

Impact

An Overview of Current Legal Events of Concern and Interest

Spring 2003

Securities Arbitration May Help Damaged Investors

By: William K. Flynn



Three short years ago, few could have imagined the upheaval in the stock markets or the resulting devastation to individual investment and retirement accounts. In the Spring of 2000, the bull market was ten years strong, the internet bubble had yet to burst, IPOs were coming out about one per day, day-trading was considered a legitimate career option, and unprecedented household wealth was tied up in the equity markets. The reversal was swift and furious. By October 2002, fallout from the "dot.bombs" was still toxic, the NASDAQ had collapsed 77% from its high of more than 5000, the Dow was off more than 25%, and previously respected corporate giants like Enron, WorldCom, Tyco, Xerox, QWest and Adelphia had erased billions of phony profits in a sea of scandal. Tragically, September 11th forever erased any sense of American invulnerability, and in the end, millions of individuals lost trillions in invested wealth and retirement savings.

Now, previously shunned investment fundamentals such as asset allocation, fixed income, and dividend yields are all the rage as brokers try to tell investors how to rebuild portfolios after the "tech wreck." For many, this advice is too late for comfort, especially for retirees who have to go back to work. Throughout all is heard a common theme: "We only did what our stock broker told us ... we thought we could trust him because he was the professional ... is there nothing we can do?"

Sadly, in many cases the answer is no. If stock brokers make informed recommendations consistent with their customer's objectives and risk tolerance, they generally cannot be held responsible for investment losses. Still, financial recovery is an option in many cases because state and federal laws do hold registered securities representatives (i.e., stock brokers) accountable under a wide umbrella of legal obligations. The most commonly asserted claims fall under broad complaints of unsuitable recommendations, excessive trading ("churning"), and unauthorized transactions.

Stock brokers owe a high degree of care and must act fairly, honorably and in good faith.

Securities regulators hold stock brokers to "high standards of commercial honor and just and equitable principles of trade," which means they must "deal fairly" with customers, follow only "good business practices," and not do anything manipulative, deceptive or fraudulent. Brokers are prohibited from acting for their own interests or for anyone else's interests that conflict with their customer's, without the informed consent of their customer. These conflict of interest rules are at the core of recent Wall Street scandals of investment analysts pushing false or misleading positive stock recommendations while their co-workers lobbied for profitable investment banking work from the same companies.

Investment recommendations must be suitable.

Brokers often rationalize failure by pointing to the obvious fact that any investment can go up or down. Yet, some investments are inherently more volatile (i.e., more likely to drop further and faster than the market), and thus inappropriate for some investors. Therefore, brokers must have reasonable grounds to believe that a recommendation is "suitable." They must be "diligent" to learn the essential facts about customers and their investment experience and sophistication and recommendations must be tailored to a customer's particular risk tolerance and objectives. Common examples of unsuitable recommendations would be suggesting aggressive trading strategies to an investor who wants to preserve capital, over-concentrating investments in the stocks of only a few companies, or placing a retired fixed-income investor exclusively in stocks and no bonds or cash.

A broker may not cause excessive trading activity.

Excessive trading, commonly referred to as "churning," clearly violates a broker's obligation of fair dealing. Warning signs of churning could be short term "in-and-out" trades, buying and selling the same stock over again, high velocity or turnover, or trouble understanding account activity. Account turnover is measured as the ratio of total purchases to average account equity. For

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example, if average annual account equity is \$250,000 with \$1 million of total purchases, the annualized account turnover is four. For the average long-term investor, a turnover of even one time per year could be considered excessive. For an aggressive stock trader, a turnover of five might be normal. Another way to spot check for excessive activity is to calculate the “cost-maintenance” factor. This is done by adding all account expenses, including commissions, management fees, loads, and margin interest expense, and dividing by average account value. For example, a \$250,000 account with annual expenses of \$25,000 has a cost factor of 10%. Assuming 2% inflation, this means the account would have to return more than 12% simply to stay even!

A broker must investigate and may not misrepresent investments.

Brokers must investigate any recommendation before giving it to a customer. This means they must know the particular risks of a transaction and may recommend it only upon “studying it sufficiently to become informed as to its nature, price, and financial prognosis.” Brokers must not misrepresent the nature, quality, or risk of any particular investment. For instance, promising a customer a particular “risk-free” return on investment is a misrepresentation of fact, as would be soothing reassurances that an investor is certain to make a large amount of money.

A broker must explain the specific risks and financial impact of investment activity.

