Award
FINRA Office of Dispute Resolution

In the Matter of the Arbitration Between:

Claimants Jan E. Tullis Scott K. Tullis	Case Number: 16-01261
vs.	
Respondents Ameriprise Financial Services, Inc. Andrew Joseph Hall	Hearing Site: Portland, Oregon

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Nature of the Dispute: Customers vs. Member and Associated Person

This case was decided by an all-public panel.

REPRESENTATION OF PARTIES

For Claimants Jan E. Tullis, and Scott K. Tullis, hereinafter collectively referred to as "Claimants": Joshua L. Ross, Esq., Stoll Stoll Berne Lokting & Shlachter PC, Portland, Oregon.

For Respondents Ameriprise Financial Services, Inc. ("Ameriprise") and Andrew Joseph Hall ("Hall"), hereinafter collectively referred to as "Respondents": Howard M. Klausmeier, Esq., Ameriprise Financial Services, Inc., Troy, Michigan.

CASE INFORMATION

Statement of Claim filed on or about: May 3, 2016.
Claimants signed the Submission Agreement: May 3, 2016.

Statement of Answer filed by Respondents on or about: July 5, 2016.
Hall signed the Submission Agreement: June 14, 2016.
Ameriprise signed the Submission Agreement: July 1, 2016.

CASE SUMMARY

Claimants asserted the following causes of action: mishandled accounts, negligence, breach of fiduciary duty, violation of Oregon securities laws and applicable regulation laws, unsuitability, and failure to supervise. The causes of action relate to Claimants' investments in First Trust Unit Investment Trust ("UITs").

Unless specifically admitted in the Statement of Answer, Respondents denied the allegations made in the Statement of Claim and asserted various affirmative defenses.

RELIEF REQUESTED

In the Statement of Claim, Claimants requested:

1. Compensatory damages in the amount of $195,044.41;
2. Recovery of all commissions, fees, and profits realized by the Respondents in an amount to be proven at hearing;
3. Interest at the rate of 9% per annum; and
4. Attorneys' fees and costs.

In the Statement of Answer, Respondents requested:

1. Dismissal of the Claimants' Statement of Claim with prejudice;
2. An Award to Ameriprise of its Forum costs and fees in having to defend this matter; and
3. Expungement of this matter from Hall's Central Registration Depository ("CRD") record.

At the close of the hearing, Claimants requested damages in the amount of $191,772.00.

OTHER ISSUES CONSIDERED AND DECIDED

The Arbitrators acknowledge that they have each read the pleadings and other materials filed by the parties.

During the recorded evidentiary hearing, the Panel considered oral argument and evidence on Respondents' request to expunge Respondent Hall's CRD record.

Arbitrator Paul R. Meyer concurs with the majority decision regarding the amount of compensatory damages awarded and Respondents' expungement request and issues a dissent with regards to the start date for Claimants' awarded interest.

The Arbitrators have provided an explanation of their decision in this award. The explanation is for the information of the parties only and is not precedential in nature.

The parties present at the hearing have agreed that the Award in this matter may be executed in counterpart copies or that a handwritten, signed Award may be entered.

FINDINGS

The Panel finds that Hall's overall strategy was unsuitable. Hall took Claimants' asset allocation to 100% equities, from 70%. Accounting for expected margin leverage, this amounted to 133% equity exposure. Hall compounded leverage by investing in UITs comprised of closed-end funds ("CEF"), many of which used leverage as a component of their strategy. This further increased Claimants' equity exposure. UITs were less liquid due to high costs, and CEFs were more volatile than comparable investments in similar asset classes. Hall compounded the unsuitability in February 2015, by selling the original UITs and placing fully 50% of Claimants' portfolio in a single sector, which was tightly linked to oil prices—UITs of CEFs of master limited partnerships. The balance of the portfolio was invested in an unsuitable UIT, which was not well-diversified because it held only 12 – 13 individual stocks. The strategy was unsuitable for asset preservation and liquidity needs.

