

# SECURITIES ARBITRATION COMMENTATOR

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### DATABASE SUBSCRIBERS

If you were a subscriber to SAC's Award Database during 1996, you may be eligible for a discount next time you renew your \$200 annual subscription. Your 1996 account statement, which will be sent to you shortly, indicates whether that discount might be 25%, 50%, 75%, or a full \$100! Please review the 1996 account statement when it comes in the mail!

## SAC Award Survey How Fares the *Pro Se* Investor in Arbitration?

People often ask whether investors should obtain representation when entering arbitration. There are many ways to answer this question, some glib, many obvious, but we often fall back upon statistical findings we recall from the General Accounting Office's 1992 study of securities arbitration, "Securities Arbitration: How Investors Fare" (5 SAC 1(1)).

GAO's exhaustive survey found that investors are represented about 90% of the time, when the claimed amount is \$20,000 or more. The Study also observed that investors with counsel settled about 1.7 times more frequently. Then, there was this interesting fact: represented investors did not necessarily win more frequently than investors who represented themselves (*i.e.*, *pro se* investors), but when they won, represented investors' recoveries were 1.6 times more likely to exceed the average recovery rate.

Of course, GAO's statistical study, while comprehensive at the time and far more analytical than SAC's liberal arts majors could produce, is almost five years old. It only covered an 18-month period from January 1989 to June 1990, whereas we now have the ensuing Awards to survey as well. The success of *pro se* investors in arbitration is an area SAC has not previously surveyed. This article reports the results of a recent canvassing of securities arbitration Awards rendered during the five-year period from July 1991 to June 1996.

### Survey Caveats

Not all of the 8,092 customer-initiated Awards surveyed disclose information about the parties' representa-

tion. We chose June 1991 as our start date because the major SRO forums were not required to disclose the names of counsel in the Awards until the early half of 1991. AAA did not begin making Awards public with that information until mid-1993 and some of the smaller forums (*e.g.*, MSRB, PHLX) still do not. When Awards do disclose information about party representation, SAC's Award Database captures whether the investor is *pro se* or represented by counsel.

The 8,092 customer-initiated Awards surveyed were examined in two distinct groups: (1) those involving \$10,000 or less, which would have been processed at the SRO arbitration forums under the existing Small Claims procedures ("Small-Claims Awards"); and, (2) those involving more than \$10,000 in compensatory claims ("Customer-Member Awards"). For purposes of presentation, we deal with the first group, in which there were 2,961 Small Claims Awards, separately from the second group, in which there were 5,131 Customer-Member Awards (about 5% of this second group involves investor claims against individual brokers only, with no broker-dealer respondent, but we lump all such Awards under the Customer-Member designation).

### Small Claims Awards

More than three-quarters of the 2,961 Small Claims Awards surveyed were identified by SAC as rendered in cases involving *pro se* investors. These 2,263 Awards yielded the *pro se* investor some monetary award in 1,014 instances. This "win rate" of 44.8% for *pro se* investors in Small Claims Awards compares to a 49% "win rate" for inves-

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**PRO SE SURVEY** *cont'd from page 1*

tors generally in Small Claims matters, as disclosed in SAC's latest Public Award Survey (8 SAC 2(11)). "Represented" investors as a group had a 52.5% "win rate."

Besides a lower win rate than the average, *pro se* investors also recovered less, as a percentage of what they sought, when they did win. Of the approximately \$5.1 million in aggregate compensatory claims in the 1,014 winning cases, *pro se* investors received monetary awards totalling about \$3.6 million. From these figures, we calculated a 70.2% "recovery rate." This may seem relatively high, but the average recovery rate for winning Small Claims Awards in our Public Award Survey was 77%. Represented investors actually achieved a recovery rate on winning Small Claims Awards that exceeded 100%, by winning \$2.2 million on total compensatory claims of \$2.1 million.

Since the greatest concentration of *pro se* cases lies in the Small Claims area, we decided to dig deeper. To do so, we split the Small Claims Awards into two varieties: those in which the investor had requested a hearing before the single Arbitrator ("live hearing" cases) and those in which a hearing had been waived by the investor and decided by the single Arbitrator on the basis of the parties' submissions ("on-the-papers" cases).

