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The Level Playing Field

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Cover Page Footnote

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THE LEVEL PLAYING FIELD

Constantine N. Katsoris*

I. Introduction

It was the best of times, it was the worst of times, it was the age of wisdom, it was the age of foolishness, it was the epoch of belief, it was the epoch of incredulity, it was the season of Light, it was the season of Darkness, it was the spring of hope, it was the winter of despair, we have everything before us, we have nothing before us It was the year of Our Lord one thousand seven hundred and seventy-five.¹

Similarly, the years 1987-1989 (hereinafter the "Dickens years" or "Dickens period") could be described as among the best and the worst of times for the securities industry. During this period the Dow Jones Industrial Average (DJIA) pierced two historical highs,² only to be followed by one day declines of unprecedented proportions.³ On October 19, 1987 ("Black Monday"), the Dow plunged 508 points (22.6%) in one trading day,⁴ and two years later, after a dramatic comeback to a new high in 1989, this key indicator again suffered a one-day decline of 190.58 points (6.91%) on October 13, 1989 ("Bloody Friday").⁵

This feverish volatility has been attributed to many reasons, including program trading⁶ and excessively leveraged buyouts.⁷ Other con-

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1. C. DICKENS, *A TALE OF TWO CITIES* (Washington Square Press ed. 1957).

2. See *Small Investors Tiptoe Back to Wall St.*, BUS. WK., Aug. 14, 1989, at 99; *October Rerun?*, WALL ST. J., Oct. 16, 1989, at 1, col. 6 [hereinafter *October Rerun?*].

3. See *Welcome Back To The Wall Street Funhouse*, BUS. WK., Oct. 30, 1989, at 27.

4. *Id.*

5. *October Rerun?*, *supra* note 2. Of equal significance was the speed of the decline. The DJIA dropped 154 points in only 65 minutes, pausing only as the market close neared. *Id.*

6. See *A Pox on Program Traders*, BARRON'S, Oct. 30, 1989, at 6, col. 1; *Is Program Trading a Threat Again?*, U.S. NEWS & WORLD REP., Sept. 18, 1989, at 76; *Programmed For Trouble?*, FINANCIAL WORLD, Nov. 28, 1989, at 108. But see *Don't Shoot the Computer*, THE ECONOMIST, Nov. 11, 1989, at 16. For a concise discussion of program trading, see

tributing causes have been interest rates, a fluctuating dollar, the lingering trade deficit and the persistent national budget deficit.⁸ Understandably, much confusion abounds, and unfortunately, precious

Ball, "The Stand We Took Against Program Trading Two Years Ago Still Stands," (Advertisement from the Wall Street Journal), *reprinted in Prudential Bache Securities Marketwise* at 2 (Dec. 1989). Ball writes:

Program trading explained

Program trading or stock-index arbitrage became possible when, in 1982, futures indexes were introduced into the market through the commodities exchange. The futures index was intended to be a useful vehicle for hedging against market risk. Under normal market conditions, portfolio managers could reduce their exposure to stock price movement by selling index futures and locking in a reasonable profit.

In theory, reducing the risk would encourage stock purchases, which would enhance capital formation, which would enable new companies to form and older ones to re-form, which would promote a healthy economy. Sounds wonderful, doesn't it?

What actually happens is that every so often a discrepancy develops between the current price and the price offered on a futures contract. Traders can program computers to spot those discrepancies—buying the one that's cheaper and selling the one that's more expensive. By playing the spread, portfolio managers can profit without making any judgment on the quality of the stocks being brought and sold. And keep in mind: with computers you hit a few keys, and—zap—you've fired hundreds of orders through the wires. Excessive volatility can then result, as the stock market becomes driven by the commodities market. In other words, the primary market has become the derivative. The futures tail is wagging the stock market dog. . . .

The concern here is that, from time to time, the two markets once linked feed on each other independent of fundamental economic values. Volatility is induced by the mindless activity of the market trading on the market, rather than on the inherent value of the stock. Program trading, thus, replaces sound human judgment with a machine that scans numbers and plays a spread. This creates distortions reflecting neither good business nor economic values.

It also diminishes the confidence of the individual investor. And, please, do not underestimate the place of the individual investor. In aggregate they are a powerful force in the market. More importantly, take away participation through individual judgment and you begin to unravel the fabric of our society.

Id.; see also *Brady Backs SEC's Bid for More Power Over Index Futures*, Wall St. J., Mar. 12, 1990, at C13, col. 3; *Measure Giving the SEC Power to Curb Program Trades Is Voted by House Panel*, Wall St. J., Mar. 13, 1990, at C9, col. 1.

7. See *Watch Dog Awake!*, Barron's, Nov. 13, 1989, at 6, col. 1; *The Loud Clank of Junk*, Newsweek, Sept. 25, 1989, at 32, col. 1; *LBO Stakes Benefit Pension Funds, Study Concludes*, Wall St. J., Dec. 18, 1989, at B 5C, col. 4. "In a leveraged buy-out, a group of investors acquires a company in a transaction financed largely with borrowing. Ultimately, the debt is paid with funds generated by the acquired company's operations or the sale of its assets." *Id.*; see also *The LBO Isn't A Superior New Species*, BUS. WK., Oct. 23, 1989, at 126.

8. See *The Quiet Crusader*, BUS. WK. Sept. 18, 1989, at 80; *U.S. Should Reduce Its Budget Deficit And Alter Tax Structure, OECD Says*, Wall St. J., Nov. 27, 1989, at A2, col. 3; *GNP Upgrading Seen But Coming Data Expected To Signal Still Weak Future*, Wall St. J., Nov. 27, 1989, at A2, col. 3; *Week In Business, The Trade Deficit Takes Off Again*, N.Y. Times, Dec. 17, 1989, § 3 (Business), at 14, col. 1.

little has been done to temper this plague of extreme volatility.⁹

Regardless of the causes, however, this volatility has become a fact of life resulting in enormous profits for some and enormous losses for others. One outgrowth of these losses is the explosion of litigation between the individual investors and the securities industry:¹⁰ the former usually seeks recoupment of losses, and the latter often seeks to collect on the debit balances when sudden market gyrations wipe away the equity in many margin accounts. Not only has the amount of litigation mushroomed, but the disputes have become significantly more complex.¹¹

During the Dickens years, the forum for the resolution of these disputes has shifted from the courtroom to arbitration.¹² This dramatic switch is largely the result of the United States Supreme Court opinions in *Shearson/American Express, Inc. v. McMahon*¹³ and *Rodriguez de Quijas v. Shearson/American Express Inc.*,¹⁴ which basically held that cases arising under the federal securities laws were arbitrable.¹⁵

Arbitration provides the advantage of speedy dispute resolution by persons knowledgeable in the area, without excessive costs.¹⁶ Unless arbitration procedures are fair in fact and appearance, however, their present popularity as a means of resolving securities disputes will greatly diminish.¹⁷ In this regard, the public *perception* of fairness must be zealously guarded, for it extends far beyond the issue of arbitration. Indeed, it goes to the very heart of the public investors' trust in the securities markets themselves, and it is this trust which must be preserved for those very markets to remain healthy.¹⁸

9. See *Wall Street Puts Futility Index at High*, Wall St. J., Oct. 19, 1989, at C1, col. 3; *Down With Program Trading*, Daily News, Oct. 22, 1989, at 8, col. 1; see also *People Invest Little Faith in Wall Street*, Wall St. J., Sept. 25, 1989, § 2, at 1, col. 3.

10. The Security Regulatory Organizations (SROs) arbitration forums have experienced a manyfold increase recently in the number of claims filed each year. See *infra* at 483 (Appendix A).

11. See *infra* notes 328-33 and accompanying text.

12. Katsoris, *Securities Arbitration After McMahon*, 16 FORDHAM URB. L.J. 361, 368-89 (1988) [hereinafter Katsoris I]; *Arbitration and Recent Rule Changes*, N.Y.L.J., July 27, 1989, at 3, col. 3.

13. 482 U.S. 220 (1987).

14. 109 S. Ct. 1917 (1989).

15. See *infra* notes 46-49 and accompanying text.

16. See Katsoris, *The Arbitration of a Public Securities Dispute*, 53 FORDHAM L. REV. 279 [hereinafter Katsoris II].

17. See Katsoris II, *supra* note 16, at 310; see generally Serota, *The Unjustified Furor Over Securities Arbitration*, 16 PEPPERDINE L. REV. 105 (1989).

18. See Katsoris, *The Double Jeopardy of Corporate Profits*, 29 BUFFALO L. REV. 1, 13-26.

In Part II this Article traces the origin of arbitration and examines the shift in the resolution of securities disputes from the courtroom to arbitration. The remaining sections deal with the issues of creating and maintaining a "level playing field," i.e., ensuring that the resolution of securities disputes are conducted in a manner that is fair to both investors and the securities industry. In shaping such a field, inquiry must be made concerning the *rules* governing the arbitration procedure, the *arbitrators* who preside over and decide the matters in controversy, and the *forum* where the matter will be heard.

Part III traces the evolution and discusses the present form of the Uniform Code of Arbitration, the body of rules which governs Security Regulatory Organization (SRO) arbitration. Part IV discusses the profile and conduct of the arbitrators who will decide the cases. Part V discusses the forum that would best achieve the goal of a level playing field. In seeking to create this level playing field, however, we must also be careful that partisan politics do not tilt the field in such a manner which would prevent "the greater good from being recognized,"¹⁹ i.e., a fair system for all. With this goal in mind, the Article concludes with certain recommendations and suggestions²⁰ which go beyond the ambit of, and yet directly or indirectly affect securities arbitration.

II. Background of Securities Arbitration

Arbitration is hardly a modern day phenomenon. It was Aristotle who wrote:

[e]quity is justice in that it goes beyond the written law. And it is equitable to prefer arbitration to the law court, for the arbitrator keeps equity in view, whereas the judge looks only to the law, and the reason why arbitrators were appointed was that equity might prevail.²¹

The arbitration of securities disputes can be traced back to the New York Stock Exchange (NYSE) in 1872.²² Since that time, numerous other SROs have established arbitration programs for the settlement of such disputes.²³

19. Hoblin, *The Case For a Single Securities and Commodities Arbitration Forum*, COMMODITIES L. LETTER 3, 5 (Aug. 1989) [hereinafter Hoblin I].

20. For a discussion of these suggestions, see *infra* notes 419-46 and accompanying text.

21. THE ARBITRATOR'S MANUAL i; see *infra* notes 335-36 and accompanying text.

22. P. HOBLIN, SECURITIES ARBITRATION: PROCEDURES, STRATEGIES, CASES 1-2 (1988) (hereinafter HOBLIN II).

23. *Id.*

To fully understand the present rules governing arbitrations at SRO forums, and elsewhere, we must look to the development of the present system. We must explore the judicial developments that have largely channeled such disputes into arbitration.²⁴ We must also examine legislative attempts to alter or influence the area of securities arbitration.²⁵ Finally, we must look to the establishment and work of the Securities Industry Conference on Arbitration (SICA) and the oversight role of the Securities and Exchange Commission (SEC or Commission).²⁶

A. Judicial Development

An unresolved dispute between an investor and his broker ordinarily ends in arbitration because of an arbitration agreement executed at the time a customer opens an account with his broker.²⁷ Indeed, a persistent complaint is that the public investor is often forced, when opening a securities account with a broker, to sign an agreement to arbitrate future disputes.²⁸

24. See *infra* notes 27-49 and accompanying text.

25. See *infra* notes 50-51 and accompanying text.

26. See *infra* notes 52-78 and accompanying text.

27. SROs require by rule that their membership consent to arbitrate disputes with their customers. By belonging to the SRO, its members agree to be bound by the SRO's rules. Consequently, customers of an SRO may compel a member of an SRO to arbitrate; however, absent a written contract, the member cannot compel the customer to arbitrate. See *HOBBLIN II*, *supra* note 22, at 2-3 to 2-4. The standard arbitration clause "authorizes the customer to elect the arbitration forum from a list of several organizations. If the customer does not elect the forum within five days after receipt from the broker-dealer of a notification requesting such election, the broker-dealer becomes authorized to make the election." Exchange Act Release No. 15,984 n.4 (July 2, 1979), reprinted in 17 SEC Docket 1167, 1169 n.4 (June-Aug. 1979). The extent to which customers are, as a practical matter, "required" to sign what can basically be described as a typical industry-wide agreement containing a pre-dispute arbitration clause is a critical question. This is particularly so if "the customer may be precluded from doing business with the broker-dealer if he or she refuses to sign the agreement or the broker-dealer is unwilling to accept any modification of its terms." *Id.* at 1169. It would appear that such agreements are largely in effect with respect to margin, option and commodity accounts, and, to a lesser degree, cash accounts. See Stansbury & Klein, *The Arbitration of Investor-Broker Disputes: A Summary of Development*, 35 ARB. J. 30, 32 (1980); see also C. FLETCHER, DYNAMISM IN SECURITIES ARBITRATION, SECURITIES ARBITRATION PRACTICE AND PROCEDURES SEMINAR 14 (Nov. 17, 1989). A "1988 SEC study of 65 brokerage firms showed that 61% of all cash accounts had no arbitration agreement in effect; 6% of margin accounts had no arbitration agreement; and, 5% of option accounts had no arbitration agreement." *Id.* This difference probably stems from the fact that the latter two usually involve greater risk or an extension of some form of credit by the firm to the customer, thus increasing the need for speedy resolution of problems through arbitration.

28. Although some courts have recognized the issue of adhesion, it would appear that most courts do not consider it to be a problem in the case of securities arbitration clauses. See *Katsoris I*, *supra* note 12, at 373-74; see also *Graham v. Scissor-Tail, Inc.*, 28 Cal. 3d

Under the United States Arbitration Act (Federal Arbitration Act or Arbitration Act),²⁹ agreements to arbitrate future disputes are, in general, specifically enforceable.³⁰ In the pre-Dickens period, however, there was an exception recognized for customers' claims which arose under the Securities Act of 1933³¹ (1933 Act or Securities Act).³² This exception resulted from the Supreme Court's decision in

807, 623 P.2d 165, 171 Cal. Rptr. 604 (1981); *Hope v. Superior Court of Santa Clara County*, 122 Cal. App. 3d 147, 175 Cal. Rptr. 851 (1981). Adhesion arises when a standardized contract, usually drafted by a party of superior bargaining power, is presented to a party whose choice is limited to accepting or rejecting the contract without the opportunity to negotiate its terms. Such agreements are usually used when a party enters into similar transactions with many individuals, and the agreements resemble ultimatums or laws rather than mutually negotiated contracts. See J. CALAMARI & J. PERILLO, *CONTRACTS* §§ 9-41 to 9-46 (3d ed. 1987). As to the enforceability of such contracts generally, see *Katsoris II*, *supra* note 16, at 306-09.

SICA had never specifically addressed the issue of pre-dispute arbitration agreements in depth because many of the SRO members believed that such agreements were private contractual issues between the customer and the broker. Nevertheless, this author repeatedly expressed concern about the voluntariness of the arbitration agreement before *McMahon*. *Id.* The issue should be examined, however, because it strikes at the very heart of the public's overall perception as to the fairness of the arbitration process. Investors should not be *forced* to agree to a pre-dispute arbitration agreement as a condition to access to the securities markets. See *supra* note 27. Such an agreement should be entered into freely, and only after the full effect and meaning of such a clause is disclosed. After *McMahon*, SICA did consider the form of such agreement. See *infra* notes 261-68; see also *infra* notes 264-65, regarding separate initialling. Moreover, such informed consent would eliminate a troublesome issue that often arises, concerning whether a customer understood or even read the arbitration clause. Although it *may* presently be the case that the public investor does have a choice—particularly with respect to cash accounts (see *supra* note 27)—such *de facto* coercion may someday become the case. See *Katsoris I*, *supra* note 12, at 375. In that event, Congress should insist upon market access without executing a pre-dispute arbitration clause. *Id.*

If, however, a customer does *freely* execute a pre-dispute arbitration agreement, that agreement should thereafter be binding, particularly since the industry is generally automatically bound to arbitrate. See *HOBLEN II*, *supra* note 22, at 2-3 to 2-4. To hold otherwise would make a mockery of the law of contracts. On the other hand, if the industry insists upon loading such agreements with choice of law provisions or other restrictions (i.e., the inclusion of a provision expressly prohibiting punitive damages) which would prevent relief otherwise available in court, then the issue of adhesion should be re-examined by the courts. See *infra* notes 245-48, 266 and accompanying text.

29. 9 U.S.C. §§ 1-14 (1982).

30. Section 2 of the Arbitration Act provides: "[a] written provision in . . . a contract evidencing a *transaction involving commerce* to settle by arbitration, a controversy thereafter arising out of such contract . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." *Id.* § 2 (emphasis added). Because the Federal Arbitration Act applies to claims arising from transactions involving interstate commerce, *id.*, and because securities dealings usually involve such transactions, state securities claims, as well as those arising under the federal securities laws, are usually arbitrable.

31. 15 U.S.C. § 77 (1982).

32. See *Katsoris II*, *supra* note 16, at 293-95.

1953 in *Wilko v. Swan*,³³ in which the Court had to decide between the mandate of the Arbitration Act to arbitrate and provisions in the Securities Act intended to protect the customer's rights.³⁴ In essence, the *Wilko* Court resolved this conflict between the Arbitration Act and the Securities Act in favor of the latter by concluding that Congress' desire to protect investors would be more effectively served by holding unenforceable any pre-dispute arbitration agreements relating to issues arising under the 1933 Act.³⁵ Prior to 1987, most federal courts presumed that the *Wilko* prohibition also extended to the Securities Exchange Act of 1934 (1934 Act or Exchange Act),³⁶ and thus—despite pre-dispute arbitration agreements—refused to order arbitration for customers' claims arising under the 1934 Act.³⁷

The confusion regarding the *Wilko* extension to claims under the 1934 Act was further exacerbated when a public customer joined a non-arbitrable *Wilko* federal claim with an arbitrable non-federal securities claim. Some courts bifurcated the two and ordered that the federal *Wilko* claim be litigated, and the other claim be arbitrated. Other courts, however, found the two claims to be so intertwined that it was impractical or impossible to separate them, and therefore, ordered that both be litigated together.³⁸

The intertwining/bifurcation issue, however, was settled in 1985 in *Dean Witter Reynolds, Inc. v. Byrd*.³⁹ *Byrd* raised two issues: first, whether *Wilko* extends to 1934 Act claims; and second, whether the federal and non-federal claims should be bifurcated or, if intertwined, tried together.⁴⁰ Although the Court declined to specifically resolve the issue of whether *Wilko* applied to 1934 Act claims,⁴¹ the Court

33. 346 U.S. 427 (1953).

34. *Id.* The Court noted that the Securities Act was designed to protect investors from fraud by requiring full disclosure on the part of the dealer. *Id.* In order to effect this policy, Congress included three special provisions in the 1933 Act. Section 12 specifically gave investors a *special* right to recover for misrepresentation which differs substantially from the common-law action in that this special right imposes upon the seller the burden of proving lack of scienter. *Id.*; 48 Stat. 84 (codified as amended at 15 U.S.C. § 771 (1982)). Under § 14 of the Act, 48 Stat. 84 (codified at 15 U.S.C. § 77n (1982)), an investor could not waive this *special* right. Finally, § 22 of the Act specifically affords the plaintiff national service of process and a broad choice of forum by making the right enforceable by the investor in any court of competent jurisdiction, federal or state. 48 Stat. 86 (codified as amended at 15 U.S.C. § 77v(a) (1982)).

35. 346 U.S. at 432.

36. 15 U.S.C. § 78 (1982).

37. *See* Katsoris I, *supra* note 12, at 364-67.

38. 346 U.S. 366 (1953).

39. 470 U.S. 213 (1985).

40. *Id.* at 214-15.

41. *Id.* at 214 n.1. The Court declined to resolve this issue because Dean Witter

did hold that when an arbitrable claim is joined with a non-arbitrable *Wilko* claim, the claims need not be tried together involuntarily.⁴² Thus, *Byrd* rejected the concept of "intertwining" and supported the principle of automatic bifurcation, whenever a non-arbitrable *Wilko* claim is joined with an arbitrable claim.⁴³ In other words, the two claims may be tried separately and simultaneously.⁴⁴ Whatever the merits of automatic bifurcation, it would unleash and set in motion two separate forums on a collision course.⁴⁵

In 1987, the Supreme Court in *Shearson/American Express, Inc. v. McMahon*⁴⁶ resolved the question left unanswered in *Byrd*, by holding that the *Wilko* exemption did not apply to 1934 Act claims. Finally, in 1989 the Supreme Court in *Rodriguez de Quijas v. Shearson/American Express*⁴⁷ undid the *Wilko* exception entirely and held that pre-dispute arbitration agreements would be upheld, even as to issues arising under the 1933 Act.⁴⁸ Because of the *McMahon* and *Rodriguez* decisions, most securities disputes are now arbitrated pursuant to pre-dispute arbitration agreements.⁴⁹

That has not ended the story, however. In the aftermath of the *McMahon* decision, both Congress and the legislatures of several states made attempts to render pre-dispute securities arbitration agreements unenforceable.⁵⁰ To date, such efforts have proven

Reynolds, Inc., did not seek to compel arbitration of the federal securities claims at the district court level. *Id.*

42. *Id.* at 217.

43. *Id.*; see also Katsoris I, *supra* note 12, at 366-67.

44. 470 U.S. at 217; see *First Step To Heighten Role of Arbitration*, Legal Times, March 11, 1985, at 5, col. 1.

45. See Katsoris, *The Securities Arbitrators' Nightmare*, 14 FORDHAM URB. L.J. 3, 8 (1985-86) [hereinafter Katsoris III]. The essence of the problem is that two separate forums would often be ruling essentially on the same set of facts with the possibility of contradictory findings. *Id.* at 9-11.

46. 482 U.S. 220 (1987).

47. 109 S. Ct. 1917 (1989).

48. *Id.* at 1922; see *Arbitration and the Demise of Wilko v. Swan*, N.Y.L.J., June 15, 1989, at 3, col. 3.

49. SIXTH REPORT OF THE SECURITIES INDUSTRY CONFERENCE ON ARBITRATION 1 (Aug. 1989) [hereinafter SIXTH REPORT] (available at Fordham Urban Law Journal office).

50. See *Draft Bill To Restrict Use of Pre-Dispute Agreements*, 1 SEC. ARB. COMMENTATOR 3, 4 (June 1988); *Markey to SEC: What Happened?*, 1 SEC. ARB. COMMENTATOR 4, 1 (July 1988); *State Actions on Pre-Dispute Clauses*, 1 SEC. ARB. COMMENTATOR 9 (Aug. 1988).

A particularly serious attempt by a state to regulate arbitration agreements was that undertaken by Massachusetts. See Neeseman, *After McMahon and Rodriguez: The State of the Law*, SEC. ARB. 217, 279.3 (1989). The Massachusetts rule bars licensed broker-dealers from requiring investors to sign pre-dispute arbitration agreements, and mandates that brokers must disclose fully to investors the legal effects of arbitration

unsuccessful.⁵¹

B. Creation of SICA and the Role of the SEC

Prior to 1976, most SROs had differing rules for the administration of securities arbitration disputes.⁵² In June 1976, the SEC solicited comments from interested persons on the feasibility of developing a "uniform system of dispute grievance procedures for the adjudication of small claims."⁵³ After conducting a public forum at which written and oral comments were received, the SEC's Office of Consumer Affairs issued a report recommending the adoption of procedures for handling investor disputes and the creation of a new entity to administer the system.⁵⁴

Before implementing the proposal for a new arbitration forum, the Commission invited further public comment.⁵⁵ In response to this invitation, several SROs proposed the establishment of a securities industry task force to consider the development of "a uniform arbitration code and the means for establishing a more efficient, economic and appropriate mechanism for resolving investor disputes involving small sums of money."⁵⁶ As a result of this suggestion, a Securities Industry Conference on Arbitration (SICA) was established

agreements. MASS. REGS. CODE tit. 950, § 12.204 (1978). In a recent case, *Securities Indus. Ass'n v. Connolly*, both the District and Circuit courts ruled that state regulations such as this one were preempted by the Federal Arbitration Act. 703 F. Supp. 146, 153 (D. Mass. 1988), *aff'd*, 883 F.2d 1114, 1120 (1st Cir. 1989). However, the defendants have applied for certiorari to the Supreme Court, and although the Court has not yet granted certiorari, it did request further information. See 58 U.S.L.W. 3457 (U.S. Jan. 16, 1990) (No. 89-894).

51. See S. Hinden, GAO Asked To Investigate Securities Arbitration Issues, Wash. Post, Feb. 7, 1990, at 2, col. 1; Markey to SEC: What Happened?, 1 SEC. ARB. COMMENTATOR 4, 1 (July 1988); *Securities Indus. Assoc. v. Connolly*, 883 F.2d 1114 (1st Cir. 1989), petition for cert. filed, 58 U.S.L.W. 3457 (U.S. Jan. 16, 1990) (No. 89-894) (filed Nov. 29, 1989); see also *Securities Indus. Ass'n v. Connolly—Massachusetts Arbitration Rules Preempted*, 2 SEC. ARB. COMMENTATOR 2 (Aug. 1989). But see Stock Arbitration Case in Top Court, Newsday, Jan. 23, 1990, at 37, col. 1. As to whether the public voluntarily enters into such agreements, see *supra* notes 27, 28 and accompanying text; see also R. Ryder, *Securities Arbitration in 1989: Reviewing the Case Law, Securities Arbitration Practice and Procedures*, SEC. ARB. INST. AND SEC. ARB. COMMENTATOR 37 (Nov. 17, 1989) (seminar).

