Award
FINRA Office of Dispute Resolution

In the Matter of the Arbitration Between:

Claimant
[redacted]

Case Number: [redacted]

vs.

Respondent
City National Securities, Inc.

Hearing Site: Los Angeles, California

Nature of the Dispute: Associated Person vs. Member

REPRESENTATION OF PARTIES

For Claimant [redacted] ("Claimant"): Owen Harnett, Esq., HLBS Law, Westminster, Colorado and Dochtor Kennedy, MBA, J.D., AdvisorLaw, LLC, Westminster, Colorado.

For Respondent City National Securities, Inc. ("Respondent"): Stephen Young, Esq., Keesal, Young & Logan, Long Beach, California.

CASE INFORMATION

Statement of Claim filed on or about: June 6, 2018.
Claimant signed the Submission Agreement: June 6, 2018.

Answer to Statement of Claim filed by Respondent on or about: July 26, 2018.
Respondent signed the Submission Agreement: July 26, 2018.

CASE SUMMARY

Claimant asserted a claim seeking expungement of a FINRA arbitration case, occurrence number [redacted] ("Underlying Arbitration") from his Central Registration Depository ("CRD") records.

In the Answer to the Statement of Claim, Respondent advised that it takes no position as to Claimant's request for expungement but denied that Claimant is entitled to any damages and denied all liability.

RELIEF REQUESTED

In the Statement of Claim, Claimant requested:

1. Expungement of the Underlying Arbitration from his CRD records pursuant to

FINRA Rule 2080(b)(1)(A) as the claim, allegation, or information is factually impossible or clearly erroneous;
2. Expungement of the Underlying Arbitration from his CRD records pursuant to FINRA Rule 2080(b)(1)(C) as the claim, allegation or information is false;
3. Compensatory damages in the amount of $1.00 from Respondent; and
4. Any and all other relief that the Arbitrator deems just and equitable.

In the Answer to Statement of Claim, Respondent did not set forth a specific relief request.

At the hearing, Claimant withdrew his request for $1.00 in compensatory damages from Respondent.

OTHER ISSUES CONSIDERED AND DECIDED

The Arbitrator acknowledges that he has read the pleadings and other materials filed by the parties.

By Initial Pre-Hearing Conference Order dated September 20, 2018 ("IPHC Order"), the Arbitrator instructed Claimant to provide a copy of the Statement of Claim to the three customers in the Underlying Arbitration ("Ms. C" and her daughters, "Ms. O" and "Ms. M", hereinafter collectively referred to as "Complainant Customers")[1] on or before October 12, 2018, including a copy of the IPHC Order, and to submit proof of service. The IPHC Order further provided that any of the Complainant Customers wishing to respond to the Statement of Claim may do so in writing or may participate in the November 20, 2018 expungement hearing conducted via telephone.

On October 9, 2018, Claimant provided notice that the Statement of Claim, the IPHC Order and notice of the expungement hearing was served on the Complainant Customers. On October 16, 2018, Claimant submitted an Affidavit of Service signed by Claimant's counsel advising that the Complainant Customers were served with a copy of the Statement of Claim.

The Arbitrator conducted a recorded telephonic hearing on November 20, 2018 so the parties could present oral argument and evidence on Claimant's request for expungement.

Respondent participated in the expungement hearing and did not contest the request for expungement. The Complainant Customers did not participate in the expungement. The Arbitrator found that the Complainant Customers had notice of the expungement hearing.

The Arbitrator reviewed the BrokerCheck® Report for Claimant.

The Arbitrator also reviewed the settlement documents, considered the amount of payments made to any party, and considered other relevant terms and conditions of the settlement. The Arbitrator noted that the settlement was not conditioned on the Complainant Customers not opposing the request for expungement. The Arbitrator also

[1] Four family members invested in the subject Fund, but only three of the four customers made a complaint against Claimant and Respondent. Unless otherwise noted, "Customers" refers to all four family member investors.

noted that Claimant made a sizable settlement contribution for a claim of debatable merit, but as discussed below, Claimant provided a persuasive explanation regarding why his contribution was appropriate in this scenario.

The Arbitrator noted that Claimant did not previously file a claim requesting expungement of the same disclosure in the CRD.

