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IN THIS ISSUE

Arbitrator Selection Under the Securities Arbitration Rules of the American Arbitration Association

by George H. Friedman*

Introduction

One of the most important factors in selecting an arbitration forum is the pool of arbitrators who will hear and determine disputes. This article describes the panel of arbitrators available to resolve securities cases filed with the American Arbitration Association, focusing on who the arbitrators are and how they are appointed to individual cases.

List of Arbitrators

Following the filing of the Demand for Arbitration, the case is assigned by the AAA to a staff member in the regional office, called a tribunal administrator, who would be responsible for overseeing the administration of the case from the time it is filed until it is concluded. The administrator would within seven days send a letter to both parties, acknowledging receipt of the Demand and enclosing a list of potential arbitrators from which the parties are to make their selection. Both parties have twenty days to examine the list, strike any unacceptable names, and return the list to the administrator.[1]

Arbitrators

The arbitrators the Association lists are not AAA employees; rather, the AAA maintains a panel of over 50,000 qualified arbitrators who have volunteered to serve on AAA arbitration cases.[2] Of these, about 1,400 are qualified to hear securities cases. The affiliation breakdowns are as follows:

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Arbitrator Assignment — The Case for Agency Selection

by Edward W. Morris, Jr.*

Perhaps no aspect of the securities industry has recently received as much scrutiny as arbitration. The Shearson v. McMahon decision and the October '87 market break concentrated the attention of the bar and the public on the process. The SEC's letter to SICA of September 10, 1987 and SICA's continuing effort to develop rules and policies to accommodate the concerns of the Commission also served to focus the eyes of the industry on the process.

On January 17, 1989 the New York Stock Exchange filed its latest (and hopefully final) amendment to our Rule 19b-4 filing, NYSE-SR 88-29. By this filing, the Exchange submitted for public comment and Commission approval the result of the Exchange's and SICA's efforts in arbitration over the past year. Upon approval, all of the SICA amendments to the Uniform Arbitration Code are to be incorporated into the arbitration rules of the NYSE. The filing covers most of the topics which received attention and publicity last year including discovery, the classification of public arbitrators, the arbitrator's duty to disclose, and the con-

*Mr. Morris is the Arbitration Director at the New York Stock Exchange, Inc.

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AAA List Selection *continued from page 1*

— affiliated with the industry	796
— customer's bar	88
— knowledgeable, but no affiliation	516

Individuals may be nominated to become arbitrators by attorneys, parties, other arbitrators, AAA staff, or may be self-nominated. Applications are carefully screened by the Association's Panels Department before individuals are empanelled as arbitrators. The Association also conducts periodic training of arbitrators.

Number of Arbitrators

The rules provide that where the disclosed claim of any party exceeds $25,000, exclusive of interest and arbitration costs, the dispute is heard and determined by three arbitrators.[3] All other cases are heard by one arbitrator.

Qualifications of Arbitrators

In a single-arbitrator case, the arbitrator cannot be affiliated with the securities industry. Similarly, as a matter of practice, the arbitrator in a single arbitrator case will not be an attorney whose practice is devoted to representing customers in securities arbitrations. In a three-arbitrator case, two of the arbitrators cannot be affiliated with the securities industry, although the rules permit the parties to agree to some other arrangement. For example, the parties can agree that each side will appoint an arbitrator, who will in turn appoint the neutral chair of the panel. Also, they can agree to waive the listing procedure and have the AAA directly appoint the arbitrators.[4]

Each party receives an identical list containing two "blocks" of names; one block contains the names of five proposed arbitrators who are affiliated with the securities industry, and one block contains the names of ten proposed arbitrators who are not affiliated with the industry. The parties are afforded the opportunity to review the list and return it, striking the names of unacceptable arbitrators. The AAA completes the panel from among those names remaining on the list (i.e., one arbitrator is selected from the first block, and two from the second).

Although the listing process is not as expeditious as having the administering agency directly appoint arbitrators without submission of lists, one of the key benefits of AAA-administered arbitration is that it affords the parties an opportunity to become involved in the selection of the neutrals who will decide their case. When one considers that the overall processing time for AAA cases administered to an award in 1988 was a median 168 days — less than six months — the time expended in selecting an arbitrator is well-spent. Also, the SEC for the past year and a half has been urging the industry-sponsored arbitration fora to take steps to increase customer perceptions of their neutrality; giving the parties a voice in selecting their arbitrator is surely one way to accomplish this.

Although the rules do not define the term "affiliated with the securities industry," the AAA has administratively defined the term to mean those individuals, knowledgeable of securities matters, whose business (or whose firm's business) derives twenty-five percent or more of its income from securities matters (i.e., representing or acting as broker/dealers or issuers). This includes "persons who have, directly or indirectly, within the last five years been employed by or acted as counselors, consultants, advisers, or attorneys to any SRO or SRO affiliate. Partners or employees in law firms that derive substantial income from representing SRO's or SRO affiliates are considered to be affiliated with the securities industry."[5] Arbitrators whose spouses derive substantial income from the industry, but who do not themselves possess knowledge or expertise of securities matters, cannot serve on AAA securities cases.

During 1988, the AAA revised its arbitrator data sheet, the form sent to arbitrator applicants and those arbitrators on the panel who are updating their records. The form now asks for more detailed information on not only the arbitrator's securities experience, but that of the arbitrator's spouse as well. A new section was added requesting information on any governmental or professional disciplinary proceedings which have involved the arbitrator candidate. The entire securities panel has been updated using this new form, resulting in more accurate arbitrator biographical information for the AAA to transmit to the parties and to use in preparing lists of proposed arbitrators.

The arbitrators appointed must be completely impartial, and are obligated to disclose any past, present or potential relationships, business or personal, with the parties, their attorneys, planned witnesses and others involved in a case.[6] The AAA is empowered to remove an arbitrator from a case where there is a substantial relationship.[7]

Arbitrator Appointment

When the lists of arbitrators are returned, the administrator will compare the lists to see if any of the names proposed were acceptable to both parties. Assuming an acceptable name was contained on a list, that arbitrator would be contacted by the administrator to see if the arbitrator is available to serve. If the parties are unable to agree on a name, the Association is empowered under its rules to appoint another arbitrator, whose name did not appear on the list, to serve on the case.[8] As a matter of practice, the AAA in cases involving in excess of $100,000 will on request of a party submit a second list where the first list does not result in the designation of a full panel of arbitrators.

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SRO Agency Selection *continued from page 1*

tent and form of arbitration contracts. The summary data included in the award and the determination to make information concerning arbitration decisions publicly available are also covered in the filing.

The Selection Process

One procedure which has not changed, despite receiving a great deal of attention from SICA and the SRO's, is the method of selecting arbitrators to serve on cases. The current method both of obtaining arbitrators and of assigning those arbitrators to particular cases used by the SRO's were found by SICA to foster the quick and fair resolution of securities disputes.

A national SRO such as the NYSE may list thousands of capable men and women as arbitrators. The Exchange obtains their names from bar associations, community groups and existing arbitrators. Others are referred by securities organizations or governmental agencies. Rarely will an individual have sufficiently strong credentials to make the list without a recommendation. Generally, the arbitrators are grouped by city and are only asked to serve in a major commercial center close to their home or business. Only rarely is an SRO arbitrator asked to travel.

Once an arbitrator is recommended, he or she receives a letter from the SRO which describes the program and also requests the completion and return of an arbitrator profile. The profile contains the name, business history and the educational background of the arbitrator, and also asks about business and professional relationships with the securities industry. Prospective arbitrators are also asked to disclose any professional disciplinary action which might have been taken against them. The profile is then reviewed, and in the case of securities arbitrators, checked with the CRD before the individual is accepted as an arbitrator.

In assigning arbitrators to particular cases, the staff typically reviews the pleadings and then the arbitrator profiles for the city in which the hearing will be held. In order to ensure confidentiality, potential arbitrators are first asked if they are available on the scheduled date. Only after they have indicated their availability is the case described to them.

The staff relates the names of the parties, the names and firms of the attorneys, the names of witnesses, if known, and a brief description of the dispute. The arbitrators are then asked if they have any conflict. If the potential arbitrator affirms that no conflict exists, he or she is assigned to the panel for the case.

Once the panel, typically three arbitrators, is complete, the parties are notified, generally by letter, and given copies of the arbitrator profiles. At the same time, the arbitrators are sent the pleadings and are asked to review them. The arbitrators are also sent the Code of Ethics for Arbitrators in Commercial Disputes and are reminded of their continuing duty to disclose any real or apparent conflict.

