The Use Of Experts In Securities Arbitration

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I. THE ROLES/PURPOSES OF THE EXPERT

Experts can be used in many different roles other than to simply testify at trial. Experts can be used to help draft a claim, to help draft discovery, to evaluate settlement offers, to provide opinions on technical issues, and to help prepare for the cross examination of your opponent's expert, among other things. In each of these roles, though, the expert's role is to explain and to summarize.

A. Explainer - Simplifies Complex Subjects

You should use your expert to explain critical points you want to make in your case. In doing so, however, you must make sure that your expert can explain those key points in a manner in which the average person can understand. Otherwise, expert testimony can be too complicated and cryptic, and thus boring. Good experts can take complex subjects and by using every-day language bring them down to a level that most persons serving as arbitrators can understand.

B. Summarizer

Your expert should also be used to summarize critical points you want to make in your case. A good expert is almost like having a closing argument during the course of your trial or hearing. He can take facts on which prior testimony and exhibits have been offered and summarize those facts and exhibits and state his opinions. Having an expert go through the handful of critical points you want to emphasize from prior testimony and from exhibits that have already been introduced can be invaluable.

Limit your expert's testimony only to those key points you want to highlight in your case. If you try to get your expert to go through too many facts and exhibits and fail to summarize the material, you run the risk of boring your arbitrators.

II. THE DECISION TO USE AN EXPERT

A. Do You Need an Expert - Some Considerations

1. Subject Matter

Before you hire an expert witness, think carefully about whether one is needed and whether your client can afford an expert. If you have a particularly strong case and the wrongdoing is clear and easily understood, you may not even need an expert. For example, if you are in an arbitration and you represent an elderly widow living on social security whose account had an annualized turnover rate of 15, do you really need an expert to tell the arbitrators that her account was excessively traded? Remember that at least one panel member will be from the industry and will be

familiar with acceptable standards of conduct within the industry. If you were in court with the same case, you could very well need an expert to explain turnover rates and standards of excessive trading to a jury.

In other cases in which you have a particularly exotic investment, such as a derivative product, you may need to hire an expert to explain the investment to the arbitrators.

Determine the area in which you likely will need an expert. If you have a large complicated case encompassing a great deal of trading, you will probably need an expert on damages unless you and your opponent can stipulate as to what the damages are. If you have a claim pursuant to a very particular section of the federal securities laws or your state's securities laws, you may want an expert on the law such as a professor. If supervision and the broker's activities with regard to his handling of your client's accounts are key issues, you may want to hire an expert who has experience in the brokerage industry as a branch manager or compliance officer.

2. Cost

The cost of the expert is another consideration. Can the elderly widow living on social security afford a $300 per hour expert? Generally in cases involving losses of less than $100,000, great consideration should be given to proceeding without the use of an expert or with only limited use of an expert. For example, in a case involving less than $100,000 you may want to hire an expert for the limited purpose of helping you pinpoint the strengths of your case and directing you to the documents you will want to gather in discovery.

3. Consider Your Forum

Arbitration brings with it an entirely different set of considerations in determining whether to employ an expert. In most arbitrations in which a public customer is a party, you will be presenting your case to a panel of three arbitrators, one of whom will be classified as an “industry arbitrator.” [FN1] The industry arbitrator presumably will bring some basic knowledge of the securities industry to the table which he or she can share with the other nonindustry panel members. The two “public” panel members will generally be professionals of some sort - attorneys, accountants, business owners, corporate executives, or college professors. Most of these individuals also will have some basic understanding of the securities industry, especially if they are experienced arbitrators who have sat through several prior securities arbitrations. Thus, while it may be essential to have an expert that can explain simple and basic concepts involving the securities industry to a jury, such an expert is likely insignificant in arbitration.

The use of experts in arbitrations is also more flexible than in court. Not only can you use experts to explain complicated investment products to the panel, you may wish to present experts on the applicable law in your case. Unlike in court, you may be able to offer unusual experts, such as polygraph experts if the case warrants such.