AWARD

After considering the pleadings, the testimony and evidence presented at the hearing, the majority of the Panel has decided in full and final resolution of the issues submitted for determination as follows:

1. Respondents are jointly and severally liable for and shall pay to Claimants the sum of $191,772.00 in compensatory damages.

2. Respondents are jointly and severally liable for and shall pay to Claimants interest on $191,772.00 at the rate of 9% per annum from the date of this award through the date of payment of the award of $191,772.00.

3. Respondents' request for expungement of Hall's CRD record is denied.

4. Any and all claims for relief not specifically addressed herein, including attorneys' fees, are denied.

Dissenting Decision

While the parties did not request a reasoned decision, this Arbitrator considers that most decisions deserve to be explained in order to create a body of precedent unavailable now that most courts no longer have jurisdiction over most securities litigation. Hopefully, this decision may help contribute to that body of law.

Facts

Claimants seek damages on a "well-managed" account damages theory. They alleged violations of FINRA "suitability rules" (Rule 2009 and 2111) "know your customer" and "unsuitability" of the strategy selected as well as the particular investments made.

Scott K. Tullis is currently 60 years old and Jan E. Tullis is 58. Scott obtained a B.A. in Business Administration in 1980 and an MBA from the University of Phoenix in 2002. From 2004 to 2010 Scott had a relatively high-paying job, which he lost in 2010. Jan held a part-time position with Portland Public Schools which became full-time in late 2011.

While Scott was hired at a less well-paying job in May 2011, he lost that job a year later. However, in late 2011 Claimants opened a yogurt retail store (TWIST) to which Scott subsequently devoted full time. In Sept. 2013, they opened a second store (TWIST II) that did not flourish and was closed the following year.

Claimants have two children, currently 24 and 25, who during this period went to colleges which subsequently exhausted all funds Claimants had put aside in Ameriprise accounts and 529 plans.

Claimants' first accounts with Ameriprise were opened in February 2011, totaling $243,242.60:

Son Jonathan education account	$3,576.80
Daughter Sari education account	$22,412.25
Scott's IRA	$196,094.40
Jan's IRA	$5,889.10
Jan and Scott's savings account	$34,188.56

In 2011, Claimants could not withdraw funds from their IRAs without penalty for another five years (Scott's) and seven years (Jan's). Their personal savings (available for current emergencies) totaled only **$34,188.56**. (This doesn't include other banking accounts and business accounts which may have held some cash.) During 2012 they virtually exhausted their savings account by withdrawing $32,000, leaving a balance of **$535.80**. As a result, they closed their Ameriprise accounts in March 2013 and transferred their IRAs into 401k accounts with TWIST. In late 2013 they sold their home to pay off increasing TWIST [debt].

To pay for the opening and losses incurred by TWIST in 2013 and to cover their children's need for further funds to finish their college educations, by April 2014 Claimants had ran up credit card debts, with high interest rates, of over **$120,000**. In sum, they were drowning.

The *Deus Ex Machina* for release from their financial troubles came in April 2014 in the form of an inheritance from Scott Tullis' mother, of nearly $800,000. This consisted of an outright bequest of $515,000 and an inherited IRA of $283,000, subject to a tax of approximately $25,000. This IRA account was not available for withdrawals without penalty until 2016.

By then, Amy Groshong ("Groshong"), Claimants' long-standing financial advisor, had left Ameriprise. Claimants, having met Hall during prior meetings with Groshong, consulted him in April 2014 to handle these inheritances and straighten out their financial problems.

Both parties faced a formidable task: analyze the current situation, deteriorating rapidly over the past three years and:

1. determine how to use this inheritance to stop the downward spiral,
2. put the remaining working years of Claimants on a reasonably sound financial footing and
3. maximize their ultimate retirement resources.

