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FINANCE

## A Tortuous Road for Investors

**Arbitration battles to recover losses will be tough, but fresh ammo from regulators may help**

When Harold and Reather Weathers, a retired couple living in the Atlanta suburbs, sold some inherited property for more than \$600,000 in 1999, they hoped the proceeds would carry them through their golden years. The couple, then in their late 60s, hired a broker, David Simmons of Merrill Lynch & Co., who recommended in a 92-page analysis of their risk profile that they should put 60% of their assets into bonds. They agreed. But Simmons, they claim, later invested as much as 78% of their assets in risky and volatile stocks such as WorldCom Inc. -- with predictable results.

By September, 2002, their windfall had been halved. And when the Weatherses closed their account and merely threatened to sue, Merrill sent a terse, three-page lawyer's letter defending Simmons' actions. "Merrill was making it clear: 'If you even think about suing us, you're in for a fight,'" says Atlanta attorney J. Pat Sadler, who in March filed an arbitration claim on the Weatherses' behalf. A Merrill spokesman says: "We take vigorous issue with the allegations" made by the Weatherses.

Their plight, now being slugged out in compulsory arbitration, is far from unique. With \$7 trillion in stock market wealth wiped out since March, 2000, legions of small investors devastated by the crash are fighting back. They're arguing that their losses were due more to fraud than bad luck. Last year, a record 7,704 arbitration cases were filed by investors against brokers. New claims through March are running 24% ahead of last year's pace. "I feel like I'm running a triage unit in the plague years," says Diane A. Nygaard with a sigh. This Kansas City (Mo.) securities lawyer says she's getting 10 times as many client inquiries as she did three years ago.

A whole lot more cases are coming. State regulators, including New York State Attorney General Eliot L. Spitzer, and the Securities & Exchange Commission are planning to unveil the final terms of their \$1.5 billion global settlement with Wall Street firms over charges that their analysts' research was tainted. "Anywhere we have have an e-mail or document that's relevant to our case, we're going to make those public," vows Christine A. Bruenn, securities administrator for Maine. Legal experts say that such documents could trigger thousands of additional arbitration claims against investment banks, including Merrill, Citigroup's Salomon Smith Barney unit, and Credit Suisse First Boston.

If not prevented by the settlement, plaintiffs' attorneys hope to use the documents to launch class actions by arguing that they show massive fraud involving large numbers of investors. "If Spitzer releases the 'smoking gun' documents, you ain't seen nothing yet," says Edward J. Dovin, an Atlanta attorney with law firm Page Gard Smiley & Bishop LLP, which represents 70 clients of a former A.G. Edwards & Co. broker.

The stakes are highest for Wall Street's biggest firms. Georgetown University law professor Donald C. Langevoort predicts the total tab for settling all government and civil cases could potentially exceed \$20 billion. The bulk of that will fall into the lap of a couple of the largest firms. Brad Hintz, a brokerage analyst at Sanford C. Bernstein & Co., estimates that resolving all of the pending civil actions including arbitration cases could cost Citigroup as much as \$7 billion beyond the \$400 million it has already agreed to pay Spitzer and the SEC. For Merrill, which agreed to pay Spitzer \$100 million, settling the private suits could require an additional \$4 billion. While Hintz believes the major Wall Street houses can survive this litigation wave, it "will still be problematic and painful -- and will weigh on their stocks for the next several years." A Citigroup spokesperson notes that in December the bank established a \$1.3 billion reserve for fines and litigation, saying at the time that the charge was a "prudent measure toward putting all of these matters behind it." Merrill declined to comment.

The brokerage industry is taking off the gloves, refusing to cave in to clients just because they lost big in the market. Investors' lawyers claim that firms such as Merrill are far less ready to settle cases. According to the NASD, which oversees arbitration, the number of cases settled by firms declined seven percentage points, to 37%, in 2002. Beverly Hills attorney Phil Aidikoff says that Merrill is offering to settle fewer than one complaint out of every 10. A Merrill spokesperson says: "Where a claim has merit, we attempt to resolve it. And where it doesn't, we defend ourselves. Unfortunately, we have seen a surge in baseless claims as a result of the bear market."

Investors' lawyers claim that banks are using delaying tactics to clog up the process and wear down their opponents in arbitration proceedings. Nygaard says that on two occasions in April, an NASD staff attorney in Chicago, who manages arbitration claims, has called asking her to fax legal papers that the NASD had lost.

The combination of record complaints, coupled with Wall Street's stall tactics, could cripple the arbitration process, plaintiffs lawyers charge. Already, the average time to resolve disputes through arbitration has edged up from an average 15.7 months in 1999 to 17.4 in 2002. The NASD argues that the increase is in part because the regulators are allowing litigants more time both to select mutually acceptable arbitrators from the NASD pool and to reach settlements. "I'm not at all distressed about our turnaround time," says Linda D. Fienberg, who heads the NASD's dispute-resolution program.

An example of the arbitration miasma can be found in the plight of about 80 former Procter & Gamble Co. workers who, on the promise of 20% annual returns, quit their jobs and entrusted their retirement savings to William F. Gibbs Sr., manager of A.G. Edwards' branch in Augusta, Ga. (BW -- Feb. 24). Lawyers representing Edwards in those claims, the St. Louis firm of Blackwell Sanders Peper Martin LLP, have assigned the P&G cases to just two of the firm's 300 attorneys. One of the attorneys informed the plaintiffs' lawyer Page Gard's Dovin in a Mar. 18 letter that they couldn't handle more than 11 cases a year between the two of them -- roughly one a month, with time out for summer vacations. Attorneys for Edwards declined comment.

At that rate, Dovin says, it could take eight years for his clients to get their proverbial day in

court: "What am I supposed to tell any client who walks in tomorrow -- 'Sorry, but we can't get you an arbitration hearing before 2010 or 2011'?" Growing old and gray while awaiting justice - a scenario that could have been written by Kafka. But it's everyday stuff in the circle of Hades called "arbitration."

By Dean Foust in Atlanta