Brokers must make reasonable efforts to inform customers about all relevant facts and the specific risks of a recommended investment. If an investment is particularly risky or complex (such as options trading), brokers may not simply pass along a form risk disclosure document. Instead, they must personally explain the risks, even if a customer is highly educated or sophisticated. Importantly, for investors who are not financially sophisticated, brokers must explain any investment in terms the customers can understand. Brokers must plainly and honestly explain the nature of the expenses, losses, and profits that are being generated in the customer’s account. And, if brokers trade with discretionary authority (see below), they must honestly explain the impact and the potential risks.

Brokers may not act without prior authorization for every transaction.

Most brokerage accounts are non-discretionary, which means brokers may never buy or sell anything without explicit advance approval from their customers. Causing transactions without the advance authorizations of a customer “clearly violates” a broker’s obligation of fair dealing.

Discretionary accounts, are ripe for abuse and the source of many shattered dreams. Discretionary trading means brokers can initiate transactions on their own initiative—without asking and without even informing customers in advance. The danger of this type of account should be self evident, which is why securities regulations are clear that brokers must never exercise any discretionary power without advance written authorization from the customer and unless the account has been properly approved by management.

Securities Arbitration As An Option.

Since 1987 when the U.S. Supreme Court said that brokerage firms could require customers to give up their right to sue in a court of law, arbitration is about the only means available to resolve most common broker-customer disputes. Arbitration is a modified adversary proceeding available only by

agreement of the parties, and virtually every brokerage account agreement includes arbitration language. Most securities arbitrations are administered by the National Association of Securities Dealers (NASD) and the New York Stock Exchange (NYSE). The parties may be represented by counsel, hearings are held in designated cities (e.g., Cincinnati, Columbus, and Louisville), and decisions and awards are generally made by a panel of three impartial arbitrators, two selected from a pool of “public” panelists and one who is affiliated with the securities industry. Arbitrators are trained in the process but are not necessarily attorneys or otherwise experts in the securities business.

Each party has the opportunity to discover information and exchange documents in advance of the hearing. Attorneys may examine and cross-examine witnesses, and experts are often employed to testify about industry standards and the calculation of damages. An arbitration panel will generally rule within a few weeks after a hearing, and any awards must be paid within thirty days. Two features of arbitration different from a lawsuit are that the panel is not required to explain the reasons for its decision (although they often do) and their ruling is binding – meaning there is almost no opportunity for appeal to a higher authority.

Statistically, the securities arbitration glass is either half-empty or half-full. According to the NASD, approximately 70% of all filed arbitrations are resolved by settlement or withdrawn before a hearing. For cases that did go to hearing in 2002, approximately 55% were decided in favor of the customer, down from 61% in 1991. In 2002, arbitrators awarded damages totaling \$139 million, including \$23 million in punitive damages. This compares to \$97 million and \$15 million respectively for 2001. The average award is approximately one-half of the amount claimed by the customer. The average time from filing a claim to resolution is just over 12 months, but because of the increased rate of filings, this time is on the rise.

Although arbitration rules do not require that customers be represented by counsel, it is certain that the brokerage firms will have experienced attorneys on their side. An experienced investor’s attorney will not only know the law, but will be able to advise whether there is a viable claim in the first instance. If so, he or she will know how to present the best claims and most importantly, how to calculate and prove the best possible damages model. Most investors’ attorneys will work on a contingent fee basis in appropriate cases. Finally, investors should be aware that there are time limitations that may impact the availability of arbitration as a remedy, so investors should first seek advice from qualified counsel.

To learn more about the arbitration process, go to – www.nasdr.com and search on “investor resources.” To get information about your broker, click on “about your broker.” To find an attorney in your state who concentrates in representing investors in securities arbitrations, you can search the Public Investor Arbitration Bar Association (PIABA) attorney database located at www.piaba.org.

Mr. Flynn, a partner at Strauss & Troy, concentrates his practice in securities arbitration, securities and investment fraud, and general corporate law. He is a charter member of the Public Investor Arbitration Bar Association (PIABA), a national association of attorneys committed to representing public investors in disputes with their brokers or other financial advisors.

News of the Firm

Attorneys on the Move



Thomas C. Rink

The thoughts of all at Strauss & Troy are with the members of our military who at the time of this writing are actively engaged in our country's efforts in Iraq. We urge our friends and clients to join us in our prayers for the safe return of our nation's sons and daughters.

