	750.00
26	53,156.09	41,515.85

EXHIBIT 2

May 14, 1990

Deborah Masucci, Esq.
National Association of Securities Dealers
NASD Financial Center
33 Whitehall Street
New York, New York 10004

Re: Dr. Clean/Demand for Arbitration

Dear Ms. Masucci:

The undersigned represent Dr. Clean ("Dr. Clean") in connection with certain claims he possesses against Churnem & Burnem Securities ("Churnem & Burnem") and its registered representatives, C.D. Broker and I.M. Crook ("Churnem & Burnem, C.D. Broker and I.M. Crook here-

inafter collectively referred to as “Respondents”). Dr. Clean has instructed us to write this letter of complaint demanding arbitration of disputes arising between Dr. Clean, on the one hand, and Respondents, on the other.

In summary, Dr. Clean is seeking the recovery of significant damages which he has suffered as a result of fraudulent and deceitful practices perpetrated by Respondents. During the period that Dr. Clean maintained his account at Churnem & Burnem, the fraudulent and manipulative practices committed by Respondents included:

(a) Directing and effecting excessive trades in Dr. Clean's account and churning said account for the primary purpose of producing substantial amounts of commissions;

(b) Making and effecting unauthorized and discretionary trades in Dr. Clean's account without having been granted formal discretionary authority and without implementing the appropriate procedures for handling a discretionary account;

(c) Directing and effecting unsuitable trades in Dr. Clean's account; and

(d) Misrepresenting or omitting to state material facts to Dr. Clean.

These acts constitute breach of contract, breach of duty, violations of federal and state securities laws, breach of fiduciary duty, and violations of the rules and regulations of the National Association of Securities Dealers, Inc. (“NASD”) and various exchanges. Churnem & Burnem is liable to Dr. Clean for all losses sustained by Dr. Clean as a result of the misconduct practiced by Churnem & Burnem's account representatives, C.D. Broker and I.M. Crook. In addition, Churnem & Burnem is liable for its failure to reasonably supervise or prevent the fraudulent activities which occurred in Dr. Clean's account.

PARTIES

Because of the complexity of this arbitration proceeding and the multiple individuals involved, the following is a list of individuals mentioned in this complaint letter:

Dr. Clean	-	Claimant.
C.D. Broker	-	Churnem & Burnem Vice President, Investments who directed and controlled Dr. Clean's account.
I.M. Crook	-	Churnem & Burnem Account Executive who in partnership with C.D. Broker, directed and controlled Dr. Clean's account.
Churnem & Burnem Securities	-	Brokerage firm that employed C.D. Broker and I.M. Crook and which held Dr. Clean's account from September, 1986 through June, 1987.

FACTS

Dr. Clean, age 45, graduated from the Medical College of Georgia in 1968 with a degree in

medicine. Dr. Clean interests lie in emergency medicine and he is board certified in said specialty. Dr. Clean worked as an emergency staff physician at various hospitals including Floyd Medical Center in Rome, Georgia and Hamilton Medical Center in Dalton, Georgia. In June of 1986, Dr. Clean accepted a position as a full partner with Emergency Physicians, P.C., providing emergency services to St. Johns Hospital in Snellville, Georgia. As an emergency room physician, Dr. Clean works rotating twelve hour shifts of 8:00 a.m. to 8:00 p.m., 4:00 p.m. to 12:00 a.m. or 8:00 p.m. to 8:00 a.m. The twelve hour shifts are usually scheduled to be worked for six consecutive days with the following four days off. Needless to say, Dr. Clean's work schedule and his duties as an emergency room physician leave Dr. Clean with very little unoccupied time.

Prior to September 1986, Dr. Clean was a relatively unsophisticated investor who had very little investment experience. At this time, Dr. Clean previous investments consisted of purchases of three stocks which had an aggregate cost of $7,000.00.

During the Summer of 1986, Dr. Clean became interested in possibly investing in equity options. Dr. Clean's interest arose from a book entitled Making Money. The book recommended purchasing equity options, and stated that equity options were available from Churnem & Burnem at low sales-commission markups. Dr. Clean also subscribed to a newsletter, The Market Times. The Market Times was an advocate of investing in equity options.