52. See Katsoris II, *supra* note 16, at 283.

53. Sec. Exch. Act Release No. 12,528 (June 9, 1976), reprinted in 9 SEC Docket 833, 834 (Mar.-July 1976).

54. Sec. Exch. Act Release No. 12,974 (Nov. 15, 1976), reprinted in 10 SEC Docket 955-56 (July-Dec. 1976).

55. See *id.* at 955, 956.

56. See *id.*; FIFTH REPORT OF THE SECURITIES INDUSTRY CONFERENCE ON ARBITRATION 2 (Apr. 1986) [hereinafter FIFTH REPORT] (available at Fordham Urban Law Journal office).

in April 1977, consisting of representatives of various SROs,⁵⁷ the Securities Industry Association (SIA)⁵⁸ and the public.⁵⁹

The Commission then invited proposals from SICA to improve the methods for resolution of investors' small claims.⁶⁰ After holding numerous meetings throughout the country, SICA developed a simplified arbitration procedure for resolving customer claims of \$2,500 or less,⁶¹ and issued an informational booklet describing small claims procedures (Small Claims Booklet).⁶² Realizing, however, that the development of a small claims procedure was only a first step, SICA then developed a comprehensive Uniform Code of Arbitration (Uniform Code or Code) for the securities industry.⁶³ The Code established a uniform system of arbitration procedures to cover all claims by investors.⁶⁴ In addition, SICA prepared an explanatory booklet

57. The following SROs were represented: the American (ASE), Boston (BSE), Cincinnati (CSE), Midwest (MSE), New York (NYSE), Pacific (PSE) and Philadelphia (PHSE) Stock Exchanges, the Chicago Board Options Exchange (CBOE), the Municipal Securities Rulemaking Board (MSRB) and the National Association of Securities Dealers, Inc. (NASD). FIFTH REPORT, *supra* note 56, at 3.

58. *Id.* The SIA is a trade association for the securities industry.

59. Peter R. Cella, Jr., Esq., Mortimer Goodman, Esq., and the author have served as Public Members of SICA since its creation in 1977. *Id.* In 1983, Justin Klein, Esq., was added as the fourth Public Member of SICA. *Id.* The current public members' terms shall expire, one a year, beginning on December 31, 1989. *See SICA: Pre-dispute Clauses Stay in Customer Agreements*, 1 SEC. ARB. 6, at 1 (Sept. 1988). They are each eligible for reappointment for a new four-year term. All *new* members will serve for four years and are eligible for one additional four-year term. The public members whose terms are not expiring will determine the appointment of new members or reappointment. *Id.* The appointment, or reappointment, may be vetoed by a two-thirds vote of the non-public members of SICA. *Id.* Mortimer Goodman did not seek re-appointment as a public member as of the end of 1989, and a new public member will be selected by the remaining public members to fill this vacancy.

60. Implementation of An Investor Dispute System, Exchange Act Release No. 13, 470 [1977-1978 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 81,136, at 83905 (Apr. 26, 1977) [hereinafter Investor Dispute System].

61. FIFTH REPORT, *supra* note 56, at 3. SICA subsequently raised the jurisdictional limit of small claims to \$5,000, and then again to the present \$10,000. *See* SEC Approves NASD Proposal to Raise Ceiling for Simplified Arbitrations, Sec. Reg. & L. Rep. (BNA) No. 20, at 560 (Apr. 15, 1988).

62. *See* REPORT OF THE SECURITIES INDUSTRY CONFERENCE ON ARBITRATION TO THE SECURITIES AND EXCHANGE COMMISSION: *Proposals to Establish a Uniform System for the Resolution of Customer Disputes Involving Small Claims*, "How to Proceed with the Arbitration of a Small Claim" (Appendix D) (Nov. 15, 1977) [hereinafter FIRST REPORT] (available at Fordham Urban Law Journal office).

63. *See* Uniform Code of Arbitration (as amended), reprinted in FOURTH REPORT OF THE SECURITIES INDUSTRY CONFERENCE ON ARBITRATION, Exhibit C (Nov. 1984) [hereinafter FOURTH REPORT] (available at Fordham Urban Law Journal office). The small claims procedure was incorporated into § 2 of the Code. *See* Uniform Code § 2, *infra* at 484-86 (Appendix B).

64. FIFTH REPORT, *supra* note 56, at 2.

for prospective claimants (Procedures Booklet),⁶⁵ explaining procedures under the Code. To a large extent, the Code incorporated and harmonized the rules of the various SROs and codified various procedures that the SROs had followed, but had not included in their existing rules.⁶⁶

The original Code was adopted by the participating SROs during 1979 and 1980,⁶⁷ and appears in the Second Report of SICA to the SEC.⁶⁸ Between the time of its initial adoption and the *McMahon* case, various revisions were made to both the Code and the Procedures Booklet. These changes were reported in the Third, Fourth and Fifth SICA Reports to the SEC.⁶⁹

Shortly after *McMahon*, the SEC dispatched to SICA a list of recommendations for changes in SRO arbitration, and requested SICA's comments on these proposed changes.⁷⁰ SICA responded in a letter which represented a consensus view of its members.⁷¹ Several mem-

65. See THIRD REPORT OF THE SECURITIES INDUSTRY CONFERENCE ON ARBITRATION TO THE SECURITIES AND EXCHANGE COMMISSION 5 (Jan. 31, 1980) [hereinafter THIRD REPORT] (available at Fordham Urban Law Journal office); SECURITIES INDUSTRY CONFERENCE ON ARBITRATION, ARBITRATION PROCEDURES (1980) [hereinafter PROCEDURES BOOKLET] (available at Fordham Urban Law Journal office). After *McMahon*, SICA consolidated the Small Claims booklet, see FIRST REPORT, *supra* note 62, into the PROCEDURES BOOKLET. See SIXTH REPORT, *supra* note 49, at 3.

66. See Katsoris II, *supra* note 16, at 284.

67. FIFTH REPORT, *supra* note 56, at 4. Once SICA adopts a new rule, each SRO must then generally go back to their respective organization in order to get a rule change which is then usually submitted to the SEC for approval. Accordingly, there is often a time lag between SICA approval and SRO action.

68. See SECOND REPORT OF THE SECURITIES INDUSTRY CONFERENCE ON ARBITRATION TO THE SECURITIES AND EXCHANGE COMMISSION, Exhibit A (Dec. 28, 1978) [hereinafter SECOND REPORT] (available at Fordham Urban Law Journal office).

69. See THIRD REPORT, *supra* note 65; FOURTH REPORT, *supra* note 63; FIFTH REPORT, *supra* note 56.

70. See Letter from SEC to SICA (Sept. 10, 1987) [hereinafter SEC Letter], reprinted in J. SCHROPP, SECURITIES ARBITRATION, NEW APPROACHES TO SECURITIES COUNSELING AND LITIGATION AFTER *McMahon* 141-53 (1988) [hereinafter J. SCHROPP]. The SEC's proposals principally revolved around such issues as: selection, qualification, background training and evaluation of arbitrators; challenges for cause; method of transcribing and preserving the record of arbitration hearings; written outline and explanation of the basis for an award; pre-hearing discovery, depositions and exchange of documents; expanding the use of educational pamphlets; increased pressure on SRO arbitration systems brought about by the anticipated increased case load; adherence to Rule 19b-4; notification of abuses to disciplinary authorities; and large cases. *Id.*

71. See SICA Letter to Richard G. Ketchum (Dec. 14, 1987) [hereinafter SICA Letter], reprinted in SCHROPP, *supra* note 70, at 154-69. It is noteworthy, however, that the composition of SICA is: 10 SROs, the SIA and 4 public members. Obviously, the public members are in the minority, which means they cannot effect change unilaterally or as fast as they wish. Nevertheless, even before the intense scrutiny of arbitration brought on by *McMahon*, a productive and generally cooperative spirit has prevailed at SICA which

bers of SICA, however, also sent separate responses.⁷² Many of these issues had already been previously discussed at SICA, and SICA's response was generally in agreement with the SEC's proposals.⁷³ Because there were some honest disagreements on certain points, further discussions between SICA and the SEC ensued, leading to many of the recent changes to the Code which are discussed hereafter⁷⁴ and found in SICA's Sixth Report.⁷⁵

Since these latest amendments to the Code, SICA continues to meet in order to monitor the performance of the Code in action, with a view towards further fine-tuning and adjusting its provisions. Indeed, SICA has made additional amendments to the Code since the Sixth Report, which are discussed hereafter in the following section on the Code.⁷⁶ To date, over 25,000 cases, including small claims, have been filed with the participating SROs since the initial approval of the Code.⁷⁷ In 1988, the first calendar year after *McMahon*, the trend accelerated when over 6,000 such arbitrations were filed before the participating SROs.⁷⁸

III. The Arbitration Code—the Rules of the Game

A. Themes of the Code: Economy, Speed and Above All, Fairness

What is attractive about arbitration is that it is expeditious and economical.⁷⁹ While speed and economy are important, they cannot be achieved at the expense of fairness. Fairness, however, is not mutually exclusive of speed or economy, because speed and particularly economy increase the fairness to public investors who may not have the resources to sustain the cost of a lengthy proceeding,⁸⁰ or who

has led to greater uniformity and steady progress and improvement in the Uniform Code over the years.

72. See, e.g., Letter from Public Members of SICA to Richard G. Ketchum (Oct. 9, 1987) [hereinafter Public Members' Letter], reprinted in SCHROFF, *supra* note 70, at 170-72.

73. See SICA Letter, *supra* note 71, at 155.

74. For discussion of the Code, see *infra* notes 84-268 and accompanying text.

75. See SIXTH REPORT, *supra* note 49. This Report was sent to the SEC in the summer of 1989.

76. See *infra* notes 84-268 and Uniform Code of Arbitration, *infra* at 484 (Appendix B).

77. The bulk of said arbitrations are handled before the NASD and the NYSE. See SIXTH REPORT, *supra* note 49, at 3-4. A breakdown of the arbitrations handled by the arbitration facilities of the various SROs appears *infra* at 483 (Appendix A).

78. *Id.*

79. M. DOMKE, DOMKE ON COMMERCIAL ARBITRATION 1, ¶ 1.01 (1968).

80. Besides attorneys fees and other related costs—including the loss of time by attending hearings—forum fees are also based upon hearing sessions. See Uniform Code of Arbitration at § 30(c), *infra* at 499-500 (Appendix B).

may have only very small claims.⁸¹ It is thus critical that the Code's rules facilitate and maintain these essential characteristics—for justice unduly delayed, or made prohibitively costly, is justice denied. This is hardly an insurmountable problem, for all three goals can and should co-exist, with fairness as the paramount consideration.

Therefore, in maintaining arbitration as an alternative dispute resolution process, it has been necessary for SICA to provide safeguards to ensure a fair and complete hearing, without destroying the fabric of arbitration in the process.⁸² Because such safeguards often slow the proceedings down,⁸³ the benefits of each new procedure must be weighed against the resultant escalation of time and cost. It is against this background that SICA adopted the original Arbitration Code and continues to amend it to this day.

B. The Present Code

The original SICA Code of Arbitration appeared in the Second SICA Report⁸⁴ and was amended many times before *McMahon* (as reported in the Third, Fourth and Fifth Reports)⁸⁵ evolving into the version which appears in the Sixth SICA Report submitted to the SEC during the summer of 1989.⁸⁶ With minor modifications this Code, as it appears in the Sixth Report, has largely been adopted by the participating SROs.⁸⁷ Since the Sixth Report, however, SICA has made some additional amendments which will be reported on herein, and the entire Code (hereinafter "present Code" or "latest Code"), as amended to reflect all changes (including the latest SICA meeting on January 17, 1990), appears at the end of this Article as Appendix B.⁸⁸

The latest Code has thirty-one sections, and the remainder of this Part discusses these Code provisions as most recently amended. This Part also tracks their changes from the original version, particularly those made *after McMahon*, and discusses the rationale behind those changes. Finally, this Part suggests possible future alterations of certain Code provisions.

81. See Uniform Code of Arbitration § 2 (Small Claims), *infra* at 484-86 (Appendix B).

82. See *supra* notes 52-78 and accompanying text.

83. See *infra* notes 175-202 and accompanying text.

84. See *supra* note 68 and accompanying text.

85. See *supra* note 69 and accompanying text.

86. See SIXTH REPORT, *supra* note 49.

87. See *supra* notes 70-75 and accompanying text.

88. See *infra* at 484 (Appendix B).

*Section 1—Arbitration*⁸⁹

Section 1 of the Code sets out the jurisdictional guidelines of SRO arbitration which permits an SRO to accept a matter upon the demand of a customer or nonmember, even absent an agreement.⁹⁰ It further recognizes, however, the SRO's right to decline the use of its facilities where the dispute, claim or controversy is not a proper subject matter for arbitration.⁹¹ The present section 1 is basically unchanged from the original version.

*Section 2—Simplified Arbitration*⁹²

This section deals with the Small Claims Simplified Arbitration procedures.⁹³ Simplified arbitration is a process by which smaller claims can be resolved more quickly and at less cost than larger claims.⁹⁴ This section has the effect of increasing the fairness of small claims arbitration, because otherwise, the cost to arbitrate would often exceed any recovery. Initially this section applied only to situations where the dollar amount did not exceed \$2,500. The amount was later raised to \$5,000,⁹⁵ and, finally increased to its present \$10,000 limit.⁹⁶ Except for raising the limits, the language of the section has changed little other than to increase the deposit and other costs from a flat \$15 fee to a present sliding scale (\$15 to \$200) reflecting the increase from the original \$2,500 limit to the present \$10,000 limit.⁹⁷

*Section 3—Hearing Requirements—Waiver of Hearing*⁹⁸

This section mandates that each dispute, claim or controversy shall require a hearing, unless the parties waive their right to a hearing, or the dispute involves a small claim. Section 3 remains unchanged from the original version.⁹⁹

89. Uniform Code of Arbitration § 1, *infra* at 484 (Appendix B).

90. *Id.* at § 1(a).

91. *Id.* at § 1(b).

92. Uniform Code of Arbitration § 2, *infra* at 484-86 (Appendix B).

93. *Id.*

94. In essence this enhances the fairness of Arbitration procedures, for even those with small claims can partake.

95. See FOURTH REPORT, *supra* note 63, at 3; see also Uniform Code of Arbitration § 2(a), *infra* at 484 (Appendix B).

96. See SEC Approves NASD Proposal to Raise Ceiling for Simplified Arbitrations, Sec. Reg. & L. Rep. (BNA) No. 20, at 560 (Apr. 15, 1988).

97. See FOURTH REPORT, *supra* note 63, at 3; see Uniform Code of Arbitration § 2(c), *infra* at 484-85 (Appendix B).

98. Uniform Code of Arbitration § 3, *infra* at 486 (Appendix B).

99. *Id.*

*Section 4—Time Limitation Upon Submission*¹⁰⁰

Section 4 sets out a six year time limitation under the Code from the time of the occurrence or event giving rise to the claim.¹⁰¹ It specifically provides, however, that this six year provision does not extend applicable statutes of limitation.¹⁰² As a result of an amendment prior to *McMahon*, the six year provision is also inapplicable where a case is directed to arbitration by a court of competent jurisdiction.¹⁰³

*Section 5—Dismissal of Proceedings*¹⁰⁴

The original version of Section 5 gave arbitrators the discretion to dismiss the arbitration proceedings at any time upon their own initiative or upon the joint request of the parties.¹⁰⁵ The section was subsequently changed before *McMahon* to its present version by extending the discretionary power to dismiss to situations where only one party so requests,¹⁰⁶ and by making the dismissal mandatory where the request is jointly made by the parties.¹⁰⁷

*Section 6—Settlements*¹⁰⁸

This section provided that "all settlements upon any matter submitted shall be at the election of the parties," and it remained unchanged from the original version¹⁰⁹ until very recently. After the Sixth Report, SICA removed the words "upon any matter," as redundant, so that the section now simply reads: "[a]ll settlements submitted shall be at the election of the parties."¹¹⁰

*Section 7—Tolling of Time Limitation(s) for The Institution of Legal Proceedings*¹¹¹

This section originally provided for the tolling of time limitations for the institution of legal proceedings from the time when *all* parties filed duly executed submission agreements and continued for such period as the SRO retained jurisdiction over the matter.¹¹² The section was subsequently expanded prior to *McMahon* to its present version

100. Uniform Code of Arbitration § 4, *infra* at 486-87 (Appendix B).

101. *Id.*

102. *Id.*

103. See FOURTH REPORT, *supra* note 63, at 4.

104. Uniform Code of Arbitration § 5, *infra* at 487 (Appendix B).

105. See SECOND REPORT, *supra* note 68, at A-4.

106. See THIRD REPORT, *supra* note 65, at C-3

107. *Id.*

108. Uniform Code of Arbitration § 6, *infra* at 487 (Appendix B).

109. See SECOND REPORT, *supra* note 68, at A-4.

110. Uniform Code of Arbitration § 6, *infra* at 487 (Appendix B).

111. *Id.* § 7, *infra* at 487 (Appendix B).

112. See SECOND REPORT, *supra* note 68, at A-4.

which requires: (1) that applicable time limitations for the institution of legal proceedings would be tolled from the time a duly executed submission agreement is filed by the claimant or claimants (instead of all the parties),¹¹³ and (2) that the six year limitation for the bringing of arbitration proceedings, as provided in Section 4, is to be extended by any period during which a court of competent jurisdiction retains jurisdiction over the matter submitted.¹¹⁴ The key reasoning behind this section is that it would be unfair to the claimant for such limitations to continue to run once the claim is in arbitration, or conversely, while the dispute is being adjudicated in court.

*Section 8—Designation of the Number of Arbitrators*¹¹⁵

This section deals with the composition of the panels. In particular, it grants to the SRO Director of Arbitration the authority to choose the panel and its chairman, and directs that the *majority* of any panel shall consist of arbitrators who are *not* from the securities industry (public arbitrator), *unless* the public customer or "nonmember" requests otherwise.¹¹⁶

The original section provided for panels of three members where the matter in controversy did not exceed \$100,000 and five members in excess of that amount.¹¹⁷ Largely for reasons of economy and efficiency, that has been whittled down to three person panels for controversies exceeding \$10,000, or where no money claim is involved or disclosed.¹¹⁸ In claims involving \$10,000 or less, only one arbitrator need be appointed.¹¹⁹ The NASD has extended this one arbitrator rule to situations involving \$30,000 or less.¹²⁰ Nevertheless, many arbitrators—particularly those from the public who are independent of, but not necessarily familiar with the securities industry practices—feel uncomfortable sitting alone without the counsel of an industry arbitrator.

Although this section always provided that the majority of the arbi-

113. See FOURTH REPORT, *supra* note 63, at C-3; see also Uniform Code of Arbitration § 7(a), *infra* at 487 (Appendix B).

114. See FOURTH REPORT, *supra* note 63, at C-3; see also Uniform Code of Arbitration § 7(a), *infra* at 487 (Appendix B).

115. Uniform Code of Arbitration § 8, *infra* at 487-88 (Appendix B).

116. *Id.* § 8(a). The term nonmember was added to the section after *McMahon*. See SIXTH REPORT, *supra* note 49, at 6.

117. See THIRD REPORT, *supra* note 65, at C-4.

118. See SIXTH REPORT, *supra* note 49, at 6.

119. *Id.*

120. See 2 SEC. ARB. COMMENTATOR 5, 4; see also Masucci, *Maintaining The Fairness of Arbitration*, SECURITIES ARBITRATION PRACTICE AND PROCEDURE SEMINAR at 144-45 (Nov. 17, 1989) [hereinafter Masucci].

trators on any panel be public arbitrators, no further guidance was given by the original Code as to who qualified to be a public arbitrator.¹²¹ The original version of the Procedures Booklet, however, described public arbitrators as "individuals who are neither associated with, nor employed by a broker-dealer or securities industry organization."¹²² SICA initially left this test flexible so that the vast experience of many needed and qualified persons would not be lost. As time went on, however, it became apparent that the category of public arbitrator had to be more clearly defined. Accordingly, Guidelines for the Classification of Public Arbitrators were added to the Procedures Booklet.¹²³ After *McMahon*, however, SICA further tightened the classification by amending Section 8 of the Code to specifically exclude as public arbitrators: (1) brokers and registered investment advisers and persons who are retired from the securities industry; (2) persons who had been employed in the industry in the past three years; (3) professionals, i.e., attorneys or accountants, who devote 20% or more of their work efforts to securities industry clients; and (4) spouses of industry personnel.¹²⁴

*Section 9—Notice of Selection of Arbitrators*¹²⁵

Before the *McMahon* decision, this section merely required that the Director of Arbitration inform the parties of the names and business affiliations of the arbitrators at least eight business days prior to the

121. See FIFTH REPORT, *supra* note 56, at 32.

122. See THIRD REPORT (Proposed Uniform Booklet Explaining Arbitration Procedures), *supra* note 65, at Exhibit B.

123. See FIFTH REPORT, *supra* note 56, at 17.

Guidelines for the Classification of Persons as Public Arbitrators

No one may serve as a public arbitrator who has been an employee or partner of a member organization or subsidiary thereof, or a shareholder of a non-publicly owned member organization or subsidiary thereof for a period of three years immediately preceding his or her appointment as a public arbitrator.

Additional information concerning a particular arbitrator may be obtained by a party or the party's attorney upon request directed to the Director of Arbitration prior to the commencement of the hearing or a submission to the arbitrator without a hearing.

Id.

124. See SIXTH REPORT, *supra* note 49, at 6-7. The NYSE guidelines for the classification of public arbitrators are even more stringent. See Katsoris I, *supra* note 12, at 378 n.98. Indeed, such NYSE guidelines provide that "[a]ny close question on arbitrator classification or on challenges for cause shall be decided in favor of public customers." *Id.*; see also Neal, *Securities Arbitration Administration and Procedures at the Chicago Board Options Exchange, Inc.*, SECURITIES ARBITRATION 1989, PLI SEMINAR, at 656-57; Noah & Stroughter, *Arbitration At The American Stock Exchange*, SECURITIES ARBITRATION 1989, PLI SEMINAR at 579-80.

125. Uniform Code of Arbitration § 9, *infra* at 488-89 (Appendix B).

date fixed for the initial hearing session.¹²⁶ Since *McMahon*, the section has been significantly expanded.¹²⁷

The Director of Arbitration must now also inform the parties of the arbitrators' employment histories for the past ten years in addition to the expanded disclosures required by Section 11.¹²⁸ Moreover, the right of a party to make *further inquiry* of the Director concerning an arbitrator's background is now included in the rule.¹²⁹ Previously, this right was only mentioned in the Procedures Booklet.¹³⁰ In addition, the expanded section 9 grants to the Director the power to designate a replacement arbitrator should an appointed one become disqualified, resign, die, refuse, or otherwise be unable to perform prior to the first hearing.¹³¹ Consistent with the other provisions of Section 9, the replacement provision imposes disclosure requirements upon the Director, so as to meaningfully preserve the right to challenge the replacement arbitrator under Section 10.¹³² Vacancies occurring *after* the commencement of the first hearing are specifically covered by Section 12.¹³³

*Section 10—Challenges*¹³⁴

Initially, this section dealt only with peremptory challenges and granted *one* such challenge to each party only when panels consisted of more than one arbitrator.¹³⁵ Thereafter the peremptory challenge was extended (similar to the present rule) to all panels (regardless of size).¹³⁶ However, the new section does limit multiple claimants, respondents and third-party respondents to one peremptory challenge, unless the Director determines that justice requires the granting of additional such challenges.¹³⁷ The section was further amended at that time to specifically permit *unlimited* challenges *for cause*.¹³⁸

126. See SECOND REPORT, *supra* note 68, at A-5.

127. See SIXTH REPORT, *supra* note 49, at 7.

128. See *infra* notes 139-43 and accompanying text.

129. See Uniform Code of Arbitration § 9, *infra* at 488-89 (Appendix B).

130. See Procedures Booklet, *supra* note 65, at 3.

131. See Uniform Code of Arbitration § 9, *infra* at 488-89 (Appendix B).

132. See *infra* notes 134-38 and accompanying text; see also Uniform Code of Arbitration §§ 9, 10, *infra* at 488-89 (Appendix B).

133. See *infra* notes 144-50 and accompanying text.

134. See also Uniform Code of Arbitration § 10, *infra* at 489 (Appendix B).

135. See SECOND REPORT, *supra* note 68, at A-5.

136. See FOURTH REPORT, *supra* note 63, at C-4.

137. *Id.*; see also Uniform Code of Arbitration § 10, *infra* at 489 (Appendix B).

