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PERSONAL FINANCE

Is your broker consistent with objectives?

In 2000 and 2001, did you cringe when you received your investment account statement in the mail? Did you experience a deep sinking feeling as your account dramatically dropped month by month? Did you blame yourself? Well, maybe it wasn't totally your fault; perhaps your broker had something to do with it.

GUEST COLUMN

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To determine whether your broker or brokerage firm bears some responsibility for the bad things that happened in your account, the first thing you need to do is review the objectives you established with the broker.

Most brokerage firms require that you identify your investment objectives and risk tolerance when you open your account. If you don't recall what objectives you gave, your broker may have sent you a form confirming them or, in some cases, brokerage firms list your objectives on your account statements.

Next, you need to consider whether your broker's actions were consistent with your investment objectives. If you gave your broker complete discretion to buy and sell investments on your behalf

without prior approval, then he owed you special duties including the duty to advise you of risks inherent in his choice of securities for your account. He also was directly responsible for ensuring that the composition of your portfolio met your objectives.

If your account was non-discretionary, meaning that your prior approval was required for all trades, your broker's duty depended upon the action taken. If your broker made a recommendation for the account, he had to satisfy himself that the recommendation was appropriate in light of your investment objectives, financial status and needs.

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In the securities industry, this obligation is referred to as the "suitability rule." Your broker may have recommended a certain security, a portfolio allocation or a general course of trading. If the recommendation was inconsistent with your objectives and financial picture, you may have a claim even if you went along with the recommendation.

For example, say you were 50 years old in 2000 and planning to retire within five years to live off the income from your investment portfolio. You explained your plans to your broker and told him you were willing to take some risk. Your broker then encouraged you to invest heavily in technology, communications and Inter-

net stocks.

On his recommendation, you purchased several stocks that concentrated your portfolio in those market sectors. When the market fell, your account was hit particularly hard. Given your financial needs and investment objectives, the broker's recommendations were likely unsuitable.

Another possibility could be that the stocks recommended by your broker were suitable, but he pushed you to frequently buy and sell in your account. It is not suitable for a broker to encourage a moderate growth-oriented client to actively trade, particularly where the account's returns are more than offset by the commissions and fees generated by the recommended trading.

Or perhaps the broker failed to sell when you told him to or bought stocks for your account which you did not authorize.

In each of these scenarios, the brokerage firm may also be responsible to reimburse you if you prove your case. And the brokerage firm may be directly responsible to you if it should have stopped the broker's wrongful actions but did not.

This is the first of two columns addressing the responsibilities of investment brokers to their clients.

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