On the basis of the foregoing, Dr. Clean called Churnem & Burnem in Atlanta to determine how Churnem & Burnem handled equity options and what risks were involved with trading equity options. At that time, Dr. Clean was referred to C.D. Broker who told Dr. Clean that too much risk was involved with equity options and that the profit to be realized was not as rewarding as stock index options which C.D. Broker reported he had extensive experience trading. C.D. Broker told Dr. Clean that 98% of all investors who invested in stock index options lost money. However, C.D. Broker said that the trading techniques he used for his clients made his clients part of the 2% of investors who realized profits in the stock index option market. Dr. Clean informed C.D. Broker that he was concerned about the risks involved in stock index option trading but C.D. Broker assured Dr. Clean that the techniques he and I.M. Crook used to trade stock index options greatly minimized risk and provided for considerable rewards. In fact, C.D. Broker represented to Dr. Clean that if he invested with C.D. Broker's and I.M. Crook's program, he could expect a 44% increase in the value of his account over a one year period.

In September of 1986, while attending a scientific assembly in Atlanta, Dr. Clean arranged a meeting with C.D. Broker and I.M. Crook. At the meeting, Dr. Clean was given a tour of Churnem & Burnem's offices and C.D. Broker and discussed I.M. Crook's stock index option program. At that time, Dr. Clean again informed the Respondents that he was concerned about the risks involved with stock index option trading and that he had no experience whatsoever with the options market. C.D. Broker reiterated to Dr. Clean, as he had in their first phone conversation, that the techniques he and I.M. Crook used in trading stock index options greatly minimized the risks that were involved and increased the profitability of stock index option trading. C.D. Broker told Dr. Clean that the techniques which were going to be used to trade Dr. Clean's funds had been developed by the same individual who had developed a computerized system to track the movement of Soviet submarines. C.D. Broker told Dr. Clean that the underlying theories of the submarine tracking system had been adapted into a stock index option strategy to follow the

shifts and changes in the stock index options market. After Dr. Clean's discussions with Respondents, Dr. Clean felt secure in entrusting his funds with the Respondents.

As a direct and proximate result of Respondent's inducements, representations and promises, on or about September 17, 1986, Dr. Clean decided to open an account with Churnem & Burnem. On or about that date, Dr. Clean delivered a check for $50,000.00 to Respondents. At that time, C.D. Broker told Dr. Clean that Dr. Clean would receive a weekly computer printout showing the positions of the stock index options he had purchased so that Dr. Clean would have an idea of what trades were being done in his account and could get a basic understanding of stock index option trading.

Thereafter, on or about September 18, 1986, Respondents opened two brokerage accounts for Dr. Clean. One of the accounts was a “securities account” and the other was an “options account”. Respondents immediately commenced trading in Dr. Clean's securities account. Initially, $50,000.00 worth of treasury bills were purchased in the securities account to collateralize and serve as margin for trading in the options account. Trading activity in the options account began in September of 1986 with purchases and sales of stock index options and continued in said account through May of 1987. During said period, trading in the options account was extremely heavy and Respondents, directly and indirectly, controlled Dr. Clean's accounts and, with one exception, directed all transactions therein to Dr. Clean's detriment. Specifically, Respondents executed trades without Dr. Clean's prior approval and advised him of the trades afterwards, despite the fact that Dr. Clean had never granted discretionary authority to any of the Respondents. Monthly statements from Churnem & Burnem evidencing such transactions in the options and securities accounts are attached hereto as Exhibits and made a part hereof. Moreover, a summary of said transactions is attached hereto as an Exhibit and made a part hereof.

The trading activity in Dr. Clean's account during the above-referenced period was excessive and unsuitable for Dr. Clean. During said period of time there were 195 purchases in Dr. Clean's account. Eighty percent (80%) of the 195 purchases were held in the account for fewer than seven days. Specifically,

(1) Seventy-eight (78) of the transactions were same day transactions.
(2) Twenty-eight (28) of the transactions were held for one day.
(3) Fourteen (14) of the transactions were held for two days.
(4) Eleven (11) of the transactions were held for three days.
(5) Nine (9) of the transactions were held for four days.
(6) Seven (7) of the transactions were held for five days.
(7) Seven (7) other transactions were held for six days.
(8) Five (5) transactions were held for seven days.