138. See FOURTH REPORT, *supra* note 63, at C-4.

*Section 11—Disclosures Required by Arbitrators*¹³⁹

Originally, Section 11 merely required each arbitrator to disclose to the Director of Arbitration any circumstances which might preclude such arbitrator from rendering an objective and impartial determination.¹⁴⁰ The section was soon expanded to specifically authorize the Director to remove such an arbitrator before the commencement of the first hearing, or in the absence of removal, to inform the parties of any such information.¹⁴¹

After *McMahon* the section was significantly expanded to parallel Canon II of the Code of Ethics for Arbitrators in Commercial Disputes (Code of Ethics) by explicitly imposing a duty upon the arbitrator to disclose any potential conflict, which continues throughout the proceeding.¹⁴² To facilitate this process, arbitrators now receive a copy of the Code of Ethics each time they are assigned to a case in order to highlight the types of disclosures required. For example, the Code of Ethics requires that an arbitrator reveal any direct or indirect financial or personal interest in the outcome of the arbitration, and any existing or past financial, business, professional, family or social relationships, which are likely to affect impartiality or that might reasonably create an appearance of bias.¹⁴³

*Section 12—Disqualification or Other Disability of Arbitrators*¹⁴⁴

Before *McMahon*, this section simply provided that if an arbitrator became disabled or disqualified after the commencement of the first session, the Director of Arbitration could either appoint a replacement or allow the arbitration to proceed with the remaining panel.¹⁴⁵ In either case, further arbitration proceeded only with the consent or waiver of the parties.¹⁴⁶ In the absence of consent or waiver, the hearing had to start *de novo*.¹⁴⁷

Because this often resulted in a waste of time and effort, the section was recently amended to allow the hearings to continue before the

139. Uniform Code of Arbitration § 11, *infra* at 489-90 (Appendix B).

140. See SECOND REPORT, *supra* note 68, at A-5. For a lengthier discussion of disclosure requirements as they relate to the arbitrator, see *supra* notes 128-30 and *infra* notes 142-43 and accompanying text.

141. See THIRD REPORT, *supra* note 65, at C-5.

142. See SIXTH REPORT, *supra* note 49, at 7-8. As to a Code of Ethics for arbitrators, see *infra* notes 296-97 and accompanying text, and as to judges, see *infra* note 298.

143. See SIXTH REPORT, *supra* note 49, at 7-8. For discussion of conflict of interest see *infra* notes 283-317 and accompanying text.

144. Uniform Code of Arbitration § 12, *infra* at 490 (Appendix B).

145. See SECOND REPORT, *supra* note 68, at A-5, A-6.

146. *Id.*

147. See SIXTH REPORT, *supra* note 49, at 2.

remaining arbitrators when a vacancy occurs, unless one of the parties objects.¹⁴⁸ In the event of an objection, the Director shall appoint a new member to fill the vacancy.¹⁴⁹ The section as it presently stands preserves the requirements of background disclosure, as well as the right to challenge the new panel member.¹⁵⁰

*Section 13—Initiation of Proceedings*¹⁵¹

Initially this section set out the requirements for the commencement of an arbitration proceeding by setting out the general pleading and service requirements regarding such items as the statement of claim, submission agreement, answer, counterclaims and/or cross-claims and claims over.¹⁵² The section also permitted joinder and consolidation, which the Director of Arbitration would rule on initially, leaving the ultimate decision to the arbitration panel.¹⁵³

SICA subsequently tightened this section by permitting arbitrators to bar evidence at a hearing where only a general denial was pleaded, or where available defenses were not pleaded.¹⁵⁴ The authority to bar evidence at the hearing was further extended¹⁵⁵ to situations where a party fails to file a timely answer.

After *McMahon*, and largely for purposes of trimming costs, SICA amended Section 13 to require the parties to serve certain pleadings.¹⁵⁶ The arbitration staffs, however, continue to be responsible for serving the claim.¹⁵⁷ Thereafter, however, the parties will serve all other pleadings and file copies with the arbitration departments.¹⁵⁸ To aid this new procedure, Section 13(b) specifically permits service by mail.¹⁵⁹

After the issuance of the Sixth Report, SICA amended Section 13(d) into its present form. In changing the section, SICA revised subparagraph one to parallel the language of Federal Rule of Civil

148. *See id.* at 8.

149. *Id.*; *see also* Uniform Code of Arbitration § 12, *infra* at 490 (Appendix B).

150. *Id.*

151. Uniform Code of Arbitration § 13, *infra* at 490-94 (Appendix B).

152. *See* SECOND REPORT, *supra* note 68, at A-6, A-7.

153. *Id.*

154. *See* FOURTH REPORT, *supra* note 63, at C-5, C-6; *see also* Uniform Code of Arbitration § 13(c)(2)(i), *infra* at 491 (Appendix B).

155. *See* FIFTH REPORT, *supra* note 56, at 33-34; *see also* Uniform Code of Arbitration § 13(c)(2)(iii), *infra* at 492 (Appendix B).

156. *See* SIXTH REPORT, *supra* note 49, at 8-9; *see also* Uniform Code of Arbitration § 13(a), *infra* at 490-91 (Appendix B).

157. *Id.*

158. *Id.* § 13(c).

159. *Id.* § 13(b).

Procedure 20(a) on permissive joinders.¹⁶⁰ SICA also revised the second subparagraph of 13(d) to clarify the fact that multiple claimants may file together, eliminating the implication that filings must first be made separately and then joined; but, as to such jointly filed claims, the Arbitration Director is still authorized to sever such claims.¹⁶¹ However, SICA retained the Arbitration Director's right to consolidate separately filed claims in subparagraph three,¹⁶² as well as the proviso that arbitrators shall make all final determinations on all of these issues, in subparagraph four.¹⁶³

SICA has also studied the rather complex problem of class actions in arbitration and has concluded, for a variety of reasons—particularly the difficult problem of class determination—that court-ordered arbitration be a prerequisite for SRO acceptance of a class action matter.¹⁶⁴ Absent such court order, parties similarly situated could still avail themselves of the remedies of joinder and consolidation provided under the section.¹⁶⁵

*Section 14—Designation of Time and Place of Hearings*¹⁶⁶

This section originally provided that “[u]nless the law directs otherwise,” the Director of Arbitration determines the time and place for the initial hearing upon notice of at least eight business days; thereafter, the arbitrators would determine the time and place of hearings.¹⁶⁷ Subsequent to the Sixth Report, however, SICA has amended Section 14, eliminating the reference “unless the law directs otherwise.”¹⁶⁸ This was done so as to nullify selection of hearing provisions incorporated into brokerage contracts, thus preventing a member firm from unfairly controlling the selection of a hearing location, and thereby causing the customer to bear unreasonable expenses in pursuit of a claim.

*Section 15—Representation by Counsel*¹⁶⁹

This section, which has never changed, simply provides that all

160. *Id.* § 13(d)(1).

161. *Id.* § 13(d)(2); see also *infra* notes 276, 279-80 and accompanying text.

162. *Id.* § 13(d)(3).

163. *Id.* § 13(d)(4).

164. See 2 SEC. ARB. COMMENTATOR 9, at 7 (Sept. 1989); see also generally *Classwide Arbitration and 10(b)-5 Claims in the Wake of Shearson/American Express, Inc. v. McMahon*, 74 CORNELL L.R. 380 (1989).

165. See Uniform Code of Arbitration § 13(d), *infra* at 492-93 (Appendix B).

166. *Id.* § 14, *infra* at 493 (Appendix B).

167. See SECOND REPORT, *supra* note 68, at A-8.

168. See Uniform Code of Arbitration § 14, *infra* at 493 (Appendix B).

169. *Id.* § 15, *infra* at 493 (Appendix B).

parties have the right to representation by counsel.¹⁷⁰

*Section 16—Attendance at Hearings*¹⁷¹

Section 16 provides that except for parties and their counsel, the arbitrators decide the attendance or presence of other parties at the hearings. This section has not changed since the original Code.¹⁷²

*Section 17—Failure to Appear*¹⁷³

This section has provided since the original Code for a hearing to be held and an award rendered despite the fact that a party fails to appear after due notice was given.¹⁷⁴

*Section 18—Adjournments*¹⁷⁵

Originally, this section merely authorized arbitrators to grant adjournments.¹⁷⁶ Unfortunately, the issue of adjournments has become chronic. A horseback survey at several of the SROs revealed that approximately one-third of the cases heard have their first hearing date adjourned after the panel has already been appointed.¹⁷⁷ Furthermore, even this first adjourned date is often subsequently adjourned again one or more times before the first hearing is held.

Although most of the time, all the parties have agreed to these ad-

170. See SECOND REPORT, *supra* note 68, at A-8; see also Uniform Code of Arbitration § 15, *infra* at 493 (Appendix B).

171. *Id.* § 16, *infra* at 493 (Appendix B).

172. *Id.*; see also SECOND REPORT, *supra* note 68, at A-8. SICA recently amended the Arbitrator's Manual (see *infra* note 335) to add thereto a new paragraph dealing with the "Attendance of Witnesses at the Hearing." See Supplemental Text for the SICA Arbitrator's Manual, 2 SEC. ARB. COMMENTATOR 15 (Sept. 1989).

Arbitrators have the authority under the Uniform Code to determine who may attend the hearing. Sometimes there is a disagreement among the parties as to whether an expert witness should be permitted to attend the hearing sessions at times other than when he is testifying. Arbitrators should consider that expert witnesses often serve an important role in assisting parties and their counsel in the presentation of their cases, and also may be asked to testify about what has been said at the hearing in addition to the facts known to them prior to the hearing. Barring countervailing reasons, expert witnesses who are assisting parties in the presentation of their cases should be permitted to attend all hearings. Generally, there is a presumption that expert witnesses, as opposed to witnesses testifying as to the facts pertinent to the case, will be permitted to attend the entire proceedings.

Id.; see also Goldberg, *An Argument for Non Sequestration of Expert Witnesses*, 2 SEC. ARB. COMMENTATOR 1 (Apr. 1989).

173. Uniform Code of Arbitration § 17, *infra* at 493-94 (Appendix B).

174. *Id.*; see also SECOND REPORT, *supra* note 68, at A-8.

175. Uniform Code of Arbitration § 18, *infra* 494 (Appendix B).

176. See SECOND REPORT, *supra* note 68, at A-8.

177. Katsoris, *Adjournments, The Arbitration Virus*, 2 SEC. ARB. COMMENTATOR 2 (Jan. 1989) (hereinafter Katsoris IV).

journments, they have a crippling effect on the arbitration process. Often it results in having to replace arbitrators, who have already cleared the challenge and conflict processes,¹⁷⁸ because their schedules cannot accommodate the new adjourned date. This generally causes additional delay, because the SRO staff must then find a replacement arbitrator or arbitrators, who must then also clear the challenge and conflict hurdles *de novo*. Furthermore, such repeated cancellations discourage many excellent arbitrators from serving, either because it results in their replacement, or their having to set aside two or three dates before the first hearing is actually held.

Thus, these seemingly harmless adjournments undercut the two advantages of arbitration—speed and economy.¹⁷⁹ The more adjournments that are granted, the longer the day of resolution is delayed, and the more expensive it becomes to the parties and to the arbitration forum in administering the system.

This is not to suggest that legitimate requests for adjournments should not be granted. In fact, parties should be given the benefit of the doubt in this regard. However, the practice of seemingly automatic granting of adjournments, when both parties consent, is straining and undermining the legitimate goal of keeping arbitration speedy, economical and fair.

Before *McMahon*, SICA addressed this problem by amending Section 18.¹⁸⁰ Originally the section provided that if a party requested an adjournment (after the arbitrators have already been appointed) and the adjournment was granted, that party had to pay a fee equal to the deposit of costs, but not more than \$100.¹⁸¹ It became evident that this penalty was not a sufficient deterrent.¹⁸² Accordingly, *after* the Sixth Report SICA repealed the then subdivision (b) and replaced it with the following:

(b) [a] party requesting an adjournment after arbitrators have been appointed shall, if an adjournment is granted, deposit a fee, equal to the initial deposit of forum fees for the first adjournment and twice the initial deposit of forum fees, not to exceed \$1,000, for a second or subsequent adjournment requested by that party. The

178. See *supra* notes 134-50 and accompanying text; see also Uniform Code of Arbitration §§ 10, 11, 12, *infra* at 489-90 (Appendix B).

179. See *infra* notes 79-83 and accompanying text; see also Katsoris I, *supra* note 12, at 381.

180. See FIFTH REPORT, *supra* note 56, at 35.

181. *Id.*

182. The persistence of the issue of repeated adjournments became of great concern to SICA, which lead to a change in the rule. See Katsoris I, *supra* note 12, at 381.

arbitrators may waive the deposit of this fee or in their awards may direct the return of the adjournment fee.

(c) Upon receiving a third request consented to by all parties for an adjournment, the arbitrators may dismiss the arbitration without prejudice to the claimant filing a new arbitration.¹⁸³

In sum, this section articulates the important policy that adjournments be limited to those instances where they are truly necessary.¹⁸⁴ It would be ironic that after all the effort to improve the substance and image of securities arbitrations, the *virus* of unnecessary adjournments could sap its vitality and usefulness.¹⁸⁵

*Section 19—Acknowledgement of Pleadings*¹⁸⁶

Ever since the original Code, this section has required that the arbitrators acknowledge to all parties present that they have read the filed pleadings.¹⁸⁷

*Section 20—General Provisions Governing A Pre-Hearing Proceeding*¹⁸⁸

The present Section 20 contains the provisions of the original Code Sections 20 (Subpoena Process)¹⁸⁹ and 21 (Power to Direct Appearances).¹⁹⁰ Under those provisions the parties were expected to exchange documents informally as would "serve to expedite the arbitration."¹⁹¹ There was, however, no established mechanism to ensure that parties cooperate in document production. Accordingly, some parties did not produce documents until the day of the hearing. Such a practice was patently unfair.¹⁹²

Under their broad powers, arbitrators have always had the authority to resolve discovery disputes in advance of the hearing.¹⁹³ Indeed, even before *McMahon*, some SROs forwarded discovery disputes to arbitrators prior to hearings on the merits, giving the panel chairman

183. Uniform Code of Arbitration § 18(b)-(c), *infra* at 494 (Appendix B).

184. See Katsoris IV, *supra* note 177.

185. *Id.*

186. Uniform Code of Arbitration § 19, *infra* at 494 (Appendix B).

187. *Id.*; see also SECOND REPORT, *supra* note 68, at A-8.

188. Uniform Code of Arbitration § 20, *infra* at 494-96 (Appendix B).

189. See FIFTH REPORT, *supra* note 56, at 35.

190. *Id.*

191. *Id.*; see also Uniform Code of Arbitration §§ 20(f), 20(g), *infra* at 496 (Appendix B).

192. This forced the demanding party into the unenviable choice of proceeding with the hearing without having an adequate opportunity to examine the produced documents, or of seeking a delay from arbitrators who had planned to start the hearings on that day. It often resulted in trial by ambush.

193. See Katsoris I, *supra* note 12, at 372.

the authority to resolve discovery disputes in advance of the first hearing.¹⁹⁴ Some arbitrators, however, particularly those who were not attorneys, were reluctant to exercise such powers without specific authorization in the Uniform Code.

It became apparent after *McMahon* that the time had arrived to codify the informal practice of some SROs to get the arbitrators involved in discovery disputes *before* the first hearing. Accordingly, in addition to collapsing the old Sections 20 and 21 into the present Section 20, SICA added specific provisions relating to prehearing conferences and document and information production.¹⁹⁵

Under the new Section 20, a request for documents or information can be served as soon as twenty business days after service of the Statement of Claim.¹⁹⁶ If a party objects or fails to honor a request, a prehearing conference may be called to resolve the impasse.¹⁹⁷ Section 20 authorizes a sole arbitrator from the proposed panel to issue subpoenas and set deadlines for compliance with discovery orders.¹⁹⁸ These deadlines may fall prior to the hearing date. Prior to the initial hearing date, the new Section 20 also requires the parties to exchange witness lists and the documents that they intend to use in their direct case.¹⁹⁹ Finally, all parties to a dispute must now receive copies of any subpoenas issued.²⁰⁰

In practice, some of the pre-hearing discussions are held by conference call. Although this method is cheaper and more convenient, it is not always productive. In that case, the arbitrator overseeing the discovery should order a formal face-to-face hearing. The best hope for preventing these procedures from dragging out and increasing the cost of the litigation—as often happens in court proceedings—is to have experienced and knowledgeable arbitrators who will not let matters get out of hand.

The Uniform Code omits any reference to pre-hearing depositions.²⁰¹ However, the circumstances under which such depositions will be ordered by the arbitrators are discussed in the SICA Arbitra-

194. *Id.*

195. See SIXTH REPORT, *supra* note 49, at 2.

196. See Uniform Code of Arbitration § 20(b)(1), *infra* at 494-95 (Appendix B).

197. *Id.* § 20(b)(4); see also *Spiralling Discovery Costs Compel Amending Rule 26 and Adopting New Local Rule*, 22 N.Y. ST. B.A. REPORTS 3, at 20 (Trusts and Estates law section) (Fall 1989).

198. *Id.* § 20(e).

199. *Id.* § 20(c).

200. *Id.* § 20(f).

201. *Cf. id.* § 20.

tor's Manual.²⁰²

On the whole, the new procedures enhance rather than detract from the arbitration process. Admittedly, the new procedures under Section 20, which are also addressed in the Arbitrator's Manual, may initially involve some additional cost and time, but that is more than counterbalanced by the equitable consideration of preventing undue surprise and possible prejudice to either party once the hearing on the merits begins. In fact, the resolution of such disputes before the first hearing will often save time and expense at the hearing.

*Section 21—Evidence*²⁰³

Section 21 provides that the arbitrators determine the admissibility of evidence and in so doing are not bound by the Federal Rules of Evidence, or state evidentiary rules.²⁰⁴ Section 21 remains unchanged except that after *McMahon*, its number was changed from 22.²⁰⁵

*Section 22—Interpretation of the Code*²⁰⁶

Section 22 provides that arbitrators have the final authority to interpret the provisions of the Code, and remains unchanged except that after *McMahon*, its number was changed from 23.²⁰⁷

*Section 23—Determinations of Arbitrators*²⁰⁸

Section 23 provides that rulings and determinations of the panel

202. See *infra* note 337 and accompanying text. The Arbitrator's Manual was recently amended to include the following explanation regarding arbitrator's powers:

This includes the ability to issue orders for the production of witnesses for depositions when deemed appropriate by the arbitrators and where it is impossible to compel the attendance of the person to be deposed. Access to depositions should be granted to preserve the testimony of ill or dying witnesses, or of persons who are unable or unwilling to travel long distances for a hearing and may not otherwise be required to attend the hearing, as well as to expedite large or complex cases, and in other situations deemed appropriate by the arbitrator. Balanced against this ability, however, is a traditional reserve towards the overuse of depositions in arbitration. The effective use of discovery tools such as depositions rests in the careful exercise of judgment by the arbitrators. Care should be taken to avoid unnecessary expense or burdens to the parties and to avoid unnecessary delay. It is appropriate for arbitrators to consider whether the witness will be able to appear at the arbitration hearing, the necessity of preserving the witness' testimony, and other factors that bear on the efficiency and fairness of the proceeding.

See Supplemental Text for the SICA Arbitrator's Manual, 2 SEC. ARB. COMMENTATOR 15 (Sept. 1989).

203. Uniform Code of Arbitration § 21, *infra* at 496 (Appendix B).

204. *Id.*

205. See SIXTH REPORT, *supra* note 49, at 10.

206. Uniform Code of Arbitration § 22, *infra* at 496-97 (Appendix B).

207. See SIXTH REPORT, *supra* note 49, at 10.

208. Uniform Code of Arbitration § 23, *infra* at 497 (Appendix B).

shall be made by a majority of the panel.²⁰⁹ Aside from its number, which was 24 prior to *McMahon*, this section also remains unchanged.²¹⁰

*Section 24—Record of Proceedings*²¹¹

Before *McMahon*, this Section was numbered 25 and did not require that a record of the arbitration proceeding be kept.²¹² After *McMahon* the section was renumbered 24 and amended to require that a stenographic record or tape recording of all proceedings be kept.²¹³ This flexibility as to the method of recording takes into account the significant cost differential between a stenographic record and a tape recording. Nevertheless, in a multi-session proceeding spanning over a long period of time, the printed record is preferable, because it more easily enables arbitrators to refresh their recollection of past testimony.

*Section 25—Oaths of the Arbitrators and Witnesses*²¹⁴

Before *McMahon*, this was numbered Section 26.²¹⁵ Other than that, the section has always provided that the oath or affirmation shall be administered to the arbitrators before the first session and that all testimony shall be under oath or affirmation.²¹⁶

*Section 26—Amendments*²¹⁷

In the original Code, this was known as Section 27 and simply provided that amended pleadings would not be permitted after receipt of a responsive pleading without the consent of the arbitrators.²¹⁸ Before *McMahon*, however, the section was amended by setting up a procedure for amending pleadings—even after receipt of a responsive pleading—before the appointment of the arbitration panel.²¹⁹ The substance of this section has remained intact after *McMahon*, although it was renumbered Section 26.²²⁰

209. *Id.*

210. See SIXTH REPORT, *supra* note 49, at 10.

211. Uniform Code of Arbitration § 24, *infra* at 497 (Appendix B).

212. See FIFTH REPORT, *supra* note 56, at 36.

213. See SIXTH REPORT, *supra* note 49, at 11.

214. Uniform Code of Arbitration § 25, *infra* at 497 (Appendix B).

215. See FIFTH REPORT, *supra* note 56, at 36.

216. See SIXTH REPORT, *supra* note 49, at 11.

217. Uniform Code of Arbitration § 26, *infra* at 497 (Appendix B).

218. See SECOND REPORT, *supra* note 68, at A-10.

219. See FOURTH REPORT, *supra* note 63, at C-8.

220. See SIXTH REPORT, *supra* note 49, at 11.

*Section 27—Reopenings of Hearings*²²¹

Other than the recent number change from 28 to 27,²²² this section has since its inception permitted the reopening of hearings by the arbitrators on their own motion, or in the discretion of the arbitrators, upon application of a party at any time before the award is rendered.²²³

*Section 28—Awards*²²⁴

Prior to *McMahon*, this section was numbered 29 and basically provided that: (1) all awards had to be in writing and signed by a majority of the arbitrators; (2) all awards were deemed final and not subject to review or appeal; (3) arbitrators should endeavor to render the award within thirty business days from the date the record was closed; and (4) there are particular means by which the Director of Arbitration was to serve the award on the parties.²²⁵

After *McMahon*, Section 29 was renumbered Section 28, and SICA amended it to require that the award also include summary data, such as a description of the issues in controversy and the amounts claimed and awarded.²²⁶ This data is to be available to the public in accordance with the policies of the sponsoring SRO.²²⁷ Indeed, presently an outside vendor is publishing such awards.²²⁸

Even with these additional requirements, however, the section still falls short of requiring written opinions, *although arbitrators are free to do so*. At first blush, this may seem to be a weakness of the Code, and perhaps to some, a weakness of arbitration in general.²²⁹ The argument is that written opinions should be required, because they would give insight to the parties as to the rationale for the award. In addition, it would help the parties in formulating opinions about arbitrators with a view to exercising their peremptory challenges.

On the other hand, *requiring* written opinions would certainly slow down the rendering of awards, for awards are often arrived at on the basis of consensus.²³⁰ For example, suppose there are three arbitra-

221. Uniform Code of Arbitration § 27, *infra* at 498 (Appendix B).

222. See SIXTH REPORT, *supra* note 49, at 11.

223. See SECOND REPORT, *supra* note 68, at A-10.

224. Uniform Code of Arbitration § 28, *infra* at 498 (Appendix B).

225. See FIFTH REPORT, *supra* note 56, at 36-37.

226. See SIXTH REPORT, *supra* note 49, at 11.

227. *Id.*

228. See 2 SEC. ARB. COMMENTATOR 6-7 (Award Report) (June 1989); see also SEC. ARB. COMMENTATOR 2-7 (Award Report) (Oct. 1989). Indeed, some awards are being analyzed and commented upon. *Id.* at 8-10.

229. See Katsoris I, *supra* note 12, at 382.

230. *Id.*

tors, A, B & C, and they found damages of \$10,000, \$20,000 and \$30,000, respectively, and they ultimately agree on a \$20,000 award. When they write the opinion, however, A bases his award on unsuitability, B on churning and C on unauthorized trading. Can A, B and C issue an award for \$20,000, even though they cannot agree on the reasons? Moreover, would they?

Written opinions would not necessarily enhance the cause of fairness.²³¹ In some instances mandatory opinions might even result in fewer awards in favor of claimants on general equity grounds.²³² It would also put additional pressure on the already strained staffs of the administering forum while drafts of written opinions would be circulated and recirculated among the various arbitrators for corrections, redrafts and finalization.²³³

In addition, it is respectfully submitted that instead of being used as a window into the rationale of arbitrators, a written opinion will be used as a platform and blueprint for many more appeals, because it identifies targets, meaningful or otherwise, for the losing party to attack. Appeals are both costly and time consuming and ultimately result in undue delay in the payment of any award.²³⁴

231. *Id.* at 383.