In the SRO system, parties also have an obligation to assure impartiality of the panel. Parties are asked to review the profiles and disclose any real or apparent conflict they may have with the arbitrator. To ensure a high degree of comfort with the panel, parties also have the right to ask the SRO's for additional relevant information beyond that contained on the arbitrators' profiles. Parties also have unlimited challenges for cause and are entitled to one peremptory challenge. In exceptional cases, they may receive additional peremptory challenges. Upon the exercise of a peremptory challenge or upon the granting of a challenge for cause, a new arbitrator will be appointed to the panel. The new arbitrator will also be screened by the staff, and the parties will receive the new arbitrator's profile and be again asked to review it for conflicts.

Advantages of the SRO System

The prime advantage of the SRO system of selection is that it establishes an entire panel of neutral arbitrators. They have no duty or obligation to any party as they do in the tripartite system. Moreover, a party cannot frustrate the system by striking a venire as is possible in the AAA's system of selection. It is interesting to note that the AAA uses the agency selection method as a fallback when parties have stricken all potential arbitrators.

In addition, the SRO system fosters speed in the dispute resolution process. Anyone who has tried to coordinate the calendars of five or more busy professionals knows that months can go by before they are all available on the same date. By first establishing a date and then selecting arbitrators, the SRO system permits swift and sure case scheduling. It has enabled the NYSE to conclude the average case in 8.2 months in 1988. The SRO system also permits greater use of arbitral resources. Rather than have to provide routinely the names of up to 30 arbitrators per case as may happen under AAA rules, the SRO's need only provide as many names as necessary to ensure a fair and impartial panel.

Since the SRO's offer a standard honorarium, the issue of arbitrator compensation can never taint the arbitration selection process. The arbitrators look to the SRO rather than parties for assignments, compensation and other services. Arbitrators are freed from setting rates and parties need not worry about expensive versus inexpensive arbitrators when striking lists.

The SRO system also permits the assignment of particularly knowledgeable arbitrators in complex or highly technical cases. The assignment of arbitrators who are screened for their expertise has the potential to save or reduce the expenses of the parties for expert witnesses. Many times the "industry" arbitrator assigned to a case by an SRO is more of an expert in the area in controversy than the paid expert of either party.

Conclusion

The SRO system of arbitrator selection has been proven effective by over 100 years of use. It conserves arbitral resources. It eliminates the potential for abuse by a party who wishes to use delay as an adversarial technique and eases the parties' burden in the selection process. Most importantly, the system results in the impaneling of fair, impartial and knowledgeable neutrals.

Punitive Damages: On Trial

The turbulent debate swirling about the issue of punitive damages in arbitration seems to be forking in two distinct directions. First, there is the issue of whether arbitrators can lawfully award punitive damages. While there exists good authority for the positions of both sides, those who argue in the negative seem increasingly to be leaning against the wind. Still, the law remains very uncertain. Even in the New York federal courts, where Garrity v. Lyle Stuart, Inc., 353 N.E. 2d 793 (N.Y. 1976) remains the home state's rule, the cases are divided.

In a financial services case, the Eleventh Circuit held last year, in Bonar v. Dean Witter Reynolds Inc. (1 SAC 1 (3)), that arbitrators can award punitive damages, even when a New York choice of law clause is present. The Supreme Court's McMahon opinion is frequently used by those advocating punitive damages in arbitration, first, on the premise that RICO treble damage claims, which the Court held arbitrable, are punitive in nature, and, secondly, by reasoning that it would be inconsistent with the Court's apparent view of SRO arbitration as simply an alternative forum to limit arbitrators' ability to remedy perceived wrongs.

In California, a state appellate court affirmed the authority of an arbitrator, in a non-securities, employment dispute, to award punitive damages for wrongful discharge and breach of the implied covenant of good faith and fair dealing (Belko v. AVX Corp., 204 Cal.App.3d 894 (4Dist., 9/20/88). The arbitrator awarded $85,421.72 in compensatory damages, $500,000 in punitive damages, and $100,000 in general damages for emotional distress. While no New York choice of law provision was present in the contract of employment, the Court did consider and reject, as "unduly restrictive," the Garrity rule that arbitrators, even with the party's consent, cannot consider punitive damages. While arbitrators can only consider such issues as the parties have contractually agreed to present, the existence of a broad arbitration clause and indications of a mutual intent to have the arbitrator consider the punitive damage claim were sufficient to place the issue within the arbitrator's authority.

On December 8, 1988, the California Supreme Court depublished the Belko opinion and refused to hear an appeal of the case. Depublication, under the rules of the Court, means that the case cannot be cited as authority. Depublication, we are told, is not uncommon in cases where the Court accepts an appeal, but it is unusual to have the opinion simply tossed out without further word as to why. This action also casts suspicion on an earlier Court of Appeal decision, Baker v. Sadick, 162 Cal.App. 3d 619 (4Dist., 1984), upholding a punitive damage award under the special rules of CCP 1295 applicable to arbitration of medical malpractice disputes.

Clamor for Standards

The real storm brewing over punitive damages is a national dispute about the need for restraints on when punitives should be awarded and in what amounts. For years, the standards guiding factfinders in the award of punitive damages have been nebulous and the limits placed upon the amounts a court or jury can award have been virtually undefined. Illustrative of this point in a securities setting was the observation of the Eleventh Circuit concerning the appeal of a jury verdict awarding $46,675 in compensatory damages for churning and $300,000 in punitive damages: "In Florida, it is within the jury's discretion whether or not to award punitive damages and to determine the amount which should be awarded." (Arceneau v. Merrill Lynch, 767 F.2d 1498 (11th Cir. 1985).

The underlying currents in several states have begun to shift, though. Florida, for example, passed legislation in 1987 which establishes a rebuttable presumption in civil actions based upon negligence or misconduct in commercial transactions that punitive damage awards in excess of a ratio of 3:1 to compensatory damages are excessive. Moreover, 60% of any punitive damage award is payable to the State's General Revenue Fund. FLA. STATS. ANN. §767.73 (West Supp. 1988).

Colorado, long a jurisdiction feared by defendants for its awesome punitive damage awards (See, e.g., Malandris v. Merrill Lynch, 703 F.2d 1152 (10th Cir.) (en banc), cert. denied, 464 U.S. 824 (1983) ($3 million in punitives —cut to $1 million on appeal—compared to

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AAA List Selection *cont'd from page 2*

Conclusion

The AAA's Securities Arbitration Rules were published on September 1, 1987. In the relatively short time that has elapsed, over 600 cases have been filed under these rules. The positive user response indicates that AAA securities arbitration is perceived to be fair and impartial, a perception which is based in part on the neutral quality of the AAA panel.

Footnotes

1. American Arbitration Association, Securities Arbitration Rules, Sec. 13 (Jan. 1, 1989) [hereinafter "SAR"].

This article describes the procedures used where the claim of any party exceeds $25,000. Where the disclosed claims of all parties are less than $25,000, exclusive of interest and arbitration costs, disputes are administered under special expedited procedures. SAR Sec. 9. Under the expedited procedures, notices are provided by telephone, and relatively short time periods (generally seven days) are provided for various administrative items.

Cases are heard by one arbitrator, not affiliated with the securities industry, selected from a list of five names and biographical sketches provided to the parties. Hearings are generally concluded in one day and awards are due within fourteen days after completion of the hearings (awards are due within thirty days under the regular procedures). SAR Secs. 57, 41. The rules also presume that oral hearings are waived where the claims of both parties are less than $5,000, unless a party objects to this procedure. SAR Sec. 37.

2. SAR Sec. 4.

3. SAR Sec. 17. But see NYSE Rule 607 (3 to 5 arbitrators appointed by NYSE Director of Arbitration; 5 arbitrators if claim exceeds $500,000).

4. SAR Sec. 13. See NYSE Rule 607 (majority of arbitrators "not from the securities industry").

5. Definition drawn from N. Brown, G. Shell, and W. Tyson, "Arbitration of Customer-Broker Disputes Arising Under the Federal Securities Laws and RICO," 15:3 SECURITIES REGULATION L. J. 35 (1987).

6. SAR Sec. 19. See NYSE Rule 610 (Arbitrators to disclose "any circumstance which might preclude such arbitrator from rendering an objective and impartial determination").

7. Id.

8. SAR Sec. 13.

Punitive Damages *continued from page 4*

$30,000 in trading losses), recently adopted legislation generally limiting punitive damage awards to the amount of compensatory damages in actions involving injury to individuals or property. Moreover, evidence of the financial condition of the defendant is specifically rejected as a relevant factor in determining punitive damages. COLO. REV. STAT. §13-21-102 (1987).

Other examples: Virginia and Alabama have imposed ceilings on punitive damage awards in most civil actions (VA. CODE ANN. §8.01-38.1 (1988 Supp.) — $350,000; ALA. CODE §6-11-21 (1988 Supp.) — $250,000, where intentional wrongful conduct, actual malice, or defamation are not involved). Montana has bifurcated jury liability and damage proceedings and sets forth eight factors upon which to review punitive damage awards. MONT. CODE ANN. §27-1-221 (1987). Kansas requires courts to consider seven factors in awarding punitive damages and establishes some limitations on the size of the awards. KAN. STAT. ANN. §60-3701 (1987 Supp.).