Overall, the average holding period for a purchase in the account was 6.62 days.

Moreover, during this period total commissions paid to Respondents totaled $23,610.00. The average daily equity in the account was $45,439.00. This resulted in an annual cost equity maintenance factor for Dr. Clean's account of 51.95. (See Exhibit attached hereto and made a part hereof). In other words, during the relevant period, Dr. Clean had to earn an average return on his

investment of 51.95% per annum just to pay the commissions charged by Respondents against his account.

Throughout the time period that Dr. Clean's account was opened with Respondents, Dr. Clean had problems following the status of his account. Specifically, Dr. Clean reviewed the transactions in his account each time he received a confirmation; however, the trading became so voluminous that Dr. Clean was unable to follow the activity in his account and determine the status of the account. When Dr. Clean could no longer follow what was happening in his account he contacted C.D. Broker and told him he was concerned over the high volume of trades. C.D. Broker told Dr. Clean not to be concerned about the number of transactions in the account but to focus on the alleged net profits in the account.

In February of 1987, Dr. Clean finally became suspicious about how his account was being managed. At that time, Dr. Clean had his account statements reviewed by a registered representative employed with Conn Securities who told Dr. Clean it looked like his account was being excessively traded. After excessive trading was suggested to Dr. Clean, he confronted C.D. Broker with the questionable handling of his account and C.D. Broker reassured Dr. Clean that his account was being handled properly. Shortly thereafter, on or about February 24, 1987, Dr. Clean received a letter from I.R. Bad, the Manager of the Churnem & Burnem office where C.D. Broker and I.M. Crook were employed. (See Exhibit attached hereto and made a part hereof). In the letter, I.R. Bad stated basically that he assumed Dr. Clean's account was being handled in accordance with Dr. Clean's instructions, desires and investment objectives unless Dr. Clean informed him to the contrary. On or about March 19, 1986, Dr. Clean contacted I.R. Bad and told him that he did not feel that his account was being handled properly. I.R. Bad reassured Dr. Clean that nothing was improper in the handling of his account.

Subsequent to Dr. Clean's conversations with I.R. Bad, the trading activity in Dr. Clean's account dropped substantially. However, in May, 1987, Dr. Clean lost all confidence in the Respondents handling of his account when trades solicited by Respondents resulted in additional losses in his account. At that time, Dr. Clean instructed Respondents to stop all trading in his account and on June 4, 1987, Dr. Clean closed the account. Thereafter, Dr. Clean sought professional advice regarding the Respondent's handling of his account. This undertaking culminated in the filing of this action.

ANALYSIS

An analysis of the facts clearly establishes that Respondents engaged in excessive and unauthorized trading in Dr. Clean's account and that Respondents recommended and directed investments for Dr. Clean account that were completely unsuitable for an investor of Dr. Clean's sophistication and position. Contrary to Dr. Clean's position (including his lack of sophistication as an investor and unavailability of time to monitor his investments) it is inconceivable that a prudent investment advisor would have engaged in such excessive activity, extensive unauthorized trading or recommended such investments that were totally unsuitable for an investor of Dr. Clean's sophistication. Based upon the foregoing facts, it is readily apparent that Dr. Clean has myriad of legal claims against Respondents supporting his recovery of actual damages, as well as recovery of punitive damages, interest, commissions, attorney's fees and costs. Respondents undoubtedly

failed to satisfy legal and professional standards of conduct to which they are bound to adhere and, as a result, caused substantial damage to Dr. Clean. Such inadequacies or improprieties, standing alone, certainly justify Dr. Clean recovery of his actual damages plus interest and commissions. The nature and character of Respondents' misconduct, however, is not limited in negligent conduct or inadvertent mistake. To the contrary, the Respondents have recklessly and deliberately ignored their legal and professional standards of conduct with actual knowledge that such standards of conduct were being violated, and that such violations involved serious potential problems and abuses. It is this willful and deliberate failure to act in a professional manner that supports Dr. Clean's right to recover further damages from Respondents.