232. *Id.*

233. *Id.*

234. The scope of judicial review of an arbitration award is very limited. Goldberg, *A Supreme Court Justice Looks at Arbitration*, 20 ARB. J. 63 § 6.03 at 61 (1965), [hereinafter *Supreme Court Justice*]. "If the award is within the submission, and contains the honest decision of the arbitrators, after a full and fair hearing of the parties, a court of equity will not set it aside for error, either in law or fact." *Burchell v. Marsh*, 58 U.S. 344, 349 (1854). In fact, the typical grounds for vacating an arbitration award are surprisingly uniform throughout the United States, namely:

- (1) There was an undisclosed relationship between an arbitrator and a party or his counsel affecting the arbitrator's impartiality or appearance of impartiality.
- (2) An arbitrator was corrupt.
- (3) The arbitrators did not schedule or conduct the hearing in a fair and judicious manner.
- (4) The arbitrators granted relief that they were not authorized to grant under the contract pursuant to which the arbitration was held.

See *Supreme Court Justice*, *supra*, § 6.03 at 63; see also § 10 of the United States Arbitration Act, 9 U.S.C. § 10 (1982); see also B. N. Smiley, *Stockbroker-Customer Disputes: Making A Case For Arbitration*, 23 GEORGIA STATE BAR J. 195 (1987).

The greatest advantage of arbitration is that awards are almost irreversible.

This is perhaps its greatest peril as well. . . . An award which has a legal or factual basis which may be rationally inferred from the evidence will be upheld.

Arbitration awards will not be set aside for a mistake of law unless the arbitrators have acted in 'manifest disregard' of the law.

Id. at 200 (footnote omitted) (emphasis added). For an award to be vacated on this ground, "[t]he error must have been . . . readily and instantly perceived by the average person qualified to serve as an arbitrator." *Merrill Lynch, Pierce Fenner & Smith v.*

Undue delay is particularly injurious to the small investor, who may have an immediate need for the money. Indeed, SICA was concerned that some dealers unduly delayed payment of awards issued against them. Accordingly, *after* the Sixth Report, Section 28 was further amended by adding subdivisions (g) and (h) thereto, which provide:

- (g) In addition, arbitrators may award interest as they deem appropriate. All awards shall bear interest from the date of the award until payment at the legal rate, if any, then prevailing in the state where the award was rendered, or at a rate set by the arbitrator(s) in the award.
- (h) All monetary awards shall be paid within thirty (30) days of receipt unless a motion to vacate has been filed with a court of competent jurisdiction.²³⁵

At one point, SICA considered the inclusion of a bond or escrow requirement in the Uniform Code to insure such prompt payment.²³⁶ Instead, SICA abandoned the bond or escrow idea because it was unduly burdensome, and merely settled on the aforementioned thirty day rule.²³⁷ This payment requirement is a distinct advantage over court-litigated awards or those issued at the AAA, which has no disciplinary authority over the dealer.²³⁸

Bobker, 808 F.2d 930, 933 (2d Cir. 1986). "Moreover, the term 'disregard' implies that the arbitrator appreciates the existence of a clearly governing legal principle but decides to ignore or pay no attention to it." *Id.* (citing *Bell Aerospace Co. Div. of Textron v. Local 516, United Auto Workers of Am.*, 356 F. Supp. 354, 356 (W.D.N.Y. 1973), *rev'd on other grounds*, 500 F.2d 921 (2d Cir. 1974)). SICA did consider broadening the scope of review of securities arbitration awards. See Minority Report of Mortimer Goodman, Public Member Security Industry Conference on Arbitration, *In Respect of a Right of Review of an Arbitration Award* (filed with the SEC on Dec. 15, 1977) (available at Fordham Urban Law Journal office). The proposal was rejected as inimical to the simplicity and brevity of arbitration procedures. See Uniform Code of Arbitration, § 28b, *reprinted in* SIXTH REPORT, *supra* note 49. It is also interesting to note that the American Arbitration Association (see *infra* note 369) does not encourage written opinions. See Coulson, Securities Arbitration at the American Arbitration Association, Securities Arbitration 1989, PLI Seminar 683, at 696 [hereinafter Coulson]. Moreover, in an attempt to wean written opinions, it has recently been suggested that such requests be accompanied by an undertaking that the award would not be challenged. See 2 SEC. ARB. COMMENTATOR 7 (May 1989); see also *Challenging Securities Industry Arbitration Awards*, N.Y.L.J., Feb. 16, 1990 at 1, col. 1.

235. See Uniform Code of Arbitration § 28(g), (h), *infra* at 499 (Appendix B); see also 2 SEC. ARB. COMMENTATOR 12 (June 1989).

236. A stricter 20 day rule with an escrow provision was, however, approved by the Municipal Securities Rulemaking Board. See § 31 MSRB Rules of Arbitration, *reprinted in* Arbitration Information & Rules, Municipal Securities Rulemaking Book (1989), at 30 (available at the Fordham Urban Law Journal).

237. *Id.*

238. The NASD, however, is proposing to include the AAA in its resolution authoriz-

The issue of punitive damages and treble damages under the Racketeer Influenced and Corrupt Organization Act (RICO),²³⁹ in arbitration, which are punitive in nature, have also presented a problem. Indeed, of late, the problem has become more urgent because they are with greater frequency pleaded as alternative relief in statements of claim.²⁴⁰ In any event, if an award was made either for punitive damages or under RICO it should be so stated separately in the award.²⁴¹

The *McMahon* decision clearly recognized the arbitrability of RICO claims.²⁴² Much discussion has been generated, however, over whether RICO should be restricted or abolished—not just in securities arbitration, but civil litigation generally.²⁴³ The overall merits of permitting RICO allegations in securities arbitration are questionable. Such claims are routinely pleaded, but seldom proven, and yet the

ing discipline for non-payment of an award. See NASD 19-b-4 Proposed Rule Change, File No. SR-NASD-89-47, Amendment No. 1 at 12 (hereinafter NASD 19-b-4).

239. 18 U.S.C. §§ 1962-1964 (1982). Treble damages are allowed under a RICO claim. See generally Abrams, *Civil RICO's Cause of Action: The Landscape After Sedima*, 12 TULANE MAR. L. J. 19 (1988) [hereinafter Abrams]; see also Katsoris I, *supra* note 12, at 368 n.52.

240. See generally *supra* notes 151-55 and accompanying text.

241. See Morris, *Arbitration At The New York Stock Exchange*, SECURITIES ARBITRATION PRACTICE AND PROCEDURE 95, 119 (Nov. 17, 1989) (available at Fordham Urban Law Journal office).

242. See Katsoris I, *supra* note 12, at 368.

243. See *Rico v. Rico* (Editorial) Wall St. J., Dec. 14, 1989, at A22, col. 1; *RICO's Taxing Problem*, Wall St. J., Aug. 22, 1989, at A14, col. 3; *RICO: The Law as Thug* (Letter to Editor) Wall St. J., Nov. 13, 1989, at A1, col. 1; *Uncertain Future For RICO Cases, Business and the Law*, N.Y. Times, Nov. 13, 1989, at D2, col. 1; *High Powered Bid to Gut RICO Law Is Derailed By Unrelated Scandals, Backers' Seeming Greed*, Wall St. J., Nov. 9, 1989, at A18, col. 1. It is interesting to note the following *pro* and *anti* RICO lobbies:

For Proposed RICO limits:

- * National Association of Manufacturers
- * AFL-CIO
- * American Civil Liberties Union
- * American Institute of Certified Public Accountants
- * American Bar Association
- * American Bankers Association
- * Securities Industry Association
- * American Life League (anti-abortion group)
- * Defendants in pending civil RICO cases

Against proposed RICO limits:

- * Public Citizen (Ralph Nader consumer group)
- * U.S. Public Interest Research Group (state consumer groups)
- * National Association of Insurance Commissioners
- * National Association of Attorneys General
- * National Association of Securities and Commercial Law Attorneys (plaintiffs' lawyers)
- * Plaintiffs in pending RICO cases.

Id.

mere allegation clearly bogs down the arbitration proceeding.²⁴⁴ For that reason, the application of RICO in securities matters should be narrowed, leaving punishment, the goal of treble damages, to be doled out in the form of punitive damages and SRO discipline.

The issue of the awardability of punitive damages, however, is in itself problematic. There are those who argue that arbitrators cannot award punitive damages, citing cases such as the New York Court of Appeals' decision in *Garrity v. Lyle Stuart, Inc.*,²⁴⁵ particularly when the arbitration agreement contains a New York choice of law provision.²⁴⁶ If arbitration is to be a viable alternative to court litigation, however, it cannot be used as a procedure to strip claimants of remedies. Accordingly, punitive damages should be uniformly allowed, albeit in a *national* system of SRO arbitration, so as to eliminate the inequitable effect of some choice of law provisions.²⁴⁷ On the other hand, if such restrictive provisions become common practice, and are given effect by the courts, then the issue of *adhesion* in the context of pre-dispute arbitration agreements should be reexamined by the courts.²⁴⁸

Section 29—Agreement to Arbitrate²⁴⁹

This section (previously numbered 30 and captioned "Miscellane-

244. As to the complexities of RICO, see generally *Abrams*, *supra* note 239.

245. 40 N.Y.2d 354, 353 N.E.2d 793, 386 N.Y.S.2d 831 (1976). The New York Court of Appeals held that an arbitrator had no power to award punitive damages. "The law does not and should not permit private persons to submit themselves to punitive sanctions of the order reserved to the [s]tate." *Id.* at 360, 353 N.E.2d at 797, 386 N.Y.S.3d at 834.

246. I.e., a provision in an agreement that says New York law applies. See *Punitive Damages: On Trial*, 2 SEC. ARB. COMMENTATOR 4 (Feb. 1989). Even in the New York federal courts, where *Garrity* "remains the home state's rule, the cases are divided." *Id.*

247. See Stipanowich, *Punitive Damages in Arbitration: Garrity v. Lyle Stuart, Inc. Reconsidered*, 65 B.U.L. REV. 953 (1986); D. Robbins, A Practitioner's Guide To Securities Arbitration, Securities Arbitration 1989, PLI seminar at 183. But see *Volt Information Serv. Inc. v. Board of Trustees of the Leland Stanford Junior Univ.*, 109 S. Ct. 1248 (1989). In *Volt*, the Supreme Court recognized a choice of law clause providing that the contract would be governed by the law of "the place where the [p]roject is located." *Id.* at 1251 (citation omitted); see also *Punitive Damages—What are the Limits?*, 2 SEC. ARB. COMMENTATOR 7 (Aug. 1989).

248. See *Katsoris II*, *supra* note 16, at 306-09; see also *supra* note 28. Moreover, in view of the *Volt* decision, *supra* note 247, it is uncertain what effect the amendment to § 31 of the Code (see *infra* notes 260-68)—which prohibits any limitation upon the arbitrators' ability to make any award—will have upon clauses prohibiting punitive damages. In the final analysis, it may have to be Congress that effects a trade-off in securities arbitration by limiting RICO claims in exchange for a *national* recognition of punitive damages awards.

249. Uniform Code of Arbitration § 29, *infra* at 499 (Appendix B).

ous")²⁵⁰ was renumbered 29 after *McMahon*,²⁵¹ but has remained virtually unchanged since its inception. It simply incorporated the Code *by reference* into every duly executed *submission agreement*, which shall be binding on all parties.²⁵² After the Sixth Report, however, SICA amended Section 29, changing the title from "Miscellaneous" to "Agreement to Arbitrate," and extending the automatic incorporation of the Code to *agreements to arbitrate*.²⁵³ Thus, the present section ensures that a party who does not sign a submission agreement is still bound by the provisions of the Uniform Code.²⁵⁴

*Section 30—Schedule of Fees for Customer Disputes*²⁵⁵

Section 30 (previously numbered 31)²⁵⁶ provided for the schedule of fees in customer disputes. These fees have varied since the original Code. After *McMahon* the section was amended to specifically define a hearing session.²⁵⁷ Furthermore, the section now allows the arbitrators to award additional costs beyond hearing session charges in their decisions.²⁵⁸ After the Sixth Report, SICA further amended Section 30(e) so that it now also provides: "[i]n any matter settled or withdrawn within [eight] business days prior to the first scheduled hearing session, the SRO may retain the amount deposited as forum fees or a portion thereof. This section shall not apply to [small] claims filed under Section 2 of this Code."²⁵⁹

*Section 31—Requirements When Using Pre-Dispute Arbitration Agreements With Customers*²⁶⁰

This section is new to the Code.²⁶¹ It provides that any pre-dispute arbitration clause be highlighted and immediately preceded by certain disclosure language that describes arbitration and its effect.²⁶² The impetus behind this addition was legislative pressure to render unenforceable pre-dispute arbitration clauses.²⁶³

250. See SECOND REPORT, *supra* note 68, at A-11.

251. See SIXTH REPORT, *supra* note 49, at 11.

252. See FIFTH REPORT, *supra* note 56, at 36-37.

253. See SIXTH REPORT, *supra* note 49, at 11; see also Uniform Code of Arbitration § 29, *infra* at 499 (Appendix B).

254. *Id.*

255. *Id.* § 30.

256. See FIFTH REPORT, *supra* note 56, at 37-38.

257. See SIXTH REPORT, *supra* note 49, at 11-12.

258. *Id.*

259. Uniform Code of Arbitration § 30(e), *infra* at 500 (Appendix B).

260. *Id.* § 31.

261. See SIXTH REPORT, *supra* note 49, at 12.

262. See Uniform Code of Arbitration § 31(1), *infra* at 500-01 (Appendix B).

263. See *supra* notes 50-51 and accompanying text; see also Hoblin II, *supra* note 22, at 52-57 (Supp. 1988). California had proposed a statute that would restrict arbitration

This SICA rule also provides that immediately preceding the signature line there shall be a statement, which shall be highlighted and *separately initialed* by the customer, that the agreement contains a pre-dispute arbitration clause.²⁶⁴ Despite approval by SICA, no SRO has approved this requirement as to *separate initialling*.²⁶⁵ Consequently, such a requirement does not appear in their arbitration rules. This is regrettable, because from the point of view of the customer and the broker, separate initialling more clearly calls the arbitration clause to the customer's attention. Moreover, an initialling requirement would likely reduce the amount of litigation based upon the customer's lack of awareness of the clause.

What makes the industry response to Section 31 even more puzzling is that in inserting this requirement, SICA never intended that failure to initial would *void* any agreement to arbitrate. On the contrary, violations would only result in *possible* disciplinary action against the offending broker. Furthermore, in order to prevent the insertion of restrictive clauses in customers' agreements that would conflict with the provisions of the Code, Section 31 also specifically *prohibits* conditions that *limit or contradict the rules of the SROs*, or *limit the ability of a party to file any claim in arbitration or limit the ability of the arbitrators to make any award*.²⁶⁶

Since Section 31 is new, it includes a grandfather clause, which states that the requirements of the section shall apply only prospectively to new agreements signed by an existing or new customer after 120 days have elapsed from the date of SEC approval of the rule.²⁶⁷ Thus, a broker-dealer who thereafter attempts to limit contractually a customer's right to select any of the available SROs, might be subject to disciplinary action by any SRO that has adopted Section 31, of which it is a member.²⁶⁸

C. The SRO Codes

The Uniform Code of Arbitration represents a major step in the development of securities arbitration as a fair, economical and expeditious dispute resolution process. It also represents a significant effort

(McCorguodale Committee), and that Committee agreed that if SICA adopted disclosure rules comparable to theirs, they would withdraw the proposal. *Id.* As SICA did adopt the disclosure rules, the proposal was presumably withdrawn. *Id.*

264. See SIXTH REPORT, *supra* note 49, at 12.

265. For a comparison of different SROs, see *infra* at 502-03 (Appendix C).

266. See SIXTH REPORT, *supra* note 49, at 12.

267. *Id.*; see also Uniform Code of Arbitration § 31(5), *infra* at 501 (Appendix B).

268. For an example of such disciplinary authority, see NASD Code of Procedures, Art. IV, § 1, in NASD Manual, (CCH) ¶ 3049, at 3151.

to make the SRO securities arbitration rules uniform throughout the country.

A chart which generally tracks the Code provisions into the separate code sections of the various SROs is attached to this Article as Appendix C.²⁶⁹ It should be noted, however, that once SICA adopts a new rule, each SRO must then generally go back to their respective organization in order to get a rule change which is then usually submitted to the SEC for approval.²⁷⁰ Accordingly, there is often a time lag between SICA approval and SRO action, with the result that the SRO codes do not always mirror the SICA Code.²⁷¹

Adding to the confusion are inconsistencies that exist between the various SROs regarding implementation or interpretation of the SICA rules. For example, the NYSE uses one arbitrator when the amount of the claim involves \$10,000 or less, whereas the NASD has adopted a one arbitrator rule in claims up to \$30,000.²⁷² Another example is the different application of award collection procedures.²⁷³ The general rule requires an award to be paid within thirty days, with no escrow provision, while the MSRB cuts that down to twenty days and imposes escrow features.²⁷⁴ Still another example is the order of closing arguments. The ASE and the NYSE procedures provide that the claimant closes last, whereas the NASD provides for the claimant to close first.²⁷⁵ Yet another inconsistency in SRO procedures is the handling of consolidation and joinder. Some SROs will accept a joinder at the time of filing, with the objecting party then moving to sever, while one SRO required that separate claims be filed, with the parties then moving to consolidate.²⁷⁶ In addition, the form of the award

269. See *infra* at 502-03 (Appendix C).

270. See Katsoris I, *supra* note 12, at 364.

271. See *infra* at 502-03 (Appendix C).

272. See *supra* notes 92-97; see also Wynn, *Seminar Highlights: "Securities Arbitration Update,"* SEC. ARB. COMMENTATOR 7 (Oct. 1989).

273. See Uniform Code of Arbitration § 28, *infra* at 498 (Appendix B).

274. See *supra* notes 235-38 and accompanying text.

275. See Arbitration at the American Stock Exchange, Appendix D, SECURITIES ARBITRATION 1989 at 621; see also *When Naivete Meets Wall Street*, N.Y. Times, Dec. 3, 1989, § 3 (Business), at 1, col. 4 [hereinafter *When Naivete Meets Wall Street*].

As for the NASD's shift, Peter R. Cella, a New York lawyer who serves on an industry arbitration oversight panel, condemned the move, which enables brokerages to offer summaries of their cases last. He said it is 'a radical departure' from the common law practice, which gives the last word to the party with the burden of proof, in this case, the investor." *Id.* at 6, col. 5.

276. See Hoblin I, *supra* note 19, at 4 n.5. But see SICA's recent amendment to subdivision (d)(2) of the Uniform Code of Arbitration § 13, *supra* note 161 and accompanying text.

varies among the SROs.²⁷⁷ Finally, because each SRO experiences differing budget constraints, separate fee schedules may surface in an attempt to close the deficit gap.²⁷⁸

These inconsistencies²⁷⁹ can lead to confusion or forum shopping, and to the extent possible, should be eliminated, because such differences defeat the goal of uniformity that SICA sought to accomplish in creating the Code.²⁸⁰

IV. The Arbitrators

The task of achieving a *level playing field* would be unfinished without focusing on the quality and integrity of the arbitrators who administer it. Indeed, even the slightest *appearance* that the deciding panels were "stacked" in favor of the securities industry would render the present system of securities arbitration useless. It is for this reason securities arbitrators have come under so much scrutiny over the past few years.

We must understand, at the outset, that good arbitrators do not grow on trees. Similarly, they are also not potted plants. Thus, in weighing the practicality of many of the suggestions discussed above regarding arbitration procedure, consideration must also be given as to whether they discourage intelligent, honest and knowledgeable arbitrators from serving.²⁸¹ Such consideration is especially urgent in light of the continuing need to recruit and retain the large numbers of competent arbitrators essential in order to staff hearings at locations dispersed throughout the country.²⁸²

Certainly, an arbitrator must be capable and honest. To fashion such a profile, however, we must also examine such relevant and related areas as conflicts of interest, training, and evaluation of performance during the course of an arbitration.

277. See HOBLIN II, *supra* note 22, at 53-78; see also *supra* notes 224-28 and accompanying text.

278. See NASD 19-b-4, *supra* note 238, at 12-16; see also *infra* note 399.

279. By the time this article is published, one or more of these inconsistencies may have been eliminated; however, so long as there are separate SRO programs, the potential for differing interpretations and procedures exists.

280. See *supra* notes 63-66.

281. As was alluded to above in the discussion at § 18 of the Code pertaining to adjournments, procedural abuses such as multiple adjournments inhibit the retention of a capable pool of arbitrators. See *supra* notes 175-89 and accompanying text; see also Katsoris I, *supra* note 12, at 380-81.

282. See D. Lipton Study, 1 SEC. ARB. COMMENTATOR 5 (June 1988). "The size of the arbitrator pools range from about 15 in small cities to more than 500 in major urban areas. Prospective arbitrators are recommended to the Director of Arbitration and ultimately approved by an oversight committee of the SRO." *Id.*

A. Conflicts of Interest

The SICA Procedures Booklet provides that arbitrators are to be impartial persons who are knowledgeable in the areas in controversy.²⁸³ Each sponsoring organization maintains a roster of individuals who are not employees of the sponsoring organization but whose professional qualifications and experience qualify them for service as arbitrators.²⁸⁴ The Uniform Code of Arbitration specifically provides that unless the public customer requests otherwise, the matter will be arbitrated by a panel "at least a majority of whom shall not be from the securities industry,"²⁸⁵ i.e., are public arbitrators.²⁸⁶

The Code also safeguards the level playing field through provisions that are common to all classifications of arbitrators.²⁸⁷ These provisions are intended to offer parties an opportunity to challenge panel members not to their liking²⁸⁸ and to insure that arbitrators are free from conflicts of interest.²⁸⁹ In furtherance of this goal, the Code contains disclosure requirements which seek to make challenges more informed and have conflicts of interest issues surface early.²⁹⁰

The selection of arbitrators at SRO forums does not employ the so-called *tri-partite* system where basically each party picks an arbitrator and the two appointees pick a third. Instead, the SRO forums pick the arbitration panels,²⁹¹ consisting of both the public as well as the industry arbitrators. As mentioned previously, the classification of an

283. See PROCEDURES BOOKLET, *supra* note 65, at 3.

284. *Id.*

285. See Uniform Code of Arbitration § 8, *infra* at 487-88 (Appendix B). It has been suggested that arbitration panels should consist *only* of public members. See *SIA, NASAA Split Over Fairness of Securities Arbitration Procedures*, Sec. Reg. & L. Rep. (BNA) No. 20, at 870 (June 10, 1988); *Seeking 'Fairness' in Brokers' Disputes*, N.Y. Daily News, June 26, 1988, at 10 (Business), col. 1). The principal problem with this suggestion, is that in eliminating arbitrators affiliated with the securities industry, it would also eliminate sources of invaluable insight into the workings of the securities industry from the arbitration panels. In addition, the adoption of such exclusionary rule would undoubtedly be perceived by the industry as stacking the deck in favor of the investors. This is particularly significant, because if the industry loses faith in the feasibility of arbitration, it is likely that the industry would seek to avoid its use. If avoidance of arbitration became the rule and not the exception, the interests of public investors would generally not be well served. See, e.g., the discussion of the additional costs and time required in resolving disputes via litigation, *supra* notes 16, 79-83 and accompanying text.

286. See *supra* notes 116-24 and accompanying text.

287. See Uniform Code of Arbitration §§ 9-12 *infra* at 488-90 (Appendix B). For a discussion of these sections, see *supra* notes 125-50 and accompanying text.

288. See *supra* notes 134-38 and accompanying text.

289. See *supra* notes 139-43 and accompanying text.

290. *Id.*

291. Morris, *Arbitrator Assignment—The Case for Agency Selection*, 2 SEC. ARB. COMMENTATOR 1, 3 (Feb. 1989).

arbitrator as industry or public is basically a mechanical test.²⁹² Once classified and so selected, however, the distinction between industry and public disappears. From that point on, both have a similar duty to hear and decide the controversy fairly and with an open mind.²⁹³ In this context, both must be free from bias and prejudice as well as any circumstances evidencing a conflict of interest.²⁹⁴

Disqualification for bias or prejudice may occur when the arbitrator, through overt acts, has shown he is unable to render a fair decision. Disqualification for conflicts of interest, however, is more apt to be based upon the premise that in spite of no overt act of wrongdoing, the arbitrator *may* not be objective in his judgment because of his conflicting interest. Consequently, the standard of such disqualification for conflict is not always crystal clear. To avoid subsequent problems, disclosure of potential conflicts should be made early and promptly, and it is precisely for this reason that the disclosure rules of the Code seek early disclosure and notification.²⁹⁵ Moreover, if there is any doubt whether to disclose or not, it is wisest to disclose.

