HOW TO PROVE DAMAGES AND ASK FOR THE RIGHT REMEDY

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1. What Causes of Action Should Be Plead? Does "The Kitchen Sink" Approach Work?

We have all seen these Statements of Claim, and some of us may have even drafted them more than once. A relatively straightforward unsuitability case, with a nice, but misguided and inexperienced broker. Just the wrong product for the retired widow. No real evidence of fraud. But the statement of claim contains twelve violations including 10b-5 Fraud; common law fraud; violations of State Securities Laws; violations of Rules of Fair Practice; Negligence; Breach of Fiduciary Duty, etc. etc.

The threshold question, of course, is does it really make much sense to allege, for example, a 10b-5 violation for what is essentially an unsuitability, failure to supervise case? The simple answer is rarely, if ever, for several reasons. First and foremost, by alleging a full panoply of wrongs using the shotgun approach, some of which just don't fit the fact pattern, you invite defense counsel, who of course get paid by the hour, to crank out motions to dismiss the claims that don't apply. It's like losing the first battle of a war. Why risk poisoning your own well by having the first thing the Panel learns about your case is that some of the causes of action either are untimely (i.e. the short statute of limitations of Rule 10b-5 alleged violations); don't provide a private cause of action (i.e. the long standing dispute over whether there is, in law, a private cause of action for violations of NASD Rules of Practice); or simply do not apply. Why allege those? You certainly can refer to them during your case, but they rarely get you anywhere other than more work by pleading them.

2. How to Present the Law at the Hearing Using the K.I.S.S. Method.

We have all heard it a number of times, "Keep it Simple Stupid". Oftentimes we forget that the Panel has not been spending the last few months researching the relevant law in preparation for the hearing. As an active NASD panelist, having sat on numerous cases and having decided many motions to dismiss, Erwin Shustak, who tries to be prepared as possible, usually does not read the relevant papers until the evening before, or the morning before the hearing or telephonic motion. Often, Claimant submits a 10 page pre-hearing brief. The Respondents submit a 20 page brief with 150 citations, most of them string cites, and the Panel comes to the hearing either "dazed and confused" if they actually read the briefs, or "wide-eyed" and usually unsure of what the relevant law really is.

A. Present the Relevant Law at the Hearing

In our experience, the K.I.S.S. method is certainly the way to go. Prepare a simple pre-hearing brief focusing on favorable law. Forget long recitations of the facts; the facts will come out at hearing and the Panel will have read a diametrically opposed factual scenario in the opposing papers. Prior to the hearing, we find it very helpful to prepare simple handouts for the panel and present them on an E.L.M.O. (much better than the old fashioned overhead projectors) during

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our opening. We display relevant, simple quotes and statements of the law in our "show and tell" presentation. Panels typically will recall a simple quote shown bigger then life on a screen than they will finding it buried in a lengthy complicated brief. Don't forget that most panelist are not attorneys and briefs and string cites mean nothing to most of them. They need to be spoon-fed, in very small spoonfuls, the few, salient legal points. This forces the panel to read and listen to the law; while at the same time giving them something simple they can rely on when awarding damages.

B. <u>Use a Law Professor</u>

We have also found it very helpful to use a law professor to assist in presenting legal authority. Not only does this enhance the credibility of your argument, it also really helps the Panel understand the law. Remember, law professors, at least the good ones, are accustomed to teaching concepts to law students in a way they will understand. Obviously, hiring a law professor as an expert can be costly and may be economical only in a large damage case, but we have had excellent results using law professors who are specialists in their respective areas. We have used a Dean of a law school whose specialty was securities law; a Professor who wrote the book on broker-dealer law and, most recently, our own Professor Joe Long, one of the best legal experts we have used, who recently testified in a case we had in Utah involving State Securities Laws of California, Arizona and Utah. Joe Long wrote the two-volume treatise on "State Securities Laws", published by West. He put his two volumes on the table and proceeded to give a complete and thorough discourse on why the various state securities laws did not apply in our case (it was a defense case for a national charity). Law professors are like "talking briefs". The sole arbitrator (it was a AAA case) was also a law professor and paid very close attention to Joe's testimony. Arbitrators, in our experience, are much more apt to listen to what an expert has to say than they are to read a brief.

