REUTERS

ECONOMY

CORRECTED-Merrill ordered to pay couple $1.34 mln over Fannie Mae shares

Tue, Oct 16 18:21 PM EDT

(Corrects year in first paragraph, and ninth paragraph to show that arbitrators did not award punitive damages)

By Suzanne Barlyn

Oct 16 (Reuters) - Merrill Lynch must pay $1.34 million to a Florida couple who alleged the brokerage misrepresented the risks of Fannie Mae preferred shares in 2008, when the housing finance company was on the brink of collapse, an arbitration panel ruled on Tuesday.

Robert and Michele Billings of Naples, Florida invested $2.3 million in Fannie Mae preferred shares in July, 2008, a move that was "strongly recommended" by their broker, according to a statement of claim filed with the Financial Industry Regulatory Authority's arbitration unit in 2011.

The Billings, former owners of a pest control business, were long-time clients of Merrill Lynch, now a Bank of America Corp unit.

The broker, Miles Pure, allegedly told the Billings that the investment was "safe," had an attractive yield and that the U.S. government "stands behind" Fannie Mae preferred shares, according to the statement of claim.

But that was not the case and Fannie Mae was losing billions of dollars at the time because of its exposure to the collapsing residential real estate market, the investors said. As the stock's price slid, the broker also discouraged the couple from selling shares. Then, just over a month later, Fannie Mae entered government conservatorship and the Billings' investment was rendered worthless, according to the statement of claim.

The case is an example of the ongoing fallout for investors and their brokers from the U.S. financial crisis. Arbitration claims related to losses tied to everything from toxic bond funds to auction rate securities are still winding their way through FINRA's arbitration system, say industry lawyers. FINRA is Wall Street's self-regulator.

A Merrill Lynch spokesman said the brokerage disagrees with the arbitration panel's decision. Regulatory filings show Pure is now a broker for Morgan Keegan & Co, a unit of Raymond James Financial Inc. He did not immediately return a call requesting comment. A Raymond James spokeswoman declined to comment.

The Billings, who are retired and involved with breeding thoroughbred horses, filed their arbitration case against Merrill Lynch in 2011. The couple alleged civil fraud and also alleged that the brokerage was negligent in supervising Pure, among other things, according to the arbitration ruling.

They asked for more than $1 million plus punitive damages and other relief, according to the ruling. Arbitrators denied the claimants' punitive damages request. As is customary, they did not explain the reasons for their decision.

"We are pleased that the FINRA arbitration panel agreed with the Billings that Merrill Lynch breached its legal obligations to their clients in recommending Fannie Mae preferred shares," said Jeff Erez, a lawyer in Fort Lauderdale, Florida, who represented the couple.

Pure, the complaint alleged, did not disclose to the Billings that Merrill Lynch's own research indicated trouble at Fannie Mae. For example, Merrill Lynch removed Fannie Mae from a list of "recommended" preferred stocks shortly before Pure's recommendation, according to the statement of claim.

What's more, the Billings' ordered Merrill to sell their stock when the price began to decline shortly after they invested. Instead, Merrill Lynch, advised them to hold their position, they alleged. The Billings followed their advice, but the stock soon became nearly worthless, they alleged.

The panel also denied a request by Pure, who was not a party to the case, to remove a disclosure about the arbitration from his public record.

Securities industry rules require arbitration cases to appear on the public records of licensed securities brokers who had ties to a transaction in dispute - even if they are not named in the case.

Arbitrators did agree to remove the disclosure about the arbitration from a brokerage manager's record, because he was not directly involved in the daily dealings with the Billings. (Reporting By Suzanne Barlyn; Editing by Jennifer Merritt and Tim Dobbyn)