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FINANCIAL ADVISERS

(Non)Binding Arbitration

Disputes between investors and brokerages are handled by arbitrators. But their rulings aren't always the end of the line.

By SUZANNE BARLYN

Binding arbitration is meant to be the last word in disputes between investors and brokerage firms. But in a growing number of cases it isn't, securities lawyers say, as more and more awards are being challenged in court.

Journal Report

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Two celebrities are among the most recent to learn that, for any investor, winning at securities arbitration doesn't always mean the check is coming soon—or even that it will ever come.

Former professional basketball star Horace Grant hasn't seen a dime of a \$1.5 million award ordered by arbitrators in September 2009 in his case against Morgan Keegan & Co.; the [Regions Financial Corp.](#) unit is seeking to overturn the ruling in federal court in California. In February, a California state court threw out an \$11.6 million arbitration award to actor Larry Hagman—including \$10 million in punitive damages to go to a charity of his choice—for losses he incurred as a client of a unit of [Citigroup Inc.](#) Mr. Hagman is appealing that decision.

A firm's ability to challenge an award in court may come as a surprise to many investors, because securities firms typically require customers to agree to resolve any disputes through arbitration. But federal law gives either party the right to appeal an arbitration award under very limited circumstances; common allegations are that an arbitrator violated the law in handling the case or was biased.

The lengthy court battles that often ensue impose a financial burden on investors, who not only have to do without the money an arbitrator awarded but also have to pay additional legal fees. The delay can grind an investor down, says Constantine Katsoris, a professor at Fordham University School of Law in New York and a longtime arbitrator. Sometimes investors settle for less than the amount an arbitrator awarded rather than continue to fight in the courts.

Grant Denied

The Financial Industry Regulatory Authority, which runs the nation's securities arbitration forum, says it doesn't keep statistics on how many rulings are challenged. But the number is rising, says Peter Mougey, president of the Public Investors Arbitration Bar Association, a Norman, Okla.-based group whose members represent investors in securities arbitration. He adds that high-profile cases like Mr. Hagman's and Mr. Grant's may dissuade some investors from bringing arbitration claims in the first place.

An arbitration panel awarded Mr. Grant \$1.5 million in 2009 in a case involving a family of bond funds with extensive mortgage-backed holdings that lost as much as 80% of their



Getty Images

Last month Horace Grant attended an event marking 20 years since the Chicago Bulls' 1991 championship

value when the market crashed. Morgan Keegan asked a California federal court to overturn that ruling, arguing that statements made by the arbitrators during the proceeding showed they had "predetermined the outcome," according to legal documents. The firm lost that challenge in July 2010 but has appealed that decision to the Ninth Circuit Court of Appeals. "It's a long way from conclusion," says Andrew Stoltmann, Mr. Grant's Chicago-based lawyer.

Mr. Grant, 45 years old, says the financial strain of the challenge led him to opt for a lump-sum payment of his National Basketball Association pension last year, rather than wait for annual payments to start when he reaches age 50. In November, he filed a \$3 million arbitration case against Morgan Keegan to make up for the difference between the one-time pension payment and the amount he would have received if he had waited for annual payments, according to Mr. Stoltmann.

"You have these billion-dollar companies trying to—for lack of a better word—starve you out so that you can settle with them," says Mr. Grant. But Morgan Keegan says it tries to vacate awards only when justified. "Our motions to vacate an arbitration award are focused on a singular issue—that is, we appeal when it is clear to us that there has been a reversible

miscarriage of justice," a spokeswoman says.

Time and Money

Morgan Keegan tries to vacate about 15% of the arbitration awards against it and defends against an equal number of appeals by investors, the spokeswoman says. Citigroup, which appealed Mr. Hagman's award, "occasionally" seeks to have arbitration decisions overturned and has defended itself against numerous appeals of arbitration cases by investors, says spokesman Alex Samuelson. As an example of what might prompt the company to contest an award, he says that arbitrators who fail to disclose certain information might be in violation of Finra rules and other laws.



Agence France-Presse/Getty Images

Larry Hagman, best known for the TV series "Dallas," posed at a film festival last year

In the Hagman case, Citigroup alleged among other things that an arbitrator didn't disclose that he, the arbitrator, had filed a lawsuit against his real-estate partner for investment losses and was involved in another suit related to his mother's finances. A California state judge agreed and threw out the award. Mr. Hagman's lawyer, who recently filed an appeal of that decision with a state appeals court, declined to comment on the case. The arbitrator didn't return phone calls seeking comment.

Lawyers representing investors say many struggle financially to defend against the appeals process, which can drag on for years and generate thousands of dollars in legal fees. In the original arbitration cases, lawyers normally work for a share of the award or settlement; to defend against appeals, they

normally charge an hourly rate for their time or take a bigger percentage of the award.

As an example of how long it can take for a case to run its course, Scott Silver, a lawyer in Coral Springs, Fla., recalls a case on behalf of a semiretired construction worker that was appealed for nearly four years. The investor, who won \$1.3 million in a commodities arbitration case in 2006, alleged he was sold risky

investments and was charged excess commissions. He had to defend against appeals in federal court and courts in two states, including the Illinois Supreme Court. The case ended in 2010 with \$750,000 in punitive damages vacated, leaving the investor with \$550,000 for damages and legal fees.

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