Supreme Court Review

The maelstrom enveloping punitive damages is centering now over Washington, D.C., where the United States Supreme Court has granted certiorari in a commercial anti-trust case, Browning-Ferris Industries of Vermont, Inc. v. Kelco Disposal, Inc., Dkt. No. 88-556, 57 U.S.L.W. 3390 (12/6/88). The Court will review the decision of the Second Circuit (845 F.2d 404) that a jury verdict to Kelco of $6 million in punitive damages for interference with contractual relations under Vermont law and $51,000 in compensatory damages is not an "excessive fine" under the Eighth Amendment to the Constitution. The case is one of first impression for the Court, as it has not previously decided whether the Excessive Fines clause applies to the states or whether it applies to civil fines, such as punitive damages.

The list of amici curiae in the Kelco case is mind-boggling, in its length and in its roster of major U.S. corporations and representative organizations. Three major brokerage firms have submitted a joint brief in support of Browning-Ferris' petition. Counsel of record on the brief is Louis R. Cohen, Wilmer, Cutler & Pickering, Washington, D.C. Of Counsel are George A. Schieren, First VP & Assistant General Counsel, Merrill Lynch, Loren Schechter, General Counsel, Prudential-Bache, and Robert Dinerstein, General Counsel, Shearson Lehman Hutton.

Penalty vs. Offense

The brief's arguments are, in summary: "(1) Punitive damages are 'fines' within the meaning of the Excessive Fines Clause.... Punitive damages are 'excessive' when they are not proportionate to the misconduct proved in the case at bar.... The laws of Vermont and other states do not effectively limit punitive awards to amounts proportionate to the wrong proved. To the contrary, state law commonly requires, as it did here, that the jury be told that it has virtually unlimited discretion to impose what it considers an appropriate penalty.... (2) The Court's ruling in this case can encourage state legislatures to adopt appropriately detailed standards for making such awards. Standard-setting legislation would reduce the arbitrariness of the awards and would lead to more meaningful and less frequent appellate review."

Without such standards, argue the amici, consideration of punitive damages tends to focus on net worth in cases involving substantial corporate defendants. Such "open permission to take into account 'financial standing,' together with the typical plaintiff's argument that a substantial award is needed to 'send a message' to a large and insensitve corporation, lead repeatedly — as here — to disproportionate, excessive awards."

While it is admittedly speculative to guess when the storm will dissipate and where we will land, two things seem to flow from a result that limits punitive damage awards. First, there will be a greater level of comfort among all concerned, including the arbitrators, in permitting punitive damages in arbitration, if limits exist and the standards for when they apply are better-defined. Secondly, a relative distinction that some see between arbitration and litigation will narrow, as windfall awards on small losses are moderated.

(Editor's note: Our thanks to W. Reece Bader, Orrick Herrington & Sutcliffe and Michael J. Lawson, Steefel, Leavitt & Weiss, San Francisco, and to Ronald J. Greene, Wilmer Cutler & Pickering, Washington, D.C. for much of the information contained in this article.)

In Brief

CFTC Rule 180.3(b)(4): As SAC indicated in a special notice to subscribers in January, CFTC adopted its rule proposal concerning the mandatory inclusion of the National Futures Association as a qualified forum on lists provided to customers who have signed a pre-dispute arbitration agreement with registrants other than a floor broker and who have notified the registrant, or been notified by the registrant, of an intent to submit a claim to arbitration. The amended Rule became effective on February 16, 1989 (54 Fed. Reg. 1682, 1/17/89).

SRO Rule Filings: SAC also notified subscribers in the January special notice of a comprehensive rule filing by the **New York Stock Exchange** of proposed amendments to its arbitration rules (54 Fed. Reg. 3883, 1/26/89). A number of subscribers took advantage of our offer to provide copies of the release and/or the text of the proposed rules. The comment period ended February 16, 1989.

The **Municipal Securities Rulemaking Board** and the **American Stock Exchange** rule filings were also noticed in the Federal Register at about the same time (MSRB: 54 Fed. Reg. 3705 (1/25/89); ASE: 54 Fed. Reg. 3878 (1/26/89)). The SEC's request for comments on the ASE rule proposals was similar to that in the NYSE-related release, with one striking exception. In the NYSE-related release, the SEC referred to an express power (in NYSE Rule 619) to order depositions, which we cannot find; in the ASE-related release, the SEC stated the power was only implicit and requested comment on whether it should be made express.

In the MSRB-related release, the request for comment section specifically anticipates some minor changes to the initial filing and requests specific comment on a narrower "work effort" test for public arbitrators, one which, among other things, relates only to "municipal securities activities."

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Seminar Highlights: "Securities Arbitration Update"

Coming as it did at the start of a new year in arbitration, in the cusp between the completion of the arbitration rules package and the implementation of the new system, this "Securities Arbitration Update," sponsored by Prentice-Hall Law and Business, was marked by a distinctly practice-oriented emphasis. The Seminar took place on January 30, 1989 at the Westbury Hotel, NYC.

Now that the intellectual dialogue about the shape of SRO arbitration has crystallized in a new structure for arbitration, the focus has begun to shift to the pragmatic concerns of strategy and techniques for dealing with the new environment. NYSE Director of Arbitration Edward W. Morris, Jr., one of the seminar panelists, emphasized the shift by labeling 1989 as "the Year of the Practitioner." 1988, he said, was a year in which the "theoreticians" did their work. With much of the rule-making task done, the focus will be on the changes in arbitration practice the new rules will work.

Co-Chairmen of the seminar's faculty were **Mark D. Fitterman**, Associate Director, SEC Division of Market Regulation, and **Theodore A. Krebsbach**, SVP and head of broker-dealer litigation, Shearson Lehman Hutton Inc. Panel speakers were **Anthony W. Djinis**, Pickard & Djinis, Wash. D.C., **Theodore G. Eppenstein**, Eppenstein & Eppenstein, NYC, **Philip J. Hoblin, Jr.**, Executive VP, Shearson Lehman Hutton Inc., , Professor **Constantine N. Katsoris**, Fordham Law School, **Robert Love**, SEC Division of Market Regulation and member of the SEC Arbitration Oversight team, **Philip M. Mandel**, VP & Senior Counsel, Merrill Lynch, **Deborah Masucci**, Director of Arbitration, NASD, **Edward W. Morris, Jr.**, Director of Arbitration, NYSE, **A. Edward Moulin**, Director of State Governmental Affairs, Dean Witter Reynolds Inc., and **Tower C. Snow, Jr.**, Orrick, Herrington & Sutcliffe, NYC.

Given the wide range of subjects discussed, informal exchanges between the panelists during presentations, and the random occurrence of tactical nuggets offered by this experienced group, we have organized our summary of the seminar's highlights by subject, rather than speaker.

Litigation vs. Arbitration

Mr. Snow and Mr. Djinis were the primary speakers on this topic. Mr. Djinis stated that the most significant disadvantage to arbitration, in his view, is the lack of formal discovery and motion practice, primarily because these elements in litigation are conducive to settlement talks. That the new discovery procedures in SRO arbitration provide for greater prehearing involvement of the staff and arbitrators as intermediaries should weigh in favor of more frequent settlements.

Mr. Snow presented a checklist of twelve factors that distinguish litigation from arbitration and should be considered in deciding where a particular dispute is best heard. These are, in brief: Expense; Speed; Industry expertise (reliance on emotional pleas, need for expert witness, etc.); Discovery; Settlement prospects; Precedent; Publicity; Business relationship; Rules of evidence (reliance on hearsay; need to exclude, etc.); Damage claims; Finality; Enforcement of award or judgment.

Speaking to the element of expense, Mr. Morris cited the NYSE's survey (1 SAC 7, "Special Supplement") as indicating that legal costs in litigation are significantly higher than in arbitration. Public statements by Mr. Eppenstein and other claimants' attorneys who testified before Congress during the 1988 arbitration hearings support the proposition that a claim should exceed $100-200,000 to be worth pursuing in litigation.

Pre-Dispute Arbitration Agreements

Mr. Eppenstein cautioned that claimants' attorneys should review the language in all customer agreements that a client may have signed, since the language in each agreement can be measurably different. For example, where a client has signed one agreement with broad, unqualified language and another agreement with a Rule 15c2-2 disclaimer, it may be possible to utilize the latter to preclude arbitration of federal securities disputes.