Dr. Clean's claims against Respondents include, but are not limited to the following:

(1) Claims for breach of contract based upon Respondents failure to provide competent, professional services in accordance with the Rules and Regulations of the NASD and New York Stock Exchange and industry customs, practices and standards;
(2) Claims for breach of duty based upon the same inadequacies in providing professional service;
(3) Claims for common law fraud based upon the fraudulent and deceitful trading activity which the Respondents directed in Dr. Clean's account;
(4) Violations of Federal and State Securities Laws.

RESPONDENTS FAILED TO PROVIDE DR. CLEAN WITH COMPETENT PROFESSIONAL SERVICES AND THEREBY BREACHED THEIR CONTRACTUAL AND LEGAL DUTIES TO DR. CLEAN

Respondents were obligated to provide Dr. Clean with competent and professional services in accordance with applicable industry rules, regulations, customs and practices. Such obligations were mandated by the very nature of Respondents' business, business affiliations and undertakings for Dr. Clean. As securities broker-dealers and financial advisors, who are members of the NASD, New York Stock Exchange and various other exchanges, Respondents were obligated to conduct their business in accordance with various industry rules, regulations, customs and practices.

Among the obligations Respondents owed to Dr. Clean under industry rules, regulations, customs, practices and standards, were the following:

(1) Rule 401 of the New York Stock Exchange (Good Business Practices);
(2) Rule 405 of the New York Stock Exchange (Know Your Customer Rule);
(3) Rule 723 of the New York Stock Exchange (Suitability);
(4) Rule 724 of the New York Stock Exchange (Discretionary Accounts);
(5) Rule 1 of the NASD Rules of Fair Practice (High Standards of Commercial Honor/Equitable Principles of Trade);
(6) Rule 2 of the NASD Rules of Fair Practice (Suitability);
(7) Rule 18 of the NASD Rules of Fair Practice (Use of Fraudulent Devices);
(8) Rule 27 of the NASD Rules of Fair Practice (Supervision); and

(9) Rule 33 of the NASD Rules of Fair Practice (Options).

Respondents violated each of the foregoing duties and standards by inducing and directing unsuitable transactions for Dr. Clean's account, by engaging in excessive trading in Dr. Clean's account, by executing unauthorized trades in Dr. Clean's account, by failing to establish and implement appropriate supervisory procedures and by failing to investigate the investments recommended and directed for Dr. Clean.

RESPONDENTS ENGAGED IN FRAUDULENT CONDUCT AND VIOLATED DUTIES THEY OWED TO DR. CLEAN BY INDUCING AND DIRECTING EXCESSIVE TRADING AND ENGAGING IN UNAUTHORIZED TRADING IN DR. CLEAN'S ACCOUNT.

A simple review of Dr. Clean's account indicated that Respondents engaged in excessive trading in Dr. Clean's account. It is apparent that Dr. Clean's account was excessively traded. A review of said account shows that the average holding period for the 195 purchases in Dr. Clean's account was 6.62 days. In fact, as stated earlier, 80% of all trades in Dr. Clean's account were held less than 7 days. Moreover, although the average daily equity of Dr. Clean's account was $45,439.36, commissions of $23,610.00 were generated off Dr. Clean's account to Respondents. Therefore, the cost equity maintenance factor in Dr. Clean's account was 51.95% or in other words, Dr. Clean had to make 51.95 cents for every dollar he invested in the account just to pay the Respondents commissions. Such trading in Dr. Clean's account is clearly excessive when compared to acceptable standards for judging excessive trading. It is outrageous to believe that any investor would choose an investment vehicle that required a 51% return on their initial investment before any profit could be realized. Moreover, this is clearly contrary to C.D. Broker's earlier representation to Dr. Clean that Dr. Clean would realize a 44% return on his investment.

Additionally, it is clear that Respondents engaged in unauthorized trading and controlled Dr. Clean's account. Dr. Clean had absolutely no prior experience in options trading and was certainly not qualified to be engaged in heavy trading in stock index options transactions. Furthermore, it is clear that Dr. Clean lacked the expertise, time and qualifications to appreciate such trading. Dr. Clean relied upon and placed his full trust in Respondents to recommend and direct such trades as were in his best interest. However, Dr. Clean expected to have the opportunity to approve or disapprove of the activity in his account. Dr. Clean never had the opportunity to approve or disapprove of the transactions in his account because he was never (with one exception) contacted by the Respondents prior to the executions of transactions in his account. In light of the foregoing, it is clear that Respondents are guilty of excessive trading and unauthorized trading in Dr. Clean's account.