In recommending expungement, the Arbitrator relied upon the following documentary or other evidence: pleadings, including the original Statement of Claim and Statement of Answer; the Statement of Claim filed by the Complainant Customers; news articles provided by Claimant; Investment Policy Statements for two of the three Complainant Customers; Investment Advisory Agreements for the Complainant Customers; Investment Policy Addendums for the Complainant Customers; Private Placement Subscription Agreements for the Complainant Customers; Settlement and Mutual Releases; Claimant's current BrokerCheck® Report; copies of the notice Claimant sent to Complainant Customers regarding the expungement request and hearing; and Claimant's testimony.

The parties present at the hearing have agreed that a handwritten, signed Award may be entered.

AWARD

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

1. The Arbitrator recommends the expungement of all references to the Underlying Arbitration, occurrence [redacted] from registration records maintained by the CRD for Claimant [redacted] (CRD# [redacted], with the understanding that, pursuant to Notice to Members 04-16, Claimant [redacted] must obtain confirmation from a court of competent jurisdiction before the CRD will execute the expungement directive.

   Unless specifically waived in writing by FINRA, parties seeking judicial confirmation of an arbitration award containing expungement relief must name FINRA as an additional party and serve FINRA with all appropriate documents.

   Pursuant to Rule 13805 of the Code, the Arbitrator has made the following Rule 2080 affirmative findings of fact:

   The claim, allegation, or information is false.

   The Arbitrator has made the above Rule 2080 findings based on the following reasons:

FACTS

This expungement request concerns a November 10, 2015 arbitration claim filed by the Complainant Customers regarding a $1.5 million investment in an unregistered, private equity fund ("Fund"). In the Underlying Arbitration, the three Complainant Customers alleged that Claimant "failed to disclose adequately the risks of and made unspecified representations that lacked reasonable grounds in connection with a hedge fund investment they made in October 2011."

As adduced from the documentary and testimonial evidence made as part of the record, the Complainant Customers are family members, i.e., a mother and two of her adult daughters. In 2010, the family business was sold for several hundred million dollars and a substantial portion of the proceeds were distributed to Ms. C and her three adult daughters, all of whom became Claimant's customers and invested in the Fund. The Customers had a pre-existing banking relationship with Respondent's affiliate, City National Bank. At all relevant times, Respondent had a subsidiary entity, Convergent Wealth Advisors, LLC ("Convergent"), which specialized in managing large personal investment portfolios and handling related needs. Claimant was affiliated and registered with both Respondent and Convergent. In late 2010, the Customers were seeking retirement planning advice and consequently, a banking acquaintance introduced them to Claimant and they became his customers.

The Customers' ages ranged from mid '50s to late '20s. They maintained separate and independent lives with different residences in three states. The Customers all had broad professional business experiences and education. Among other things, Ms. C held a significant executive position in the family business for approximately twenty years and had been involved in the daily operations of that business. Ms. O held college degrees that included a Masters in Real Estate Development and was a practicing realtor who had been involved in several family-owned real estate ventures. Ms. M held a college degree in interdisciplinary studies and served as an executive assistant. The fourth customer had a Masters in Business Administration. Claimant conferred with the Customers regarding each individual's investment objectives and financial needs via several formal and informal meetings. Claimant determined that each of the Customers had low liquidity needs, primary investment objectives of income and secondary investment objectives of growth with moderate risk tolerance. Given their respective ages, the Customers anticipated having a lengthy investment horizon of approximately forty or more years. By all accounts, Claimant created a balanced and diversified investment portfolio for each of the four Customers. Each portfolio contained a broad range of equities, real assets, arbitrage holdings as well as a majority position in fixed income.

The Customers held multiple hedge fund investments prior to their Fund investments. For each such investment, the Customers had completed subscription agreements in which each acknowledged understanding the risks of hedge fund investments, including risks of illiquidity, volatility and lack of transparency. One or more of the Customers also reportedly experienced placement investment losses, some of which involved significant, if not a total, principal loss. In December 2010, each of the Customers opened separate Convergent discretionary investment accounts that included completing separate

"Investment Advisory Agreements." Each agreement contained a customer acknowledgment that the account might contain "Non-Managed" assets, for which "[the customer], and not Convergent, shall be exclusively responsible for the investment performance of these assets."

Sometime in 2011, Claimant told the Customers about the Fund, a commodity-oriented private equity hedge fund, and that he was also an investor in the Fund. A primary focus of the Fund was various small-scale African mining operations. Claimant testified that he explained the broad terms, risks, fees, advantages and disadvantages of this fund to the Customers, and that the Fund could possibly be used as an inflation hedge for each of the Customers' portfolios. Claimant testified that the Customers found the Fund's potential for significant profits unencumbered by management fees particularly attractive. The Customers also reportedly found great appeal in the Fund's potentially beneficial impact on local African communities via the likes of improved water treatment, infrastructure development and job creation. The Customers personally met with the Fund's CEO/Manager, and had the opportunity to evaluate that individual, and his general business plan for the Fund.