Claimants' attorneys should note, said Mr. Eppenstein, that Rule 15c2-2 required broker-dealers to send notices to existing customers that arguably modified existing agreements with broad, unqualified language to exclude federal securities claims from the scope of the clause (See 1 SAC 6(6)). Mr. Love, who participated as staff in the Rule's promulgation, noted that the Commission developed express disclaimer language for the notice to existing customers, due to a strong view that existing agreements required clarification.

Because some SRO's have or are considering jurisdictional limits on the cases they will accept, Mr. Hoblin suggested that broker-dealers revising their pre-dispute clauses list, as an available forum, the SRO where the disputed trading took place. This will guard against the possibility that the forums listed in the clause all decline jurisdiction over the dispute.

SICA and SIA have urged broker-dealers to offer the AAA in their pre-dispute clauses. Mr. Morris recommended that those broker-dealers who favor the SRO method of "agency selection" of arbitrators might still include AAA, but specify the method by which the arbitrators will be selected. This is permitted under Sections 1,13, and 17 of the AAA's Securities Arbitration Rules.

Mr. Fitterman stated that the staff was generally "satisfied" with SICA and SRO responses to its recommendations for procedural changes to the arbitration rules. The issue of "free choice" versus SICA's "disclosure" approach to the use of pre-dispute clauses is still an open one. He would not hazard a guess as to the Commission's ultimate view on this question.

Mr. Moulin predicted that the Markey House Subcommittee on Tele-

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Seminar Highlights *continued from page 6*

communications and Finance will propose legislation on "free choice" again this year, perhaps in a different form, though. It may, for instance, appear in a "bill of rights" for investors in the securities markets.

Choosing a Forum

Ms. Masucci and Mr. Morris presented statistics for their respective forums. NASD in 1988 received 3,998 new cases versus 2,886 cases (38% increase) in 1987. NYSE tallied 1629 new cases filed in 1988 versus 1,050 (55% increase) in 1987. NASD has hearing panels in 52 cities. NYSE has established panels in 33 cities, but will select panels in other cities, if warranted, for a particular dispute. Average turnaround time for NASD in 1988 was 12.1 months versus 12.9 months in 1987. At NYSE, 1988 turnaround time was 8.2 months versus 9.0 months in 1987. In New York City, time from filing to hearing is generally 2-4 months and runs 6-7 months elsewhere, said Mr. Morris.

NASD has been scheduling cases for hearing as soon as pleadings are complete. Cases coming ready currently are being scheduled for hearing dates in June or July 1989. To discourage unnecessary adjournment requests, NASD staff now refer the parties to the arbitration panel for approval. The Arbitration Department is also looking into mediation as a possible device to foster more settlements and lower its hearing caseload.

The expense factor for NASD, in subsidizing this huge arbitration program (Mr. Morris, prior to Ms. Masucci's appearance, had referred to an NASD budget study which showed the arbitration program to be the largest cost center in the NASD's budget), is of looming concern. Ms. Masucci stated that the Association is "looking very carefully" at the types of claims presented for NASD arbitration. She "suspects" that NASD may soon begin declining arbitral jurisdiction over commodity futures disputes.

Mr. Eppenstein offered three reasons for favoring AAA as an arbitration forum for investor-clients. Although not subject to SEC oversight, AAA is, nevertheless, "totally independent" of the industry. The "strike right" accorded parties in the selection of arbitrators offers a degree of party participation not present in SRO arbitration. Finally, the "quality" of arbitrators is better, in his view. Former judges are often among the candidates. Industry expertise is not a plus, since the investor is better served with a panel that is more aligned with an investor's perspective.

Pleadings

Mr. Eppenstein stressed the necessity to gather account agreements, new account documents, and correspondence before filing. This will tell you if you must arbitrate and will avoid surprises later. If you are certain of your facts, it is preferable to provide a narrative, detailing the events leading to your claim. NASD or the state securities bureaus can provide information on the broker's background and disciplinary history. This data can either be presented at hearing on the issue of supervision or attached to the Statement of Claim.

Mr. Djinis cautioned that credibility is a critical factor in arbitration. Claimants should not overstate their claim. There is no need to fear dismissal of the claim as insufficiently pled. On the other hand, the Complaint should be as detailed and complete as practicable. Damage claims should be based upon "hard figures" and claimants should be prepared to prove them at hearing. The Statement of Answer in arbitration, according to Mr. Snow, also requires careful review of documentation and witness interviews to allow a detailed response to the Claim. Similarly, respondents should avail themselves of the leeway granted to attach documentation to the Answer.

Mr. Morris emphasized that the 6-year time limitation in the SRO arbitration rules is not a "statute of limitations," but rather a jurisdictional limitation on stale disputes. Shorter statutes of limitations may be asserted, either before the arbitrators or in an Article 75 proceeding (within 20 days of the demand) under New York law.

Discovery

The investor is generally at a disadvantage in discovery, Mr. Eppenstein observed, since the broker-dealer controls most of the documentation needed at hearing. One advantage to a bifurcated case, where federal securities claims are maintained in litigation and state or common claims are arbitrated, can be that discovery in the litigation will produce information useful in the arbitration. Mr. Eppenstein suggested that one might delay filing the arbitration claim until discovery in the litigation proceeds to an appropriate point.

Mr. Hoblin countered that this tactic could be blocked by the broker-dealer filing its Answer and the investor's Complaint with the appropriate arbitration forum, citing the order compelling the state and common law claims to arbitration. Either party is permitted to submit a dispute to arbitration, not just the complaining party.

In discussing the new discovery procedures, Mr. Mandel stated that they may help to encourage settlements, but he believes the greater incidence of settlements in litigation relates to the cost involved in litigating. The primary purpose of these new rules is to establish "more formalized procedures to have predetermination of production of documents in dispute." Bad faith objections or stubborn refusals to produce documentation risk leaving the arbitrators with the impression that the offending party has something to hide. These new procedures will expose such tactics sooner.

Mr. Snow added that he "welcomes the hardball approach" from adversaries, since it is easy to make them look bad. Counsel should decide early on what documents will be provided and seek to work out differences. When refusing access to documentation, one should put the reasons in writing and provide a copy to forum counsel. Then, in the event arbitrator intervention is required, a complete record is available for review.

Arbitrator Selection

Prof. Katsoris suggested that attorneys should assist in avoiding delayed recognition of arbitrator conflicts by disclosing their witnesses before the arbitration selection process and by checking arbitrator names with witnesses, as well

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Seminar Highlights *continued from page 7*

as the parties.

In response to a question from Mr. Krebsbach, Mr. Morris stated that he was not fearful of court challenges to arbitral awards, based upon a purported misapplication of criteria for the classification of industry vs. public arbitrators. That an attorney might, for example, mistakenly serve as a public arbitrator, though he dedicates slightly more than 20% of his work effort to industry clients should not permit vacatur. No "fraud" is involved, nor is "evident partiality" established. The classifications are arbitrary in character and mechanical in nature. All SRO arbitrators, whether public or industry, have a duty to be neutral.

Hearing Presentation

Spelling out the environmental factors which distinguish arbitration from litigation, Mr. Snow described arbitration as an "equitable" forum, where it is easier to recover, but harder to land a windfall award. Arbitration is "common sense," "sophisticated," and "dispassionate" in nature and one's presentation should consider these factors. The focus will be on the credibility of the evidence. Witnesses should generally testify in the narrative, presenting their story chronologically and unemotionally.

Similarly, defensive techniques must focus upon undermining the credibility of the opposition's witnesses, rather than utilizing the rules of evidence to exclude documents or testimony. Of great importance are the questions asked by arbitrators, as they can provide a "roadmap" to the panel's thinking. Witnesses should be prepared to answer such questions fully and directly. If they do not, counsel should cover the point in closing argument. Closing statements should stress fairness, be unemotional and emphasize points relating to damages.

Mr. Hoblin underscored the importance of presenting well-prepared damage analyses. Calculate the interest figures; do not expect the arbitrators to do that. Mr. Snow added that he often presents step-down damage calculations, presenting alternative damage figures for each likely factual scenario.

Awards

Several of the panelists emphasized the extreme circumstances under which arbitrators might award punitive damages, but felt they could. Another disputed the proposition that arbitrators are empowered to grant them. Mr. Morris indicated that NYSE staff generally advise arbitrators that they are authorized to award punitive damages, if appropriate. NASD takes a more neutral stance, advising the arbitrators to request argument from the parties on the point.

Failure to honor an arbitration award may be grounds for disciplinary action under SRO rules. Nevertheless, in at least one instance, a brokerage firm apparently launched court challenges to awards against it in order to defer payment and stave off insolvency. The Municipal Securities Rulemaking Board has proposed rules for comment which would require amounts awarded to be escrowed until the debt is extinguished. SICA will consider a similar proposal for all participating SRO's.