Thomas C. Rink has been selected to be included in the 2003-2004 edition of The Best Lawyers in America®. Only 1880 attorneys from throughout the country have been selected to appear in this publication. As inclusion is based solely upon an exhaustive peer review, this is considered a singular honor.



Charles G. Atkins

As they have for the past several years, **Charles G. Atkins** and **Thomas L. Stachler** are again teaching a Trial Practice course at the University of Cincinnati College of Law.



Thomas L. Stachler

Charles Atkins will speak on the topic of Nursing Malpractice at a Nursing Conference at Middletown Regional Hospital in April. Additionally, Mr. Atkins is one of the contributing authors of the newly published *Disability Evaluations* (second edition, Mosby 2003), sponsored by the American Medical Association. *Disability Evaluations* is the standard text in the field for the physician's medical assessment and evaluation of patient disabilities, as well as physician compliance with authorized requests from governmental or private third-party insurers seeking medical assessments and diagnoses in the context of patient eligibility for medical disability coverage.



Claudia Allen

Claudia Allen is scheduled to speak at a summer seminar entitled "Counseling the Small Business Client in Ohio," sponsored by the National Business Institute. Ms. Allen will make a presentation on employee benefits and pensions to an audience of lawyers, accountants, and financial advisors who work with small businesses.



Philomena S. Ashdown

Philomena S. Ashdown spoke at the Annual Seminar of the Bankruptcy Committee of the Cincinnati Bar Association. Her topic was "Preferences." Additionally, Ms. Ashdown was recently appointed to the Executive Committee of the Board of Trustees of Catholic Social Services.



Charles Ashdown

Charles C. Ashdown has accepted an appointment as the new Secretary of the Black Lawyers Association of Cincinnati/Cincinnati Bar Association Roundtable. The Roundtable addresses concerns and challenges faced by minority attorneys and creates constructive ways for their integration into

all aspects of the legal profession. The organization provides funds for law-related charitable endeavors, including the Summer Work Experience in Law (SWEL) program and minority clerkship programs. For several years, Strauss & Troy has supported the BLAC/CBA Roundtable, including active participation in the SWEL program.

Paul B. Calico has been elected Secretary of the Board of Women Helping Women, a non-profit organization devoted to assisting women in connection with such matters as divorce, domestic violence, and life changes. Women Helping Women strives to secure adequate funding and broad-based community support to meet the needs of those who often have no where else to turn. Mr. Calico was also selected to serve on the Nominating Committee of the Cincinnati Bar Association.

As an adjunct faculty member, **Steven F. Stuhlberg** is again teaching Legal Drafting at the University of Cincinnati College of Law. Mr. Stuhlberg and Paul Calico are again team-teaching a class on Law and Public Policy in the MBA program at Northern Kentucky University. Mr. Stuhlberg recently participated in a Legal Ethics presentation for the Potter Stewart Inn of Court at the Cincinnati Bar Association.

On Friday, June 13, 2003, **Gordon H. Hood** will be honored as a "Senior Counselor" by the Kentucky Bar Association at a ceremony at the Hyatt Regency in Louisville, Kentucky. Mr. Hood will be among 70 lawyers who are 75 years old and/or have practiced law for 50 years.

R. Guy Taft is currently serving on the Board of Trustees of the Cincinnati Bar Foundation, and was recently selected to chair the Grant Review Committee for 2003.

MAKE A DIFFERENCE TEAM

Strauss & Troy's Make a Difference Team is the proud recipient of the Northern Kentucky United Community Mid-Size Business Recognition Award, presented by the Community Recorder Newspapers and United Way of Northern Kentucky at a ceremony held at The Marquise Banquet Hall in Wilder, Kentucky.



Paul B. Calico



Steven F. Stuhlberg



Gordon H. Hood



R. Guy Taft

Client Spotlight



Building a Future with Handyman Connection®



Marvin Belkin

Handyman Connection® has revolutionized the repair and remodeling industry. It provides worry-free home repair and remodeling services throughout 80 markets across North America. Handyman Connection® is the largest organization of its kind, with 145 franchises. Its network of franchisees works with more than 4,000 experienced craftsmen who specialize in small- to medium-sized home repair. Each craftsman has a minimum of ten years experience in trades such as carpentry, plumbing, painting, and electrical work.

Marvin Belkin co-founded Handyman Connection® in 1990. Belkin and a partner were successful businessmen who had retired from their previous companies, but then discovered that retirement was a bit slow. So they created another opportunity.

