

Latin Americans seen likely victims of broker malpractice

By GILLES POUZIN

Are Miami brokers misleading Latin American investors?

Miami attorney Leoncio de la Peña suggests some do.

"In recent years, growing numbers of Latin American citizens have turned to brokerage houses in the US," says a recent media advisory about Mr. de la Peña's activities, warning it has brought "increasing numbers of cases in which funds have been mismanaged and investment strategies have been ill-conceived."

"In most cases it's been a deliberate ploy by the broker, designed to drive commissions with little regard for the interest of the investor."

From his Brickell Key office, Mr. de la Peña says he has handled between 40 and 50 cases for investors against brokers in the past seven years and receives two or three such claims a month.

"In the type of market we have, where people think it's impossible to lose money, some unscrupulous brokers are able to take advantage of people," said Michael Jones, vice president of the office of individual investors at the National Association of Securities Dealers Regulation in Washington, DC.



Photo by Sergio Alsina

Miami attorney Leoncio de la Peña says he's seeing a big increase in fund mismanagement and bad investments by brokers serving Latin American clients.

actions can occur with both restricted and unrestricted accounts if the transaction is unsuitable for the investor's risk tolerance.

Mr. de la Peña said he had such a case.

"This Argentine client had all his investments in secure blue chip stocks. The broker sold all his portfolio and placed it in zero coupon bonds, which were too risky for a 77-year-old man."

The case was settled but the client never recovered all his losses.

"It's not necessarily highly recommended to give unrestricted access to your account," Mr. Jones says. But regulators recommend one way to monitor any possible unauthorized transaction is "to read the account statements and the transaction confirmation statements that you should receive within three to five days after the completion of any transaction."

If you have problems receiving them, the regulators recommend contacting the brokerage firm's compliance officer. Each firm has one to make sure people in the firm are operating in line with securities rules and regulations.

Churning, Mr. de la Peña says, can be particularly costly for a client.

"A factor in determining if there has been some churning is to check what kind of stocks the broker has bought and sold for his client," he says. "Very often they are the same stocks."

That, he says, means that unscrupulous brokers are trading in and out of the same companies,

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Michael Jones

such as IBM or Coca-Cola, just to generate commissions.

The speed of this "churning" is another important factor, Mr. de la Peña says.

"We've seen some turnover in the area of two to three times in a single quarter," he says, meaning the client's portfolio has been entirely sold and bought back two or three times over that period — as many as 12 times in one year.

Most professional investors, such as pension funds or cautious mutual funds, by comparison, sell and buy back an entire portfolio only once every five years.

When investors feel cheated they can complain — but they don't always do that.

"Some of them don't do anything when they've been misled," Mr. de la Peña says. "South Americans don't know they have recourses and they don't have much faith in their litigation system in general."

Should they have more trust in the arbitration system that prevails in brokerage disputes rather than in regular courts?

The National Association of Securities Dealers, like the New York Stock Exchange, is considered self-regulatory, meaning it

does its own policing to protect investors and discipline members. For instance, the association has received 5,997 arbitration filings in '97, up 6% from '96.

But arbitration is not a panacea.

"You rarely get 100% of your damage in an arbitration," Mr. de la Peña says.

"The arbitration system is not necessarily designed for clients to recover what they claim they lost," Mr. Jones adds. One reason for that, he says, is that some

people involved in brokerage malpractices may be insolvent and their employer may not be held liable for their mistakes.

A number of rules concerning arbitration have been submitted to the Securities & Exchange Commission, which has not approved them yet.

Besides, arbitration is also expensive. To bring a case to that stage, Mr. de la Peña would ask for a full contingency fee of up to 40% of the amount recovered, an hourly fee of \$250 for his legal work or offer hours at half price with a 10% to 20% contingency fee.

This is one reason why more and more investors chose to settle their case through mediation, an expedited way of negotiating disputes whose use grew by 34% last year, according to the National Association of Securities Dealers Regulation.

"Before entering into a relationship with a broker the best thing is to interview a number of brokers," Mr. Jones says. "Ask them for their references and check disciplinary history by calling our toll free number."

"You can also contact NASD offices as well as NASD Regulation to request information and

file a complaint. You can even do it on-line at our web site."

National Association of Securities Dealers Regulation would agree with Mr. de la Peña that most foreign investors are not sophisticated.

"There are cases where people want to act as if they knew more than they actually do," he said. "Investors also bear some responsibility in taking steps to guard themselves. If you don't know, you should ask. Otherwise it's better to hold on to your money than lose it."

Details: National Association of Securities Dealers Regulation, (800) 289-9999, or on the Internet at nasdr.com.

Securities Regulators To Contact

U.S. Securities and Exchange Commission
450 5th Street, NW
Washington, DC 20549
Office of Consumer Affairs
(202) 942-7040 TTD (202) 942-4066

North American Securities Administrators Association, Inc.*
One Massachusetts Avenue, NW, Suite 310
Washington, DC 20001
(202) 737-0900

American Stock Exchange
86 Trinity Place
New York, NY 10006-1881
(212) 306-1391

Boston Stock Exchange
One Boston Place
Boston, MA 02108
(617) 723-9500

Chicago Board Options Exchange
400 S. LaSalle Street
Chicago, IL 60605
(312) 786-7705

Chicago Stock Exchange
440 S. LaSalle Street
Chicago, IL 60605
(312) 663-2222

Cincinnati Stock Exchange
400 S. LaSalle Street
Chicago, IL 60605
(312) 786-8898

Municipal Securities Rulemaking Board
1150 18th Street, NW, Suite 400
Washington, DC 20036-2491
(202) 223-9347

National Association of Securities Dealers, Inc.
NASD Regulation, Inc.
1735 K Street, NW
Washington, DC 20036-1500
(301) 590-6500

New York Stock Exchange
11 Wall Street (main address)
New York, NY 10005
(212) 656-3000

Pacific Stock Exchange
301 Pine Street
San Francisco, CA 94104
(415) 393-4000

Philadelphia Stock Exchange
1900 Market Street
Philadelphia, PA 19103
(215) 496-5000

* NASAA can provide you with the telephone number of your state securities regulator
Source: National Association of Securities Dealers Regulation

Mr. de la Peña says typical cases involve three types of mismanagement: inappropriate investments, unauthorized transactions and "churning," which is excessive activity designed to generate huge commissions from a customer's account.

"Brokers have a duty to know their clients," Mr. de la Peña says. "A big factor in determining if there has been any misdoing is who the investor is."

He said a young professional with a high income can take more risks than a retired person managing his life's savings.

"What we do is look to see if there's some logic in the pattern," he adds. "There are two kinds of accounts. Restricted accounts, in which the broker cannot do anything, and unrestricted accounts, where the broker can do whatever he wants."

"As a matter of fact, very few brokers are able to do it properly. At the beginning the brokers have a tendency to be careful and to make money for their clients. Most accounts start as restricted, and if they do well, they shift to unrestricted accounts — and that's where the troubles begin."

To avoid trouble, the National Association of Securities Dealers Regulation office advises individual investors to be very clear about what their goals are.

"We also recommend you receive and read a prospectus of the investment before you buy it," Mr. Jones says.

They may not be entertaining reading, he said, but they should be made available upon request by the broker for any securities he tries to sell.

Cases of unauthorized trans-