RESPONDENTS VIOLATED DUTIES THEY OWED TO DR. CLEAN BY MISREPRESENTING INVESTMENTS AND RECOMMENDING

UNSUITABLE INVESTMENTS

Respondents promoted their own interest over that of Dr. Clean by recommending and directing purchases of stock index options which were entirely unsuitable for an investor of Dr. Clean level of sophistication. Respondents were informed prior to and during the course of their dealings with Dr. Clean that he had no prior investment experience with options and that he was concerned about the risks involved with stock index options. However, relying on C.D. Broker's representations that the risks involved with stock index options were minimized under trading techniques he and I.M. Crook used, Dr. Clean agreed to open an account to trade stock index options. Nevertheless, despite Dr. Clean's unsophistication and concern of risks, Respondents recommended to Dr. Clean investments that involved substantial risks and which were purchased in great excess. Respondents' misrepresentations of the lack of risk and excessive investments shows at the very least, a callous and reckless disregard for Dr. Clean investment interests.

CHURNEM & BURNEM FAILED TO REASONABLY

SUPERVISE C.D. BROKER AND I.M. CROOK

IN CONNECTION WITH THEIR DEALINGS WITH

DR. CLEAN AND THEREBY BREACHED THEIR

CONTRACTUAL AND LEGAL DUTIES TO DR. CLEAN

Churnem & Burnem did not use reasonable diligence in its supervision of C.D. Broker and I.M. Crook in connection with the investments recommended and directed for Dr. Clean. Churnem & Burnem failed to take affirmative steps to establish the level of sophistication of Dr. Clean to transact business in the high risk investments in which he was trading. Moreover, Churnem & Burnem failed to inquire or check whether Dr. Clean's account was being handled on a discretionary basis and to insure that appropriate steps were taken to implement discretionary trading procedures if the same were necessary. Had Churnem & Burnem conducted a reasonable investigation, it would have undoubtedly realized that the stock index options recommended and directed for Dr. Clean's account were not prudent and were being excessively traded. Churnem & Burnem should not have permitted excessive stock index option trading to be conducted in Dr. Clean's account.

DAMAGES

The rule of the Eleventh Circuit Court of Appeals regarding damages in excessive trading cases is well established. This rule of damages allows the investor to recover both the excess of commissions paid to the brokerage firm and the excessive portfolio decline resulting from the trading violations. Miley v. Oppenheimer & Co., 637 F.2d 318 (5th Cir. 1981). (See Exhibit attached hereto and made a part hereof). [Adopted as the law of the Eleventh Circuit in the decision of Bonner v. City of Prichard, 661 F.2d 1206 (11th Cir. 1981)]. In the Miley case, the Court held as follows:

> Once the gravamen of the churning complaint is clearly identified, the argument that awarding both excess commissions and excess portfolio decline constitutes double recovery appears to be without merit. The willful misconduct at the core of a churning complaint is the broker's excessive trading of an account in an effort to amass commissions. While excessive commissions represent the sole source of gain to the broker from his misconduct, there are in fact two distinct harms which may be proximately caused by the broker's churning of an account. It is necessary to remedy both harms in order to fully compensate the victimized investor. First, and perhaps foremost, the investor is harmed by having had to pay the excessive commissions to the broker- the 'skimmed milk' of churning violation. The broker's wrongful collection of commissions generated by the intentional, excessive trading of the account constitutes a compensable violation of both the federal securities laws and the broker's common law fiduciary duty, regardless of whether the investor's portfolio increased or decreased in value as a result of such trading. Second, the investor is harmed by the decline in the value of his portfolio - the 'spilt milk' of the churning violation - as a result of the broker's having intentionally and deceptively concluded transactions aimed at generating fees, which were unsuitable for the investor. The intentional and deceptive mismanagement of a client's account, resulting in the decline in the value of that portfolio, constitutes a compensable violation of both federal securities laws and the broker's common law fiduciary duty, regardless of the amount of the commissions paid to the broker. In sum, once a jury finds the broker has churned an investor's account, it may also find that the investor would have paid less commissions and that his portfolio would have had a greater value had the broker not committed the churning violation ... where there is excessive trading in an account ('churning'), the customer can be damaged in many ways. He must pay the brokerage commissions on both purchases and sales, he may miss dividends, incur unnecessary capital gain or ordinary income taxes depending on the holding period, and, most difficult to measure, he may lose the benefits that a well-managed portfolio in long-term holdings might have brought him.... 'Most often, the customer complains the broker churned unsuitable securities. Then, both causes of action are appropriate and both damage theories [excess commissions and excess decline in portfolio value] should be considered..'