They got the idea for the business when they discovered that condominium residents and homeowners at large couldn't find reputable repairmen to do small repair and remodeling jobs. Belkin did additional market research and found there was a definite void in the marketplace for these types of home improvement services, and it was a niche they could fill.

Handyman Connection® brought experience, self-respect, accountability, solid business approaches, and guarantees into the small- and medium-sized home repair marketplace. As a result, the founders created not just a business, but also an industry; an industry with the sales potential of \$40 Billion out of the larger \$150 Billion home remodeling marketplace.

The Franchise Division of Handyman Connection® was founded in 1993. Since then the growth has been rapid, reaching 145 franchises in the United States and Canada. People from all walks of life with the dream of owning their own business have discovered the impressive opportunities of Handyman Connection®, and the satisfaction of meeting busy homeowners' needs.

The founders have built a solid foundation—one that's built to last. Already, Handyman Connection® has successfully transitioned from the founders' stage by adding the professional management and expertise necessary to continue its expansion and development. Today, key personnel and experienced managers are in place to provide more support for its franchisees in ways that increase their revenues, strengthen their competitiveness and improve their market penetration.

There is also a new marketing focus to drive sales both nationally and internationally. Senior management believes that Handyman Connection® is only beginning its journey through the vast opportunities that the 'do it for me' marketplace has to offer.

Handyman Connection® proudly partners with Habitat for Humanity® International to provide training to volunteers at Women Build sites across the United States and Canada.

Handyman Connection® - The Original Home Improvement Specialist™

*More information can be accessed by visiting
<http://www.handymanconnection.com>*

Protecting Yourself Against The Unauthorized Use Of Your Credit

By: Charles C. Ashdown



The use of bank cards (credit, debit, and ATM cards) is prevalent, and most find them to be more convenient than carrying cash. That same convenience, however, makes bank cards attractive to thieves. The unauthorized use of your cards by others can be costly and may damage your credit rating.

Your first line of protection against the unauthorized use of your cards is diligence. If your bank cards are lost or stolen, you can limit your liability for unauthorized charges by following the procedures of the Fair Credit Billing Act ("FCBA") and the Electronic Fund Transfer Act ("EFTA").

For credit and debit cards, the FCBA provides that you cannot be held responsible for any unauthorized charges if you report the loss before the cards are used. If you dispute an unauthorized charge within 60 days after the first bill containing the error was mailed to you, then your responsibility for unauthorized charges is limited to \$50. If you wait to notify your credit card issuer, you could be held responsible for some or all of charges before you file the report. Because the timeliness of your notice is important, you should first report the loss by telephone, but you must follow up that notice in writing.

If you report a missing ATM card before it is used without your permission, the EFTA protects you from liability for unauthorized withdrawals. If unauthorized use occurs before you report your card lost or stolen, you can be liable for some of the charges; the amount of liability depends on how quickly you report the loss. If you report the loss within two business days, your liability is limited to \$50. Your exposure is unlimited if you fail to report an unauthorized transfer or withdrawal within 60 days after the bank statement reflecting the transaction is mailed to you.

If your purse or wallet is lost or stolen, you should cancel all credit, debit, and ATM cards that were inside. You should keep in a secure place a list of all card numbers, card issuers, and the toll free numbers to report lost or stolen cards. No other identifiable information should be kept on this list. The card issuers should be able to open a new account for you and send you a new card once you have notified them of the loss. You should also file a report with the local police department immediately. Keep a copy of the report in case your creditors need proof of the crime.

If you have questions about one or more transactions on your monthly statement and believe that one of your cards is being used fraudulently, report the suspicious activity to the card issuer first by telephone, then in writing. Identify the date, amount, and merchant (if applicable) involved in the unauthorized charge. A sample letter is included at the end of this article. Most card issuers have a separate address for reporting questionable charges. Do not send your letter to the payment address unless you are directed to do so.

The three major credit bureaus will place a 90-day "fraud alert" on your file if you believe that you are the victim of unauthorized use of your identity and/or your credit. This fraud alert requires you to be notified prior to any credit

being issued under your name. Equifax can be reached at 1-800-525-6285 (www.equifax.com); Experian (formerly TRW) can be reached at 1-888-397-3742 (www.experian.com); and TransUnion can be reached at 1-800-680-7289 (www.transunion.com).

You can also notify your financial institutions that you want a password or personal identification number (PIN) placed on your accounts. If you believe your social security number and/or date of birth have been used fraudulently, you can report the fraud to the Federal Trade Commission at 1-877-FTC-HELP or file an on-line report using their Identity Theft Complaint Input Form at www.ftc.gov. Additionally, you should notify the Social Security Administration if your social security card is stolen. The toll-free number is 1-800-269-0271.