3. <u>The Measure of Damages-How to Get Away From the Pure Out Of Pocket Approach</u>

A. <u>The California State Securities Act - The Perfect Cause of Action if Applicable</u>

In order to determine if the California State Securities Act applies to a particular transaction, review California Corporation Code Section 25008, which provides that a sale of a security is made in California, for purposes of the Act, when the offer to sell emanates from this state, *or* when the offer to buy is accepted in this state. California Corporations Code § 25008(a) and (b). Thus, a sale occurs "in this state" even if the purchaser is in, and communicates acceptance of the offer to sell from, for example, New York. *Diamond Multimedia Sys., Inc*. v. *Superior Court*, 19 Cal 4th 1036, 1050 (Cal S. Ct. 1999).

i. Civil Liability for Non-Registration Securities

If the case involves a private offering of unregistered securities in California, we conduct extensive discovery on the offering, usually with the guidance of an expert in California Blue Sky laws, to determine if the offering was properly exempt from registration. If a sloppy transactional lawyer failed to properly qualify the offering for an exemption, you may have a great opportunity to seek rescission of an investment in a case that may otherwise be difficult to win. Evidence of non-registration can be demonstrated by obtaining a certificate of non-registration, or similar document, from the California Department of Corporations. The

Respondent must then prove that a valid exemption applies as an affirmative defense.[2] Cal. Corp. Code §§ 25110, 25102.

ii. Misrepresentations or Omissions Under Cal. Corp. Code § 25401

Cal. Corp. Code § 25401 prohibits the offer, sale or purchase of a security through communications that include an untrue statement or omit a material fact.[3] Cal. Corp. Code § 25501 provides the remedies available to a plaintiff victimized by a violation of § 25401 and includes a suit for damages or rescission.[4]

Cal. Corp. Code §§ 25401 and 25501 differ from common law negligent misrepresentation in that: (1) proof of reliance is not required, (2) although the fact misrepresented or omitted must be "material," no proof of causation is required, and (3) plaintiff need not plead defendant's negligence. Rather, § 25501 provides that as an affirmative defense to a § 25401 cause of action, a defendant may: (1) prove that he exercised reasonable care and did not know of the untruth or omission; (2) show that even if he had exercised reasonable care, he would not have known of the untruth or omission; or (3) show that the plaintiff knew the facts concerning the untruth or omission. Cal. Corp. Code § 25501; *Bowden* v. *Robinson*, 67 Cal. App. 3d 705, 715 (Cal. Ct. App. 1977).

B. <u>The Boam Case</u>

In *Boam v. Trident Financial Corporation*, (1992) 6 Cal.App.4th 738, Plaintiffs purchased limited partnership interests and successfully brought an action against the general partner for statutory securities fraud under California Corporations Code § 25401. Plaintiffs were awarded damages consisting of their entire investment of $182,130.00. Plaintiffs appealed, however, arguing the verdict was defective, as a matter of law, because they were not awarded mandatory interest pursuant to Cal. Corp. Code § 25501.

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[2] If the offering is not public and less than 35 unaccredited investors are involved, who are each sophisticated, Respondents may relay on a Federal Rule 506 exemption, which preempts state Blue Sky laws. A Rule 506 exemption may apply where Respondents reasonably believed the unaccredited investors were sophisticated and capable of evaluating the merits and risks of the prospective investment. 17 CFR § 230.506(B)(2)(ii). One way to avoid this is to demonstrate that the offering was public, via a seminar to prospective investors who were not properly screened and pre-qualified.

[3] Cal. Corp. Code § 25401 states: It is unlawful for any person to offer or sell a security in this state or buy or offer to buy a security in this state by means of any written or oral communications which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading.

[4]Cal. Corp. Code § 25501 states: Any person who violates Section 25401 shall be liable to the person who purchases a security from him or sells a security to him, who may sue either for rescission or for damages (if the plaintiff no longer owns the security), unless the defendant proves that the plaintiff knew the facts concerning the untruth or omission or that the defendant exercised reasonable care and did not know (or if he exercised reasonable care would not have known) of the untruth or omission. **Upon rescission, a purchaser may recover the consideration paid for the security, plus interest at the legal rate, less the amount of any income received on the security, upon tender of the security.**

After interpreting the definition and use of the word "may" contained in § 25501, the court likened it to "must" or "shall", and held that when a violation of a California state securities law is involved, the damages **must** be calculated as follows: "Consideration" + "Interest" – "Income received" = "Recovery". Failure to grant the statutory damages, including interest in this case, violates the law and provided grounds to set aside the award. *Boam*, 6 Cal. App. 4th at 744, 745.

