

# Errors & Omissions Claims Against Investment Advisers



The following are samples of the types of suitability claims and breach of contract/trading error claims that can be filed against investment advisers.

## 1. Suitability Claims

### **Unbalanced Account**

The client, a semi-retired professional, hired an investment adviser (the insured) to manage his account with these objectives: modest growth, preservation of capital, and a balanced account (equities to bonds). After the first year, the client's account was 60% equities and 40% bonds. After the second year, it was 80% equities and 20% bonds. The client sued, alleging that the investment adviser failed to reallocate and balance the mix of equities to bonds.

### **Use of Model Portfolio**

An elderly, widowed housewife alleged that her investment adviser (the insured):

- Liquidated her "blue chip" portfolio.
- Invested the proceeds in unsuitable technology stocks.
- Caused her to suffer a large financial loss.

The investment adviser advertised that he tailored accounts to individuals but, in reality, he used a model portfolio with growth emphasis. The housewife filed an arbitration claim with the NASD.

### **Change in Objectives**

The client hired an investment adviser and stated that he wanted his account invested in growth and aggressive growth stocks. After several years, the client changed his investment objective to moderate growth, capital preservation and conservative. The client filed a lawsuit, alleging that the investment adviser failed to change the investment mix to reflect his new objectives.

### **Change in Circumstances**

The claimant was a long-term client with an investment adviser (the insured). After a while, the claimant suffered poor health and financial adversity. The claimant alleged that, after his health problems, the investment adviser should have moved him out of high-risk tech securities and into low-risk securities and bonds. The investment adviser's documentation was poor. The claimant sought lost market value and lost profits.

## **2. Breach of Contract/Trading Errors**

### **Custodial Bank Miscommunication**

A claim arose over a miscommunication between an investment adviser (the insured) and a client's custodial bank regarding a large deposit for the client's investment account. An employee at the investment adviser received a transaction sheet for the client's account, which showed a large deposit and other entries.

The employee:

- Contacted the custodial bank.
- Misunderstood and thought the transaction sheet was for "general awareness".
- Filed it.

No new money was invested for three months during a market upturn, and the client sued, claiming he lost several hundred thousand dollars in profits.

### **Ministerial Error/Miscommunication**

A miscommunication or misunderstanding of an insured's sell order to a trading desk resulted in the wrong stock being sold. The investment adviser (insured) purchased the stock back after it had jumped in price, resulting in a large reduction in the client's accounts. The client sued the investment adviser, seeking to recover the lost profits.

### **Delayed Execution and Violation of Objectives – Socially Responsible Stocks**

A client alleged that the investment adviser (insured) failed to invest timely – and waited three months to begin investing – because the client had not arranged for a transfer of funds. The client also alleged that the investment adviser failed to invest in socially responsible stocks, and instead invested in two companies that offended the client. The client sued, seeking damages for delayed execution and violation of objectives.

### **Adverse Tax Consequences from Discretionary Trading**

An investment adviser (insured) raised cash for a client from annuity accounts instead of raising it from taxable mutual fund accounts. This action triggered a tax penalty for the client, and the client sued the adviser to recover the amount of the tax penalty.

### **Breach of Investment Guidelines**

An investment adviser's software did not detect that its purchase of a Canadian company stock violated a client's investment guidelines (which stated she only wanted to purchase stock from companies headquartered in the United States). Although the portfolio made money overall, the client sued the investment adviser to recover the loss from the Canadian stock.

All of these hypothetical claims are of a type expressly included within the coverage provision for "professional services". However, the scenarios are offered as examples only. Coverage depends on the actual facts of each case, and the terms, conditions and exclusions of each individual policy. Anyone interested in the Investment Adviser

product should request a copy of the policy itself for a description of the scope and limitations of coverage.