A major component was how to handle their ballooning personal debt, which by April 2014 had grown to more than $120,000, and which was likely to continue to escalate -- which it did, in fact (under Respondent's recommended investment plan) exceeding $140,000 by mid-2015. Claimants' spendthrift habits were obvious from the beginning of the relationship in 2014 and were repeatedly manifested throughout the relationship, including using this inheritance immediately to lease a luxury car.

Hall, "acted as the Claimants' **financial advisor** during the relevant period of time" (Respondents' Answer; emphasis added). Having just described Hall as a "financial advisor," Respondents then argue:

"when an account is non-discretionary and control of the account remains with the customer, such as the Claimants' accounts, the duties owed by a **stockbroker** to the investor **do not constitute a fiduciary relationship."**

This rather widespread idea is not correct. Prior to the late 1980s, securities litigation between customers and brokers were mostly decided by the courts – both state and federal, depending on whether based on state or federal laws or diversity of citizenship. Since then, all such cases have been and are subject to arbitration – first by the NYSE and NASD and now by FINRA. These panels are not required, unless requested by both parties, to write "reasoned decisions", resulting in a lack of precedents. Prior decisions, even though not binding, are seldom available because FINRA arbitrators are seldom compensated for writing well-reasoned decisions.

Legal standards applicable to this case

In the realm of investment advisors and brokers there are distinctions that determine the degree of fiduciary duty imposed. Some work exclusively on a fee for advice basis and receive no compensation from securities bought or sold. Other investment advisors are also brokers whose compensation derives from their commissions. Brokers may buy and sell based solely upon orders from customers to whom they have made no recommendation. Others effect transactions after giving advice to their client. Still others have discretion to buy and sell without specific consent from the client for each transaction.

In this case, Respondents acted as investment advisors, as well as brokers, by exercising discretion to invest in specific securities without getting advance approval from Claimants. Hall's notes indicate that his discussions with Claimants were mainly to review investments he had already made. For example, in June 2015, the notes report, **"**We reviewed asset allocation and ***he wanted to be more aggressive and just buy things that go up*."** [Emphasis added. Note that Claimants' naiveté equated "aggressive" with "things that go up."] At one point Claimants questioned investment in Europe and, on another occasion, spoke of having only 25% of the account in stocks. Generally, it does not appear that Claimants were directly involved in the selection of specific securities, which was left to the discretion of Respondents.

In writing this decision, we have examined the applicable legal precedents under Oregon cases, See: Sherrock v. Merrill Lynch, 1977 WL 1064 (D. Or 1977), applying Oregon law, which suggest the law provides that in situations such as this

Panel is facing, fiduciary duties exist. Fiduciary relationships are not monolithic. They are nuanced and vary depending on situations. The highest level, of course, exists when the beneficiary is totally incompetent and the power of the obligor is complete, i.e., a guardian or trustee of a totally disabled person. In addition to Oregon case law, FINRA has applicable rules which articulate **specific "fiduciary" obligations** owed by brokers to customers, in addition to those imposed by state and/or federal laws. These must be examined and applied to the facts of this case.

FINRA Rule 2009 provides as follows:

2090. Know Your Customer

Every member shall use reasonable diligence, in regard to the opening and maintenance of every account, to know (and retain) ***the essential facts concerning every customer*** and concerning the authority of each person acting on behalf of such customer. (Emphasis added)

FINRA Rule 2111 provides as follows:

"2111. Suitability

(a) A member or an associated person must have a reasonable basis to believe that a recommended transaction or ***investment strategy*** involving a security or securities is suitable for the customer, based on the information obtained through the reasonable diligence of the member or associated person to ascertain the customer's investment profile. A customer's investment profile includes, but is not limited to, the customer's age, other investments, ***financial situation and needs*****,** tax status, ***investment objectives, investment experience***, ***investment time horizon, liquidity needs, risk tolerance,*** and any other information the customer may disclose to the member or associated person in connection with such recommendation. (Emphases added)