Mr. Love discussed the new award format under the proposed rules, indicating that most of the information in the expanded format will be publicly available. Ms. Masucci explained the NASD's view that arbitrators names should not be disclosed in the public award, due to the "unnecessary pressures" that it would place on arbitrators. Parties will still be able to learn the past voting record of selected arbitrators through inquiry to the NASD staff. NYSE will disclose the arbitrator's names in the public award.

Both Ms. Masucci and Mr. Morris agreed, however, that arbitrators should view confidentiality as a continuing obligation and should not discuss the case with the press or any third parties. Mr. Morris added that the cloak of arbitral immunity may not be available to an arbitrator after the award has been issued and made public.

State Actions

Mr. Moulin discussed the efforts by NASAA and some individual states to effect changes in the arbitration process, stating that NASAA had brought focus to the "grass root" concerns among the public about the fairness of arbitration. Many wonder why, if arbitration is so good, it must be enforced through a system of mandatory pre-dispute agreements. NASAA has advocated a prohibition against mandatory pre-dispute agreements.

Mr. Moulin's firm, Dean Witter Reynolds, does not require customers to sign pre-dispute agreements for cash accounts, which comprise 86% of the firm's total account base. Some smaller broker-dealers, in contrast, cannot risk the jeopardy of costly litigation expense and sky-high damages that can result from a single, large case. In the lending area, he continued, litigation costs are an expense which can affect the ability of securities firms to compete with the banking community.

Mr. Moulin introduced Craig Goettsch, Iowa Superintendent of Securities and Chairman of NASAA's Ad Hoc Arbitration Committee, from the audience. Mr. Goettsch spoke briefly on NASAA's model rule prohibiting mandatory pre-dispute clauses. He offered his "personal view" that the First Circuit's decision in SIA v. Connolly (2 SAC 1(9)) will have a "critical effect" upon whether NASAA continues its current push for state regulation of the agreements to arbitrate.

In Brief: *cont'd from page 5*

MSRB Escrow: The Municipal Securities Rulemaking Board is considering a proposed amendment to its Rule G-35, "Arbitration," which would require brokers, dealers, and municipal securities dealers which receive a monetary award rendered against them to pay the award within 10 business days or deposit the award in an interest-bearing escrow account with a bank, pending the disposition of any appeal of the award. The purpose of the proposed rule is to "promote the prompt payment of arbitration awards while permitting dealers to pursue legitimate appeals of arbitration awards." (MSRB Reports: December 1988).

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Forum Statistics and Updates

NYSE: Products in Dispute

New York Stock Exchange Arbitration Director Edward W. Morris, Jr. recently conducted an informal survey of 250 customer cases presently on the NYSE docket, in order to determine the primary "product" or investment instrument involved in each case. The breakdown resulted as follows:

Product	Number of Cases	% of Total
Equities	125	50.0%
Options	60	24.0
Bonds	16	6.4
Commodities	9	3.6
Firm Product	5	2.0
Other	35	14.0

"Firm Product" includes such instruments as money market funds, cash management accounts, and "firm name" funds. The "Other" column includes miscellaneous items, such as limited partnerships, mutual funds, and IRA's. Cases which involve stocks, as well as other products, were listed as "Equities." Of the 125 equity cases, 34 (27.2%) did not involve a NYSE-listed stock. One of the 34 concerned an American Stock Exchange stock and the other 33 concerned over-the-counter stocks only.

AAA Update (1988)

The American Arbitration Association reports that 495 securities cases were filed in 1988 with its national network of regional offices. This compares with 187 securities cases filed in 1987, a 265% increase. AAA administrative staff tell us that these cases include securities-related disputes, whether arbitrated under the AAA's Commercial Arbitration Rules or the new (9/87) Securities Arbitration Rules. The figures do not, however, include commodities-related disputes, although such disputes are eligible to utilize the new SAR procedures.

The incidence of case filings was fairly evenly distributed among the four quarters of the year, but the highest quarterly results were in the final quarter, when 135 cases were filed. Of some 34 regional offices nationwide, the most securities cases by far were filed in AAA's Miami office (105). New York finished second (73), followed by Los Angeles (47), Dallas (37), Philadelphia (23), Boston (22), San Francisco (20), Detroit (19), Chicago (15), Minneapolis (15), San Diego (14), and Washington, D.C. (13). Total claims filed in 1988 aggregated $266.8 million.

AAA amended its Securities Arbitration Rules, effective January 1, 1989, primarily in an effort to harmonize SAR with the provisions of the Commercial and Construction Arbitration Rules. The primary differences lie in the time frames, panel composition, and some adjustments (upward) to the fee schedule. Copies of the new rules brochure are available from AAA, 140 W. 51st St., NYC 10020-1203.

NASD: Products in Dispute

NASD Arbitration recently conducted an internal survey of some 4,000 cases in its inventory of disputes awaiting arbitration. SAC has the results of that survey, but NASD Director of Arbitration Deborah Masucci admonishes that, since the survey was designed to obtain only a rough view of NASD's case breakdown, the figures should be regarded with some degree of tolerance. Below is a chart of the primary results:

Stocks	38%
Options	24%
Other Products	20%
Industry Cases	18%

Assuming that the 82% of non-industry cases are virtually all disputes between broker-dealers and their customers, the product breakdown reflects that stocks are involved in more than 46% of the customer disputes and options in more than 29%. Stock disputes were labeled in the survey as either "NASDAQ" or "Big Board" disputes. Based upon that distinction, 68% of the stock disputes concerned NASDAQ stocks and 32% concerned Big Board stocks.

Other products most often involved in customer disputes were limited partnerships (approx. 5%), mutual funds (approx. 5%), government securities (approx. 4%), corporate bonds (approx. 2%), commodities (approx. 1%), and warrants (approx. 1%).

"Industry cases" are categorized in the survey as either commission disputes (25%), employment disputes (64%), or trading disputes (11%). The stocks involved in the "trading disputes" category are classified as either NASDAQ (56%) or Big Board (44%).

NFA Update

During the last calendar quarter of 1988, NFA's second fiscal quarter, the National Futures Association received 101 demands for arbitration. Ninety of the claims were filed by customers, 3 were filed by Members or Associates against customers, 3 were filed by customers who are also Members or Associates, and 5 were straight industry disputes. During the same time period, 66 cases were closed, 5 for lack of jurisdiction, 36 via award, and 25 cases were settled. Twenty-six hearings were held during the quarter.

While the number of new filings represents a slight downturn from the 118 cases filed in the first fiscal quarter, the first-half total, on an annualized basis, is still running well ahead of fiscal 1988's 340 cases. The NFA's major revision of its arbitration rules (1 SAC 8(2)), formalizing discovery procedures and deleting the prohibition against punitive damage requests, is currently on file with the CFTC and awaiting approval (Surprisingly, CFTC is evidently not required to publish self-regulatory rule proposals in the Federal Register or to seek public comment). NFA has also submitted to the CFTC proposed rules governing the arbitration of disputes between U.S. customers and non-Member foreign firms.

In Brief *continued from page 8*

Cert. Filed: Kathryn A. Heily, a stockbroker, has filed a petition for certiorari (Dkt. No. 88-922, 11/30/88; 57 U.S.L.W. 3423 (12/20/88)) with the U.S. Supreme Court, seeking review of a California Court of Appeal decision (Heily v. Merrill Lynch, Pierce, Fenner & Smith, Inc.,1 SAC 4(11), 202 Cal.App.3d 255 (1Dist., 6/20/88)), which compelled arbitration of her wrongful discharge claim. Ms. Heilly questions whether a state's judicially created rule, permitting courts to consider the presumptive bias of an arbitration forum prior to enforcing the arbitration agreement, should have been disregarded by the Court of Appeal as an arbitration-specific rule and, therefore, inapplicable to the issue of unconscionability of an agreement subject to the Federal Arbitration Act. The Court of Appeal rejected Heily's challenge to NYSE arbitration as unconscionable, despite supporting affidavits from five NYSE and NASD arbitrators, including Ms. Heily, who stated their opinions that NASD and NYSE arbitrators are likely to favor brokerage firms in disputes involving employees. Merrill Lynch has opposed the petition.

State Update: State actions on rules prohibiting the use of mandatory predispute arbitration agreements appear to be on hold, pending the First Circuit's review of the decision in SIA v. Connolly (2 SAC 1(9). In January, Montana proceeded with its revisions to the Montana Securities Act (2 SAC 1(9)) without including its proposed rules regarding arbitration agreements. Similarly, we understand that the sponsors of the New Jersey (2 SAC 1(9)) and Maryland (S.B. 72) legislative bills are not proceeding at this time. In the Connolly appeal, NASAA, failing to obtain consent from the respondent-appellees to file an amicus brief, simultaneously filed its brief and sought filing permission from the First Circuit on February 14, 1989.

