

THE ART
OF
RESPONSIBILITY

THE TALE
OF THE
STOCKBROCKER

by Rabbi Chaim Kohn
provided by The Business Halacha Institute



People like advice, and they like to hold the adviser responsible if his advice fails. This is true in general but particularly when it comes to monetary matters. Today more than ever, complex matters – from dealing with medical issues to purchasing stocks – require experts’ assistance; indeed, an entire industry of professional assistance has come into existence to advise and guide people in all areas of life.

Generally, there will be some sort of signed disclaimer limiting the adviser’s liability, but as with any legal dispute, one can never be certain that a contract will cover all possible claims. Many times, professional advice is offered not in a contractual context but as part of a potential business venture, and if matters don’t work out as expected, a claim against the consultant is not unlikely.

What are the provisions of Torah law in terms of liability for bad advice? Let’s look at one scenario and then explore the applicable principles:

Rick is a close friend of Sam and a known stockbroker. He alerts Sam to a stock that, in his opinion, has great potential for growth and urges him to join him in this investment. Stocks are Rick’s area of expertise as well as his trade, and there is an implied understanding that Sam will pay for Rick’s professional services.

Sam follows the broker’s advice but loses his money after the value of the shares plunges. He is visibly upset about his losses and, not surprisingly, blames Rick. He suspects that the broker did not properly research the stock before advising him, relying instead on his instincts, and therefore he wants Rick to compensate him for his losses.

For his part, the broker claims that he never misrepresented any facts, nor did he accept responsibility for Sam’s decision to invest, and in fact he is upset over his own personal losses. The two men decide to bring their case to a Jewish court, called a Beis Din, and to follow the Torah laws that apply to them.

He suspects that the broker did not properly research the stock before advising him and wants to be compensated for his losses.

Interestingly, the legal guidelines established by the SEC (Securities and Exchange Commission) for a broker/client relationship in such a case are quite ambiguous. Although there is general agreement that the broker would be liable in a clear case of deceit, most of the time there is no real deceit involved – only a breach of trust.

According to some legal opinions, a broker who knowingly misrepresents facts and risks is certainly guilty of fraud, but there is no statutory obligation for the broker to do research; his only obligation is to see to it that all his statements are truthful. Therefore, there is no legal claim for liability if he did not properly research the stock and relied instead on his gut feeling.

The SEC asserts that the so-called "shingle theory," which obligates the broker to deal fairly with the client, implies that any breach of this obligation can be deemed fraudulent. However, in the words of one well-received article on the subject, "This theory — and the duty it creates — pretty much comes from nowhere." That is to say, the rulings on such cases in court are arbitrary and as such do not provide useful information about clear industry standards.

All this is important to our question because these types of standards, called *minhag hasochrim*, can have a bearing on the applicable Torah law. Unlike the laws that govern this country, such as common law, statutes or laws established by judges, through which liability is often ascertained by arbitrary rules based on moral and assumed

behavioral standards, Torah law is subject to clear, preset definitions of law that categorize liability. Although clear behavioral standards can be relevant to an area of Torah law known as *minhag hamedinah* (local practice) or *minhag hasocharim* (industry practice), nevertheless, unless a practice is proven to be the recognized standard, the Torah law on the books will prevail.

There are two theories of liability in Torah law that could potentially be relevant to our case.

There are two theories of liability in Torah law that could potentially be relevant to our case: One would require that the liable party has voluntarily assumed responsibility to pay damages. The other would require that damages were caused by a wrongful act (tort).

Two examples of the voluntary assumption of liability are a guarantor on a loan (called an *arev*), and a guardian, or bailee, with whom someone entrusts their property (called a *shomer*). These are responsibilities people choose to take upon themselves and, assuming there is acceptance of fiduciary responsibility — whether verbally or by implied behavior — they can be liable for losses suffered on their account. Examples of implied acceptance of responsibility would be a clear directive from a guarantor to the lender to forward money to the borrower, or a guardian instructing the owner to deliver to him the item he is to watch. It then becomes the duty of the guardian to ensure that no harm comes to the item entrusted to his care.

Legal liability for causing damage is generally limited to acts of tort. However, responsibility for consequential, or indirect, damages is a contentious issue. For example, although crashing into someone's car is clearly a tort, hiding a

cab driver's car keys, for example, resulting in his losing a day's income is not. Though such behavior would certainly be a violation of Torah law, nevertheless, the actions of this wrongdoer cannot be prosecuted legally, and the driver cannot recover his losses in a *Beis Din*.

Even so, there are consequential damages that are considered acts of tort under the category of *dina degarmi* [pronounced DEEnah d'garMEE]— a kind of tort that can include indirect damages. One such case is that of a consultant who has assured a lender that a particular borrower is creditworthy. If it is apparent that this consultant is being relied upon, he is held responsible for the consequences of his recommendation.