In arbitrations, oftentimes the expert witness can sit through the entire presentation of the case before he is called upon to testify. According to the *Arbitrator's Manual:*

> Arbitrators have the authority under the Uniform Code to determine who may attend the hearing. Sometimes there is a disagreement among the parties as to whether an expert witness should be permitted to attend the hearing sessions at times other than when testifying. Arbitrators should consider that expert witnesses often serve an important role in assisting parties and their counsel in the presentation of their cases, and also may be asked to testify about what has been said at the hearing in addition to the facts known to them prior to the hearing. Barring countervailing reasons, expert witnesses who are assisting parties in the presentation of their cases should be permitted to attend all hearings. Generally, there is a presumption that expert witnesses, as opposed to witnesses testifying as to the facts pertinent to the case, will be permitted to attend the entire proceedings.

Arbitrator's Manual, p. 26. (October 1996). Remember also that in arbitration proceedings, as opposed to court, generally there are no depositions. Thus, you will not have the opportunity to take the deposition of your opponent's expert witness prior to the hearing.

B. How Do You Pick An Expert?

Coming up with the appropriate expert witness for your case can be a daunting task. Start by determining what type of expert you may need and then start talking to your colleagues. Find out whom they have used and their experiences, both good and bad, with certain experts. Once you have several experts for consideration, do some background investigation of the expert. Get a copy of your expert's CRD (if he is a licensed securities professional). Are there any disclosure items on the CRD which would hurt his credibility? For example, you might not want to use someone as your expert to argue a brokerage firm did not exercise adequate supervision over a registered representative if he has been sanctioned for lack of supervision.

If you need an industry expert from a particular area of business, such as the hotel industry, look into various professional societies and organizations to determine whom the “experts” are in that particular industry. Look also in trade journals to see who is writing articles on the subjects at issue in your case.

Review the expert's credentials. Look him up on the internet and in other databases to see what has been written about him in the press, if he has ever been quoted on any particular subject, what prior positions he took on certain issues, and what he may have written. If the expert has written any treatises governing the subject matter of his proposed testimony, get a copy of the treatise.

Once you have narrowed your search of potential experts, contact the experts and see if they have any interest in taking on your case. First, screen the expert for conflicts of interest. Tell him who your client is and who you are bringing a claim against or defending. If the expert is interested in your case and has no conflicts, offer to send him some basic information about the claim for him to review. Likewise, ask the expert you are considering if he has any transcripts of any of his prior testimony that you could review. If he does not have any transcripts, ask him about his prior cases and contact the attorneys who handled the cases to get their impressions and any transcripts they may have of his testimony.

If possible, meet the expert prior to hiring him. What is your first impression? Does he make a good impression? If not, why? Talk with the expert about your case. Does he seem interested in the facts and your client? If not, find someone else. Find out how busy the expert is. If the expert has already been hired in too many other cases, he may have problems devoting the appropriate time to your case.

Is the expert credible? Arbitrators often decide who wins a case based on the credibility of the witnesses and the attorneys. If the arbitrators think that your client is not telling the truth, then you will likely lose your case even if
your expert witness is the most credible witness in the entire proceeding. If the arbitrators think that your expert is not believable, his testimony could very well detract from your case.

Use an expert who is well-respected and that has some experience suitable to your needs. Don't try to stretch an expert on damages into an expert on supervision if he has no experience in a supervisory role.

III. TYPES OF EXPERTS

Experts most commonly used in securities cases generally fall within two categories - financial experts and industry experts.

A. Financial Experts

Financial experts can include accountants, economists, and academics, among others. Financial experts can provide useful assistance in calculating damages and evaluating the accounts at issue to determine losses incurred. Such an expert can also assist you in scheduling the trades in the accounts at issue. If needed, a financial expert can assist you in calculating turnover ratios, cost equity maintenance factors, in and out trading patterns, holding periods, and other ratios that may be important to your particular case. Financial experts can also be useful in analyzing offering memoranda and quarterly and annual reports to help spot accounting irregularities that are at issue in a misrepresentation or nondisclosure case.