It is often difficult to determine when a present or prior relationship creates a conflict which should disqualify an arbitrator from sitting on a panel. The circumstances may vary and often hinge on a question of degree and judgment. An excellent beginning is the Code of Ethics for Arbitrators in Commercial Disputes,²⁹⁶ which provides:

arbitrators 'should err on the side of disclosure' because 'it is better that the relationship be disclosed at the outset when the parties are free to reject the arbitrator or accept him with knowledge of the relationship.' At the same time, it must be recognized that 'an arbitrator's business relationships may be diverse indeed, involving more or less remote commercial connections with great numbers of people.' Accordingly, an arbitrator 'cannot be expected to provide the parties with his complete and unexpurgated business biography,' nor is an arbitrator called upon to disclose interests or rela-

292. See *supra* notes 115-24 and accompanying text.

293. Uniform Code of Arbitration §§ 9, 10, 11 and 12 apply to all arbitrators in the same way. See *supra* notes 125-50 and accompanying text. Only § 8, the selection rule, distinguishes between public and industry arbitrators. See *supra* notes 115-24 and accompanying text.

294. See Uniform Code of Arbitration § 11 *infra* at 489-90 (Appendix B); see also *supra* notes 139-43 and accompanying text.

295. See the Uniform Code of Arbitration §§ 9, 11 *infra* at 488-90 (Appendix B); see also *supra* notes 125-33, 139-43 and accompanying text.

296. CODE OF ETHICS FOR ARBITRATORS IN COMMERCIAL DISPUTES [hereinafter CODE OF ETHICS]. This code was created by a Joint Committee consisting of a Special Committee of the American Arbitration Association and a Special Committee of the American Bar Association in 1977. See Coulson, *Securities Arbitration at the American Arbitration Association*, SECURITIES ARBITRATION 1989, PLI SEMINAR 683, 723.

tionships which are merely 'trivial.'²⁹⁷

As helpful as the statement is, it may still be unclear as to when its application would disqualify an arbitrator for having an interest or relationship that is likely to affect impartiality, or that might create an appearance of partiality or bias.

As a starting point, it might seem appropriate to ascribe to arbitrators the same standards applied to judges²⁹⁸ because both decide cases

297. Canon II, CODE OF ETHICS, *supra* note 296, at 7 (quoting *Commonwealth Coalings Corp. v. Continental Casualty Co.*, 393 U.S. 145, 151-52 (1968)).

298. The conduct of judges is largely governed by the American Bar Association's Canons of Judicial Ethics, which was adopted by Congress when it set down the standard for disqualification of federal judges. *See* 28 U.S.C. § 455 (1982). The statute provides in pertinent part:

- (a) [a]ny justice, judge, or magistrate of the United States shall disqualify himself in any proceeding in which his impartiality might reasonably be questioned.
- (b) He shall also disqualify himself in the following circumstances:
 - (1) Where he has a personal bias or prejudice concerning a party or personal knowledge of disputed evidentiary facts concerning the proceeding;
 - (2) Where in private practice he served as lawyer in the matter in controversy, or a lawyer with whom he previously practiced law served during such association as a lawyer concerning the matter, or the judge or such lawyer has been a material witness concerning it;
 - (3) Where he has served in governmental employment and in such capacity participated as counsel, adviser or material witness concerning the proceeding or expressed an opinion concerning the merits of the particular case in controversy;
 - (4) He knows that he, individually or as a fiduciary, or his spouse or minor child residing in his household, has a financial interest in the subject matter in controversy or in a party to the proceeding, or any other interest that could be substantially affected by the outcome of the proceeding;
 - (5) He or his spouse, or a person within the third degree of relationship to either of them, or the spouse of such a person;
 - (i) Is a party to the proceeding, or an officer, director, or trustee of a party;
 - (ii) Is acting as a lawyer in the proceeding;
 - (iii) Is known by the judge to have an interest that could be substantially affected by the outcome of the proceeding;
 - (iv) Is to the judge's knowledge likely to be a material witness in the proceeding. . . .
- (d) For the purposes of this section the following words or phrases shall have the meaning indicated . . .
 - (4) "financial interest" means ownership of a legal or equitable interest, however small, or a relationship as director, adviser, or other active participants in the affairs of a party, except that:
 - (i) ownership in a mutual or common investment fund that holds securities is not a (financial interest) in such securities unless the judge participates in the management of the fund; . . .
- (e) No justice, judge, or magistrate shall accept from the parties to the pro-

brought before them. Unlike full-time judges, however, arbitrators are usually only part-time arbitrators. Indeed, they spend most of their time in other occupations, often in the same industry or trade involved in the litigation.²⁹⁹ In addition, the judicial forum is furnished by the government itself, and therefore presumably it is neutral. In contrast, SRO arbitrations are conducted at a forum which is supported by the securities industry itself,³⁰⁰ thus leading many public claimants to perceive it with greater concern and suspicion.

Because of these fundamental differences between SRO arbitration and courtroom litigation, the standards as to securities arbitrators would appear to be, and indeed should be stricter. For example, a judge who was a former prosecutor for a good part of his life, would not necessarily be precluded from presiding over a criminal case; but in SRO securities arbitration, the majority of the arbitrators must *not* be from the securities industry.³⁰¹ For some, the taint of former securities involvement could disqualify them as a public arbitrator forever.³⁰² Moreover, even the spouse of an industry person usually does not qualify as either a public or securities arbitrator,³⁰³ whereas a judge would not generally be disqualified from banking cases merely because his spouse is employed at an unrelated bank.

It is difficult under any circumstance, however, to reconcile arbitration ethics with judicial ethics, which permits both the trial and appellate judges to hear cases presented by attorneys who made substantial contributions to their election campaigns.³⁰⁴ If such conduct oc-

ceeding a waiver for any ground for disqualification enumerated in subsection (b). Where the ground for disqualification arises only under subsection (a), waiver may be accepted provided it is preceded by a full disclosure on the record of the basis of disqualification.

28 U.S.C. 455 (1982).

The language in § 455 is nearly identical to the language of Canon 3(C) of the Code of Judicial Conduct, entitled Disqualification, S. GILLERS & N. DORSON, REGULATION OF LAWYERS: PROBLEMS OF LAW AND ETHICS 597 (§ VIII(f)) (1985) [hereinafter S. GILLERS]. Beyond § 455, 28 U.S.C. § 144 requires district court judges to recuse themselves in the event of personal bias or prejudice against or in favor of any party. 28 U.S.C. § 144 (1982); GILLERS, *supra*, at 597.

299. Roughly one-third of SRO public securities arbitration panels consist of industry arbitrators. See *supra* notes 115-21.

300. See *supra* notes 52-78.

301. See *supra* note 116 and accompanying text.

302. See *supra* note 124 and accompanying text.

303. *Id.*

304. See *U.S. Orders Texas to Restructure the Way Its Judges are Elected*, Wall St. J., Nov. 11, 1989, at B6, col. 2; see also *The Plaintiff Attorney's Great Honey Rush*, Forbes, Oct. 16, 1989, at 197, 199.

Where judges are elected, the role of the plaintiff attorneys has become notorious: campaign contributions. In Texas, the fundraising drive supported by Joe

curred in SRO arbitration, however, there would be a Congressional inquiry, and rightly so.

Although a stricter standard is clearly warranted in the case of SRO arbitrators, some relationships are so obscure that even disclosure of a relationship is ridiculous. For example, if an arbitrator shops at Sears, he should not have to reveal that if he sits on a case where Dean-Witter is a party.³⁰⁵ Similarly, if he has an American Express card, he should not be compelled to reveal that, if he arbitrates a dispute involving Shearson.³⁰⁶ Such revelations would be ludicrous. Otherwise, an SRO arbitrator would turn into a recluse who could speak or interact with no one. Such a result would be wholly impractical, and only another recluse would want such an arbitrator. In essence, it is necessary to avoid requirements of disclosure and disqualification that are so extreme that they discourage or eliminate otherwise capable arbitrators.

What then should be revealed, and when should that result in disqualification? Although reasonable people may differ and conclusions might vary depending on differing circumstances, a few *personal* observations and judgments seem appropriate.³⁰⁷

1. Relationship with Parties or Their Attorneys

An arbitrator should not sit on a case involving his own firm or close relative as a party. Similarly, an arbitrator should not sit on a case involving a present client as a party. In a case involving a prior client, the arbitrator should be presumed biased, but disqualification would ultimately depend upon surrounding circumstances.³⁰⁸

Another potentially problematic situation is when a public arbitrator has a small securities account with a large brokerage house which is appearing before him. This is close, but it is probably not a case for automatic disqualification, because prejudice or bias could go either way in such a relationship. The relationship, however, should certainly be revealed, and as a practical matter, most SRO Arbitration

Jamail and Pat Maloney (\$6 million) was so successful that, according to one Texas attorney, 'until last year the plaintiff bar owned and controlled the Texas Supreme Court.' Maloney is confident that 1988's election reversal will be corrected in 1990: '[w]e are resilient, and we will bounce back.'

Id.

305. Dean Witter is a subsidiary of Sears.

306. Shearson is a subsidiary of American Express.

307. These observations are largely the product of experience as a public arbitrator. Consequently, they are for the most part given without supporting footnotes.

308. The presumption is that a person who was once a client, is always a potential client.

Directors would wisely avoid the issue and not appoint the arbitrator in such a case.

More troublesome is the situation where an attorney sits as an arbitrator in one case, and then subsequently represents claimants or respondents before other panels at the same SRO. This is somewhat akin to a sitting judge appearing before his fellow judges. Certainly attorneys who also sit as securities arbitrators should avoid appearing before arbitrators with whom they have served as fellow arbitrators on previous cases. In any event, that fact should certainly be disclosed.

A somewhat related situation was involved in *Jenkins v. Sterlacci*,³⁰⁹ where an attorney (X) was representing a litigant against another who was represented by a particular law firm (Y), and Y was also representing a different party in a totally unrelated proceeding in which X was the special master.³¹⁰ Thus, in relation to the other law firm, X served as both an adversary and an adjudicator. After noting that a substantial question was raised whether the special master should have been disqualified on the basis that these activities raised the "appearance" of a conflict of interest, the court concluded that based on other facts in the case, such objection had been waived.³¹¹

Finally, the cumulative effect of isolated relationships can also become problematical. An example would be if an arbitrator and one of the parties had gone to the same grade school, belonged to the same golf club, took the same commuting train every morning, belonged to the same church and worked for the same conglomerate. In such a case, clearly the wisest course would be for the arbitrator to excuse himself and sit on another case.

Even though there is an endless variety of conflicts of interest, securities arbitrators should not be paranoid. After all, not every relationship results in disqualification. The arbitrator can disclose the relationship, and then independently determine whether to disqualify himself. In addition, following disclosure, the parties may choose not to object and allow the arbitrator to continue to sit on their case. In sum, disqualification is not always automatic.

2. Relationship with Witnesses

Before leaving this topic, it should also be pointed out that similar compromising relationships can also surface (although not as often)

309. 849 F.2d 627 (D.C. Cir. 1988); see also *Suite Sharing, Arbitrator's Friendship With Winning Lawyer Imperils Huge Victory*, Wall St. J., Feb. 14, 1990, at A1, col. 1.

310. *Jenkins v. Sterlacci*, 849 F.2d 627, 629-30.

311. *Id.* at 630-34.

between an arbitrator and a witness of one of the parties. This troublesome connection should be avoided. For example, if used only as a character or expert witness, the burden of finding another one would be less objectionable than removing the arbitrator. Thus, a balancing of the equities would not seem to dictate the removal of the arbitrator in such a situation. On the other hand, if a fact witness is involved, the result will depend on how vital that testimony is: if it is only duplicative and superfluous, then the arbitrator should remain;³¹² if, however, that witness's testimony is absolutely essential, then serious consideration must be given to removing the arbitrator. Fortunately, however, the new SICA rules provide for the filling of such a vacancy and letting the arbitration proceed.³¹³

Accordingly, at the time the parties consider whether to challenge an arbitrator³¹⁴ they should discuss with their witnesses the possibility of a witness/arbitrator conflict. If one exists, it is best for all concerned that it surface and be dealt with early in the arbitration process.

3. Other Conflicts

Recently, an interesting form of conflict has cropped up in situations where an arbitrator—either in pre-hearing proceedings³¹⁵ or during the hearing³¹⁶—must examine sensitive material, *in camera*, with a view to whether it should be produced or admitted into evidence. After such inspection and ruling of non-production or inadmissibility, a challenge is then often asserted against the arbitrator who conducted the inspection on the ground that his mind has already been poisoned by the excluded materials he has examined. Unless the arbitrator felt he could not thereafter be impartial, however, such motion for disqualification should normally be denied.³¹⁷

312. Whether the witness testifies depends on the circumstances, but it would probably be wisest for the offering party to get the opposition's consent.

313. See *supra* notes 148-50 and accompanying text.

314. See *supra* notes 134-38 and accompanying text.

315. See *supra* notes 188-202 and accompanying text.

316. See *supra* notes 203-05 and accompanying text.

317. Judges continue to sit in such situations all the time, and we should expect no less of arbitrators as to their ability to proceed impartially thereafter. In addition, if an arbitrator had to be replaced in every such situation, it would render arbitration virtually useless as an effective means of resolving disputes, for it would mean that in most arbitrations, at least one new arbitrator would have to be appointed in the course of the arbitration. This would of course greatly increase the length of time required for the completion of the arbitration, resulting in an escalation in costs.

B. Evaluation of Arbitrators

It is the obligation of the SROs to recruit, train and retain a diversified pool of competent arbitrators.³¹⁸ This requires some sort of evaluation process so as to enable the SRO to weed out arbitrators who may not be performing well. It should be done, however, in a dignified and professional manner so as not to intimidate, insult or otherwise embarrass sitting arbitrators.³¹⁹ The evaluation process should also not become a popularity contest initiated by parties who may be either jubilant or disgruntled after an award.

Before *McMahon*, this evaluation process was done informally by the SRO staffs. After *McMahon*, SICA undertook to expand the process by involving a broader spectrum of input. SICA decided on a three-pronged evaluation, which includes: (1) evaluations done by the party/representatives; (2) evaluations by the arbitrators' peers on the panel; and (3) evaluations by the SRO staffs.³²⁰ To be meaningful, however, each of these evaluations must be administered under differing conditions and with correspondingly different safeguards. For example, it is preferable that the party/representative evaluations be made *before* an award is rendered.³²¹ In the case of peer review, it was concluded it would best be done *after* the award was rendered.³²² As for the SRO staff review, SICA decided that it could be done at any time during the course of arbitration.³²³

The purpose of the program is to evaluate arbitrators with a view toward ensuring that the roster of arbitrators only includes highly qualified individuals.³²⁴ Accordingly, since the data contained in these evaluations is often sensitive, it should be reviewed only by senior members of the SRO staffs, and used exclusively in aid of the

318. A national SRO such as the NYSE has thousands of arbitrators. It obtains their names from bar associations, community groups, and existing arbitrators. Others are referred by securities organizations or governmental agencies. Generally, the arbitrators are grouped by city and are asked to serve in a major commercial center close to their home or business. Only rarely is an SRO arbitrator asked to travel. See Morris, *Arbitrator Assignment—The Case for Agency Selection*, 2 SEC. ARB. COMMENTATOR 2 (Feb. 1989).

319. The key is that we do not want to discourage good, capable arbitrators from serving. See, e.g., *supra* notes 175-85, 281-82 and accompanying text; see also Katsoris I, *supra* note 12, at 376-81.

320. 2 SEC. ARB. COMMENTATOR 1, 4 (Nov. 1989).

321. In that way, the evaluations are likely to be less partisan, because they will not be tainted by the emotion of victory or defeat.

322. The peer evaluations are most informative when they take into account observations made throughout the arbitration including the deliberative process.

323. Staff must make their evaluations whenever they can, because unlike peers, they do not sit in on deliberations, and are often absent from the hearings.

324. See generally Katsoris I, *supra* note 12, at 379-80.

administration of the arbitration departments. The evaluations, therefore, will not be available to the parties, because public disclosure would be counter-productive in that it would discourage many fine arbitrators from serving, and could even invite defamation litigation.³²⁵ Moreover, public disclosure of the evaluations would surely lead to appeals³²⁶ on the ground that a particular arbitrator should not have been appointed because *some* of his evaluations were mediocre or poor. In any event, the SRO evaluation performance is not without safeguards—it is subject to the oversight of the SEC.³²⁷

C. Training of Arbitrators

Prior to the *McMahon* decision, the typical securities arbitration claim involved churning, unauthorized trading or unsuitability.³²⁸ Subsequently, arbitrators have often had to resolve complex claims involving Section 10(b) of the 1934 Act and related rules,³²⁹ treble damages under RICO³³⁰ and punitive damages.³³¹ In addition, arbitrators have to rule on such thorny pre-hearing issues as discovery, arbitration preclusion, *res judicata*, collateral estoppel, joinder, severance and consolidation.³³² It is imperative, therefore, that arbitrators receive more extensive training, especially since in the future, more and more arbitrations will probably be conducted without a staff administrator present.³³³

Positive steps have been taken to ensure that arbitrators are able to live up to the high expectations that have been placed on them by investors. In this regard both of the two largest SROs, the NASD and the NYSE, have held arbitration training sessions.³³⁴ In addition, sig-

325. *Id.* at 381.

326. For a discussion of appeals, see *supra* note 234.

327. For a discussion of SEC oversight, see *infra* notes 370-74 and accompanying text.

328. See Katsoris I, *supra* note 12, at 379.

329. See generally Thel, *The Original Conception of Section 10(b) of the Securities Exchange Act*, 42 STAN. L. REV. 385 (1990).

330. See generally Abrams, *supra* note 239, at 41-45.

331. For a discussion of punitive damages in the context of arbitration, see *supra* notes 245-48 and accompanying text; see also generally, Shell, *ERISA and Other Federal Employment Statutes: When is Commercial Arbitration an Adequate Substitute For the Courts?*, 68 TEX. L. REV. 3 (1990).

332. The issue of joinder and consolidation raises the difficult question of whether the possibility of substantial prejudice arising from such consolidation or joinder outweighs the "time and expense involved in separate actions or the possibility of conflicting awards." Stipanowich, *Arbitration and the Multiparty Dispute: the Search for Workable Solutions*, 72 IOWA L. REV. 473, 489-90 (1987).

333. See Morris, *Arbitration At The New York Stock Exchange*, SECURITIES ARBITRATION PRACTICE AND PROCEDURES SEMINAR 114 (Nov. 17, 1989) [hereinafter Morris].

334. See Masucci, *supra* note 120, at 143; see also SIXTH REPORT, *supra* note 49, at 2-

nificant contributions toward arbitrator training have come in the form of publications. A news letter specifically dedicated to the subject of securities arbitration is already in print.³³⁵ Other publications dealing with arbitration are also available.³³⁶

Perhaps the most significant publication for arbitrator training has been SICA's Arbitrator's Manual (Manual)³³⁷ which was developed to instruct arbitrators concerning their duties and responsibilities. As is boldly set out in its preface, the Manual was solely designed to be a *guide* for arbitrators, supplementing and explaining the Uniform Code.³³⁸ After much debate within SICA, the text of the document was carefully chosen so as to be instructive and yet fair. Any such undertaking, however, creates an attractive target for criticism by competing advocates.

Despite such clear admonition that the Manual was not intended to *restrict* a panel's discretion, it has already been criticized as an SRO Manual having an industry bias.³³⁹ Such criticism ignores the reality that it is a SICA product, not an SRO effort. Furthermore, the Manual is merely intended to be a general guide for people whose skills vary, whether they are the new arbitrator on the block, or an attorney who may be highly skilled and trained in litigation procedures. Admittedly, the Manual is a product of consensus, yet on balance, it is an excellent, worthwhile starting point in the training process. Moreover, the Manual is not cast in stone, and SICA has agreed to amend it on a continuing basis, as the need arises.

More still needs to be done, however, in the area of arbitrator training. For example, several lecture series could be offered to arbitrators throughout the country on numerous topics ranging from a basic arbitration procedures course for new inexperienced arbitrators, to one on substantive law involved in complex claims such as RICO and Section 10(b). Lecture series would also be a very good way to keep arbitrators abreast of the latest developments in arbitration through periodic update programs. These lectures could be taped or delivered

3; Masucci & Morris, *Arbitration at the NASD and the NYSE*, 1989 SECURITIES ARBITRATION, PLI SEMINAR 437, 448. [hereinafter Masucci & Morris].

335. The Securities Arbitration Commentator. (The publication, not any specific issue).

336. See BNA Alternate Dispute Resolution Report; BNA Securities Regulation and Law Report.

337. THE ARBITRATOR'S MANUAL (1989) [hereinafter Arbitrator's Manual] (available at Fordham Urban Law Journal office); see also Masucci & Morris, *supra* note 334, at 477, and ARBITRATOR'S MANUAL, 2 SEC. ARB. COMMENTATOR 8 (May 1989).

338. *Id.*

339. See R. Dyer, *The SRO Arbitrator's Manual: an Opening Inquiry, Do the SROs Show an Industry Bias?* 2 SEC. ARB. COMMENTATOR 1 (Aug. 1989).

live and beamed by satellite to various locations throughout the country to accommodate the widely dispersed pool of arbitrators. This type of lecture format has been used quite successfully by the American Law Institute's Continuing Legal Education program³⁴⁰ on a wide range of subjects.

Unfortunately, this additional training is burdened by both good news and bad. The good news is that there will be a better trained pool of arbitrators more able to cope with the increasingly complicated cases that are resolved through arbitration. The bad news is that the training will be expensive, and thus may increase the cost of arbitration for the various SROs.³⁴¹

D. Arbitrators' Confessions

Under the new Code,³⁴² arbitrators are scrutinized both as to ability and background.³⁴³ They are carefully selected, classified and evaluated, and then they may be challenged.³⁴⁴ Their awards are subject to public scrutiny so that parties can get a sense of each arbitrator's voting record and leanings.³⁴⁵ All these safeguards are constructive and have their usefulness.

On the other hand, all of these procedures must be viewed in perspective, for they can lead to a misleading and unfair impression. First of all, many awards, whether by juries, judges or arbitrators, are a result of some consensus or compromise. This, of course, makes an

340. See Fordham Law School Bulletin 1989-90, at 61. Fordham Law School is a charter affiliate of the American Law Network. *Id.* As the bulletin instructs:

the American Law Network is a joint effort on the part of the American Law Institute and the American Bar Association to provide continuing legal education programming to members of the American Bar. Courses are conducted by prominent legal scholars and transmitted via satellite to TV monitors at the Law School. This program enables practitioners the opportunity to gain valuable insights on major issues from scholars around the country. Alumni receive brochures during the year informing them of our programs. This year almost 2,000 attorneys attended our programs.

Id.

341. For a discussion on the escalating cost of arbitration, see *infra* notes 397-401 and accompanying text. It is important to note that in the absence of SRO or other subsidization, such training will never be fully implemented because the arbitrators can not be expected to pay for this training. Aside from any financial hardship, such payment would only seem to discourage capable persons from serving as arbitrators.

342. See UNIFORM CODE OF ARBITRATION, *infra* at 484 (Appendix B).

343. See *id.* § 11, *infra* at 489-90 (Appendix B); see also *supra* notes 139-43 and accompanying text.

344. See Uniform Code of Arbitration § 10, *infra* at 489 (Appendix B); see also *supra* notes 134-38 and accompanying text.

345. See Uniform Code of Arbitration § 28 *infra* at 498 (Appendix B); see also *supra* notes 226-28 and accompanying text.

accurate reading of each participant more difficult. Secondly, to characterize an arbitrator as *pro-public* or *pro-industry* based upon such awards does a disservice to the ideal that all arbitrators, public or industry, are neutral and decide only on the oral and written evidence. Suppose one arbitrator sat on *ten* consecutive cases where there was clearly no valid claim; yet, another sat on *ten* consecutive cases where there clearly was a claim—what would one expect their respective “paper” records to be? In the final analysis, the only true test of an arbitrator’s mettle is to check the “record” of each proceeding and not merely the “paper” score. Admittedly, such a process is much more laborious, but it is fairer and gives a truer reading of the arbitrator’s abilities and impartiality.

Arbitrators are human, however, and consciously or unconsciously, they may be influenced by their running “paper” record. To what extent would the ruling in a close case in favor of a public claimant, influence that arbitrator’s decision in the next case, if it also happened to be close? The answer is the prior ruling should not influence the arbitrator, but no one will ever know. Therefore, arbitrators should be reminded that each case is separate and that they must consciously forget about their paper record to do justice in each individual case.

In addition, whether they sit at an SRO forum(s), the AAA, or both,³⁴⁶ the arbitrators are by and large honest and decent people, and for that reason should not allow themselves to be intimidated. They should not be intimidated by criticism from industry counsel merely because punitive damages were awarded, or from the plaintiff’s bar simply because the award was much less than what was requested. If punitive damages are called for,³⁴⁷ then they should be assessed, and if the facts require an award that is only a small percentage of the amount claimed, that should be the amount of damages granted.³⁴⁸ If arbitration is to succeed as an alternative dispute resolution process, the particular partisan interests or complaints of the parties must remain irrelevant to the arbitrator’s decision. Accordingly, I would like to propose³⁴⁹ an Arbitrator’s Creed, as follows:

346. Many of the same arbitrators sit at more than one forum—including the AAA.

347. See *Recent Punitive Damage Awards*, 2 SEC. ARB. COMMENTATOR 6 (May 1989).

348. See *When Naivete Meets Wall Street*, *supra* note 275, at 6. Interestingly, a recent limited study indicated that claimants did better in arbitration. See Letter of J. E. Buck to Hon. David S. Ruder Oct. 14, 1988 (cited in *HOBBLIN II*, *supra* note 22, at § 2-12, 5-6).