Therefore, if it turns out that the consultant's information was based on negligent research and that the borrower was already then in bad standing and likely to default on the loan, the consultant is liable for any consequent losses under the theory of *dina degarmi*. This is because Torah law views the harm done as immediate and

expected, though neither the consultant nor the lender was aware of it at the time.

The consultant is liable not because of an implied acceptance of responsibility, in the manner of a guarantor, but because the flawed information he gave is considered to have caused damage to the lender. Additionally, even if the consultant explicitly declines to be a guarantor, he would still be legally responsible for having committed a tort, based on the principles of *dina degarmi*.

Let's now return to our case of Rick the stockbroker and Sam the investor. If a broker's advice would include an implied assumption of responsibility for any losses suffered, Rick would be liable in the same manner as a guarantor. If only it were so. Investing in the market is known to be inherently risky. Though on the one hand, a sensible investor will not make a move without consulting with a professional, on the other hand, he is fully aware that his investment may be lost. In our case, Rick has not accepted legal responsibility as a guarantor and would not be liable under that theory.



Neither did Rick commit a liable act of tort under the classic definition. Although Rick urged Sam to invest, he did not force him to invest. It was Sam's free decision and desire for profit that influenced his decision. To be liable for a tort, Rick would have had to cause direct damage.

But what about *dina degarmi*? Clearly, Sam relied explicitly on Rick's expert advice in deciding that this was a wise investment. As such, his actions compare to a consultant who recommends a borrower as being creditworthy when he is not. If, in fact, Rick was negligent in his research and gave bad advice, his recommendation would constitute a breach of trust.

As we said earlier, "breach of trust" in this case may not be a winning legal argument in a US court but for purposes of Torah Law, whether there is or is not a statutory obligation for a stockbroker to do research is not relevant. The client was counting on receiving sound advice.

➤ CONTINUED ON PAGE 60

Eretz HaChaim

C E M E T E R Y

IN THE JERUSALEM HILLS

- Beautiful, landscaped and secure memorial grounds
- 20 minutes from central Jerusalem & from airport
- Modern chapel & facilities in an ancient setting
- Easy access & wide paths for Cohanim
- All transportation and burial arrangements
- Family, group and community plots available
- Graveside minyan for yahrzeits & visits
- Bais Medrash & Kotel on premises
- Convenient payment plans available

For more information and a free Brochure/CD Please call toll free

866-437-2210

www.erezhachaim.org

**Eternal
Rest
in an
Eternal
Land**



Eretz HaChaim
C E M E T E R Y
IN THE JERUSALEM HILLS

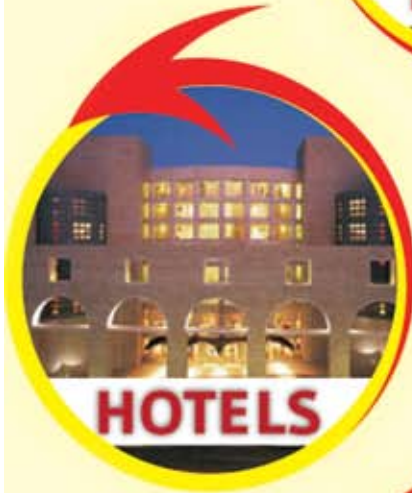
ת"וב

Artzeinu

Kotel Tunnels,
Tsfat, Galil,
Golan, Massada,
Ir Dovid, Jeeps,
Hevron, and
many more



Lowest possible
HOTEL RATES
throughout the
country



Customized,
Personalized! Be
a GUEST at your
own SIMCHA



USA Tel: 718-701-3690 (Direct line to Israel)
Israel Tel: 02-587-1718
Email: Artzeinu@netvision.net.il
Web: www.Artzeinu.co.il

Therefore, this would certainly be a case of *dina degarmi*. Consequently, if it is proven that the broker failed to research the investment diligently but relied only on a sloppy analysis, he is liable for this breach of trust under the theory of having caused damages. In that instance, even the fact that the broker lost his own money in this investment does no excuse his negligent behavior.

If, in fact, Rick was negligent in his research and gave bad advice, his recommendation would constitute a breach of trust.

Words are very powerful. Good advice can create and build; bad advice can destroy. Though courts of law are necessary to determine liability and to require compensation when appropriate, the Torah's expectations of us exceed this minimal standard. All of our words should be considered and shared based on what is ultimately just and good. The mitzvah of *v'ahavta lere'acha kamocho* – love your fellow as yourself – is meant to be the guiding principle of all our personal interactions.

In all matters of Torah law, readers should consult their rabbinic authorities for all practical guidance.

The Business Halacha Institute, under the guidance of Rabbi Chaim Kohn, a noted expert in Jewish Civil Law, is committed to educating and offering services in the area of Business Law according to the Torah. To subscribe to their popular FREE weekly newsletter, Business Weekly, email subscribe@businesshalacha.com. For more information on their programs, activities and materials, visit their website: www.businesshalacha.com or email info@businesshalacha.com.