C. Violations by Registered Investment Advisers

When you have a claim involving a Registered Investment Adviser, and the Claimant entered into a contract for "advisory services," it is worth investigating whether any portion of the contract violates the Investment Advisers Act of 1940 ("Act"). If the contract does violate a Section or Rule of the Act, the United States Supreme Court has held that a limited private right of action exists under Section 215 for rescission.[5] In *Transamerica Mortgage Advisors, Inc. v. Lewis*, (1979) 444 U.S. 11, the Supreme Court concluded "that when Congress declared in § 215 that contracts are void, it intended that the customary legal incidents of voidness would follow, including the availability of a suit for rescission or for an injunction against continued operation of the contract, and for restitution." *Transamerica*, 444 U.S. 11, 19.

For example, if an advisory contract provides for "compensation to the adviser on the basis of a share of the capital gains, or the capital appreciation of the funds" of the claimant as defined in Section 205(a)(1), then the investor must be a "qualified client" pursuant to Rule 205-3.[6] If the Claimant is not a "qualified client," or does not meet any of the other exceptions, then the contract violates the Act and is void, allowing for rescission. Often, these are facts are unknown at the outset and surface only after discovery. In a recent case handled by our office, the respondents turned over a letter from the S.E.C. indicating that the Investment Advisory failed to comply with the Act in two regards. First, the Investment Advisor and the Offering Materials required the investor to be an "accredited investor" (i.e. net worth of at least $1 million) when, in fact, the law had been changed several years earlier requiring the investor to be a "qualified client" with a minimum net worth, after the investment, of at least $1.5 million. In addition, the SEC found the offering circulars were defective and misleading in that they depicted annual returns based solely on the returns received by someone who had invested early on in the program. Having had the SEC find the offering to be defective and misleading in those two regards, gave us a statutory basis for rescission, a much easier case to prove that a substantive argument of whether the investment was unsuitable.

D. California Rule: "The Benefit of the Bargain" Damages

When there are no statutory violations and the claims involve a breach of fiduciary duty (unsuitability, churning, etc.), Respondents will throw all sorts of case law in their brief

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[5] Section 215(b) of the Investment Advisers Act of 1940 states: Every contract made in violation of any provision of this title and every contract heretofore or hereafter made, the performance of which involves a violation of, or the continuance of any relationship, or practice in violation of any provision of this title, or any rule, regulation, shall be **void** (1) as regards the right of any person who, in violation of any such provision, rule, regulation, or order shall have made or engaged in the performance of any such contract…

[6] Rule 205-3(d)(1) (CFR 275.205-3) states: the term **qualified client** means…A natural person who has a net worth (together with assets held jointly with a spouse) of more then **$1,500,000** at the time the contract was entered into.

supporting “net out-of-pocket” losses as the proper measure of damages.[7] In California, however, courts have routinely granted plaintiffs the “benefit of the bargain” measure of damages in breach of fiduciary duty cases. The “benefit of the bargain” damages includes the value of the plaintiff’s securities at the time the Respondent advised the customer to alter his or her portfolio, plus the amount such securities would have earned (assumed earnings), less the value of the securities and cash returned by defendants.” *Twomey v. Mitchem, Jones & Templeton*, (1968) 262 Cal.App.2d 690, 730-731.

In *Twomey*, the defendants breached their fiduciary duty to plaintiff by advising her to switch to unsuitable investments and engage in excessive transactions. In granting the plaintiff the “benefit of the bargain” damages, the court relied on Cal. Civ. Code § 3333:

> “For a breach of an obligation not arising from contract, the measure of damages, except where otherwise expressly provided by this code, is the amount which will compensate for **all** the detriment proximately caused thereby, whether it could be anticipated or not.”