(b) A member or associated person fulfills the customer-specific suitability obligation for an institutional account, as defined in Rule 4512(c), if (1) the member or associated person has a reasonable basis to believe that the institutional customer is capable of evaluating investment risks independently, both in general and with regard to particular transactions and investment strategies involving a security or securities and (2) the institutional customer affirmatively indicates that it is exercising independent judgment in evaluating the member's or associated person's recommendations. * * *"

FINRA Rule 2111 provides that before making recommendations a representative must have:

"reasonable grounds for believing that the recommendations are suitable for their customers based upon the facts, if any, disclosed by their customers as to their other securities holdings ***and their financial situation and needs****.* (Emphasis added) and

"Registered representatives are required, before effecting any transactions for their customers, to make reasonable efforts to obtain information:

concerning their customer's financial status, tax status, investment objective,

and

such other information used or considered to be reasonable by the registered representatives in making recommendations to their customers. "

This twofold test: (1) "know your customer" and (2) "suitability" of the particular recommended securities for their circumstances applies ***both to the overall strategy to be used*** as well as to ***the specific investments to meet that strategy.***

Respondents' major defenses in this case were based on the fact that Claimants have continuously listed their investment objectives as **Growth and Income** and their risk tolerance as **Moderate to Aggressive** as if that satisfied Respondents' obligations under Rule 2111. Clearly, that did not. Although in 2011, Groshong had obtained statements, budgets, tax returns and other such data, there is no indication that Respondents, in reopening the new accounts in 2014, secured any such detailed information from clients, although he repeatedly asked for them. However, their nonproduction did not stop him from giving his advice.

Respondents' obligations under the rules apply first to determining the overall strategy for investments to be followed. Only when that issue has been properly investigated, documented and a recommendation made, is it necessary to determine, secondly, what suitable securities fulfill that strategy. To determine whether these FINRA rules were violated, one must deal with the overall strategy appropriate for these particular clients with their particular history and circumstances that brought them to Respondents in March 2014.

Discussion

Upon this once-in- a-lifetime inheritance, the first and most significant decision was whether to use it to enable Claimants to free themselves from the burden of debt so that the income generated by the remaining $400,000 investments could be used to supplement income shortages and put their business affairs in order, while Scott found a better job. The alternative was to transfer very high interest credit card debt to secured margin debt bearing 6.7 to 8% interest and use the income and hoped-for gains from the investments to pay margin interest, projected at best to take at least three to four years.

This option, of course, resulted in a larger corpus to be invested, thereby maximizing compensation to Ameriprise, both from the investments made and the margin interest (admittedly much lower than credit card interest), but also bringing a 4-6% annual return to Ameriprise. This precluded eliminating the debt burden.

Although by April 2014 Claimants had a CPA prepare tax returns personally and for their businesses, those documents were never produced by Claimants or examined by Respondents. Yet at their first meeting there were immediate requests for “borrowing an additional $20,000 as soon as the money arrives.” Claimants also mentioned having also just borrowed another $20,000 from Jan E. Tullis’ mother, which they were eager to repay. Furthermore, although they said they had just sold their house and netted about $20,000, also spent on current expenses, they nevertheless also wanted to buy another house. And straight away Scott K. Tullis immediately leased a $42,000 automobile. Requests for budgets and other financial information essentially remained unanswered by Claimants. This failure of Claimants to provide clear documentation of their spendthrift habits, and Scott K. Tullis’ pie in the sky “make me a millionaire by retirement” certainly contributed to Respondents’ failures in this case, but they don’t excuse them. Indeed, such failure should have alerted Respondents to the dangers of proceeding uninformed.