Only 30% of the Small Claims Awards derived from live hearing cases. *Pro se* investors appeared to choose a live hearing about 25% of the time. Represented investors appeared more likely to opt for a live hearing, doing so about 36% of the time. Conversely, *pro se* investors appeared more likely than represented investors to choose the on-the-papers alternative. (*ed: Remember that we are dealing here with Awards, i.e., cases that went to decision -- not with all cases filed. Thus, it cannot be said that 70% of Small Claims investors are likely to prefer the "on-the-papers" default option, since a greater percentage of investors selecting the live hearing route may have settled*

*prior to hearing than investors who selected the "on-the-papers" option. In fact, as an educated guess, we would think that settlements are considerably more likely when both sides face a hearing than when the parties are submitting "on-the-papers."*)

Of the *pro se* investors who submitted their disputes on-the-papers, 45.9% won a monetary award, whereas 51.0% of the represented investors were victorious. The disparity between represented and *pro se* investors remained, when we surveyed the live hearing Small Claims cases; in fact, the gap widened. Represented investors did somewhat better in live hearing matters than on-the-papers cases -- a 55.4% win rate. Ironically, *pro se* investors who chose to attend a hearing did worse, slipping to a 41.7% win rate.

In terms of average recovery rates, the disparities between *pro se* and represented investors were even greater than in the win rate comparisons. On the other hand, the recovery rates did not change much for either group, based upon the investor's choice of a live hearing or submission on-the-papers. For *pro se* investors, the average recovery rate was 69.5% in on-the-papers cases and 72.7% in live hearing cases. For the represented investor, the average recovery rates were dramatic: 103.8% in on-the-papers cases and 107.2% in live hearing cases!

**Customer-Member Awards**

Our findings correspond with the GAO finding that only a small percentage of investors choose the *pro se* route in larger-claim cases. Of the 5,131 Customer-Member Awards surveyed, where the claims involved exceeded \$10,000, only 909 Awards, about 18% on average, were Awards in which investors appeared *pro se*. In other words, fully 82% of investors seek representation in matters exceeding \$10,000 in compensatory claims.

In terms of achieving some monetary award in these larger-claim cases, *pro se* investors did about as well as they had done under the Small Claims

procedures. There were 396 Awards in which the *pro se* investor won some monetary amount -- a 43.6% win rate. On the other hand, our Public Award Survey results indicated that investor win rates tend to go up as compensatory claims increase; the *pro se* investor does not appear to benefit from this phenomenon. In fact, as we see below, the win rate for *pro ses* actually declined as the amount in controversy increased.

The 1996 Public Award Survey results also established that recovery rates for winning investors tend to decline as the amount in controversy increases. The 396 winning Awards for *pro se* investors in this category yielded a 39.7% recovery rate, a significant decline from the 70% recovery rates enjoyed under the Small Claims procedures, but not bad, in comparison to the overall 39% recovery rate for Customer-Member Awards disclosed in our Public Award Survey.

When we began dissecting the range of compensatory claims involved in the 909 Customer-Member disputes in which *pro se* investors were involved, we found that investors increasingly turn to counsel as the amount of the compensatory claim rises. For example, about 70% of the 909 over-\$10,000 Awards concerned compensatory claims between \$10,000 and \$50,000. Beyond \$50,000, only 286 Awards involved *pro se* investors, whereas 3,028 of the 5,131 Customer-Member Awards fell beyond \$50,000. Thus, the 18% overall incidence of *pro se* investor-claimants quickly falls to 9%, as the claim amounts grow.

Instead of rising, the *pro se* investor's win rate began to decline, as compensatory-claim amounts increased. Only 115 of the 286 Awards granted some monetary recovery -- a 40.2% "win" rate. Investors generally in the \$50,000-\$100,000 category, according to the Public Award Survey, had an average 56% win rate. This disparity confirms, as do our statistical findings in general, a divergence from

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**PRO SE SURVEY** *cont'd from page 2*

the earlier GAO observation that, overall, *pro se* investors win at about the same rate as represented investors. Whether this results from the greater technical complexity of proceedings in recent years or from some other factor, we cannot say.