In addition, the court specifically rejected the defendants argument that damages based on what the securities would have earned was too conjectural and speculative. The court stated, “It may be inferred that the portfolio selected by the defendants did not do as well because it was unsuitable for the customer’s needs, and not because of market fluctuations.” Furthermore, there would be merit in attributing part of the loss to market conditions, only if that drop would have affected the “proper portfolio for the type of customer involved”. *Twomey*, 262 Cal. App. 2d at 731-732.

The “benefit of the bargain” rational in *Twomey* has been cited in other seminal California cases when awarding damages resulting from a breach of fiduciary duty. In *Vucinich v. Paine, Webber, Webber, Jackson & Curtis*, 803 F.2d 454 (9th Cir. 1986), the court went even further and held that it was “an abuse of discretion” to not allow the plaintiff to introduce expert testimony to prove the value of the “benefit of the bargain” damages and held:

> The district court also excluded expert testimony as to what the present value would be of the stocks in the portfolio Vucinich inherited. **The established California measure of damages for breach of fiduciary duty “in advising plaintiff to switch into unsuitable investments” is the difference between what the plaintiff has now and what the plaintiff would have had on the date the fiduciary relation closed if plaintiff had retained the original portfolio and had received the benefit of its appreciation and dividends**. (Citing *Hobbs*, 164 Cal. App. 3d at 197). California rejects the view that such damages are conjectural and speculative and that the plaintiff might have done worse “if

[7] Common cases cited by the respondents supporting “net-out-of-pocket” theme, or worse, for measuring damages in various circumstances include: *Rolf v. Blyth, Eastman Dillon & Co*., 637 F.2d 77, 84 (2d Cir. 1980) (Damages measured by difference in market value of account before and after the fraud adjusted by the percentage change in the appropriate market index); *Barrows v. Forest Laboratories Inc*., 742 F.2d 54 (2d Cir. 1984) (Court rejected benefit of bargain theory as too speculative); *Messer v. E.F. Hutton & Co*., 833 F.2d 909 (11th Cir. 1987) (Court upheld J.N.O.V. on damage award holding that investor had failed to prove lost profits because he did not show the existence of a investment plan which incorporates a predetermined response to market conditions); *Resolution Trust Co. v. Strock, Strock & Laven*, 1994 WL 241639 (S.D. Fla. 1994) (Court denied claim for lost profits because comparison with standard index, was as a matter of law too speculative) *Ambassador Hotel Co. v. Wei-Chuan Inv*., 189 F.3d 1017, 1030 (9th Cir. 1999) (Measure of damages in 10b-5 case, without a breach of fiduciary duty is out of pocket losses, not benefit of the bargain)

left to her own devices" (Citing *Twomey*, 262 Cal. App. 2d at 731) If the plaintiff is entitled to such damages, she is entitled to prove them. Expert testimony was an appropriate way to introduce a mathematical calculation that could as easily been introduced by stipulation. In excluding the testimony the trial court abused its discretion. *Vucinich*, 803 F.2d 454, at 461-462.

In *Hobbs v. Bateman Eichler, Hill Richards, Inc*, (1985) 164 Cal. App. 3d 174, the court used the "benefit of the bargain" method of calculating compensatory damages and awarded punitive damages against the firm.[8]

E. Sales by Unlicensed Individuals - "Finders Law"

In January 1, 2005, a new arrow for the quiver arrived in the form of the "Finders Law." Following the passing of California Assembly Bill 2167, Cal. Corp. Code § 25501.5 was added and reads:

> (a)(1) A person who purchases a security from or sells a security to a broker-dealer that is required to be licensed and has not, at the time of the sale or the purchase, applied for or secured from the commissioner a certificate under Part 3 (commencing with Section 25200), that is in effect at the time of the sale or purchase authorizing the broker-dealer to act in that capacity, may bring an action for rescission of the sale or purchase or, if the plaintiff or the defendant no longer owns the security, for damages.
>
> (2) Upon rescission and tender of the security, a purchaser may recover the consideration paid for the security plus interest at the legal rate, less the amount of income received on the security.
>
> (4) Damages recoverable under this section by a purchaser shall be an amount equal to the difference between the following: (A) the price at which the security was bought plus interest at the legal rate from the date of purchase; (B) the value of the security at the time it was disposed of by the plaintiff plus the amount of any income received on the security by the plaintiff.
>
> (b) The court, in its discretion, may award reasonable attorney's fees and costs to a prevailing plaintiff under this section.