Each of the Customers completed a nine-page subscription agreement for the Fund that elicited each investor's qualifications. As part of the agreement, each of the Customers affirmed having: a net worth of more than $1 million; sufficient financial experience to evaluate the investment's merits and risks; and that the individual customer was not being aided by any purchaser representative. Each of the Customers affirmed having read and understood the company agreement and subscription agreement. Each of the Customers also affirmed an understanding that the investment had no public market and involved a high degree of risk, including loss of principal - without any guaranty of recovery or profitability. Claimant and the Customers had at least five discussions before the Customers decided to individually invest $500,000.00 in the Fund. Each of the Customers' investment status was approved in or around October 2011. For each of the Customers, the invested amount represented between 1% and 3% of each individual's total portfolio.

Claimant and Respondent, via Convergent, sought to ensure that each of the Customers understood that their respective Fund purchase was unsolicited, non-managed and permitted purely as an uncompensated accommodation. This understanding was memorialized in a single-page "Addendum to the Investment Policy Statement Dated January 28, 2011" separately executed by each of the Complainant Customers. Each addendum contains much of the same language found in the "non-managed assets" provision of the "Investment Advisory Agreement" which each of the Customers previously executed in December 2010. The primary difference between the two document types is that the addendum specifically referenced the Fund.[2]

[2] In relevant part, each addendum explicitly states that the Fund investment "contained within the Account and/or reflected on reports" was done solely as an accommodation and Convergent has not made an investment recommendation or given advice concerning the investment. "Convergent's services do not include investment advice, management, review, or monitoring services on the [Fund]. Furthermore

The Customers had a retinue of trusted familial and business advisors with whom they consulted concerning their investments. These advisors included: the family patriarch, who had been integral in building the family business, but was not Claimant's customer; the longtime president and CEO of the family business, who continued in that capacity after the business had been sold; the trustee for one or more family trusts; and the Customers' accountant. Claimant does not have personal knowledge regarding specific advice the Customers sought and received from these individuals, but he suggests that consultation concerning the Fund purchase with some or all of the advisors was likely. For example, the above-referenced trustee was a signatory to two of the Investment Advisory Agreements and had presumptive knowledge and an opinion regarding the Fund investment. Additionally, shortly after the Customers executed their subscription agreements, their accountant contacted Claimant and requested Fund tax information and was particularly interested in the Fund for "tax loss harvesting."

In December 2011, Claimant ended his business relationship with both Respondent and Convergence. In so doing, Claimant was no longer servicing the Customers' accounts. Claimant started his own firm, in part, to offer more independent investment advice and to avoid being at odds with Convergence's policy of recommending proprietary hedge fund products.

Claimant remained in contact with the Customers, now his former clients, and occasionally discussed the Fund's status with them. In mid-2012, a few months after Claimant ended his relationship with Respondent and Convergent, global commodity prices declined. News reports attributed the decline to European financial unrest and slowing economic growth in China, India and the United States. Increased Middle East oil production reportedly resulted in reduced oil prices. Over the next two years, the Fund's value declined by approximately 75 percent, due to a confluence of reduced commodity prices and poor management execution. Various mineral price reductions made extraction costs unprofitable. As an example of poor management execution, the Fund's operations were stymied by failure to plan for various cost disputes concerning permit requirements and local labor issues. Despite the Fund's extremely poor performance, none of the Customers expressed any alarm over the investment's decline in value nor did they mention dissatisfaction or claim misunderstanding of the investment circumstances. The Fund ceased operations in 2013.

In November 2015, the Complainant Customers (not including the fourth customer) jointly filed the Underlying Arbitration and sought compensatory

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Convergent has not conducted any due diligence on these investments. An investment in the [Fund] involves numerous risks that are detailed in the investment's offering and informational documents." Each addendum reiterated that the subject investment was a non-managed asset, a non-recommended investment and included a disclaimer that Convergent had no investment advisory authority over that hedge fund. Each Customer also independently acknowledged being "solely responsible for reviewing the offering documents and information related [to] the [subject] investments . . . as well as conduct[ing] any due diligence on the manager." Each subscribing customer further acknowledged not relying "on Convergent or its representatives in any capacity when making the decision to invest in the [Fund]. . . . As such, [the customer] and not Convergent, shall be exclusively responsible for the investment. [The customer] will not be billed on Non-Managed Assets."

damages of $1.05 million. Claimant and Respondent both denied the claim. In November 2016, without admitting any liability, Respondent and Claimant settled with the Complainant Customers for $588,277.50. Claimant paid half the settlement amount.