By the time the amount at stake rose to compensatory claims exceeding \$100,000, only 155 *pro se* investors, among 2,120 total Customer-Member Awards (7.3%), appeared. Just 57 of those 155 Awards yielded the *pro se* investor a monetary award, a dismal win rate of 36.8%, compared to the win rate taken from the Public Award Survey for matters involving \$100,00-\$500,000, of 60%.

**\$10,000-\$25,000 Range**

The Award results in this range of claims deserve separate treatment, because NASD is currently proposing to extend the use of the Small Claims procedure to the \$25,000 level. Currently, about 41% of the investor-claimants in this range of claims chose to proceed *pro se* -- 295 out of a total 716 Awards. The proposed rule change will probably increase Small Claims volume only about 25%, despite the large expansion of the eligible dollar-claim category. It may, though, have a greater impact on the percentage of investor-claimants in the \$10,001-\$25,000 category who decide to proceed *pro se*. Availability of the Small Claims procedures may influence the decision on representation. If so, we can expect to see an increase in the current 41% *pro se* percentage.

As with the other categories, *pro se* investors in this dollar category have a lower win rate, 45.4%, compared to the represented group (50.8%); their recovery rate, on average, is significantly lower as well. The *pro se* investor's average recovery rate is only 66.4%, while the represented investor's recovery rate continues quite high, at 99%. Again, our survey of this particular category of dollar-claims tends to support the observation that the likelihood of winning some monetary award in securities arbitration tends to decline

for the *pro se* investor, as the amount in controversy rises, while it tends to improve for the represented investor.

**Summary of Analysis**

Should investors seek representation in securities arbitration? Well, how important is it that you win? The "win" rate differentials we found in this Survey certainly indicate that investors win more frequently when represented by counsel, in every dollar category that we tested. Furthermore, represented investors who win achieve a significantly higher recovery rate than *pro ses*. Finally, the win rate disparities between the represented and the *pro se* investors tend to grow as the size of the compensatory claims grow.

On the other hand, there is a cost in obtaining representation. If you are looking to win and to maximize your recovery, the higher "recovery" rate differential for representation in Small Claims Awards must be weighed against that cost. This makes the cost-benefit analysis a closer call. Happily, the SRO Small Claims procedures appear to be providing a workable structure in which investors can make an appropriate cost-benefit analysis.

Investors have the flexibility to proceed in a relatively simplified process without counsel, if they so choose. Whether they opt for a "live hearing" or a decision "on the papers," the results are not terrible if they choose to proceed *pro se*. Similarly, one-quarter of the Small Claims population has found it practicable to utilize counsel in the simplified process and, with professional advice, to opt for or to forego a hearing.

Certainly, as the amounts in dispute rise to a significant dollar level, the benefits of representation become far more apparent. Whereas win rates for investor-claimants tend to climb as the amount in controversy rises, *pro se* win rates stay the same and even move lower. Only a relatively few individuals choose to take larger claims through the process on their own. Very few, less than 10%, brave this course when the

compensatory amounts claimed exceed \$50,000 and, perhaps rightly so, because, on average, this route appears to produce diminishing returns as the claimed amount rises.

With the SRO's moving to expand the Small Claims procedures to \$25,000, one wonders what changes will occur in the arbitration of these larger-claim (i.e., those between \$10,001 and \$25,000) cases. While the expansion in claim amount equals 150% of the present threshold of \$10,000, the increase in caseload appears to be reasonable. Will this remain the same? Is it likely that investors will assess their dollar claims more conservatively to bring their cases within the \$25,000 threshold? We will be interested, too, to see if more investors with claims between \$10,000 and \$25,000 now choose the *pro se* route and to see, as well, how the Award results might change.

**INFORMATION REQUESTS:**

SAC aims to concentrate in one publication all significant news and views regarding securities/commodities arbitration. To provide subscribers with current, useful information from varying perspectives, the editor invites your comments/criticism and your assistance in bringing items of interest to the attention of our readers. Please submit letters/articles/case decisions/etc.

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