B. Industry Experts

Industry experts can fall into two broad categories depending on the type of case you are pursuing. First, if you are bringing a claim against a broker/dealer in arbitration, you may need an industry expert that can testify as to what the customs, practices and standards are within the securities industry with regard to the handling of an account. Industry experts can include former employees of brokerage firms, self-regulatory organizations, government agencies, or academics.

If you are bringing a large class action or group lawsuit, you may need an “industry expert” to testify about the particular industry practices for the security which is the subject of the class action suit. For example, if you are bringing a class action suit involving the hotel industry, you may need experts who are familiar with the hotel industry and the manner in which property is acquired and fees assessed. You may want an expert to identify for you what is important from a

disclosure standpoint and to assess the fairness of the disclosure made to the class participants by the defendants.

C. Unique Experts

In a securities case, you may find that you need that you need certain unique experts to testify as to very particular facts and circumstances. For example, in arbitration you may want to hire an expert simply to educate the panel on the law at issue. This is particularly true if you believe that the panel may tend not to know or not to demand adherence to the law. You may want to use a polygraph expert to administer a polygraph exam to your client and then to testify as to the results. You may need a handwriting expert or documents examiner to testify that certain documents were forged or altered. Other experts could include linguistic experts, psychologists, or psychiatrists, among others.

IV. USE OF EXPERTS

A. When to Hire An Expert

Whether you decide to use an expert witness to evaluate your client's case or to testify at hearing depends, in part, 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 cases (whether in arbitration or in court), 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 to request in discovery.

B. Using Experts in Investigation and Drafting

Oftentimes you may want to use an expert to help you analyze a case to determine if the case is worth pursuing. For example, if you do not have anyone in-house who can calculate damages and do other mathematical calculations to indicate excessive trading, experts can be hired solely for this purpose. Experts can do basic calculations of a client's account to determine how much the client lost, when the losses were incurred, if the account was churned, if losses were incurred on only a handful of positions, if commissions were excessive, or if any other trading patterns exist which would point to potential abuses in the account such as day trading or other short term trading, mutual fund flipping, or end of the month trading. You can then use such calculations to determine how best to advise your client to proceed. For example, if the 75 year old widow living on social security and income from a modest portfolio only lost $5000 over a five year period and no blatant abuses exist in the account, you probably would not advise the client to go through the expense of pursuing a claim in arbitration. If, on the other hand, the 75 year old widow only lost $5000 over a five year period, but had a turnover rate in excess of six, then you would want to look at the commissions charged by the broker as a possible measure of damage or have your expect calculate what a well managed portfolio would have earned during the same period of time.

In addition to doing basic calculations of losses incurred pursuant to different damage theories, experts can help you decipher complicated, esoteric products prior to drafting your Statement of

Claim. For example, if your client invested in a complicated derivative product, an expert can assist you in analyzing the prospectus or private placement memorandum to determine what the product is in layman's terms, how it works, what risks it entailed, and whether those risks were adequately disclosed. Such information can be invaluable when you are evaluating the potential claims of your client and when drafting the claim you intend to file on behalf of the client.

C. Using Experts In Discovery

An expert can also assist you in discovery with a case. Experts can identify certain documents you need to seek through discovery and can assist you in explaining why you need such documents if you are forced to file a motion to compel. Once documents are gathered from your opponent, experts can assist you in reviewing the documents to determine what information may be contained therein which can be used to help prove your case.

D. Using Experts to Evaluate Settlement Demands and Offers

Experts can assist you in evaluating the settlement value of your case. Experts can help you see the strengths and weaknesses of your case and can counsel you whether offers made to settle are within the realm of reason, and can often assist you in explaining the various strengths and weaknesses of a case to your client. Often experts, and particularly those who serve as arbitrators, can offer their insight on the probably ranges of awards in similar cases.