349. This author has sat as a public arbitrator on approximately 150 SRO arbitrations over the last 20 years. Over that time, I have dissented in only two awards. I have *agonized* over some decisions, but upon reflection, I would not change even one such award. I do not keep a running record on myself, and in fact, I try to cleanse my mind of all previous cases when assigned to a new one.

- 1) I shall read and become familiar with the Code of Ethics for Arbitrators.³⁵⁰ I will disclose any conflict of interest which might possibly be perceived as having an effect on my judgment, and I will disqualify myself if such a conflict clearly jeopardizes the perceived fairness of the proceedings.
- 2) I will not be intimidated by partisan threats or criticisms.
- 3) In reaching my decision, I will exercise the necessary care that reflects the reality that for all intents and purposes the award will be the final word on the subject.
- 4) I will look upon each new case without concern for my "paper" voting record, and do justice in each case as though it was the only one I will ever sit on.

E. Consideration for the Arbitrator

Until this point, the focus of this Part has centered for the most part on what is required of the arbitrator. Much has been discussed about the necessary, yet sometimes intrusive inquiries regarding the arbitrator's ability, experience, background and conflicting relationships.³⁵¹ In addition, arbitrators are evaluated,³⁵² and expected to undergo training, if necessary.³⁵³ Furthermore, it is assumed they will conduct themselves in an impartial, fair and courteous manner. In addition, in many instances, their compensation is significantly less than that earned in their other activities.³⁵⁴ Overall, therefore, it is reasonable to describe their participation in the securities resolution process as the rendition of a public service.

Accordingly, it is not unreasonable that arbitrators should expect and are entitled to receive a certain minimum standard of conduct on the part of those that appear before them. It would seem appropriate, therefore, to briefly discuss conduct and decorum of attorneys involved in securities arbitration, because their conduct clearly affects the quality of the *playing field* over which the arbitrators preside.

As has been noted above with respect to adjournments³⁵⁵ and pre-hearing procedures,³⁵⁶ it is crucial that counsel for the parties not

350. See *supra* notes 296-97 and accompanying text.

351. See *supra* notes 283-97 and accompanying text.

352. See *supra* notes 318-27 and accompanying text.

353. See *supra* notes 328-41 and accompanying text.

354. Indeed, because SRO arbitrators are usually paid by the number of hearing sessions held, this imbalance does not take into consideration the many uncompensated hours often expended in reading papers before or after such sessions. Nor does it account for the considerable inconvenience caused by repeated adjournments. See *supra* notes 175-85 and accompanying text.

355. See *supra* notes 175-85 and accompanying text.

356. See *supra* notes 188-202 and accompanying text.

abuse these procedures and thereby excessively delay the proceedings.³⁵⁷ Delay undermines the principal characteristics of arbitration, i.e., speed, economy and ultimately even fairness. Therefore, the lawyers' conduct does indeed have a direct effect on the degree to which the playing field is level. Thus if the arbitration process is to operate at its best, the lawyers should honor prior commitments to arbitration with the same degree of respect and concern as they would court dates.³⁵⁸ To do otherwise is a disservice to the parties and to the arbitrators.³⁵⁹

Unfortunately, as the number of arbitrations has grown,³⁶⁰ as the complexity of the cases has increased,³⁶¹ and as the pre-hearing procedures are put into operation,³⁶² arbitration increasingly resembles courtroom litigation in tactics and techniques. Thus, it is clearly reasonable to require standards of conduct appropriate in the context of the courtroom. In that regard, the Texas Supreme Court and the Court of Criminal Appeals recently adopted the "Texas Lawyer's Creed—A Mandate for Professionalism" (Texas Creed).³⁶³ It provides, in part, that lawyers should endeavour not only to achieve the lawful objectives of their clients, but to achieve them as quickly and economically as possible, and in the process, to exercise civility, courtesy, fairness and due consideration with regard to the other parties and counsel involved.³⁶⁴ The Texas Creed also emphasizes that the

357. See Katsoris I, *supra* note 12, at 381.

358. See *id.*

359. *Id.*

360. See *supra* notes 77-78 and accompanying text.

361. See *supra* notes 328-32 and accompanying text.

362. See *supra* notes 188-202 and accompanying text.

363. *For The Record*, N.Y. Times, Dec. 1, 1989, at B7, col. 4.

364. The Texas Creed provides in pertinent part:

Our Legal System

I am passionately proud of my profession. Therefore, "My word is my bond."

I am responsible to assure that all persons have access to competent representation regardless of wealth or position in life.

I commit myself to an adequate and effective pro bono program.

Lawyer to Client

... I will endeavor to achieve my client's lawful objectives in legal transactions and in litigation as quickly and economically as possible . . .

I will advise my client that civility and courtesy are expected and are not a sign of weakness. . . .

I will treat adverse parties and witnesses with fairness and due consideration. A client has no right to demand that I abuse anyone or indulge in any offensive conduct.

I will advise my client that we will not pursue conduct which is intended

conduct of the lawyers should be ethical, professional and respectful of the justice system and its administrators.³⁶⁵ Finally, the Texas Creed emphasizes many factors such as speed, economy and fairness, all of which are of fundamental importance in arbitration. Indeed, *the Texas Creed should also be applicable to arbitration*.³⁶⁶ After all, not only the arbitrators, but the parties themselves must be conscious of the effect of their actions on the arbitration process, for they too contribute to the ultimate success or failure of the level playing field.

V. The Arbitration Forum

A. The Present Forums: the SROs and the AAA Alternative

In the aftermath of the *McMahon* decision, most unsettled disputes between a public customer and his broker are resolved in arbitration.³⁶⁷ The result has been that over 6,000 arbitration cases were

primarily to harass or drain the financial resources of the opposing party

...
I will advise my client regarding the availability of mediation, arbitration and other alternative methods of resolving and settling disputes.

Lawyer to Lawyer

I will be courteous, civil and prompt in oral and written communications.
I will not quarrel over matters of form or style, but I will concentrate on matters of substance. . . .

I disagree without being disagreeable. I recognize that effective representation does not require antagonistic or obnoxious behavior. I will neither encourage nor knowingly permit my client or anyone under my control to do anything which would be unethical or improper if done by me. . . .

Lawyer and Judge

I will always recognize that the position of judge is the symbol of both the judicial system and administration of justice. I will refrain from conduct that degrades this symbol.

I will conduct myself in court in a professional manner and demonstrate my respect for the court and the law. . . .

I will be punctual.

Id.

365. *Id.*; see also *How's Your Lawyer's Left Jab?* Newsweek, Feb. 26, 1990, at 70, col. 1.

366. Indeed, what if an attorney's conduct in an SRO arbitration proceeding exceeded the legitimate bounds of heated advocacy? If the client aided, abetted, or joined in such misconduct, the arbitrators should be able to dismiss the claim (with or without prejudice) or make other disposition of the matter, depending on *all* the circumstances. Also, in the case of the attorney, the matter could be brought to the attention of the appropriate bar association for disciplinary inquiry. Finally, it would appear that an SRO has the *inherent* right to protect the forum and its participants from abusive conduct by denying that attorney the right to thereafter practice before that SRO. Stark as such a measure might be, discretionary abuse is unlikely to occur because the SROs, as well as their arbitrator forums are subject to the SEC's oversight and regulatory authority.

367. See *supra* notes 46-51 and accompanying text.

filed in 1988 with the participating SROs.³⁶⁸ In addition, nearly 500 securities cases were also filed in 1988 with the American Arbitration Association (AAA).³⁶⁹

The AAA is a not-for-profit organization offering a broad range of dispute resolution services throughout the United States.³⁷⁰ Significantly, unlike the SRO forums, the AAA is not under the SEC's regulatory authority. Partly because of this independence from regulatory supervision, most arbitration clauses in customers' agreements until recently only provided for arbitration before one or more SRO forums.³⁷¹ With greater frequency, however, pre-dispute arbitration clauses have increasingly included the AAA as an alternative forum. This is largely due to action by the SEC and the Securities Industry Association (SIA). Adding the AAA as a forum in arbitration agreements was one of the SEC's recommendations in its September 10, 1987 letter to SICA.³⁷² The SIA at the behest of the SEC and SICA, asked member broker-dealers to consider including the AAA as an alternative forum in customers' agreements.³⁷³ The SIA has also included the AAA in its model customers' agreement.³⁷⁴

The growing popularity of having an AAA alternative to SRO arbitration appears to be based on several factors. From the SEC's point of view, the AAA option appears to provide constructive competition for the SROs, and in addition, the AAA acts as a "safety valve" for the backlogged SRO forums.³⁷⁵ For the SIA, the AAA alternative undermines the contention that the public is being forced into an industry sponsored forum and thus enhances the perceived fairness of the arbitration process.³⁷⁶ From the perspective of the public investors, an AAA option is an alternative which should exist as a matter of right.³⁷⁷

In spite of the considerable interest in the AAA as an alternative

368. See *supra* note 78 and accompanying text.

369. See Coulson, *supra* note 234, at 697.

370. See Morris, *supra* note 333, at 106.

371. See *id.* at 105-6; Grundfest, Fitterman, McGuire, Love, *SEC Initiatives in SRO Arbitration*, 1989 SECURITIES ARBITRATION, PLI SEMINAR 355, 361. Significantly, only 27% of all broker-dealer forums presently include the AAA in their pre-dispute arbitration clauses. Ryder, 1988: *The Year in Review*, 1989 SECURITIES ARBITRATION PRACTICE AND PROCEDURE 41, 43 [hereinafter Ryder].

372. See *supra* note 70 and accompanying text.

373. See 1 SEC. ARB. COMMENTATOR 2 (Dec. 1988).

374. See Ryder, *supra* note 371, at 43.

375. *Id.*; see also NASD Backs Single Arbitration Forum; SEC Says Penny Stock Complaints Rose, 22 Sec. Reg. & L. Rep. 6 at 191, Feb. 9, 1990 [hereinafter Single Forum Backed].

376. *Id.*

377. "If you can't give customers a choice of litigation or arbitration, at least give

forum, some within the industry continue to resist the AAA.³⁷⁸ However, even when the parties have not inserted the AAA into an arbitration clause, securities cases have also found their way into AAA arbitration through the so-called "AmEx window."³⁷⁹

The name AmEx window describes the process through which the American Stock Exchange (ASE) provides a potential "window" for investors to arbitrate before the AAA.³⁸⁰ The ASE Constitution provides that a customer may arbitrate with a member organization before the AAA in the City of New York, "*unless the customer has expressly agreed, in writing, to submit only to the arbitration procedures of the Exchange*" (waiver provision).³⁸¹ Thus, unless the waiver provision applied, claimants wishing to utilize the AAA could seek to do so despite having signed an arbitration agreement that does *not* provide for AAA as a forum of choice.³⁸²

The unfortunate use of the term "Exchange" in the waiver provision, however, has led to confusion as to how open the AmEx window is.³⁸³ If the customer is deemed to have waived his right to AAA arbitration *only* if he agreed to be bound solely by ASE arbitration procedures, then the "window" is wide open. Because few agreements are so restrictive, the customer would have the option to pursue arbitration before the AAA. On the other hand, if the term "Exchange," as used in the waiver provision includes other exchanges or SROs (as is usually the case), the opposite result is likely to occur. In that case, the "window" is open only slightly and only in a few instances will the arbitration end up before the AAA. The interpretation that will prevail is far from certain because lower court decisions seem split on the subject.³⁸⁴ The ASE has moved to clarify the issue by amending its constitution by replacing the word "Exchange" with

them the choice of a neutral forum' grumbled Robert Dyer, an attorney in Orlando, Fla." *When Naivete Meets Wall Street*, *supra* note 275, at 6.

378. See Ryder, *supra* note 371, at 43. As noted above, few broker-dealer firms presently include the AAA in their pre-dispute agreements, see *supra* note 371; see also 1 SEC. ARB. COMMENTATOR 4(b).

379. See Ryder, *supra* note 371, at 42.

380. *Id.*; see also *ASE Rule Mandates AAA Arbitration*, 1 SEC. ARB. COMMENTATOR 3 (May 1988).

381. See ASE CONSTITUTION Art. VIII, § 2 (emphasis added).

382. See Ryder, *supra* note 371, at 43.

383. *Id.* "The AmEx Window cases are the . . . most numerous representatives of a new litigation genre . . ." *Id.*

384. See *AmEx Window A Foggy Outlook*, 2 SEC. ARB. COMMENTATOR 6 (Mar. 1989); see also "*AmEx Window*": *Shutting Down?*, 2 SEC. ARB. COMMENTATOR 4 (June 1989). But see *Cowen & Company v. Jeffrey Anderson*, N.Y.L.J., Nov. 6, 1989, at 22, col.5 (N.Y. App. Div., 1st Dep't).

the words *securities industry self-regulatory organizations*.³⁸⁵ Such a change would have the effect of closing the AmEx window because it would expand the application of the waiver provision.

In the end, only time will tell whether the AAA will garner a larger share of securities arbitration.³⁸⁶ The fate of securities arbitration before the AAA depends on many factors. For one thing, it appears that AAA costs are higher than those of SRO arbitration.³⁸⁷ Moreover, just as *some* of the public is leery of SRO arbitration, *some* in the securities industry are equally hesitant about AAA arbitration. Nevertheless, despite the cost disadvantage, broker-dealer resistance and the fact that the AAA is not subject to SEC oversight, the SEC, at least for now, appears to favor the present system, with the ongoing competition between the AAA and SRO forums as opposed to a separate independent forum under SEC oversight.³⁸⁸ Ultimately, the determining factor may be the perceptions of public investors.³⁸⁹

B. A New Independent Forum

The subject of an independent forum was raised by the public members of SICA long before *McMahon*.³⁹⁰ Indeed, SICA was seriously

385. See, *When Naivete Meets Wall Street*, *supra* note 275; *Amex Moves to Close Arbitration 'Window,'* Investor's Daily, Dec. 19, 1989, at 1, col. 4; see also *Wall Street's Arbitration System: Friend or Foe?*, N.Y. Times, Dec. 24, 1989, § 3 (Business), at 12, cols. 5-6 (letters to editor by K. Leibler and T. Eppenstein).

386. In 1988, the AAA had nearly 500 securities case filings, well up from previous years. See Ryder, *supra* note 371, at 43-44.

387. See Morris, *supra* note 333, at 113-14; see also T. Kavalier, Seminar Highlights: "Securities Arbitration Update," 2 SEC. ARB. COMMENTATOR 9 (Oct. 1989). Moreover, unlike SRO arbitration the parties in AAA arbitrations pay the arbitrator's fees and other expenses incurred by the arbitrators or the AAA's representatives, thus making AAA arbitration even costlier than SRO proceedings. See Rules 48, 49 and 50 of AAA Securities Arbitration Rules (effective Sept. 1, 1987), reprinted in HOBLIN II, *supra* note 22, at XIV-16; see also Masucci & Morris, *supra* note 334, at 448 (indicating that SRO arbitrators are paid an honorarium by the SROs themselves, *not* the parties).

388. See *supra* notes 367-77 and accompanying text.

389. Although recently there has been a significant increase in filings, see Ryder, *supra* note 371, at 43-49, the AAA's caseload is still significantly less than that at the SRO filings. See *infra* at 483 (Appendix A). As noted earlier, there are several reasons for this, namely industry resistance, see *supra* note 378 and accompanying text, the failure to include the AAA in the pre-dispute arbitration clauses, see *supra* note 371 and accompanying text, the lack of SEC oversight, see *id.*, and the additional costs associated with the AAA, see *supra* note 387 and accompanying text.

390. See Statement of Constantine N. Katsoris before the Securities & Exchange Commission (Dec. 8, 1977) (available at Fordham Urban Law Journal office):

[t]o insure . . . public investments we must retain the public's confidence—confidence in the markets themselves and confidence that should a dispute arise, it will be fairly resolved. This confidence, however, can only be earned by maintaining a *de facto* as well as a *de jure* image of fairness. In other words, the procedural rules must be fair and the administration of the forum must be ob-

considering such a forum before *McMahon*.³⁹¹ However, because of the disenchantment of the SEC, the disagreement among the SROs, and the presence of the AAA alternative, the concept of a separate independent forum went into hibernation until recently, when it received the support of the SIA.³⁹² SICA has recently endorsed a study of the feasibility of an independent forum, as well as other alternatives, focusing on the costs of arbitration, funding, legal status and government oversight of any programs.³⁹³

The separate independent forum was initially suggested because of the nagging complaint that the investor was compelled to arbitrate securities claims "in a forum controlled by the securities industry."³⁹⁴ Unfortunately, despite the significant efforts of SICA, the SEC and the SROs themselves,³⁹⁵ this mistrust does not appear to have totally disappeared.³⁹⁶

Since *McMahon*, an additional compelling reason has surfaced in favor of a separate independent securities arbitration forum. That reason is the escalating costs of arbitration to the SRO forums.³⁹⁷ This is partly so because the more complicated and time consuming RICO and federal securities violations cases have now been thrust into arbitration by the *McMahon* and *Rodriguez* decisions.³⁹⁸ More-

jective and independent; [moreover] such administration should include public representation.

391. See Katsoris I, *supra* note 12, at 384; see also Schropp, *New Approaches To Securities Counselling & Litigation After McMahon*, SECURITIES ARBITRATION 1988, PLI Seminar 172 (1988).

392. See *Unified Arbitration Forum Under Discussion*, 1 SEC. ARB. COMMENTATOR 1 (May 1988) [hereinafter *Unified Arbitration Forum Under Discussion*]; see also *SIA Seeks Formation of Arbitration Group*, Wall St. J., Dec. 22, 1989, at A3A, col. 2; *Market Place, Single Arbitration Agency Is Sought*, N.Y. Times, Dec. 21, 1989, at D8, col. 1.

393. SICA decided to endorse such a study at its most recent meeting in San Francisco in January 1990. N.Y. Times, Jan. 20, 1990, at 34, col. 1.

394. *Shearson v. McMahon*, 482 U.S. 220, 260 (1987) (Blackmun, J., dissenting). "The uniform opposition of investors to compel arbitration and the overwhelming support of the securities industry for the process suggests that there must be some truth to the investors' belief that the securities industry has an advantage in a forum under its own control." See *When The Investor Has A Gripe*, N.Y. Times, Mar. 29, 1987, § 3 (Business), at 8, col. 1 ("[t]he houses basically like the present system because they own the stacked deck").

395. See *supra* notes 52-78 and accompanying text.

396. See *When Naivete Meets Wall Street*, *supra* note 275; see also *Traders, on Tape, Brag About Illegal Trading*, Wall St. J., Jan. 9, 1990, at C1, col. 5; *Scandals in Chicago, Automate the Futures Exchanges*, N.Y. Times, Dec. 31, 1989, § 3, at 2, col. 3. "[F]ormer Senator Thomas Eagleton resigned from the Board of Directors of the Chicago Mercantile Exchange, charging that the Exchange is too riddled with cronyism to discipline unethical traders." *Id.* It should be noted that the Chicago Mercantile Exchange is not a member of SICA. See *supra* note 57.

397. See generally Ryder, *supra* note 371, at 52-55; see also *infra* note 401.

398. See *supra* notes 328-32 and accompanying text; see also statements of Constantine

over, administering the numerous post-*McMahon* amendments to the Code has contributed to the explosion of costs.³⁹⁹ The costs to the SROs are likely to increase even more as a result of implementing the essential programs leading to an intensification of arbitrator training and education.⁴⁰⁰ Indeed, the aggregate arbitration expenses at competing SRO forums are escalating, with no apparent end in sight.⁴⁰¹

In the final analysis, all the rules in the world will not insure a level playing field if the administration of those rules by the host forums is wanting because of economic constraints.⁴⁰² The demands for securities arbitration will escalate beyond the abilities of various SRO forums to fund them adequately.⁴⁰³ Indeed, the globalization of the securities markets will someday necessitate the addition of several se-

N. Katsoris before the Subcommittee (Markey Committee) on Telecommunications and Finance of the House Committee on Energy & Commerce (March 31, 1988). Serial No. 100-216—Arbitration Reform at 183-199.

399. See *supra* notes 79-268, *infra* note 401 and accompanying text.

400. See *supra* note 341 and accompanying text.

401. See SEC Release No. 34-26805, May 10, 1989; see also *Hoblin I*, *supra* note 19, at 3.

Arbitration has proved to be a very expensive activity for the SRO. In the case of the NASD, it is a very significant item in 1988 as compared with previous years. The SEC in Release No. 34-26805, approving SRO rule changes, reported on the cost of SRO arbitration. Footnote 50 of this release gives the following figures which include rent allocation:

		SRO Costs	Recovery By Arbitrators Assessment	% Recovery
NYSE	1987	\$ 1,967,000	\$ 790,000	40%
	1988	2,693,000	1,264,000	47%
NASD	1986/87	4,968,072	402,543	8%
	1987/88	7,086,344	1,342,414	19%
AMEX	1987	198,500	46,760	25%
	1988	187,000	48,360	26%

The net recovery is reduced due to some arbitrators' unwillingness to assess costs against either party.

Id. at 5. After *McMahon*, SICA amended § 30 of the Code so as to specifically authorize arbitrators to assess forum fees and costs. See *supra* note 258; see also *Market Place, Single Arbitration Agency Is Sought*, N.Y. Times, Dec. 21, 1989, at D8, col. 1. "The Securities Industry Association has called on Wall Street to set up a single industrywide agency to handle the arbitration of customer disputes, rather than continuing to maintain separate programs at various exchanges and at the National Association of Securities Dealers." *Id.*

402. Moreover, the budget of the SEC—which has oversight authority over the SRO arbitration process—should be increased. But see *SEC Budget Plan Dropped*, N.Y. Times, Nov. 23, 1989, at D6, col. 5; *SEC Prods Wall Street to Police Its Own Neighborhood*, Wall St. J., Nov. 27, 1989, at C1, col. 3.

403. See *supra* notes 397-401.

lected foreign sites for the hearing of arbitration cases.⁴⁰⁴

How would the independent forum be funded? It cannot and should not be funded merely by increasing user fees, for that would render arbitration prohibitively costly.⁴⁰⁵ The independent forum could be financed with a fee imposed on each transaction, or with a combination of a transaction fee and a reasonable user fee.⁴⁰⁶ In any event, economies of scale should make a unified forum more cost efficient than the aggregate costs of competing SRO forums.

A single independent forum entails exactly what it indicates—a forum independent from actual, inferential, subtle, practical or any other kind of imaginable pressure. The forum should be independent of the industry, independent of the plaintiff's bar, and other than the SEC's general oversight role, independent of that regulatory body. Similarly, individual arbitrators and the forum staff must be free from such influences or pressures. Just as the increased caseload,⁴⁰⁷ more complex cases,⁴⁰⁸ and new post-*McMahon* Code amendments⁴⁰⁹ placed new demands upon the abilities and skills of the arbitrators,⁴¹⁰ so too has the stress upon the SRO staffs been commensurately increased. Training and retaining experienced staff personnel, therefore, is essential. In this connection, experienced staff personnel at the SROs could help staff the independent forum. Indeed, for the sake of economy, even some present SRO facilities could be used. The important thing is that the forum be governed by an independent management.⁴¹¹

404. See Morris, *supra* note 333, at 114. Moreover, suppose a foreign investor had his account churned by an account executive in the foreign office of a New York brokerage firm. To require a hearing sight in New York could in certain circumstances impose an undue hardship on the customer. See *The SEC's New World Role*, ECONOMIST, Jan. 6, 1990, at 73. See generally Grass, *Internationalization Of The Securities Trading Markets*, 9 HOUSTON J. INT. LAW 17 (1986).

405. See Katsoris I, *supra* note 12, at 385; Hoblin I, *supra* note 19, at 5. The SEC, in discussing an SRO's increase in arbitration fees, commented:

[w]e intend to monitor the future administration of this rule closely. Costs to investors for SRO arbitration historically have been low, and must remain so. The application of these fees should not be permitted to operate in a manner that weights too heavily on individual parties or serves as a disincentive to pursuing the redress of investors' grievances against broker-dealers or their associated person.

SEC Release No. 34-26805, *supra* note 401, at 43.