Claimant testified that his participation in the settlement negotiations was limited. Evidently, Respondent and the Complainant Customers had been privately discussing a settlement and Claimant only learned of the proposed settlement when Respondent "directed" him to contribute half the amount agreed upon by Respondent and the Complainant Customers. The settlement proposal was somewhat unexpected considering that Claimant and Respondent had both denied the Complainant Customers' claim. However, according to Claimant, Respondent had understandable justification to settle an otherwise disputed claim as a pragmatic business decision. Claimant testified that Respondent's position was overshadowed by the prospective sale of its Convergence subsidiary to another firm. Claimant also believed that Respondent's settlement decision was economically expedient in that the settlement of a compromised claim would likely cost less than the anticipated expense of defending the action while avoiding a protracted legal process and limiting Respondent's exposure to the remote possibility of an unfavorable award. In the end, Respondent's self-interested settlement decision left Claimant with little practical alternative other than reluctantly agree to the settlement proposal.

DISCUSSION

The evidence presented establishes that Claimant accurately and adequately represented that the subject Fund investment was unregistered, non-managed, highly speculative and suitable for each of the Complainant Customers, rendering their claim to be false.

The various subscription agreements and addenda, freely executed by the three sophisticated and experienced Complainant Customers, unambiguously emphasize the immensity of the risk and uncertainties involved in this investment and that each customer was "exclusively" responsible for determining the investment's suitability. Each subscription agreement contains a page-long list of possible risks for the Fund under the heading, "Certain Risk Factors." The documents warn of potential conflicts of interest and describe the Fund as a start-up business that is "inherently speculative" under a paragraph entitled "General Economic and Start-Up Company Risks." Other subscription agreement paragraphs make clear that the investment: might not be insured, was not part of any public market, was not registered under the Federal Securities Act or any state securities laws and "loss of the investor's entire principal is possible." Under a provision labeled: "Subscriber Able to Bear Risks and Protect Own Interest," each customer/subscriber represented that "that no assurances or guarantees have been made to Subscriber by anyone regarding whether the [Fund]'s investment objectives will be realized or whether the [Fund]'s investment strategy will prove successful. Subscriber recognizes that the Subscriber may lose all or a portion of Subscriber's nvestment [sic] in the Fund."

Without the benefit of hearing directly from the Complainant Customers, it is impossible to know the true extent of each's knowledge and understanding of the subject Fund investment and the documents they executed in connection therewith. However, the number and length of various subscription agreements that each Complainant Customer individually executed, coupled with each Complainant Customer's investment savvy provides for a strong inference that each basically understood the import of these documents including the risky nature of their investments. The inference is also bolstered by the fact that the prior to their purchases, the Complainant Customers had a shared collective understanding of their Fund investments and related documentation - and that any or all them - could have easily questioned the investment and declined to invest in it. Similarly, although the investment policy addenda included customer acknowledgments that each was solely responsible for employing independent investment judgment regarding the Fund, Claimant nonetheless had an objectively reasonable basis to believe that the Fund investment was suitable for the Customers, based on the information obtained through his reasonable diligence to ascertain each Customer's investment profile. This included detailed information for each of the Customers, including age, other investments, financial situation and needs, tax status, investment objectives, investment experience, investment time horizon, liquidity needs and risk tolerance.

At first blush, the large settlement amount seems inconsistent with both Claimant's and Respondent's denial of liability and a finding that the underlying claim, allegation, or information is false. However, Claimant's testimony, as set forth above, provides persuasive justification for the settlement. Claimant described how Respondent had a very strong impetus to settle the claim based upon self-interest and simple economics. Claimant believed that Respondent was in the midst of selling its Convergence subsidiary and that an unresolved customer claim might negatively impact the sale. Respondent also reportedly estimated that the settlement amount was less than the anticipated arbitration defense costs if the matter proceeded to hearing. Moreover, a settlement necessarily limited Respondent's potential exposure to an unfavorable award. Respondent's compelling reasons for settlement placed Claimant in an untenable position. It seems fair to conclude that Respondent's relationship with Claimant was less than harmonious. If Claimant did not agree to Respondent's negotiated terms, thereby preventing a global settlement amongst all of the parties, he risked further antagonizing an arbitration ally and undermining a collaborative defense. Conversely, if Respondent independently settled its claim, resulting in a partial settlement, Claimant risked shouldering additional defense costs in addition to possibly increasing the otherwise remote possibility of an unfavorable award.