E. Using Experts During the Arbitration Hearing

As explained above, in arbitration experts are usually allowed to sit through an entire hearing and are permitted to testify based upon the various testimony they hear during the course of the proceedings. For example, you may want an expert to testify whether in his opinion the Respondent exercised proper supervision over the broker at issue. The expert could testify based upon hearing the testimony of the broker, the manager, the compliance officer, and others and based upon any documents the Respondents produced evidencing any supervision over the broker and the accounts at issue.

Unfortunately, having an expert sit through an arbitration proceeding to listen to testimony can be prohibitively expensive in some cases. If so, you may want an expert to review transcripts of prior testimony and to testify based upon such transcripts and any documents he has reviewed. If your expert can sit through the entire hearing, he can also help you with your questions of other witnesses. For example, having just listened to a broker testify about a key issue in the case, your expert may come up with several important follow up questions for the broker. In addition, your expert may pick up on subtle nuances in the broker's testimony that deserve further questioning.

Although arbitration is less formal than court, it is generally far better to have your expert appear to testify in person than by telephone at an arbitration hearing. Having an expert testify by phone leaves the impression that your case is not important enough for him or her to appear.

If you decide that your case warrants the appearance of one or more experts at the hearing or trial, you must decide if you want your experts to prepare any written reports in conjunction with

their testimony. Such reports are generally called for in discovery, and in arbitrations, at the least must be produced to your opponent at least 20 days prior to the first scheduled hearing date.

If you are going to use an expert on damages, make sure you get your expert's reports well before your 20 day production so that you can review them to ensure that the expert has done the reports that you want to use. For example, you may want to present information regarding how a well-managed portfolio would have performed during the time in question. A well-managed portfolio could be based upon the performance of the S&P 500, a balanced mutual fund, an index fund, or simple interest at the legal rate for your state. You need to decide in advance what strategy best fits the facts of your case. Getting your expert's report early will also give you a chance to spot check it for errors. Experts are human and mistakes can certainly be made. Better to find such errors prior to the hearing than while your expert is testifying.

V. PRESENTING THE EXPERT

Your examination of your own expert should consist of the following (a) the expert's qualifications to serve as an expert; (b) the conclusions the expert has reached about your case; and (c) the basis for these conclusions.

Start your examination by briefly introducing the expert. Then, begin covering your expert's qualifications in more detail. Don't rush through your expert's background. Make sure the panel hears that your expert has experience and expertise in the areas on which you want him to testify. If your expert has been qualified to testify as an expert in other cases, have him explain that he has been qualified and what the scope of his testimony generally has been in the past. For example, if your expert has testified ten times prior to your case on the issue of proper supervision and you want him to testify about proper supervision in your case, then highlight his prior qualification as an expert in that area. While your opponent may want to paint your expert as a “professional” witness, by covering prior testimony during direct you defuse some of your opponent's attack.

If your expert has ever been denied qualification as an expert, find out why prior to calling him as an expert. Your opponent will likely ask your expert if he was ever denied qualification and you do not want to hear that the answer is yes for the first time during your case. If your expert was denied qualification for a specific reason, you may want to address the issue during your direct examination of the expert to make it seem less significant to the arbitrators.

If you intend to call an expert witness to testify on behalf of your client, do not assume that because the expert has testified previously that little or no preparation is necessary. Spend some time going through the expert's testimony prior to the hearing. If you have hired an expert to explain an exotic investment, make sure that you understand the expert's explanation. If you cannot understand your expert's testimony, then chances are the panel won't understand him either. Your expert's conclusion must make sense or he will lose credibility and you will accomplish nothing other than boring the arbitrators.

If you have a complicated investment or investment strategy to explain, consider having your expert use charts or graphs to help explain the investment or strategy to the arbitrators. Charts and

graphs can be effective if kept simple. If your expert's charts and graphs are too confusing and contain too much information, they will not be effective and the arbitrators may resent having to spend time looking at charts they do not understand.