It is a good idea from time to time to request a copy of your credit report from the three major credit bureaus to be sure it is accurate. Credit bureaus may charge up to \$8.50 for a copy of your report; however, they must give you a free copy of your report if it is inaccurate because of fraud.

Diligence is your best defense in protecting your credit and preventing unauthorized charges or withdrawals. Review your monthly statements carefully. If you find unauthorized or questionable charges, provide the proper notices promptly and in writing.

Charles Ashdown is a partner in the firm's Corporate and Business Department. He regularly practices in the area of consumer rights.

Sample Letter

To: Card Issuer
(address for billing inquiries)

Re: Your name, address, and account number

Dear Sir or Madam:

I am writing to dispute a billing error in the amount of \$____ on my account. The amount is inaccurate because (describe the problem). I am requesting that the error be corrected, that any finance or other charges related to the disputed amount be credited, and that I receive an accurate statement.

Enclosed are copies of (describe supporting information, such as sales slips, payment records, or police reports) supporting my position. Please investigate this matter and correct the billing error as soon as possible.

Names & Signatures for all account holders

Enclosures: Sales Slips
Payment Records
Police Reports

Cincinnati Residential Real Estate Tax Abatements

By: Sara E. Mills



If you have been putting off remodeling or purchasing a home in the City of Cincinnati, a new tax abatement program may change your mind. The Cincinnati City Council recently expanded the City's Community Reinvestment abatement program to include residential property located anywhere within the City limits. The new program, administered by the City's Department of Community Development and Planning, is intended to stimulate revitalization, retain residents, and attract new homeowners to the City. The program applies to qualifying renovation work and new construction of one-, two-, or three-unit homes or condominiums.

Abatement Limitations

Tax abatements are available for up to ten years for renovation and up to fifteen years for new construction. If the owner of a \$75,000 home makes \$25,000 in qualifying improvements, a ten-year abatement would exempt the \$25,000 improvement for ten years, meaning that the homeowner would pay taxes only on the original \$75,000 value. However, the owner is still responsible for increases in taxes due to voted changes (such as school levies) or reappraisals required by state law.

The maximum amount of the abatements is \$78,818 of "assessed value," which equates with approximately \$225,193 in market value. This results in a significant savings to the taxpayer — a \$78,818 abatement would save the homeowner approximately \$4,000 in yearly taxes.

While new home/condominium construction generally qualifies for the abatements, not all improvements to existing homes are eligible. Renovation work, such as the addition of a garage or deck, will qualify for an abatement,

but maintenance work, such as painting or roofing, generally does not qualify even though it improves the condition of the house. Likewise, exterior landscaping and driveway work does not typically qualify.

The Process for Obtaining a Tax Abatement

An application for tax abatement must be submitted no later than 18 months after completion of construction/renovation. The homeowner must submit the abatement application along with the following documents to the Department of Community Development and Planning:

- receipts or other documentation verifying the cost of the improvements. (For new construction, the taxpayer must include the settlement statement issued in connection with the bank loan or a notarized list of categories of work and the expenses for each category.);
- a copy of the tax bill for the property;
- a legal description of the property;
- copies of relevant building permits or certificates of occupancy.

If the work qualifies, the Department of Community Development and Planning determines the length of the abatement based on a formula that takes into account the nature of the construction or improvements. The Hamilton County Auditor's Office determines the amount of the abatement. Following an appraisal, the Auditor's Office makes the appropriate reductions to the property valuation and taxes. If a tax abatement request is denied, the owner may appeal to the Community Reinvestment Area Housing Council.

Currently, it takes six weeks to six months from submission of the application to the issuance of an abatement. For reasons relating to the timing of issuance of tax bills, applications for abatement for construction completed in 2003 should be submitted no later than December 31, 2003.

Sara Mills worked with the City in connection with the tax abatement program. Strauss & Troy attorneys Charles Postow and Andrew Shott can assist property owners in obtaining both residential and commercial tax abatements.

Certain states, including Kentucky, do not certify specialties of legal practice. Certain states, including Ohio, do not provide for recognition as a specialist in any area or field of law, except for patent, trademark or admiralty. IMPACT is published quarterly to provide information of general interest and not to provide legal advice concerning any specific situation. If you wish additional or more specific information, please contact one of the attorneys at Strauss & Troy. This is an advertisement.



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