The legislative purpose of this new law is to crack down on the unlicensed individuals who locate and solicit investors. "Finders" are normally instrumental in raising capital for private placements and are normally compensated based on the amount of funds they raise. Oftentimes, finders will actually sell a security on behalf of an issuer. As of January 1, 2005, such conduct carries harsh civil penalties that should be exploited the next time your claim involves a finder. (The full text of Assembly Bill 2167 and news article from *The Pipe Report* interpreting the same are attached in Appendix "A")

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[8] A more detailed discussion of *Hobbs* is contained the "Punitive damages" section below.

4. <u>Beefing Up the Damages</u>

A. <u>Legal Fees - Mutuality of Demand</u>

As a general rule, our firm virtually always asks for attorney's fees, primarily since we know that by asking for them, as a purely "knee jerk" reaction, defense counsel will similarly ask for them, thereby stepping into our trap. We use the series of cases that hold that where both sides in an arbitration ask for legal fees, they have implicitly authorized the Panel to award legal fees. This can be very effective for a Panel that wants to award legal fees but is on the fence.

Where both parties to an arbitration seek attorney fees, courts routinely hold the parties have thereby jointly submitted the issue to the arbitrators, who then have the parties' consensual jurisdiction to award attorney fees. *U.S. Offshore, Inc. v. Seabulk Offshore, Ltd.*, 753 F. Supp. 86, 92 (S.D.N.Y. 1990). In *Seabulk*, the Court concluded that since both parties had requested attorney fees, the arbitrators had the power and authority, given them by the parties who both asked for them, to award legal fees and costs:

> **If both parties sought attorney fees, as was apparently the case here, then both parties agreed <u>pro</u> <u>tanto</u> to submit that issue to arbitration, and the arbitrators had jurisdiction to consider that issue and to award them**. *Seabulk Offshore, Ltd.*, 753 F. Supp. at 92. See also, *Accord Prudential-Bache Secs., Inc. v. Tanner*, 72 F.3d 234, 243 (1st Cir. 1995) (finding that where both parties requested attorney's fees from the arbitration panel, the awarding of fees was within the scope of the agreement to arbitrate); *First Interregional Equity Corp. v. Haughton*, 842 F. Supp. 105, 112 (S.D.N.Y. 1994), citing *Neuberger & Berman v. Donaldson Lufkin and Jenrette Securities Corp.*, No. 91-16833 (N.Y. Sup. Ct., N.Y. County 1992).

In *Marshall & Co., Inc. v. Duke*, 114 F.3d 188 (11^{th} Cir. 1997), the Eleventh Circuit Court of Appeals reached the same conclusion., involving an appeal from a District Court judgment confirming an NASD arbitration that included attorney fees. On the issue of the Panel's authority to award legal fees and costs where both sides requested them, the Court of Appeals observed:

> First, the parties agreed to submit the issue of attorney fees and expenses to the Panel so that an enforceable "bi-lateral agreement" exists. Second, the NASD rules and the Uniform Submission Agreement executed by the Claimants provide for submission of all disputes by the parties to the arbitration. Third, every judicial and quasi-judicial body has the right to award attorneys' fees under the common law bad faith exception to the "American Rule." *Marshall & Co., Inc. v. Duke*, 114 F.3d at 189-190 (citations omitted).

The *Marshall* Court went on to note that:

> The district court held that the panel could award attorney's fees under all three sources of authority. Only one source of authority is necessary to affirm that decision. Since it appears clear that both parties sought an award of their fees, without a jurisdictional objection from the other, the issue of who should get fees

> and how much was effectively submitted by agreement of the parties. In any event, the arbitrators have the power to award attorney's fees pursuant to the "bad faith" exception to the American Rule that each party bears its own attorney's fees. *Marshall & Co., Inc. v. Duke*, 114 F.3d at 190.

In light of the fact that both Claimants and Respondent have requested an award reimbursing their legal fees in this matter, the Arbitrators are also empowered to award fees and costs. *The Arbitrator's Manuel* (May 2005), pg. 32.