Yet in April-May 2014, Respondents failed to conduct even a cursory analysis of the pros and cons of the two approaches, (1) paying off debts and using income from the balance to getting back on their feet and (2) keeping the inheritance intact and using the income to try to pay off debt. The second approach clearly encouraged Claimants to treat the margin as a “bank” account to further feed their known spendthrift behavior. However this critical matter was never analyzed, much less discussed, solely **because Claimants didn’t want to consider it**. Respondents blame this on Claimants’ misguided notion about keeping the inheritance intact, like a “Fabergé Egg,” from which they could pick off the extruding jewels, as if they would grow back, and still make Scott a millionaire by retirement. Even a cursory analysis in April-May 2014 would have demonstrated that Claimants’ “Fabergé Egg” strategy both unrealistic and unsuitable for these customers. Claimants never understood the consequences of this strategy [in particular, the potential adverse impact of financial leverage on their investment returns] and why it didn’t serve their best interests. Respondents should have realized this. They failed to “advise” on this major issue; yet that was the most important thing they had been engaged to do.

Claimants’ naiveté combined with their dire circumstances made it even more imperative for Respondents carefully to have analyzed and compared these options. Had that been done, it would have been obvious that the investment strategy chosen was unlikely to succeed. First of all, the income and gains from the investments (assuming they were to occur) could not realistically be sufficient to pay off their existing debt for years, much less continue to provide further loans to spendthrift Claimants. As should easily have been anticipated, these loans continued undiminished through 2014 and 2015. Indeed, in early 2015 debt was still at $120,000, and by June 2015, it had grown to $140,000. While we now know this with hindsight, any reasonable analysis a year earlier should have projected that this additional borrowing would likely occur. Indeed, a year later, in May 2015, Hall wrote Claimants “There will be no more withdrawals from investment accounts.”

Rather than analyze these options for the benefit of Claimants, Respondents used Claimants’ naiveté to benefit themselves with more fees and interest charges flowing to Respondents from investing a larger corpus and maintaining margin debt. This created a clear "conflict of interest," not only benefitting Respondents but also making Claimants' likelihood of getting out from under their debt far less likely.

In short, the only consideration of these alternatives was merely to state them and let Claimants choose without any analyses or input from Respondents. This violated FINRA Rules. **Respondents had a far greater responsibility to have analyzed these options, compared their comparative likelihood of success and advised Claimants that their Fabergé Egg strategy was unfeasible.**

The remaining issues have to do with the suitability of the investments in UITs. UIT investments have high up-front costs (approaching 4%) and penalties for early selling. Indeed, there were, in fact, early sales resulting in such losses. Furthermore, some of the UITs were, in addition to the higher costs and fees charged up front, unduly risky given the precarious nature of Claimants' financial situation and recent history: unemployment, failing business, and remaining monetary pressures to see their two children complete their college educations at fairly expensive schools. UITs are particularly unsuitable for an investment strategy based on very high continuing debt and the obvious need for flexibility to deal with their investments in that volatile situation. Some UITs invest in "CEFs" which may and do use additional borrowings to boost potential investment returns. UITs are suited for investors who can hold those investments to their maturity, without the myriad uncertainties, which Respondents should have known did not exist in this strategy.

Indeed, the strategy recommended to Claimants, whom Groshong had previously recommended a 70% equity exposure to, resulted in nearly 100% equity exposure. Moreover, when margin borrowing is taken into account, Claimants' equity exposure was roughly 133%. The selected UITs further increased this equity exposure through the use of leveraged CEFs.

Finally, In June 2015, Respondents sold all of the three initial UITs, and invested Claimants' remaining Ameriprise One funds in even less suitable investments. Fully half of their entire portfolio was then invested in a UIT comprised of stocks and CEFs of stocks invested in the heavily beaten-down energy sector. Thus, 50% of Claimants' investment performance would be determined by the fate of a single equity sector – energy – which was highly correlated to the global price of oil. The second UIT was invested in a basket of 13 stocks, which was too small a number of companies to adequately diversify-away company-specific stock risk. Combined with the margin leverage, these two undiversified funds were unsuitable investments and generated the majority of Claimants' realized losses.