Id. at 326 (Emphasis added).

Moreover, although Courts have realized that it is impossible to specifically determine the exact amount of the investor's loss of value of his portfolio, the Courts have also realized that a refusal to grant any compensation for the decline in portfolio value would be to assume, in effect, that all of the broker's transactions were legitimate. Accordingly, the Courts have approved an award of damages based on an estimation of losses sustained by the investor. In the Miley case, the Court held as follows:

> In order to approximate the trading losses caused by the broker's misconduct, it is necessary to estimate how the investor's portfolio would have fared in the absence of such misconduct. The trial judge must be afforded significant discretion to choose the indicia by which such estimation is to be made, based primarily on the

> types of securities comprising the portfolio.... This mode of estimation utilizes the average percentage performance and the value of the Dow Jones Industrials or the Standard and Poor's Index during the relevant period as the indicia of how a given portfolio would have performed in the absence of the broker's misconduct.

Id. at 328.

Based on the Miley damage formula, Dr. Clean is entitled to recover damages from Respondents equal to approximately $42,218.81. First, Dr. Clean is entitled to recover “skimmed milk” damages (excessive commissions) in the amount of $23,610.00. (See Exhibits attached hereto and made a part hereof). Second, Dr. Clean is entitled to recover “spilt milk” damages (trading losses caused by Respondent's misconduct) in the approximate amount of $18,608.81 (as of June 4, 1987, the day Dr. Clean's withdrew the last monies from his account at Churnem & Burnem). Dr. Clean's calculation of his spilt milk damages is based upon how Dr. Clean's account would have performed between September 18, 1986, and June 4, 1987, based on the average percentage performance and value of the S&P 500 Index during this period taking into account all deposits and withdrawals affecting Dr. Clean's account.

DEMAND FOR RELIEF

Based on the foregoing, Dr. Clean demands judgment against Churnem & Burnem, C.D. Broker and I.M. Crook, jointly and severally, as follows:

(a) for actual damages to Dr. Clean of $42,218.81; such amount to be determined based upon the proof of specific damages presented before the Arbitration Panel;

(b) for punitive damages of $25,000.00; such damages being awarded to punish Respondents for their wrongful conduct and to deter Respondents from engaging in such conduct in the future. Please note that punitive damages are expressly permitted in 11th Circuit arbitration proceedings; See Willoughby Roofing and Supply Co. v. Kajima International 776 F.2d 269 (11 Cir. 1985); Nivin v. Dean Witter Reynolds, Inc., et. al, CCH Fed. Sec. L. Rep. para. 92,257 (N.D. Fla. 1985); Willis v. Shearson/American Express, Inc. 569 F.2d 821 (N.D. N.C. 1983) (See Exhibit 12 attached hereto and made a part hereof);

(c) for all of Dr. Clean's costs, expenses and disbursements, including reasonable attorneys' fees in pursuing this arbitration proceeding;

(d) for such other relief as the arbitration panel deems just and proper.

DEMAND FOR ARBITRATION

Based upon the foregoing, Dr. Clean demands arbitration of his pending disputes with Churnem & Burnem, C.D. Broker and I.M. Crook in front of an arbitration panel in Atlanta, Georgia acting under the sponsorship of the National Association of Securities Dealers, Inc.

Respectively submitted,
PAGE & BACEK
By: J. Boyd Page
By: Brian N. Smiley
By: Sandra L. Goddard