Recent Articles and Cases

As a regular feature, SAC lists articles and cases of interest in the field of arbitration law. If you know of any we have missed, please let us know.

Articles

Securities Arbitration: Changes in Practice and Procedure. by Justin P. Klein, INSIGHTS, The Corporate & Securities Law Advisor, Vol. 3, No. 1 (January 1989).

The author provides a summary of the changes to arbitration rules proposed by the Securities Industry Conference on Arbitration, along with commentary based upon his special perspective as a former SEC staffer overseeing arbitration and as a current, public member of SICA. Besides explaining the recommendations SICA ultimately made on such aspects of arbitration as the classification of arbitrators, arbitrator evaluation, arbitrator disclosure of conflicts, publication of awards, discovery, referrals for disciplinary action, large and complex case, and pre-dispute arbitration agreements, the article juxtaposes with those recommendations the Commission's position as stated in its September 10, 1987 letter to SICA, and the ultimate rule proposals (to the extent they differ) of the major SRO's.

In addition, it deals with some items on SICA' agenda which have not received frequent airing elsewhere. For instance, the Chicago Board Options Exchange has initiated a pilot arbitrator evaluation system, at SICA's behest, to contact parties following hearings to seek their assessments of the arbitrators. As yet, Mr. Klein states, "the results of this study have been scant," but SICA intends to continue encouraging the development of SRO programs to assess arbitrator performance. Similarly, on the issue of referrals from arbitration for disciplinary action, SICA has attempted to achieve a balance between the SRO's roles as securities regulators and as providers of arbitral services. Procedures pamphlets will advise investors involved in disputes that they may contact the enforcement arm of an SRO to report purported violations of the securities laws. Arbitrators will be informed in the arbitrator manual of their right to refer matters arising from disputes on which they sit for regulatory investigation and action.

One theme which runs throughout the article and which emphasizes the sensitivity that SICA has attempted to place on the need to preserve arbitration's basic characteristics in making any adjustments to the process, is that "[t]here is some concern on the part of SICA and the SRO's that these changes will make SRO arbitration much like litigation, thereby reducing its efficiency and economy." He concludes, though, that [o]n balance,...these changes should eradicate any perception of bias or unfairness on the part of public investors in having their disputes resolved in a forum run by a broker-dealer membership organization."

Cases

Abel v. Prudential-Bache Securities, Inc., Case No. CIV-87-2363-T (W.D. Okla, 1/5/89). This case illustrates the difficulties that can arise in AAA arbitration when the broker challenges his obligation to arbitrate (see discussion of Flink v. Carlson at 1 SAC 6(11) and 1 SAC 9(5)). Plaintiff, who had been earlier ordered to arbitrate by this Court, selected AAA arbitration in accordance with the Customer Agreement and, in January 1988, filed against Pru-Bache, branch manager Colonnese, and broker Allen. Pru-Bache sought to cross-claim in the arbitration against Allen for indemnification, but Allen resisted. While agreeing to arbitrate Abel's claim at AAA, Allen petitioned in court to stay or exclude the cross-claim on the ground that AAA did not have jurisdiction to arbitrate that dispute. Pru-Bache conceded that Allen was not contractually bound to defend the cross-claim before the AAA and moved to compel arbitration of all claims before the NYSE.

Allen was contractually bound to arbitrate before NYSE, said the Court, but Pru-Bache's argument that a separate Options Agreement requires Abel to arbitrate her disputes before the NYSE has

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SAC BULLETIN BOARD

From the Editor: This space is reserved for SAC's Bulletin Board for subscribers. It is an open space for subscribers, free of charge, to use as you find fitting. The only rules right now are that the posted messages must be relevant to financial services arbitration and have a constructive purpose. I hope that readers will want to use the Bulletin Board as a place to voice opinions, comment on rule proposals, and transmit their ideas to others in the financial services arbitration community. There are also the practical needs of lawyers in arbitral conflict for information, experts, etc., which can be served. Messages can be posted either in your name or, if you prefer, anonymously. If your message anticipates replies, they can be listed for return to your address or to SAC's P.O. Box. The possibilities are open — they just need to be discovered.

Databases

I have been utilizing Compuserve as a database to historically track stock prices in order to aid in computation of damages, and to determine whether the strategies employed by brokers are correct. However, with regard to option premiums, Compuserve only keeps historical prices for approximately three months. I am interested in any information concerning a cost-effective database that can be accessed through an office PC, that carries historical price information concerning option premiums and which carries that information for several years.

In addition, research department reports from many major brokerage firms can be accessed through Lexis. However, all firms are not represented, only some. I am interested in obtaining information concerning other databases that may access firm research reports. Please contact Joel H. Bernstein, Kantor, Bernstein & Kantor, at (212) 227-3355.

Expert Services Survey

Many thanks to those who have completed and returned their Expert Services Survey (See 2 SAC 1 "Bulletin Board")! We appreciate your time and attention to considering the issues addressed. Due to delays in mail delivery reported by several respondents, we have extended the survey return date to March 17, 1989. Please complete your booklet and provide your opinions. We look forward to including your responses in the overall report! Should you require additional booklets please call (800) 225-4096 or FAX (206) 869-0357 your request to NKV Corp. We will be happy to forward copies by return mail.

Norman E. Kjono

Articles & Case Law *continued from page 10*

been waived. "The Court would prefer that all the claims be presented to the same tribunal, but has determined that the plaintiff should not be prejudiced by the obviously dilatory action of defendant Allen [in waiting seven months after the filing of the cross-claim before raising the jurisdictional issue].... [T]he court concludes that Prudential-Bache and Colonnese have waived any objection they might have to proceeding before the AAA by their reliance on the Customer Agreement as authority for their original motion to stay and by their failure to raise the jurisdictional issue until one month prior to the hearing date."

Cullen v. Paine, Webber Jackson & Curtis, Inc., No. 88-8325 (11th Cir., 1/17/89). This case represents the third set of court decisions regarding claims between appellant, a former Atlanta-based broker, and PaineWebber. The first decision compelled to arbitration the broker's claims for tortious conduct and a request for declaratory relief from an allegedly invalid promissory note (587 F. Supp. 1520 (N.D. Ga. 1984)). After Paine Webber was awarded $216,932.83 in NYSE arbitration on June 24, 1987, a New York federal court found the broker's attempt to renew his claims in litigation barred by the doctrine of res judicata (1 SAC 7 (10)). Then, when Paine Webber sought to confirm its arbitral award, via a motion filed November 20, 1987, plaintiff filed "affirmative defenses" in opposition and cross-moved to vacate.

The Court affirms the district court's findings that the motion to vacate was untimely filed. It rejects appellant's arguments that, despite the 3-month limitation on motions to arbitrate in Section 12 of the FAA, its "affirmative defenses" to confirmation should be considered. The Court holds that the three-month limitation applies both to motions to vacate and to "affirmative defenses raised in opposition to section 9 motions to confirm."

Appellant argued as well that his motion to vacate was not time-barred, based on a "due diligence" defense to the time limitation. The Court is unpersuaded. That appellant conducted settlement negotiations in which he contested the validity of the Award "falls considerably short of due diligence." The Court declines to decide whether such a defense would create an exception to the three-month limitations period, since appellant has not established any basis for his application.

Donaldson, Lufkin & Jenrette Futures, Inc. v. Barr, 530 N.E.2d 439 (Ill., 10/20/88). Again, the limited arbitral jurisdiction rules of the commodity exchanges, here the CBOT, raise unnecessary barriers to the speedy resolution of industry disputes. Barr was a senior officer of DFI in charge of the Chicago office and floor operations on five commodity exchanges. When he ceased his employment, he sought arbitration before the Chicago Board of Trade of more than $600,000 in claims regarding severance pay, a bonus based upon operating income of the Chicago office, a recruitment bonus, and unreimbursed expenses.

DFI filed a declaratory judgment action in state court. DFI requested a stay of the CBOT arbitration on grounds that the disputes between DFI and Barr did not "arise[] out of the Exchange business of such parties," as CBOT Rule 600.00 requires. CBOT intervened in the action on Barr's behalf, arguing that the issue of whether the subject claims were arbitrable under CBOT Rules should be determined by the arbitrators, not by the courts. Interpreting the Illinois Uniform Arbitration Act, the Illinois Supreme Court rules that arbitrability is a question for judicial resolution when the dispute is clearly within or outside the scope of the agreement to arbitrate. Where it is unclear whether the dispute is covered by the agreement, the question of arbitrability will be left to the arbitrators.

Applying this doctrine to the facts, the Court finds that the severance pay and expense reimbursement claims "clearly arose out of [Barr's] contract of employment with DFI and clearly did not 'arise out of Exchange business....'" Those claims must be litigated. It is unclear, though, whether the bonus claims arose out of Exchange business at the CBOT, since business on five exchanges could be involved in the calculations. Thus, the arbitrability of these claims, in whole or in part, must be initially determined by CBOT arbitrators.