406. *Id.*

407. See *supra* notes 77-78 and accompanying text.

408. See *supra* notes 328-33 and accompanying text.

409. See *supra* notes 89-268 and accompanying text.

410. See *supra* notes 342-50 and accompanying text.

411. For a discussion of a tentative organizational structure of the single forum, see *Unified Arbitration Forum Under Discussion*, *supra* note 392, at 2. Moreover, the SROs

Where would the AAA fit into the world of a single independent securities arbitration forum? That would be the AAA's decision if it wanted to compete in this new atmosphere. However, without subsidization and SEC oversight, the AAA is not the answer to the separate independent forum.⁴¹²

Furthermore, in the process of creating an independent forum we also have the opportunity to explore jurisdictional improvements,⁴¹³ as well as eliminate inconsistent rules and interpretations among the various SROs.⁴¹⁴ Moreover, this single forum should also offer mediation services, on a voluntary basis, in an attempt to resolve disputes before incurring the cost and expense of a formal arbitration proceeding.⁴¹⁵

It is also important to note that an independent forum would not require, and should not result in, any major revisions to the Code of Arbitration, Procedures Booklet, or Arbitrator's Manual. These are already intended to achieve a level playing field, and except for modifications dictated by hands-on experience, they should remain largely intact. Indeed, the greatest challenge in creating an independent forum will be avoiding the temptation to load the Code with procedures such as *mandatory* opinions,⁴¹⁶ or broadening the grounds for appeals⁴¹⁷ that will transform arbitration into a clone of courtroom litigation. Such a transformation would defeat the attributes of

might still wish to continue to maintain separate arbitration forums to service their member to member disputes. A concept somewhat analogous to the independent forum has proved workable in the accounting field. In fact, since 1977, some of the trustees of the Financial Accounting Foundation (FAF) have been selected by electors outside the accounting profession. See FINANCIAL ACCOUNTING STANDARDS BOARD, STATUS REPORT NO. 68, at 2 (June 21, 1978). The FAF appoints, oversees and finances the Financial Accounting Standards Board (FASB), which is responsible for formulating the rules by which companies account and report their financial condition. *Id.* at 1-2; see HORNGREN, INTRODUCTION TO FINANCIAL ACCOUNTING 57-58 (2d ed. 1984).

412. See *supra* notes 369-89 and accompanying text; see also *Single Forum Backed*, *supra* note 375.

413. As to jurisdictional improvements, see *Hoblin I*, *supra* note 19, at 3-4; see also *supra* note 34 regarding national service of process.

414. See *supra* notes 272-80 and accompanying text.

415. The NASD has recently embarked on a pilot program of mediation in securities arbitration cases in conjunction with the AAA or the United States Arbitration and Mediation, Inc. Moreover, the single unified forum would be better able to establish and implement procedures for the more efficient handling of the long and complex case which would require many, many sessions. See SIA Press Release to Standard & Poor's News Service (Dec. 21, 1989) (available at Fordham Urban Law Journal office); see also *Single Forum Backed*, *supra* note 375; D. Shannon, *Rent-A-Judge*, *American Way*, Feb. 1, 1990, at 33, col. 1. See generally Silberman, *Breaking the Mold of Grievance Resolutions: Pilot Program in Mediation*, 44 THE ARB. J. 40 (1989).

416. See *supra* notes 229-33 and accompanying text.

417. See *supra* note 234 and accompanying text.

arbitration that make it attractive—its speed and economy.⁴¹⁸

VI. Conclusion

During the Dickens period, many investors—so essential to the health of our securities markets—have lost faith in the markets.⁴¹⁹ Rebuilding that faith will take time and much effort. Essential to the rebuilding of such confidence is assuring the public investor that when he has a justifiable grievance against his broker, it will be resolved swiftly, cheaply, and fairly.⁴²⁰ The *McMahon* decision virtually mandated procedures to guarantee such attributes and the public is entitled to no less.⁴²¹

Indeed, *McMahon* provided both the opportunity and impetus to make the necessary adjustments to the arbitration process. Reasonable people may differ as to the specific ground rules, but in striving to achieve a *level playing field* for all participants—claimants as well as respondents—SICA has tried to avoid populist, expedient and short-term approaches which would strip arbitration of its principal attributes of speedy justice and economy. Consequently, despite its shortcomings,⁴²² SICA has acted as a constructive force in the creation of the level playing field, and should continue to independently discuss, amend and monitor the Uniform Code of Arbitration.

Whether we retain the *status quo*, or move to a separate independent forum, the SEC should continue in its oversight role.⁴²³ To prop-

418. See *supra* notes 79-83 and accompanying text.

419. See *supra* notes 2-9 and accompanying text.

420. See Katsoris I, *supra* note 12, at 386.

421. See *Shearson/American Express v. McMahon*, 482 U.S. 220, 228 (1987).

422. See *supra* note 71 and accompanying text.

423. If a separate forum is created, Congressional approval for an SEC oversight role might be necessary. See *Single Forum Backed*, *supra* note 375. Moreover, Congress might also use this opportunity to examine the extent of SIPC (Securities Investor Protection Corporation), protection in customer/broker disputes involving fraud. See § 3 of Securities Investor Protection Act of 1970, Fed. Sec. L. Rep. (CCH) ¶ 26,657. For example, let us assume customer A deposits \$50,000 in cash to open an account with an introducing broker X, who in turn clears through a clearing broker Y. Broker X—without any authorization—purchases speculative stocks on margin in A's account. When A discovers the unauthorized purchases, A rejects the trades and immediately institutes an SRO arbitration against broker X. In the meantime, the price of the unauthorized shares drops dramatically and the clearing broker Y sells out A's account because of margin requirements resulting from the recent unauthorized purchases, leaving an equity balance in A's account of only \$20,000 instead of the original \$50,000. Shortly thereafter, broker X files for bankruptcy and the SRO suspends the arbitration proceeding because of the exclusivity of the bankruptcy proceedings. X is hopelessly insolvent rendering A's claim against him virtually worthless. Should A's account be protected by SIPC to the extent of only \$20,000 (reduced liquidated value) or \$50,000 (original value)? Should the answer change if X was also the clearing broker? Furthermore, should it make any differ-

erly do this, however, its budget in turn must be supplemented, and not trimmed.⁴²⁴ You get what you pay for, and the SEC, in its crucial oversight role, is clearly no exception to this rule.

In striving to keep the playing field level, one must also examine the sidelines. Thus, the industry should take measures to prevent injury from occurring in the first place. For example, brokerage firms, when filling out new account forms should, *after* the form is filled out, get the customer's approval and *written confirmation* of the key customer data contained therein, particularly that which pertains to items such as income levels, equity, investment goals and prior investment experience.⁴²⁵ Moreover, if there is an arbitration clause in the customer's agreement, it should be *separately initialed* by the customer as well as the firm.⁴²⁶ Better supervision of customers' accounts should also become a matter of top priority, particularly where risky investments are involved.⁴²⁷ Such a tightening of back office procedures could prevent some of the damage and misunderstanding that exists between the public investor and the securities industry.⁴²⁸

Congress should also look beyond the boundaries of the playing field in seeking better investor protection by adopting measures that will lessen potential losses. Congress can do this by passing legislation which could improve and stabilize the investment climate. In the present environment, the small investor has been *terrified* by the wild market gyrations that have characterized the Dickens years.⁴²⁹ Congress' goal should be to reestablish the rule that the principal purpose

ence if the nature of A's claim against X was for churning or unsuitability, instead of *unauthorized* trading?

424. See *supra* note 402.

425. Such a form is generally filled out by the account executive and approved by his or her manager.

426. See *supra* note 264 and accompanying text. It is regrettable that the SEC does not support the concept of special initialling. See SEC Release No. 34-26805, *supra* note 401, at 48.

427. There are many examples of instances which by their virtue should require additional supervision, but of particular concern are trading in such items as index futures, naked shorts, illiquid shelters, etc., especially where they involve accounts of elderly investors or those of limited means.

428. See Mills, *Avoiding Arbitration*, 1989 SECURITIES ARBITRATION, PLI SEMINAR, 932-34; see also Krebsbach & Friedman, *Securities Arbitration: Defending a Brokerage Firm*, 1989 SECURITIES ARBITRATION, PLI SEMINAR 813, 820. Nor is a practice of tying analysts' bonuses to stock sales likely to instill trust in the public. See *Are Analysts Putting Their Mouths Where the Money Is?*, BUS. WK., Dec. 18, 1989, at 118. "Such payment schemes 'could go a long way towards showing that the investment was not suitable for the client involved,' says Theodore G. Eppenstein, a New York securities lawyer." *Id.*

429. See *supra* notes 2-5 and accompanying text; see also *Small Investors Tiptoe Back To Wall St.*, BUS. WK., Aug. 14, 1989, at 99.

for investing in the markets is not to *gamble*, but to raise capital for *sound investment*.⁴³⁰ This requires a re-examination of the competing interests of program trading, with a view toward recognizing its legitimate goals, but limiting or eliminating its disastrous side effects.⁴³¹ Bottom line, however, program trading, regardless of its usefulness to institutional investors, cannot be left unbridled so as to continue to undermine the primary investment and fund-raising functions of our capital markets.

Similarly, Congress should consider several tax amendments that would also improve and stabilize the investment climate, such as: (1) reestablishing the deduction for Individual Retirement Accounts (IRAs),⁴³² so as to induce savings by and provide a retirement nest egg for its taxpayers;⁴³³ (2) re-creating *some* differential for capital

430. If you cannot bet at the track on credit, why do we allow futures traders to operate on a 5% margin? It is an unconscionable example of misregulation courting disaster. See *A Pox on Program Trading*, *supra* note 6, at 18, 20; The Quiet Crusader, BUS. WK., Sept. 18, 1989, at 80; see also *The Purpose of America's Capital*, Barrons, Nov. 20, 1989, at 10 (statement of John J. Phelan, Jr.); *Impact of Program Trading Assessed*, *Advest Investor Journal*, Dec. 1989, at 1, col. 1. "It has been suggested that margin requirements be raised from 5% to the 50% level required of individual investors and that program traders be required to comply with the uptick rule, which prohibits short selling when the last price of a security was below that of the prior transaction." *Id.*; see also *A "Neanderthal" Speaking*, *Forbes*, Dec. 25, 1989, at 164, col. 1; *More Power to the Regulators*, N.Y. Times, Mar. 18, 1990, § 3 (Business), at 13, col. 2. "[W]e must move quickly and forcefully to bring regulatory oversight of the stock-index futures markets under a single agency." *Id.*

431. See *Market Re-Maker*, Barrons, Dec. 11, 1989, at 14, col. 2.

We have to make a decision. For whom does the market exist? For traders or for investors? Does it exist for the players in the market or does it exist for the capital formation process? Modern, up-to-date, sensible regulation that doesn't ban program trading, doesn't ban new technologies, but accommodates it to the legitimate needs of the marketplace, is what is needed.

Id. at 15; see also *Program Trading Hits the Nikkei*, N.Y. Times, Feb. 25, 1990, § 3 (Business), at 15, col. 4; *Japan's Market Wrestle With Issue of Volatility*, N.Y. Times, Mar. 1, 1990, at D2, col. 1; *U.S. Brokers Asked In Japan to Curb Program Trading*, Wall St. J., Mar. 8, 1990, at C9, col. 1. On the other hand, Congress should not expect the securities industry to police itself. See *NYSE's Call for Restraint Draws Jeers*, Wall St. J., Nov. 6, 1989, at C1, col. 3; *Bear, Stearns Will Resume Index Arbitrage For Itself*, N.Y. Times, Dec. 13, 1989, at D1, col. 1. "In explaining yesterday's decision, the firm pointed to a lack of progress by legislators or regulators in introducing corrective measure to reduce volatility. In particular, the firm said it seemed unlikely that margin requirements on financial futures would be raised, a step the firm has publicly endorsed." *Id.*; *Nomura to Enter Program Trading—With Global Aim*, Wall St. J., Mar. 13, 1990, at C1, col. 3; see also *Heavy Program Trading Disclosed by Big Board*, Wall St. J., Dec. 19, 1989, at C14, col. 3; *Programs Accounted for 56% of Dec. 15 Big Board Volume*, Wall St. J., Dec. 29, 1989, at C13, col. 2. To its credit, the NYSE has recently proposed to curb some of the volatility caused by program trading. See *Big Board Proposes Program Trade Curbs*, Wall St. J., Feb. 14, 1990, at C1, col. 5.

432. See I.R.C. § 408 (1986).

433. See Banks, *Why George Bush Wants to Bring IRAs Back*, *Forbes*, Aug. 21, 1989,

gains, so as to attract venture capital;⁴³⁴ and, *most importantly*, (3) granting some relief against the double taxation of corporate profits, so as to relieve the unfair bias toward borrowed capital as opposed to equity capital.⁴³⁵ It would be unfortunate indeed if such stabilizing incentives are denied as a result of budget infighting.⁴³⁶

at 68; *Persuading Americans To Save*, N.Y. Times, Dec. 17, 1989, at 1, col 6; see also *Mr. Bush's Piggy Bank* (Editorial), N.Y. Times, Feb. 1, 1990, at A22, col. 1.

434. See generally Katsoris, *In Defense of Capital Gains*, 42 FORDHAM L. REV. 1, (1973); *Capital-Gains Compromise, Review and Outlook*, Wall St. J., July 28, 1989, at A10, col. 1; *To Aid The Poor, Cut Capital Gains Taxes*, N.Y. Times, July 25, 1989, at A23, col. 2; *Capital Pains on Capital Gains*, U.S. News & World Rep., Aug. 7, 1989, at 42, col. 1. As to capital gains, if all income is taxed the same, then why should an investor take a short term risk for the sake of long term appreciation? See *Market Place, Tax Laws Spur Borrowing Boom*, N.Y. Times, Dec. 28, 1989, at D8, col. 1. Such philosophy will ultimately deny this nation the long term risk capital necessary to prod innovation which is essential in order to keep it competitive in a world economy. Moreover, capital gains taxation is strictly a one-sided proposition when personal assets (i.e., homes, boats, automobiles, etc.) are involved. If sold at a profit, a capital gains tax must be paid; yet, if there is a loss, it is not recognized because it is personal in nature. See Katsoris, *supra*, at 6. In addition, capital gains are taxed when realized, but there is a limitation on the deductibility of recognized capital losses. *Id.*; see I.R.C. § 1211 (1986).

435. See Katsoris, *The Double Jeopardy of Corporate Profits*, 29 BUFFALO L. REV. 1 (1980). As to the effect of the double taxation of corporate profits, every corporate executive in this country knows that it is cheaper taxwise to raise money through borrowing than through equity financing. This is so, because the interest on the debt is tax deductible to the corporation, whereas the dividends on its equity capital are not. This unequal treatment lays the groundwork for the tilting of companies' balance sheets in favor of debt over equity. It has created an atmosphere that has encouraged the recent flurry of LBO's that are made possible through the issuance of high yield debt. See *supra* note 7; see also *Market Place, Tax Laws Spur Borrowing Boom*, N.Y. Times, Dec. 28, 1989, at D8, col. 1. Certainly the government does not benefit from such debt-laden takeovers; for, the acquired corporations were previously generally paying income taxes, whereas the acquirer may now deduct the interest on the takeover debt from its tax bill. See *Big Shortfall in Corporate Taxes Thwarts Key Goal of 1986 Law*, N.Y. Times, Mar. 6, 1990, at 1, col. 1. Such scenario becomes even more unsettling when one contemplates what will happen to that debt once an inevitable downturn occurs in the economy. See *Wall Street Prepares For a Failure Boom*, N.Y. Times, Dec. 31, 1989, § 3, at 2, col. 3; *Small Firms Too, Are Feeling The Chills of Debt Fever*, Wall St. J., Feb. 5, 1990, at B1, col. 3; *'Junk Bond' Prices Fall On Worry Over Drexel*, N.Y. Times, Feb. 13, 1990, at D24, col. 1. We must give relief to this punitive double tax and restore a legitimate balance between equity and debt. This will have a stabilizing effect upon our markets. See *Treasury to Form Plan to Halt 'Double Taxation'*, Wall St. J., Dec. 12, 1989, at A6, col. 3.

436. Let us also now consider the worst case scenario and assume *arguendo* that all of these worthwhile tax changes—IRA deduction, capital gains differential and double taxation relief—will ultimately reduce tax revenues. In that case, we must consider them in light of the nagging national budget deficit and seek to neutralize any such drain; and, if increased revenues are needed, it has been suggested:

In listing revenue enhancers, I would like to employ some sort of fair, yet practical, pain index. Thus, at the outset I would first propose an increase in user fees and sin taxes—even though I smoke an occasional cigar and on occasion enjoy a dry martini. In the event such user tax increases are not enough, I would then retain the 33% maximum individual tax rate on income instead of

As far as the playing field itself is concerned, should Congress overrule the *McMahon* decision? Such a step makes little or no sense, and in the long run, neither investors nor the industry would benefit. Throwing thousands of cases back to congested court calendars is certainly not the answer.⁴³⁷ In such a scenario, the securities industry would be plagued by excessive litigation costs, which directly or indirectly, would be borne by the public as the industry's cost of doing business.⁴³⁸ In addition, the public would often be denied justice, because of the excessive costs and delays associated with courtroom litigation.⁴³⁹ The decision of whether or not to arbitrate, however, should be made freely by the customer; but once so agreed, that agreement should be binding.⁴⁴⁰

Finally, once we achieve a *level playing field*, we must insure that this field remains level, for in a less than perfect world, "[l]aws and institutions are constantly tending to gravitate. Like clocks, they must be occasionally cleansed, and wound up, and set to true

reverting back to 28% after a certain income threshold was reached (§ 1(g) IRC). Next, I would impose an oil import tax first and then, if necessary, a gasoline tax.

If all that were still not enough, I would *not* otherwise raise income tax rates; but, instead would consider some sort of national Value Added Tax. I have read many articles about some of the drawbacks of such a tax; but, on balance, it has some distinct advantages. For one thing, it addresses the number one problem of our tax system—the escaping of *billions* of dollars of revenue through our underground economy. This "might" even be helpful in detecting and/or combatting crime. Furthermore, if it is oppressive against the poor, it can be tailored to give relief through a system of exemptions or credits, such as the earned income credit (§ 32 IRC).

Letter from Constantine N. Katsoris to the Hon. Lloyd Bentsen, Chairman of the Senate Finance Committee (Jan. 25, 1989) (discussing capital gains and the double taxation of corporate profits) (copy on file in Fordham Urban Law Journal Office); *see also Live! Stupid Budget Tricks!*, Newsweek, Oct. 23, 1989, at 29, col. 1; *A Wake-up Call for Rosty*, BUS WK., Mar. 26, 1990, at 32.

437. *See New Tactics in the War on Drugs Tilt Scales of Justice Off Balance*, N.Y. Times, Dec. 29, 1989, at A1, col. 1. "'We're becoming drug courts,' says Edward R. Becker, a Federal appeals judge in Philadelphia . . . 'The short of it is that we're getting an enormous volume of drug cases, and its making it very difficult in many jurisdictions to hear civil cases.'" *Id.*; *see also The Federal Courts Have a Drug Problem*, BUS. WK., Mar. 26, 1990, at 76; *Drastic Moves Urged to Ease U.S. Court's Load*, N.Y. Times, Mar. 23, 1990, at B5, col. 3.

Indeed, in California, the Los Angeles County Bar Association filed suit in federal court to appoint more state court judges because it takes about five years for a civil case to come to trial. *See Marcotte, L.A. County Bar Sues California*, A.B.A.J., 28 (1988); *see also Lawsuits in Federal Courts*, N.Y. Times, July 16, 1987, at B6, col. 6; *see also Congress Now Considering Dispute Resolution Measures*, Nat. L.J., Feb. 5, 1990, at 1, col. 1.

438. *See Katsoris I, supra* note 12, at 374-75.

439. For a discussion of how increased costs deny justice, *see supra* notes 79-81 and accompanying text.

440. *See supra* notes 27-30 and accompanying text.

time.”⁴⁴¹ To insure against such a drift, as well as for the sake of public perception,⁴⁴² uniformity in the implementation of the Code,⁴⁴³ and *most importantly*, the problem of escalating costs,⁴⁴⁴ the time to *consider* an independent forum is at hand.⁴⁴⁵ Indeed, if the securities arbitration “system was created today, no one would propose the Hydra that now exists.”⁴⁴⁶

441. H. BEECHER, LIFE THOUGHTS 129 (1858).

442. *See supra* notes 394-96 and accompanying text.

443. *See supra* notes 272-80 and accompanying text.

444. *See supra* notes 397-406 and accompanying text.

445. *See supra* notes 390-93 and accompanying text.

446. Hoblin I, *supra* note 19, at 3.

Appendix A

Arbitration Cases Handled by SROs

American Stock Exchange, Inc.

Year	Total Cases Received	Total Cases Concluded Including Settlement	Small Claims Received	Small Claims Concluded	Public Customer Cases Decided	Awards in Favor of Public
1980	45	41	18	11	35	16
1981	39	40	7	11	42	22
1982	37	31	9	4	16	10
1983	41	42	14	8	10	6
1984	69	53	16	14	45	26
1985	64	58	21	14	41	24
1986	63	60	20	28	31	14
1987	92	74	34	24	41	24
1988	100	63	21	29	27	12

Cases carried into 1989: 87

National Association of Securities Dealers, Inc.

Year	Total Cases Received	Total Cases Concluded Including Settlement	Small Claims Received	Small Claims Concluded	Public Customer Cases Decided	Awards in Favor of Public
1980	318	234	134	113	122	56
1981	422	422	142	177	242	118
1982	606	435	157	139	276	140
1983	768	549	216	147	272	161
1984	1,108	747	298	244	381	196
1985	1,400	962	377	250	434	232
1986	1,587	1,199	390	327	476	248
1987	2,886	1,625	458	325	642	364
1988	3,990	2,169	1,084	539	934	432

Cases carried into 1989: 4,005

Boston Stock Exchange, Inc.

Year	Total Cases Received	Total Cases Concluded Including Settlement	Small Claims Received	Small Claims Concluded	Public Customer Cases Decided	Awards in Favor of Public
1980	2	2	2	2	2	0
1981	2	2	2	2	0	0
1982	1	1	1	1	1	1
1983	2	2	2	2	2	1
1984	0	0	0	0	0	0
1985	0	0	0	0	0	0
1986	2	2	2	2	2	0
1987	0	0	0	0	0	0
1988	0	0	0	0	0	0

Cases carried into 1989: 0

New York Stock Exchange, Inc.

Year	Total Cases Received	Total Cases Concluded Including Settlement	Small Claims Received	Small Claims Concluded	Public Customer Cases Decided	Awards in Favor of Public
1980	367	327	131	110	221	119
1981	477	433	117	134	214	111
1982	558	473	109	113	214	118
1983	713	532	136	122	276	137
1984	1,008	796	176	183	259	113
1985	1,095	962	198	190	424	221
1986	965	1,004	181	205	432	210
1987	1,050	1,000	225	204	378	200
1988	1,623	1,196	263	235	440	228

Cases carried into 1989: 1,269

Chicago Board Options Exchange, Inc.

Year	Total Cases Received	Total Cases Concluded Including Settlement	Small Claims Received	Small Claims Concluded	Public Customer Cases Decided	Awards in Favor of Public
1980	44	31	11	11	18	6
1981	41	32	10	8	12	3
1982	50	38	6	6	14	3
1983	75	45	5	4	13	6
1984	91	56	24	16	4	3
1985	64	38	10	5	0	0
1986	72	44	16	9	12	9
1987	130	93	29	33	22	9
1988	149	89	22	27	48	12

Cases carried into 1989: 151

Pacific Stock Exchange, Inc.

Year	Total Cases Received	Total Cases Concluded Including Settlement	Small Claims Received	Small Claims Concluded	Public Customer Cases Decided	Awards in Favor of Public
1980	24	28	12	11	4	3
1981	24	20	17	17	9	5
1982	31	21	15	11	10	7
1983	35	29	17	17	23	10
1984	45	26	21	11	10	7
1985	50	40	12	18	20	12
1986	41	37	9	13	18	8
1987	64	58	27	11	23	13
1988	99	77	30	40	45	20

Cases carried into 1989: 86

Midwest Stock Exchange, Inc.

Year	Total Cases Received	Total Cases Concluded Including Settlement	Small Claims Received	Small Claims Concluded	Public Customer Cases Decided	Awards in Favor of Public
1980	2	2	1	0	1	1
1981	2	2	0	0	0	0
1982	1	0	0	0	0	0
1983	2	2	0	0	0	0
1984	1	0	0	0	0	0
1985	1	0	0	0	0	0
1986	4	0	1	0	0	0
1987	5	3	1	1	1	1
1988	1	7	0	0	0	0

Cases carried into 1989: 2

Philadelphia Stock Exchange, Inc.

Year	Total Cases Received	Total Cases Concluded Including Settlement	Small Claims Received	Small Claims Concluded	Public Customer Cases Decided	Awards in Favor of Public
1980	7	0	16	4	4	2
1981	10	6	6	3	6	1
1982	23	15	18	11	14	8
1983	17	19	9	11	12	5
1984	14	7	6	4	3	0
1985	31	18	15	8	8	2
1986	22	15	10	6	7	2
1987	25	15	15	9	4	1
1988	24	13	4	8	4	2

Cases carried into 1989: 42

Municipal Securities Rulemaking Board

Year	Total Cases Received	Total Cases Concluded Including Settlement	Small Claims Received	Small Claims Concluded	Public Customer Cases Decided	Awards in Favor of Public
1980	21	21	7	7	3	2
1981	25	25	5	5	7	4
1982	33	16	7	7	13	6
1983	78	40	17	9	14	5
1984	113	80	20	17	34	21
1985	91	118	31	35	54	31
1986	82	89	30	21	30	15
1987	106	90	38	34	42	24
1988	115	126	49	52	63	37

Cases carried into 1989: 59

Composite Arbitration Figures

Year	Total Cases Received	Total Cases Concluded Including Settlement	Small Claims Received	Small Claims Concluded	Public Customer Cases Decided	Awards in Favor of Public
1980	830	686	332	269	410	205
1981	1,042	980	306	357	532	264
1982	1,340	1,044	322	292	558	293
1983	1,731	1,259	416	320	622	331
1984	2,449	1,762	561	489	736	366
1985	2,796	2,190	664	520	961	530
1986	2,838	2,460	657	610	1,017	506
1987	4,358	2,958	827	641	1,153	636
1988	6,101	3,740	1,473	930	1,561	743

Appendix B**UNIFORM CODE OF ARBITRATION****SECTION 1.***Arbitration*

(a) Any dispute, claim or controversy between a (customer or nonmember) and a (member, allied member, member organization, and/or associated person) arising in connection with the business of such (member, allied member, member organization and/or associated person) in connection with his activities as an associated person shall be arbitrated under the Constitution and Rules of the (name of self-regulatory organization) as provided by any duly executed and enforceable written agreement or upon the demand of the customer or nonmember.