The general impression your expert makes on the arbitrators is also important. Your expert should be used to explain a handful of important items about your case to the arbitrators. If your expert comes across as arrogant, the arbitrators may not like him and they may disregard much of what he has to say. If your expert comes across as unprepared, the arbitrators may resent having to listen to his testimony.

Make sure your expert has the time to devote to your hearing or case. Nothing leaves a bad impression on a panel of arbitrators like an expert who keeps checking his watch because he has a plane to catch. Also, beware of experts who at breaks during the arbitration are constantly on their cell phones or checking messages within view of the arbitrators. Again, it leaves the impression with the arbitrators that the expert is more concerned about his next assignment than the case at hand.

Lastly, prepare your expert for cross examination. Bring up perceived weaknesses in your case during your direct examination of your expert if he can explain and defuse them. Make sure that your expert answers questions from opposing counsel without becoming hostile. Even if opposing counsel becomes hostile and disrespectful, your expert should at all times maintain a calm, professional demeanor. In every case there are facts that favor the Claimant/Plaintiff and facts that favor the Respondent/Defendant. Make sure your expert is willing to concede those facts on cross that any reasonable person would acknowledge help the other side. If he takes too extreme of a position, he will lose credibility with the arbitrators. Also, if your expert makes a mistake in his calculations which opposing counsel finds, he should be willing to concede the mistake.

VI. ATTACKING THE EXPERT

A. General

Whether to attack your opponent's expert and how to go about doing it takes some careful thought and consideration. In arbitration, because there are no depositions, your cross examination of your opponent's expert can only be “planned” to a limited extent. You can anticipate how the expert will testify, but you will not know what he is going to say until the hearing.

1. Carefully Consider How to Attack and Whether to Attack

Sometimes the best attack of your opponent's expert is no attack. You may decide to simply question the expert to tie down his specific opinions, and then use your own expert to show that such opinions are flawed. If your opponent's expert is good, you do not want to simply give him the opportunity to regurgitate every point he already made during his direct examination.

If you do decide to cross examine your opponent's expert about his opinions, you should at all times be courteous. Being rude to the expert will not play well with arbitrators.

Try to keep your cross-examination short and focused on the main thrust of the expert's testimony. Long and drawn out testimony from experts can often bore arbitrators.

2. Importance of Depositions if Available

If you can depose your opponent's expert, do so. While depositions are generally not available in arbitrations, if the arbitrators are willing to permit depositions, take advantage of their availability. Pin down your opponent's expert's opinions and the facts upon which he bases those opinions during his deposition.

3. Preparation - prior works, writings, articles, testimony

In addition to reviewing the expert's resume (and CRD report, if applicable) and any documents the expert prepares for the case, search for additional information on the expert. Search the internet and online databases for articles either written by the expert or in which the expert is quoted. Look for books authored by the expert and read them. Try to get transcripts of the expert's testimony in other cases. Check with other attorneys who have cross examined this expert in other cases. Check any reported decisions or awards to see if the expert is mentioned and why. Review prior arbitrator awards to see what type of awards the expert has given in other securities cases in which he has sat as an arbitrator. Ask your opponent to produce a list of securities cases in which the expert has served as an expert. Get copies of the decisions or awards in those cases and review them. Check out the expert's background and credentials.

By reviewing the expert's prior testimony and any information regarding the expert from the computer, you can often predict what the expert is going to say and you can more effectively prepare your cross-examination of him.

B. Areas of Attack

1. Challenge Qualification

Just because your opponent calls a person as an expert, do not necessarily accept the person as an expert. You can make challenges to the person's qualifications as an expert, and can at times have success in getting the person disqualified as an expert in certain areas. For example, in an arbitration case, your opponent may call a person to testify about supervision. If the person has never held a supervisory position in the securities industry, has no supervisory licenses from the industry, and has never authored any of the accepted treatises on industry practices, standards and customs, you may get such person disqualified on the issue of supervision.