Forkin v. PaineWebber Inc., Fed. Sec. L. Rep. (CCH) ¶94,129 (C.D. Ill., 11/23/88). Herein lies a warning to defendants seeking the procedural benefits of motion practice, while asserting their right to arbitrate disputes. This Court compels arbitration of 1934 Act and assorted state claims, but not before dealing with a variety of defensive motions attacking Complaints in two related actions on numerous grounds, including that class action status should be refused, RICO claims are insufficiently pleaded, FRCP Secs. 9(b) and 12(b)(6) require dismissal, and that no private right of action exists under Section 15 of the 1934 Act. After a lengthy treatment of the merits of these motions, the Court agrees that arbitration of the remaining claims for four of the five plaintiffs is required. However, the Court also expresses its displeasure with defendants for challenging the merits of plaintiffs' claims before the Court and then requesting arbitration of those which were permitted to stand. "That is clearly PaineWebber's tack here, and if presented with the argument this Court

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INFORMATION REQUESTS: SAC aims to concentrate in one publication all significant news and views regarding securities/commodities arbitration. To provide subscribers with current, useful information from varying perspectives, the editor invites your comments/criticism and your assistance in bringing items of interest to the attention of our readers. Please submit letters/articles/case decisions/etc.
TO: Richard P. Ryder, Editor
Securities Arbitration Commentator
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may have been inclined to find waiver.... Plaintiffs did not raise the point, however, and so the Court cannot reach the waiver arguments."

Garfield v. Thomson McKinnon Securities, Inc., No. 88 C 3027 (N.D. Ill., 12/16/88). Court determines that broker-plaintiff is required to arbitrate her claims under the Age Discrimination in Employment Act, along with a pendent claim for breach of an oral employment agreement. Upon her employment in 1977, plaintiff signed a U-4 form for registration and a NYSE agreement, form AD-G-I, both of which contained broad arbitration clauses. That plaintiff was required to sign the application containing the arbitration clause in order to gain registration and pursue her profession does not invalidate it. As to plaintiff's claim that arbitration of ADEA claims is contrary to congressional intent, the burden of showing this intent is "on the party opposing arbitration" and plaintiff has provided no evidence "that Congress intended to preclude a waiver of judicial remedies for the statutory rights at issue...."

Distinguishing two Supreme Court rulings that claims under Title VII and the Fair Labor Standards Act should not be referred to arbitration, Alexander v. Gardner-Denver Co., 415 U.S. 36 (1974) and Barrentine v. Arkansas-Best Freight System, Inc., 450 U.S. 728 (1981), the Court notes that both cases "involved the issue of whether an individual's judicial remedy could be waived by a union when the union agreed to a collective bargaining agreement providing for arbitration. Neither, then, "provides ... insight into the question of whether Congress intended to prohibit the individual himself from waiving his right to a judicial remedy."

In fact, the legislative history of the ADEA "demonstrates a congressional intent in favor of informal methods of dispute resolution," in that ADEA claims must be first submitted to the EEOC before resorting to the courts. Finally, no "substantial legal expertise" is required to decide this case: "the arbitrator must determine whether, but for Ms. Garfield's age, Thomson McKinnon would have terminated her employment. We think that an arbitrator is capable of making such a determination...."

Gonick v. Drexel Burnham Lambert Inc., Fed. Sec. L. Rep. (CCH) ¶94,127 (N.D. Cal., 12/12/88). If you were wondering when a court might impose sanctions for frivolous opposition to a disputant's obligation to arbitrate, this case provides an answer. Mr. Gonick, an attorney, opened a joint account in 1977 with DBL and signed an account agreement containing a pre-dispute arbitration clause. When a dispute developed in 1987 he requested a copy of the Customers Agreement. He received in response a blank of DBL's then-current standard form agreement, which contained a Rule 15c2-2 disclaimer regarding the non-arbitrability of federal securities claims.

The Gonicks filed suit and DBL sought to compel arbitration. In response to DBL's motion to compel, plaintiffs asserted that the pre-dispute clause should not be enforced on grounds of unconscionability, lack of mutuality, lack of consideration, fraudulent concealment, estoppel, affirmative misrepresentations, and waiver. Plaintiffs argued that DBL's provision to them of the standard form with disclaimer in 1987 should estop DBL from asserting any right to arbitrate federal securities claims and that, having had "preferred customer" status at DBL, plaintiffs should be permitted to employ the DBL agreement in effect at the time they filed the lawsuit.

These innovative arguments and others elicited only criticism from the Court, which charged the plaintiffs with arguments unsupported by authority and defenses clearly in disregard of existing law. These factors, together with early efforts by defense counsel to persuade plaintiffs of their obligation to arbitrate, justified the imposition of Rule 11 sanctions in the amount of defendants' reasonable attorney fees and costs in pursuing the order to compel arbitration.

Jolley v. Paine Webber Jackson & Curtis, Inc., No. 88-3179 (5th Cir., 2/2/89). District court compelled all claims in this case to arbitration and refused plaintiffs' motion for §1292(b) certification. As an alternative basis for appeal, the Court rejected jurisdiction based upon 28 U.S.C. §1291(a), given the Supreme Court's decision in Gulfstream (1 SAC 5(1)). Nor was the order to stay pending arbitration appealable as a "collateral order," said the Court, repeating its finding in RPR v. Birenbaum (1 SAC 8(11)) that such orders were not "effectively unreviewable," since plaintiffs may obtain review on appeal from a final judgment after arbitration.

Admitting that its prior decisions on the question of whether such orders are "final" and therefore appealable under §1291 lacked consistency, the Court decides that "[t]he substance of the Supreme Court's decision in Gulfstream makes it clear that neither orders granting nor orders denying a stay pending arbitration are final under §1291." It matters not whether the petition is brought under Section 3 or 4 of the Arbitration Act, "[w]hen a district court order is entered as a single act in the process of an ongoing legal proceeding," it is not final. "Language to the contrary in prior decisions of this circuit has been overtaken by the Supreme Court's decison in Gulfstream." The one possible exception may be where "a district court enters an order in response to an independent proceeding to compel arbitration pursuant to §4 of the Federal Arbitration Act...." Otherwise, certification or a writ of mandamus are the only remaining avenues of appeal for orders granting or denying a stay pending arbitration. (The Court does not consider the new addition of Section 15 to the FAA (1 SAC 8(1)).

Newcome v. Esry, Fed. Sec. L. Rep. (CCH) ¶94,106 (4th Cir., 12/16/88). Appeal is taken from the district court's ruling, implying a private right of action under Section 17(a) of the 1933 Act and compelling both the 1933 Act and 1934 Act claims to arbitration. The Fourth

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Circuit determines that no private right of action does exist under Section 17(a), overruling prior precedent in the Circuit to the contrary, and dismisses that claim. The claims under Section 10(b) of the 1934 Act are compelled to arbitration, as ordered by the district court.

Newfield v. Shearson Lehman Bros., 699 F. Supp. 1124 (E.D. Pa., 11/23/88). Defendants' motion to compel arbitration is denied. Based upon plaintiff's assertions that "he was 'rushed' into signing a form that he did not have an opportunity to read, that he was told he was 'required' to do so to open an account, and that [the broker] induced him to sign without reading the form...," the Court finds that "[t]he very existence of an agreement to arbitrate is in issue, and the matter must be resolved before plaintiff's claims can be referred to an arbitrator."

Of interest as well in this case is the Court's refusal to apply retroactively the Third Circuit's holding in Data Access (1 SAC 2(4)), calling for a one year/three year federal securities limitation on Rule 10b-5 actions. Plaintiff filed his action one and one half years after discovery, four months before the Data Access decision, at a time when the operative limitations period was two years. "[B]ecause plaintiff filed suit well within the only limitations period of which he had cause to know at the time, I hold that the retrospective application of Data Access to his claim would be unfair, and that his action was timely brought."

Finally, the Court dismisses claims under Section 15 of the 1934 Act, RICO, and Section 4(b) of the Commodity Exchange Act in the face of valid challenges under FRCP 12(b)(6).

Prudential-Bache Securities v. U.S. Optical Frame Co., 534 So.2d 793 (Fla. App. 3Dist., 11/22/88). Appeals from both sides of lower court orders both denying and compelling arbitration of various fraud claims by three related accounts: a joint trading account for plaintiff-appellees Steven and Susan Lipawsky and corporate and pension plan accounts for their affiliated corporation. The Lipawskys had executed agreements with pre-dispute clauses for a separate (fourth) money market account in 1979 and for the trading account in 1982. The 1979 agreement was broad and unqualified, but the 1982 arbitration clause contained a Rule 15c2-2 disclaimer ("...except for any controversy with a public customer for which a remedy may exist pursuant to an express or implied right of action under the federal securities laws..."). Reversing the lower court order granting arbitration of claims under Section 12(2) of the 1933 Act, the Court states: "[a]ll of the transactions complained of occurred in the account covered by the 1982 agreement, the plain terms of which preserved the Lipawskys' right to a judicial forum. As a matter of contract law, the Lipawskys never agreed to arbitrate their federal securities law claims."

