Citigroup Global — formerly Smith Barney — hit with $3.1M arbitration award

Citigroup Global gets hit with a $3.1 million arbitration award after investors claimed a former Smith Barney broker steered them to a real estate development that folded. Bruce Kelly reports.

October 2, 2013 *By Bruce Kelly*

Citigroup Global Markets Inc. on Monday was hit with a hefty $3.1 million arbitration award after two investors claimed that their broker directed them into real estate developments managed by the son of a former Florida governor during the real estate boom that went bad.

The three-member Financial Industry Regulatory Authority Inc. panel yesterday signed off on the award. The plaintiffs, Dr. Nasirdin Madhany, 66, and Zeenat Madhany, 63, originally filed their claim in 2010.

Citigroup Global Markets, formerly known as Smith Barney, "is liable for breach of fiduciary duty as financial adviser to claimants, as well as negligent supervision," according to the Finra arbitration award.

"We disagree with the award, which was not supported by the facts or law," Citigroup spokesman Mark Costiglio wrote in an e-mail.

The award is split in two parts. In the first, Citigroup is on the hook for $1.04 million in compensatory damages to the claimants for investments in two developments in the Florida panhandle. The second states that Citigroup is liable to pay the Madhanys $2.1 million as part of a settlement from a separate lawsuit stemming from a loan guarantee they signed for one of the failed real estate projects.

In 2003, the Madhanys' Smith Barney broker, Scott Andrew King, referred his clients to Lawton "Bud" Chiles III, the developer of the two real estate developments in Carrabelle, Fla., according to the Madhanys' 2010 amended statement of claim. Mr. Chiles is the son of former Florida Gov. Lawton Chiles.

Mr. King no longer works for Smith Barney, which was purchased by Morgan Stanley in different tranches beginning in 2009. In 2005, Mr. King left Smith Barney to join Wachovia Securities LLC, which is now Wells Fargo Advisors LLC.

Mr. Chiles did not return a phone call Tuesday to comment. Mr. King, who also did not return a phone call, was not named liable in the Finra arbitration award.

In alleged violation of Finra rules, Mr. King arranged and/or participated in meetings between the Madhanys and Mr. Chiles by, among other things, holding events designed to introduce potential investors to Mr. Chiles, according to the investors' complaint.

"The illegal practice of 'selling away' is when a broker engages or is involved in unapproved investments 'away' from the brokerage firm," according to the complaint.

Mr. King allegedly violated Finra rules that prohibit financial advisers from participating in private securities transactions, or 'selling away,' the complaint alleged.

The Finra rule involving selling away not only refers to a broker making the sale but referring customers and introducing customers to the issuer of the securities in question, according to the complaint.

In an e-mail from March 2009, which was an exhibit in the complaint, Mr. King wrote to Mr. Chiles: "I bent over backwards to help you with my most valued contacts, which were damaged terribly."

By recommending that the Madhanys invest in Mr. Chiles' real estate projects while registered with [Citigroup Global Markets], Mr. King allegedly violated Finra rules that prohibit an adviser from engaging in outside business activities or private securities transactions, according to the complaint.

The two condominium developments went into foreclosure in 2010, and that's when the Madhanys realized their losses in the two developments, said Jeffrey Sonn, their attorney.

Mr. King attended a meeting in which Mr. Chiles pitched the Madhanys and others the real estate investments, Mr. Sonn said. "According to Finra rules, reps can't attend a meeting where an outside investment is being proposed," Mr. Sonn said.

The Madhanys and several other investors signed personal-loan guarantees in connection with a $12 million loan to one of the projects by the former Wachovia Bank, which later sued the guarantors. Citigroup must also reimburse the couple up to $10 million if they are required to pay the entire judgment amount in that case, according to the ruling.

Recent Articles by Author

Advisor revenue up at Ameriprise despite lousy year for stocks

The firm reported that its average revenue per financial advisor increased almost 4% in 2022 compared to the year earlier.

Wisconsin advisor pulled $1.9 million fraud on clients

The advisor, Anthony B. Liddle, 40, was barred from the securities industry last June by the Financial Industry Regulatory Authority Inc.

Does the 60/40 rule need revising given the surge in alts?

At a panel at FSI OneVoice, one speaker suggested the revised math for portfolios could wind up in the neighborhood of 55% stocks, 35% bonds and 10% alternative investments.

Rising interest rates not a killer for RIA M&A

Meanwhile, though, some RIA buyers are 'dancing' to get necessary capital to do deals, says Dan Seivert of Echelon Partners.

Is the new generation of nontraded REITs really any better than the last?

Wall Street has revitalized the product, but these REITs face new scrutiny because of an old problem: Investors are demanding liquidity.