B. <u>California Financial Abuse of Elder Statute</u>

Another way to beef up damages, when the facts are appropriate, is to assert that respondents financially abused an elder, and therefore, the statute mandates an award of attorney fees and costs. In an attempt to further curtail financial abuse of elders, the California legislature amended Cal. Wel & Inst Code § 15657.5 on January 1, 2005. The amended version of § 15657, for purposes of recovering attorney's fees and costs, now requires that the financial abuse of an elder be proven by a "preponderance of the evidence" instead of the prior "clear and convincing" standard. § 15657.5 now reads:

> (a) Where it is proven by a **preponderance of the evidence** that a defendant is liable for financial abuse, as defined in Section 15610.30[9], in addition to all other remedies otherwise provided by law, the court **shall award to the plaintiff reasonable attorney's fees and costs...**
>
> (b) Where it is proven by a preponderance of the evidence that a defendant is liable for financial abuse, as defined in Section 15610.30, and where it is proven by clear and convincing evidence that the defendant has been guilty of recklessness, oppression, fraud, or malice in the commission of the abuse, in addition to reasonable attorney's fees and costs set forth in subdivision (a), and all other remedies otherwise provided by law . . .

C. <u>Exemplary or Punitive Damages</u>

Due to arbitration panel's reluctance to award punitive damages, the first step in requesting such an award is to remind a panel that they are authorized to award punitive damages in excess of actual damages to punish wrongdoing. *The Arbitrator's Manual* (May 2005), pg. 32. Once the

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[9] California Welfare and Institutions Code § 15610.30 states: (a) Financial abuse of an elder or dependant adult occurs when occurs when a person or entity does any of the following:

> (1) Takes, secretes, appropriates, or retains real or personal property of an elder or dependent adult to a wrongful use or with intent to defraud, or both.
>
> (2) Assists in taking, secreting, appropriating, or retaining real or personal property of an elder or dependent adult to a wrongful use or with intent to defraud or both.
>
> (b) A person or entity shall be deemed to have taken, secreted, appropriated, or retained property for a wrongful use if, among other things, the person or entity takes, secretes, appropriates or retains possession of property in bad faith.
>
> (1) A person or entity shall be deemed to have acted in bad faith if the person or entity knew or should have known that the elder or dependent adult had the right to have the property transferred or made readily available to the elder or dependent adult or to his or her representative.

Panel is educated on their power to award punitive damages, you need to provide a statutory or other basis on which they can base their award. The Award form filled out by Panels asks if punitive damages are being awarded and, if so, the basis for awarding them. In the case of a financial abuse of an elder situation, an award of punitive damages is authorized by Cal. Wel & Inst Code § 15657.5(b). Just putting the relevant sections of that statute on the screen, highlighted, may be enough to convince a Panel that punitive damages should be awarded and gives them the hook they need on which to hand the punitive damage award.

Like most jurisdictions, punitive damage awards in California are seemingly granted in only the most egregious breach of fiduciary duty situations. For example, *Hobbs v. Bateman Eichler, Hill Richards, Inc*, (1985) 164 Cal. App. 3d 174, was a breach of fiduciary duty case that involved unauthorized trading, churning and unsuitable investments. The Plaintiff was a 65-year old widow with no investment experience. In *Hobbs*, the Court awarded $96,000 in compensatory damages against both the broker and the firm, and $220,000 in punitive damages against the firm.

In *Hobbs*, The court decided that because broker's wrongful conduct was ratified and approved by a "managing agent" of the firm punitive damages were justified. The Court stated, "punitive damages may be properly awarded against a principal because of an act by an agent if (a) the principal authorized the doing and manner of the act; or (b) the agent was unfit and the principal was reckless in employing him; or (c) the agent was employed in a managerial capacity and was acting in the scope of employment, or (d) the employer or a manager of the employer approved or ratified the act." *Hobbs*, 164 Cal. App. 3d at 193. Citing *Agarwal v. Johnson* (1979) 25 Cal. 3d 932, 950.[10]