As to Pru-Bache's appeal of the order denying arbitration of claims by the corporate and pension plan accounts, the Court affirms, noting that no corporate resolutions permitting the accounts to be opened or binding the corporation or plan to arbitrate were ever obtained. It rejects the argument that the broad language of the agreement signed by Mr. Lipawsky in the personal account binds U.S. Optical: "[a]lthough Steven Lipawsky is the principal officer and shareholder of the corporation and trustee of the pension plan, there is nothing on the face of the joint account agreement or in the signatures to suggest that the agreement covered anything more than the Lipawsky's personal account."

Schuster v. Kidder Peabody & Co., Inc., 699 F. Supp. 271 (S.D. Fla., 6/27/88). All of plaintiffs' claims are compelled to arbitration, including a claim under Section 12(2) of the 1933 Act. "There is nothing to show that judicial resolution is more necessary when 1933 Act claims are asserted than when claims are brought under the 1934 Act." Plaintiffs' assertions that the customer agreements they signed were contracts of adhesion, lacking in mutuality of obligation, and therefore unconscionable, are subject to arbitral resolution. "When claims of fraud, unconscionability, lack of mutuality or contract of adhesion pertain to the contract as a whole, not to the arbitration clause alone, those issues should be resolved in arbitration."

Simon v. Smith Barney, Harris Upham & Co., Inc., No. CIV-88-1124-T (W.D. Okla., 1/11/89). Motion to stay litigation and compel arbitration is granted as to all claims. An interesting technique is employed by plaintiffs to avoid arbitration, but fails in this case. Subsequent to the period alleged in the Complaint, but prior to the date the Complaint was filed, the plaintiffs sent "letters of rescission" to the defendant broker-dealer, attempting to rescind the customer agreement. Despite these letters, the Court determines that the predispute arbitration clauses contained in the agreements were not revoked and remain enforceable. First, federal law favors the enforceability of arbitration agreements. Second, the letters sought to rescind the entire agreement, evidencing therefore no specific intent to revoke the agreement to arbitrate. Third, Smith Barney responded and demurred. Thus, no mutual intent to rescind was evidenced. The Court similarly rejects arguments that the arbitration agreements are unenforceable contracts of adhesion, stating that "there is nothing inherently unfair or oppressive about them." Finally, claims under the Securities Act of 1933 are deemed arbitrable. Citing Fifth and Tenth Circuit precedent, the Court finds that the Wilko decision is no longer binding, in light of the Supreme Court critique of its reasoning in McMahon.

Singer v. E.F. Hutton & Co., Inc., 699 F. Supp. 276 (S.D. Fla., 6/27/88). Court finds Section 12(2) claims under the 1933 Act arbitrable, opining that "had the issue been before the [McMahon] Court, there is every likelihood that the Arbitration Act would have been held applicable to

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such claims." The truly interesting aspect of this case, however, is plaintiffs' opposition to arbitration as a forum in which their claims for punitive damages could not be heard. Turning around an argument frequently used by broker-dealers to oppose arbitral awards of punitive damages, plaintiffs assert that the existence of a New York choice-of-law clause in the arbitration agreement, together with the Garrity (40 NY2d 354 (1976)) opinion forbidding arbitral awards of punitive damages, render non-arbitrable claims involving a punitive damage demand. The claim in question, Count VIII of the Complaint, sought punitive damages based upon allegations of common law fraudulent misrepresentation, concealment, and nondisclosure.

Holding that such claims must be arbitrated, the Court first notes that, in McMahon, the Supreme Court found arbitrable RICO claims for treble damages, "which should be considered punitive in nature." That federal policy favors the arbitration of civil disputes and federal case law has found no public policy to remove punitive damages from the arbitrators' ambit compel the conclusion that the Garrity holding is "contrary to federal policy." It is, therefore, inapplicable to this case. "To allow state law to preempt the federal Arbitration Act, in a case where that Act applies, would be violative of the Supremacy Clause of the United States Constitution."

Steele v. L.F. Rothschild & Co., Inc., No. 88-7380 (2d Cir., 12/5/88). Plaintiff appeals from an order to arbitrate her federal Equal Pay Act and New York Labor Law claims that, while a LFR employee, she was paid less than comparable male employees. The district court found that plaintiff had not "borne her burden of showing Congress intended to preclude [arbitral tribunals] from hearing Equal Pay Act claims." (Steele v. LFR, No. 88-0023 (LLS) (SDNY, 4/4/88)). The Second Circuit held that such interlocutory appeals were precluded by the Supreme Court's decision in Gulfstream Aerospace and by its own decision in McDonnell Douglas (1 SAC 6(4)). Plaintiff's argument that the case should be remanded for possible certification under 28 U.S.C. §1292(b) was similarly rejected, the Court distinguishing the legal importance of this case, where an arbitration-compelling order is appealed, from one where review of an arbitration-denying order is sought. Efforts to invoke the "collateral order" exception to §1291 or a writ of mandamus to achieve appeal are summarily rebuffed. The new amendments to Section 15 of the Federal Arbitration Act (2 SAC 1(1)) are not brought into consideration.

Willis v. Rubiera-Zim, C.A. No. 87-1121 (D.N.J., 12/29/88). Court adopts recommendations in Magistrate's Report, ordering the arbitration of 1934 Act and state law claims and denying defendants' motion to strike plaintiff's punitive damage claim. Plaintiff did not oppose the arbitrability of the state law claims, but did object to arbitrating the federal securities claims. Plaintiff signed three agreements with the broker-dealer, Paine Webber, all containing a pre-dispute arbitration clause with a Rule 15c2-2 disclaimer: "Any controversy between us arising out of or relating to this contract, or breach thereof, or any account(s) maintained by you, (except any claim for relief by a public customer for which a remedy may exist pursuant to an expressed or implied right of action, under the federal securities laws), shall be settled by arbitration...." (signed 3/85)(emphasis supplied).

The parenthetical language in the pre-dispute clause does not make all federal securities claims non-arbitrable, said the Court. The "may exist" phrase renders the exlusionary effect of the language ambiguous and makes interpretation necessary. "[I]n interpeting an arbitration clause, any doubts regarding its applicability should be decided in favor of arbitration." The Court's interpretation of this clause leads to the finding that claims under Sections10(b) and 20 of the 1934 Act must be arbitrated: "...the term

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'may exist' should be viewed as 'paralleling the evolving case law....' Hence, as the Court deems particular claims arbitrable, those claims will be removed from the exclusion from arbitration."

The Court rejects defendant's efforts to strike a claim for punitive damages, based upon allegations of common law fraud and breach of fiduciary duty. The federal policy favoring arbitration requires the courts to give broad scope to arbitral authority to award suitable remedies. It is undisputed here that the arbitration clause is sufficiently broad "to empower an arbitration panel to award punitive damages."

SCHEDULE OF COMING EVENTS

If you know of an arbitration event scheduled in the coming quarter, please tell us and we'll post it here.

March 27: Oral argument set before the U.S. Supreme Court in Rodriquez v. Shearson Lehman Hutton Inc., No. 88-385.

April 2-5: Securities Industry Association Legal and Compliance Division Conference (workshop: "Overview of the Status of Arbitration"), at the Marriott Orlando World Center, Orlando, Fla. Regis. Fee: (before Mar. 17) $400. for SIA members; $550 for non-members. For info., call Hans Reich, tel: (212) 902-4093.

April 6-7: Employment Litigation 1989: A Defense and Plaintiff's Perspective, sponsored by Practising Law Institute (includes a segment on alternative dispute resolution and binding arbitration), at St. Moritz-on-the-park, NYC. Regis. fee: $425. For info., contact PLI, 810 7th Ave., NYC, Jos. J. Bracchitta, tel: (212) 765-5700.

April 14: Arbitration Day '89, sponsored by the American Arbitration Association (Discussion Group on Securities Arbitration), New York Hilton, NYC. Regis. fee: $90. For info., contact AAA, 140 West 51st St., NYC 10020-1203. Tel: (212) 484-3233.

April 27-28: Employment Litigation 1989: A Defense and Plaintiff's Perspective, sponsored by Practising Law Institute (includes a segment on alternative dispute resolution and binding arbitration), at Hyatt on Union Square, San Francisco. Regis. fee: $425. For info., contact PLI, 810 7th Ave., NYC, Jos. J. Bracchitta, tel: (212) 765-5700.