Evaluating a claim that includes nebulous language, i.e., "making unspecified representations" is difficult per se. Compounding that difficulty is viewing the language in light of an unsubstantiated allegation that the Complainant Customers "routinely accepted all investment-related advice" from Claimant as part of what was an otherwise discretionary account and other unsubstantiated allegations that Claimant facilitated the Fund purchases with "sugar coated" misrepresentations concerning the Fund's prospective profitably. Suffice it to say,

the record establishes that Claimant disclosed the Fund's risks and those risks were plainly written for the Complainant Customers to see and consider, or ignore at their own peril. Besides Claimant's Fund risk disclosures, the Complainant Customers met with the Fund's CEO/Manager and thus had a reasonable and independent opportunity to conduct their own due diligence concerning the Fund and its explicit and inherent risks.

In sum, Claimant informed each of the Complainant Customers of the Fund's immense riskiness and each was independently capable of assessing those risks and willingly accepted them. Despite the open and obvious warnings concerning the Fund's riskiness, considering that Complainant Customers' investment in the Fund constituted a very small portion of each of the Complainant Customers' portfolios, it was not objectively unsuitable for the Complainant Customers.[3]

2. Any and all claims for relief not specifically addressed herein are denied.

FEES

Pursuant to the Code, the following fees are assessed:

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

Initial Claim Filing Fee	=$ 50.00

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

Member Fees

[3] Claimant insists that the Complainant Customers were never predisposed to make, let alone pursue, a claim regarding their Fund investments, but merely fell prey to a well-crafted advertisement regarding potential Fund-related claims. Claimant notes that he also lost money as a Fund investor and that sometime after the Fund ceased operations, he received an email inquiry targeting former Fund investors. That inquiry used the words "Free Loss Recovery" or similar, from a law firm exploring prospective Fund-related claims on a contingency fee basis. Claimant posits that the Customers received the same or similar email messages and clearly found the notion of a "free recovery" appealing enough to pursue a dubious claim. In the same regard, Claimant stresses that none of the Complainant Customers expressed any alarm over the Fund's loses and that the fourth Customer's decision to not join the other family members in pursuing a claim indicates some tacit recognition that the claim lacked merit. Claimant's argument is plausible; however, the limited record on this subject makes it exceedingly difficult, if not impossible, to establish the Customers' motives in bringing or declining to pursue a claim.

The fact that Claimant was also an investor in the same unregistered Fund, thus presenting an inherent conflict of interest, is impossible to ignore. While Claimant did not receive any compensation for the Customers' Fund purchases, additional investors potentially benefitted his Fund investment and presumptively colored his Fund-related advice. Nevertheless, the previously discussed evidence strongly suggests that the Complainant Customers were informed of the conflict and possessed sufficient sophistication, experience, and independence to assess that information objectively. The same evidence also suggests that any undue reliance on Claimant was minimized by easily obtained advice from various trusted individuals – all of whom were independent from and unrelated to Claimant. Finally, the existence of a conflict does not negate or diminish the fact that these Complainant Customers received *ad nauseam* admonitions that the subject private and unregistered investment involved extreme and significant risks.

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, Respondent is assessed the following:

Member Surcharge	=$ 150.00

Hearing Session Fees and Assessments

The Arbitrator 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 a single arbitrator @ $50.00/session			=$50.00
Pre-hearing conference:	September 20, 2018	1 session	
One (1) hearing session on expungement request @ $50.00/session			=$50.00
Hearing Date:	November 20, 2018	1 session	
Total Hearing Session Fees			=$100.00

The Arbitrator has assessed $100.00 of the hearing session fees to Claimant.

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

ARBITRATOR

Elliott D. Finkel - Sole 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.

Arbitrator's Signature

/s/ Elliott Finkel
Elliott D. Finkel
Sole Public Arbitrator

March 6, 2019
Signature Date

March 6, 2019
Date of Service (For FINRA Office of Dispute Resolution office use only)