Evidence showed that the broker unmercifully churned the account, made hundreds of unauthorized trades and falsified information on the Plaintiff's customer account agreement in "conscious disregard for" the plaintiff's rights. *Hobbs*, 164 Cal. App. 3d at 194, 195; See also Code Civ. P. § 3294. The punitive damage award, therefore, was justified and not excessive under the factors laid out by the Supreme Court in *Neal v. Farmers Ins.* (1978) 21 Cal.3d 910, 928. The court considered the nature of the defendant's acts, the amount of compensatory damages, and also the firms' net worth, and concluded that the punitive damages ratio of 2.3 times compensatory damages was comparatively low. *Hobbs*, 164 Cal. App. 3d at 194, 195.
Furthermore, in computing the $96,000.00 compensatory damage award, the court followed the *Twomey* formula and added the amount the securities would have been worth had she not turned them over to Defendants in the first place. *Hobbs* 164 Cal. App. 3d at 197.

In similar breach of fiduciary duty and churning case, the court upheld a punitive damage award of $160,000 against a brokerage firm. The punitive damages were 3.6 times the compensatory award of $45,000. *Pusateri v. E.F. Hutton & Company* (1986) 180 Cal.App.3d 247. In a recent decision, the 5th Circuit Court of Appeals, interpreting California law, affirmed a $2.9 million punitive damages award in a breach of fiduciary duty case. In addition to the $6.3 million in compensatory damages, the punitive damage award was upheld even though the Panel failed to

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[10] If it is difficult to establish that a supervisor "ratified" the act of the broker, a simple way of establishing the such responsibility is California Code of Regulations § 260.210(b)(4) which states, **"A broker-dealer shall be responsible for the acts, practices, and conduct of an agent in connection with the purchase or sale of securities until such time as they have been properly terminated and the Form U-5 has been filed with the CRD of NASD."**

explain the basis for the \$2.9 million in their 21-page "Reasoned Award". *Sarofim v. Trust Company of the West*, No. 05-20309 (5^{th} Cir. 2006)

D. Interest

As noted in the *Boam* case described above, the legal rate of interest **must** be awarded when violations of state securities are involved. Additionally, the legal rate of interest of 10% **must** be applied on the date of the breach of any contract in California entered into after January 1, 1986, unless of course, the interest rate is included in the contract. In these situations, damage awards including interest must be awarded as a matter of law, and failure to do so is grounds to set aside a verdict. *Boam v. Trident Financial Corporation*, 6 Cal.App.4th 738, 744-745.

> Civ. Code § 3289: Interest on Obligation After Breach.
> (a) Any legal rate of interest stipulated by a contract remains chargeable after a breach thereof, as before, until the contract is superseded by a verdict or other new obligation.
> (b) If a contract entered into after January 1, 1986, does not stipulate a legal rate of interest, the obligation shall bear interest at a rate of 10 percent per annum after a breach.

In situations where no state security law was violated, no contract exists, or no breach occurred, an award of interest is placed in the discretion of the arbitrators.

> Civ. Code § 3288: Interst as Damages – Discretion of Jury.
> In an action for the breach of an obligation not arising from contract, and in every case of oppression, fraud, or malice, interest may be given, in the discretion of the jury.[11]

E. Statutory Offer to Compromise – Code Civ. P. § 998

Another method of increasing the amount of damages that can be awarded is to make a Code Civ. P. § 998 Offer to Compromise. The statute specifically provides that it applies to "litigations and arbitrations" in the State of California. If the offer was not accepted by the respondents prior to the arbitration, and they fail to get a more favorable award, the arbitrators, may require the respondents pay a reasonable sum to cover expert witnesses and costs. Code Civ. P. § 998(d). Present the rejected Offer to Compromise to the Panel at the conclusion of the hearing rather then waiting until the award and seeking to recover the costs (the largest costs typically are the expert fees and hearing costs, which together with copying costs, travel expenses and other hearing costs can easily exceed \$20,000). It also shows a Panel that Claimant was trying to resolve the case and, in the proper fact pattern, the Panel may be annoyed the Respondent flatly rejected the offer and took its chances on a hearing.

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[11] The NASD Arbitrator's Manuel gives the power to award interest and to determine the proper date and from which interest is to accrue. Some state statutes specify legal rates of interest that may be used for guidance when awarding interest. Arbitrator's Manuel (May 2005), Page 32.