2. Challenge Prejudice, Bias, and Interest

You may be able to challenge your opponent's expert by arguing that he is prejudiced, biased or has an interest in the litigation that clouds his judgment and renders his opinions suspect.

a) Financial Interests - Fees

First, find out what the expert's financial interests in the litigation are. Ask him how much in fees he has been paid by your opponent to give his opinion in a case. Compare your opponent's expert's fees to those of your own expert and to the damages in the case. An expert who has been paid an exorbitant amount for his work on a case may lose quite a bit of credibility.

b) Business Relationships & Friendships

Find out what sort of relationship the expert has with your opponent. If he has testified in 20 other cases on behalf of your opponent over the last three or four years, you can certainly argue that he does not want to jeopardize his long-term relationship with your opponent.

3. Challenge "Facts"/Assumptions

Tie down all essential facts/assumptions relied upon by the expert. Obtain admission that if the facts or assumptions were different, the expert's opinion might be different.

It is critical in attacking your opponent's expert that you first and foremost know your own case. You should be very familiar with all the facts and nuances of your case. It is likely that your opponent's expert will not be that familiar with the facts of the case because few experts take the time or feel that they have permission to take the time, and hence incur a large fee, just to become intimately familiar with all facts of the case.

4. Challenge Methodology/Procedure

If possible call the expert's methodology or calculations into question. If the expert has made a mathematical mistake, point it out. If you can come up with several mathematical mistakes, you can call into question the reliability of all of the expert's calculations. Likewise, question an expert about his methodology. For example, if the standard method for calculating turnover rates followed by other experts in the field is not the method followed by your opponent's expert, point it out for the panel.

5. Challenge Conclusion/Judgment

a) Seek an admission that "reasonable minds can differ"

Have your opponent's expert agree that his opinion is simply an opinion and that opinions can differ. Also get your opponent's expert to admit that his opinions are based upon his assumption that certain facts are true and that if such facts turn out not to be true, then his opinions would be flawed and would change.

b) Confront the expert with treatises or writings from authoritative sources

Bring popular treatises on the subjects at issue in your case to the hearing. Question the expert about the opinions of other "experts" in the field.

6. Convert Your Opponent's Expert to Your Expert

You can often get your opponent's expert to admit that some of his assumptions and his methodology are the same assumptions and methodology used by your own expert. You can also get your opponent's expert to agree that your expert has good credentials. Use your opponent's expert to confirm your own expert's work. Also, give your opponent's expert authoritative treatises and ask if he agrees with certain propositions that favor your case.

VII. PROBLEMS/FLAWS

One of the most common mistakes in using experts is being ill-prepared. You should never attempt to just “wing it” with your expert. Even if your expert has testified dozens of times and comes highly regarded, you should spend time with him to ensure that he

> a) knows the file. Don't assume that just because you have sent your expert a banker's box of documents to review that he has reviewed them and is familiar with what you deem most important;
> b) is familiar with the line of questioning that you will be covering with him. While you may not want to go through question by question your exact examination, you should at least have gone over a detailed outline of your examination with your expert;
> c) has thought of and is prepared to answer questions that you expect your opponent to raise. Don't wait until your expert is under cross examination to hear for the first time how he intends to answer questions governing the weaknesses in your case;
> d) has narrowed his focus of his role in the case. While your expert may have been very helpful in helping your come up with appropriate discovery in your case and may have helped you greatly in pinpointing the strengths and weaknesses of your claim, his role as an expert at the hearing should not be to educate the arbitrators about everything he knows or thinks about your case.

Another common mistake in using experts is overkill. Use your expert to make a few important points for the arbitrators. Having an expert go on and on about facts that are insignificant bores the arbitrators and detracts from the strengths of your case.

Another common mistake is having an expert who is arrogant, inflexible or blatantly partisan. Such experts generally lose credibility quickly.

[FN1]. In an all industry dispute, such as a dispute between two broker dealers or between a broker and his firm, the panel will consist of three industry arbitrators.