In sum, Respondents maximized the benefits they derived from Claimants' accounts instead of giving Claimants prudent "investment" advice, after first obtaining all the pertinent facts about their customers, as required by FINRA rules.

Conclusion

For the reasons above, I would award Claimants damages in the sum of $191,772, together with interest at 9% per annum from May 31, 2016, by which date Claimants' damages were substantially liquidated.

FEES

Pursuant to the Code of Arbitration Procedure, the following fees are assessed:

Filing Fees
FINRA Office of Dispute Resolution assessed a filing fee* for each claim:

Initial Claim Filing Fee	=$ 1,425.00

**The filing fee is made up of a non-refundable and a refundable portion.*

Member Fees
Member fees are assessed to each member firm that is a party in these proceedings or to the member firm(s) that employed the associated person(s) at the time of the event(s) giving rise to the dispute. Accordingly, as a party, Ameriprise Financial Services, Inc. is assessed the following:

Member Surcharge	= $ 1,700.00
Member Process Fee	= $ 3,250.00

Discovery-Related Motion Fee
Fees apply for each decision rendered on a discovery-related motion.

Two (2) decisions on a discovery-related motion on the papers with one (1) arbitrator @ $200.00/decision	= $ 400.00

Respondents submitted 2 discovery-related motions

Total Discovery-Related Motion Fees	= $ 400.00

The Panel has assessed $400.00 of the discovery-related motion fees jointly and severally to Respondents.

Hearing Session Fees and Assessments
The Panel has assessed hearing session fees for each session conducted. A session is any meeting between the parties and the arbitrator(s), including a pre-hearing conference with the arbitrator(s), that lasts four (4) hours or less. Fees associated with these proceedings are:

One (1) pre-hearing session with the Panel @ $1,125.00/session			= $ 1,125.00
Pre-hearing conference:	September 7, 2016	1 session	

Eight (8) hearing sessions @ $1,125.00/session	= $ 9,000.00

Hearing Dates:	May 9, 2017	2 sessions
	May 10, 2017	2 sessions
	May 11, 2017	2 sessions
	May 12, 2017	2 sessions

Total Hearing Session Fees = $10,125.00

The Panel has assessed $10,125.00 of the hearing session fees jointly and severally to Respondents.

All balances are payable to FINRA Office of Dispute Resolution and are due upon receipt.

ARBITRATION PANEL

Stephany Adriene Watson	-	Public Arbitrator, Presiding Chairperson
Rick D. Hampton	-	Public Arbitrator
Paul R. Meyer	-	Public Arbitrator

I, the undersigned Arbitrator, do hereby affirm that I am the individual described herein and who executed this instrument which is my award.

Concurring Arbitrators' Signatures

Stephany Adriene Watson
Public Arbitrator, Presiding Chairperson

26 June 2017
Signature Date

Rick D. Hampton
Public Arbitrator

Signature Date

Concurring in Part, Dissenting in Part Arbitrator's Signature

Arbitrator Paul R. Meyer concurs with the majority decision regarding the amount of compensatory damages rewarded and Respondents' expungement request and dissents with regards to the start date for Claimants' awarded interest.

Paul R. Meyer
Public Arbitrator

Signature Date

June 27, 2017
Date of Service (For FINRA Office of Dispute Resolution office use only)

ARBITRATION PANEL

Stephany Adriene Watson	-	Public Arbitrator, Presiding Chairperson
Rick D. Hampton	-	Public Arbitrator
Paul R. Meyer	-	Public Arbitrator

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Concurring Arbitrators' Signatures

Stephany Adriene Watson
Public Arbitrator, Presiding Chairperson

Signature Date

June 26, 2017

Rick D. Hampton
Public Arbitrator

Signature Date

Concurring in Part, Dissenting in Part
Arbitrator's Signature

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Signature Date

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Public Arbitrator

Signature Date

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Public Arbitrator

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