(b) Under this Code, the (name of self-regulatory organization) shall have the right to decline the use of its arbitration facilities in any dispute, claim, or controversy where—having due regard for the purposes of the (name of self-regulatory organization) and the intent of this Code—such dispute, claim, or controversy is not a proper subject matter for arbitration.

SECTION 2.*Simplified Arbitration*

(a) Any dispute, claim, or controversy, arising between a public customer(s) and an associated person or a member subject to arbitration under this Code involving a dollar amount not exceeding \$10,000 exclusive of attendant costs and interest, shall upon demand of the customer(s), or by written consent of the parties, be arbitrated as hereinafter provided.

(b) The Claimant shall file with the Director of Arbitration an executed Submission Agreement and a copy of the Statement of Claim of the controversy in dispute and the required deposit, together with documents in support of the Claim. Sufficient copies of the Submission Agreement and the Statement of Claim and supporting documents shall be provided to the Director of Arbitration for each party and the arbitrator. The Statement of Claim shall specify the relevant facts, the remedies sought, and whether a hearing is demanded.

(c) The Claimant shall deposit the sum of \$15 if the amount in controversy is \$1,000 or less, \$25 if the amount in controversy is more than \$1,000 but does not exceed \$2,500, \$100 if the amount in contro-

versy is more than \$2,500 but does not exceed \$5,000, or \$200 if the amount in controversy is more than \$5,000 but does not exceed \$10,000 upon filing of the Submission Agreement. The final disposition of this sum shall be determined by the arbitrator.

(d) The Director of Arbitration shall endeavor to serve promptly by mail or otherwise on the Respondent(s) one (1) copy of the Submission Agreement and one (1) copy of the Statement of Claim. Within twenty (20) calendar days from receipt of the Statement of Claim, Respondent(s) shall serve each party with an executed Submission Agreement and a copy of Respondent's Answer. Respondent's executed Submission Agreement and Answer shall also be filed with the Director of Arbitration with sufficient copies for the arbitrator(s) along with any deposit required under the schedule of fees. The Answer shall designate all available defenses to the Claim and may set forth any related Counterclaim and/or related Third-Party Claim the Respondent(s) may have against the Claimant or any other person. If the Respondent(s) has interposed a Third-Party Claim, the Respondent(s) shall serve the Third-Party Respondent with an executed Submission Agreement, a copy of Respondent's Answer containing the Third-Party Claim, and a copy of the original Claim filed by the Claimant. The Third-Party Respondent shall respond in the manner herein provided for response to the Claim. If the Respondent(s) files a related Counterclaim exceeding \$10,000, the arbitrator may refer the Claim, Counterclaim, and/or Third-Party Claim, if any, to a panel of three (3) or more arbitrators in accordance with Section 8 of this Code, or he may dismiss the Counterclaim and/or Third-Party Claim, without prejudice to the Counterclaimant(s) and/or Third-Party Claimant(s) pursuing the Counterclaim and/or Third-Party Claim in a separate proceeding. The costs to the Claimant under either proceeding shall in no event exceed \$200.

(e) All parties shall serve promptly by mail or otherwise on all other parties and the Director of Arbitration, with sufficient copies for the arbitrators, a copy of the Answer, Counterclaim, Third-Party Claim, or other responsive pleading, if any. The Claimant, if a counterclaim is asserted against him, shall within ten (10) calendar days either (i) serve on each party a reply to any Counterclaim, or, (ii) if the amount of the Counterclaim exceeds the Claim, shall have the right to file a statement withdrawing the Claim. If the Claimant withdraws the Claim, the proceedings shall be discontinued without prejudice to the rights of the parties.

(f) The dispute, claim, or controversy shall be submitted to a single arbitrator knowledgeable in the securities industry selected by the

Director of Arbitration. Unless the public customer demands or consents to a hearing, or the arbitrator calls a hearing, the arbitrator shall decide the dispute, claim, or controversy solely upon the pleadings and evidence filed by the parties. If a hearing is necessary, such hearing shall be held as soon as practicable at a locale selected by the Director of Arbitration.

(g) The Director of Arbitration may grant extensions of time to file any pleading upon a showing of good cause.

(h) The arbitrator shall be authorized to require the submission of further documentary evidence as he, in his sole discretion, deems advisable.

(i) Upon the request of the arbitrator, the Director of Arbitration shall appoint two (2) additional arbitrators to the panel that shall decide the matter in controversy.

(j) In any case where there is more than one (1) arbitrator, the majority will be public arbitrators.

(k) In his discretion, the arbitrator may, at the request of any part, permit such party to submit additional documentation relating to the pleadings.

(l) Except as otherwise provided herein, the general arbitration rules of the (name of self-regulatory organization) shall be applicable to proceedings instituted under this Code.

SECTION 3.

Hearing Requirements—Waiver of Hearing

(a) Any dispute, claim, or controversy, except as provided in Section 2 (Simplified Arbitration), shall require a hearing unless all parties waive such hearing in writing and request that the matter be resolved solely upon the pleadings and documentary evidence.

(b) Notwithstanding a written waiver of a hearing by the parties, a majority of the arbitrators may call for and conduct a hearing. In addition, any arbitrator may request the submission of further evidence.

SECTION 4.

Time Limitation Upon Submission

No dispute, claim or controversy shall be eligible for submission to arbitration under this Code if six (6) years have elapsed from the occurrence or event giving rise to the act or the dispute, claim, or controversy. This section shall not extend applicable statutes of

limitations, nor shall it apply to any case that is directed to arbitration by a court of competent jurisdiction.

SECTION 5.

Dismissal of Proceedings

At any time during the course of an arbitration, the arbitrators may, either upon their own initiative or at the request of a party, dismiss the proceeding and refer the parties to the remedies provided by law. The arbitrators shall, upon the joint request of the parties, dismiss the proceedings.

SECTION 6.

Settlements

All settlements submitted shall be at the election of the parties.

SECTION 7.

Tolling of Time Limitation(s) for the Institution of Legal Proceedings

(a) Where permitted by law, the time limitation(s) that would otherwise run or accrue for the institution of legal proceedings shall be tolled when a duly executed Submission Agreement is filed by the Claimant(s). The tolling shall continue for such period as the (name of self-regulatory organization) shall retain jurisdiction upon the matter submitted.

(b) The six (6) year time limitation upon submission to arbitration shall not apply when the parties have submitted the dispute, claim, or controversy to a court of competent jurisdiction. The six (6) year time limitation shall not run for such period as the court shall retain jurisdiction over the matter submitted.

SECTION 8.

Designation of the Number of Arbitrators

(a)(1) In all arbitration matters involving public customers and nonmembers where the matter in controversy exceeds \$10,000, or where the matter in controversy does not involve or disclose a money claim, the Director of Arbitration shall appoint an arbitration panel that shall consist of no less than three (3) arbitrators, at least a majority of whom shall not be from the securities industry, unless the public

customer or nonmember requests a panel consisting of at least a majority from the securities industry.

(2) An arbitrator will be deemed as being from the securities industry if he or she:

i. Is a person associated with a member, or broker-dealer, government securities broker, government securities dealer, municipal securities dealer, or registered investment adviser, or

ii. Has been associated with any of the above within the past three (3) years, or

iii. Is retired from any of the above, or

iv. Is an attorney-accountant, or other professional who devoted twenty (20) percent or more of his or her professional work effort to securities industry clients within the last two years.

(3) An arbitrator who is not from the securities industry shall be deemed a public arbitrator. A person will not be classified as a public arbitrator if he or she has a spouse or other member of the household who is a person associated with a registered broker, dealer, municipal securities dealer, government securities broker, government securities dealer, or investment adviser.

(b) Composition of Panels

The individuals who shall serve on a particular arbitration panel shall be determined by the Director of Arbitration. The Director of Arbitration may name the chairman of each panel.

SECTION 9.

Notice of Selection of Arbitrators

The Director of Arbitration shall inform the parties of the arbitrators' names, employment histories for the past ten (10) years, as well as information disclosed pursuant to Section 11, at least eight (8) business days prior to the date fixed for the first hearing session. A party may make further inquiry of the Director of Arbitration concerning an arbitrator's background. In the event that prior to the first hearing session, any arbitrator should become disqualified, resign, die, refuse, or otherwise be unable to perform as an arbitrator, the Director of Arbitration shall appoint a replacement arbitrator to fill the vacancy on the panel. The Director of Arbitration shall inform the parties as soon as possible of the name and employment history of the replacement arbitrator for the past ten (10) years, as well as information disclosed pursuant to Section 11. A party may make further inquiry of the Director of Arbitration concerning the replacement Arbitrator's background and, within the time remaining prior to the first hearing

session or the five (5) day period provided under Section 10, whichever is shorter, may exercise its right to challenge the replacement arbitrator as provided in Section 10.

SECTION 10.

Challenges

In any arbitration proceeding, each party shall have the right to one peremptory challenge. In arbitrations where there are multiple Claimants, Respondents, and/or third-Party Respondents, the Claimants shall have one peremptory challenge, the Respondents shall have one peremptory challenge, and the Third-Party respondents shall have one peremptory challenge, unless the Director of Arbitration determines that the interests of justice would best be served by awarding additional peremptory challenges. Unless extended by the Director of Arbitration, a party wishing to exercise a peremptory challenge must do so by notifying the Director of Arbitration in writing within five (5) business days of notification of the identity of the persons named to the panel. There shall be unlimited challenges for cause.

SECTION 11.

Disclosures Required by Arbitrators

(a) Each arbitrator shall be required to disclose to the Director of Arbitration any circumstances that might preclude such arbitrator from rendering an objective and impartial determination. Each arbitrator shall disclose:

(1) Any direct or indirect financial or person interest in the outcome of the arbitration.

(2) Any existing or past financial, business, professional, family or social relationships that are likely to affect impartiality or that might reasonably create an appearance of partiality or bias. Persons requested to serve as arbitrators should disclose any such relationships that they personally have with any party or its counsel, or with any individual whom they have been told will be a witness. They should also disclose any such relationship involving members of their families, or their current employers, or their current employers' partners or business associates.

(b) Persons who are requested to accept appointment as arbitrators should make a reasonable effort to inform themselves of any interests or relationships described in paragraph (a) above.

(c) The obligation to disclose interests, relationships, or circum-

stances that might preclude an arbitrator from rendering an objective and impartial determination described in subsection (a) hereof is a continuing duty that requires a person who accepts appointment as an arbitrator to disclose, at any stage of the arbitration, any such interests, relationships, or circumstances that arise, or that are recalled or discovered.

(d) Prior to the commencement of the first hearing session, the Director of Arbitration may remove an arbitrator based on information disclosed pursuant to this section. The Director of Arbitration shall also inform the parties of any information disclosed pursuant to this section if the arbitrator who disclosed the information is not removed.

SECTION 12.

Disqualification or Other Disability of Arbitrators

In the event that any arbitrator, after the commencement of the first hearing session but prior to the rendition of the award, should become disqualified, resign, die, refuse, or otherwise be unable to perform as an arbitrator, the remaining arbitrator(s) may continue with the hearing and determination of the controversy unless such continuation is objected to by any party within five (5) days of notification of the vacancy on the panel. Upon objection, the Director of Arbitration shall appoint a new member to the panel to fill any vacancy. The Director of Arbitration shall inform the parties as soon as possible of the name and employment history for the past ten (10) years of the replacement arbitrator, as well as information disclosed pursuant to Section 11. A party may further ask the Director of Arbitration about the replacement arbitrator's background and, within the time remaining prior to the next scheduled hearing session or the five (5) day period provided under Section 10, whichever is shorter, may exercise its right to challenge the replacement arbitrator as provided in Section 10.

SECTION 13.

Initiation of Proceedings

Except as otherwise provided herein, an arbitration proceeding under this Code shall be instituted as follows:

(a) Statement of Claim

The Claimant shall file with the Director of Arbitration an executed Submission Agreement, a Statement of Claim together with

documents in support of the claim, and the required deposit. Sufficient additional copies of the Submission Agreement and the Statement of Claim and supporting documents shall be provided to the Director of Arbitration for each party and each arbitrator. The Statement of Claim shall specify the relevant facts and the remedies sought. The Director of Arbitration shall endeavor to serve promptly by mail or otherwise on the Respondent(s) one (1) copy of the Submission Agreement and one (1) copy of the Statement of Claim.

(b) Service and Filing with the Director of Arbitration

For purposes of the Code of Arbitration Procedure, service may be effected by mail or other means of delivery. Service and filing are accomplished on the date of mailing either by first-class postage prepaid or by means of overnight mail service or, in the case of other means of service, on the date of delivery. Filing with the Director of Arbitration shall be made on the same date as service.

(c) Answers—Defenses, Counterclaims, and/or Cross-Claims

(1) Within twenty (20) business days from receipt of the Statement of Claim, the Respondent(s) shall serve each party with an executed Submission Agreement and a copy of Respondent(s) Answer. An executed Submission Agreement and Answer of the Respondent(s) shall also be filed with the Director of Arbitration with sufficient additional copies for the arbitrator(s), along with any deposit required under the schedule of fees. The Answer shall specify all available defenses and relevant facts that will be relied upon at the hearing. It also may set forth any related Counterclaim the Respondent(s) may have against the Claimant, any Cross-Claim the Respondent(s) may have against any other named Respondent(s), and any Third-Party Claim against any other party or person based upon any existing dispute, claim, or controversy subject to arbitration under this Code.

(2)(i) A Respondent, Responding Claimant, Cross-Claimant, Cross-Respondent, or Third-Party Respondent who pleads only a general denial as an answer may, upon objection by a party, in the discretion of the arbitrators, be barred from presenting any fact or defenses at the time of the hearing.

(ii) A Respondent, Responding Claimant, Cross-Claimant, Cross-Respondent, or Third-Party Respondent who fails to specify all available defenses and relevant facts in such party's answer may, upon objection by a party, in the discretion of the arbitrators, be barred

from presenting such facts or defenses not included in such party's answer at the hearing.

(iii) A Respondent, Responding Claimant, Cross-Claimant, Cross-Respondent, or Third-Party Respondent who fails to file an answer within twenty (20) business days from receipt of service of a claim, unless the time to answer has been extended pursuant to paragraph (5), may, in the discretion of the arbitrators, be barred from presenting any matter, arguments, or defenses at the hearing.

(3) Respondent(s) shall serve each party with a copy of any Third-Party Claim. The Third-Party Claim shall also be filed with the Director of Arbitration with sufficient additional copies for the arbitrator(s), along with any deposit required under the schedule of fees. Third-Party Respondent(s) shall answer in the manner provided for response to the Claim, as provided in (1) and (2) above.

(4) The Claimant shall serve each party with a reply to a Counterclaim within ten (10) business days of receipt of an Answer containing a Counterclaim. The reply shall also be filed with the Director of Arbitration with sufficient additional copies for the arbitrator(s).

(5) The Director of Arbitration may extend any period in this section (whether such be denominated as a Claim, Answer, Counterclaim, Cross-Claim, Reply, or Third-Party pleading).

(d) Joining and Consolidation—Multiple Parties

(1) Permissive Joinder. All persons may join in one action as claimants if they assert any right to relief jointly, severally, or in the alternative in respect of or arising out of the same transaction, occurrence, or series of transactions or occurrences and if any question of law or fact common to all these parties will arise in the action. All persons may be joined in one action as respondents if there is asserted against them jointly, severally, or in the alternative, any right to relief in respect of or arising out of the same transaction, occurrence, or series of transactions or occurrences and if any question of law or fact common to all respondents will arise in the action. A claimant or respondent need not be interested in obtaining or defending against all the relief demanded. Judgment may be given for one or more of the claimants according to their respective rights to relief, and against one or more respondents according to their respective liabilities.

(2) In arbitrations where there are multiple Claimants, Respondents and/or Third-Party Respondents, the Director of Arbitration shall be authorized to determine preliminarily whether such parties should proceed in the same or separate arbitrations. Such de-

terminations will be considered subsequent to the filing of all responsive pleadings.

(3) The Director of Arbitration shall be authorized to determine preliminarily whether claims filed separately are related and shall be authorized to consolidate such claims for hearing and award purposes.

(4) All final determinations with respect to joining, consolidation, and multiple parties under this subsection shall be made by the arbitration panel.

SECTION 14.

Designation of Time and Place of Hearings

The time and place for the initial hearing shall be determined by the Director of Arbitration and each hearing thereafter by the arbitrators. Notice of the time and place for the initial hearing shall be given at least eight (8) business days prior to the date fixed for the hearing by personal service, registered, or certified mail to each of the parties unless the parties shall, by their mutual consent, waive the notice provisions under this section. Notice for each hearing, thereafter, shall be given as the arbitrators may determine. Attendance at a hearing waives notice thereof.

SECTION 15.

Representation by Counsel

All parties shall have the right to representation by counsel at any stage of the proceedings.

SECTION 16.

Attendance at Hearings

The attendance or presence of all persons at hearings, including witnesses, shall be determined by the arbitrators. However, all parties to the arbitration and their counsel shall be entitled to attend all hearings.

SECTION 17.

Failure to Appear

If any of the parties, after due notice, fails to appear at a hearing or any adjourned hearing session, the arbitrators may, in their discretion, proceed with the arbitration of the controversy. In such cases, all

awards shall be rendered as if each party had entered appearance in the matter submitted.

SECTION 18.

Adjournments

(a) The arbitrators may, in their discretion, adjourn any hearing(s) either on their own initiative or on the request of any party to the arbitration.

(b) A party requesting an adjournment after arbitrators have been appointed shall, if an adjournment is granted, deposit a fee, equal to the initial deposit of forum fees for the first adjournment and twice the initial deposit of forum fees, not to exceed \$1,000, for a second or subsequent adjournment requested by that party. The arbitrators may waive the deposit of this fee or in their awards may direct the return of the adjournment fee.

(c) Upon receiving a third request consented to by all parties for an adjournment, the arbitrators may dismiss the arbitration without prejudice to the Claimant filing a new arbitration.

SECTION 19.

Acknowledgement of Pleadings

The arbitrators shall acknowledge to all parties present that they have read the pleadings filed by the parties.

SECTION 20.

General Provision Governing a Pre-Hearing Proceeding

(a) Requests for Documents and Information

The parties shall cooperate to the fullest extent practicable in the voluntary exchange of information to expedite the arbitration. Any request for documents or other information should be specific, relate to the matter in controversy, and afford the party to whom the request is made a reasonable period of time to respond without interfering with the time set for the hearing.

(b) Document Production and Information Exchange

(1) Any party may serve a written request for information or documents ("information request") upon another party twenty (20) business days or more after service of the Statement of Claim by the Director of Arbitration or upon filing of the Answer, whichever is

earlier. The requesting party shall serve the information request on all parties and file a copy with the Director of Arbitration. The parties shall endeavor to resolve disputes regarding an information request. Such efforts shall be set forth in the objection.

(2) Unless a greater time is allowed by the requesting party, information requests shall be satisfied or objected to within thirty (30) calendar days from the date of service. Any objection to an information request shall be served by the objecting party on all parties and filed with the Director of Arbitration.

(3) Any response to objections to information requests shall be served on all parties and filed with the Director of Arbitration and within ten (10) calendar days of receipt of the objection.

(4) Upon the written request of a party who does not receive the sought information the matter will be referred by the Director of Arbitration to either a pre-hearing conference under paragraph (d) of this section or to a selected arbitrator under paragraph (c) of this section.

(c) Pre-Hearing Exchange

At least ten (10) calendar days prior to the first scheduled hearing date, all parties shall serve on each other copies of documents in their possession and shall identify witnesses they intend to present at the hearing. The arbitrator(s) may exclude from the arbitration any documents not exchanged or witnesses not identified. This paragraph does not require service of copies of documents or identification of witnesses that parties may use for cross-examination or rebuttal.

(d) Pre-Hearing Conference

(1) Upon the written request of a party, an arbitrator, or at the discretion of the Director of Arbitration, a pre-hearing conference shall be scheduled. The Director of Arbitration shall set the time and place of a pre-hearing conference and appoint a person to preside. The pre-hearing conference may be held by telephone conference call. The presiding person shall seek to achieve agreement among the parties on any issues that relate to the pre-hearing process or to the hearing including, but not limited to, the exchange of information, exchange or production of documents, identification of witnesses, identification and exchange of hearing documents, stipulations of facts, identification and briefing of contested issues, and any other matters that will expedite the arbitration proceedings.

(2) Any issues raised at the pre-hearing conference that are not

resolved may be referred by the Director of Arbitration to a single member of the Arbitration Panel for decision.

(e) Decisions by Selected Arbitrator

The Director of Arbitration may appoint a single member of the Arbitration Panel to decide all unresolved issues referred to under this section. Such arbitrator shall be authorized to act on behalf of the panel to issue subpoenas, direct appearance and production of documents, and set deadlines. Decisions under this paragraph shall be made based on the papers submitted by the parties, unless the arbitrator calls a hearing. The arbitrator may elect to refer any issue under this paragraph to the full panel.

(f) Subpoenas

The arbitrator(s) and any counsel of record to the proceeding shall have the power of the subpoena process as provided by law. All parties shall be given a copy of the subpoena upon its issuance. The parties shall produce witnesses and present proofs to the fullest extent possible without resort to the subpoena process.

(g) Power to Direct Appearance and Production of Documents

The arbitrator(s) shall be empowered without resort to the subpoena process to direct the appearance of any person employed by or associated with any member or member organization of the self-regulatory organization and/or the production of any records in the possession or control of such persons or members. Unless the arbitrator(s) directs otherwise, the party requesting the appearance of a person or the production of documents under this section shall bear all reasonable costs of such appearance and/or production.

SECTION 21.

Evidence

The arbitrators shall determine the materiality and relevance of any evidence proffered and shall not be bound by rules governing the admissibility of evidence.

SECTION 22.

Interpretation of the Code

The arbitrators shall be empowered to interpret and determine the

applicability of all provisions under this Code. This interpretation shall be final and binding upon the parties.

SECTION 23.

Determinations of Arbitrators

All rulings and determinations of the panel shall be [by] a majority of the arbitrators.

SECTION 24.

Record of Proceedings

A verbatim record by stenographic reporter or tape recording of all arbitration hearings shall be kept. If a party or parties to a dispute elect to have the record transcribed, the party or parties making the request shall bear the cost of such transcription unless the arbitrators direct otherwise. The arbitrators may also direct that the record be transcribed. If the record is transcribed at the request of any party, a copy shall be provided by the arbitrators.

SECTION 25.

Oaths of the Arbitrators and Witnesses

Prior to the commencement of the first session, an oath or affirmation shall be administered to the arbitrator(s). All testimony shall be under oath or affirmation.

SECTION 26.

Amendments

(a) After the filing of any pleadings, if a party desires to file a new or different pleading, such change must be made in writing and filed with the Director of Arbitration. The Director of Arbitration shall endeavor to serve promptly by mail or otherwise upon all other parties a copy of said change. The other parties may, within ten (10) business days from the receipt of service, file a response with the Director of Arbitration.

(b) After a panel has been appointed, no new or different pleadings may be filed except for a responsive pleading as provided for in (a) above or with the panel's consent.

SECTION 27.

Reopenings of Hearings

Where permitted by law, the hearings may be reopened by the arbitrators on their own motion or in the discretion of the arbitrators upon application of a party at any time before the award is rendered.

SECTION 28.

Awards

(a) All awards shall be in writing and signed by a majority of the arbitrators or in such manner as is required by law. Such awards may be entered as a judgment in any court of competent jurisdiction.

(b) Unless the law directs otherwise, all awards rendered pursuant to this code shall be deemed final and not subject to review or appeal.

(c) The Director of Arbitration shall endeavor to serve a copy of the award:

(i) by registered or certified mail upon all parties or their counsel, at the address of record; or

(ii) by personally serving the award upon the parties; or

(iii) by filing or delivering the award in such manner as may be authorized by law.

(d) The arbitrator(s) shall endeavor to render an award within thirty (30) business days from the date the record is closed.

(e) The award shall contain the names of the parties, a summary of the issues in controversy, the damages and/or other relief requested, the damages and/or other relief awarded, a statement of any other issues resolved, the names of the arbitrators, and the signatures of the arbitrators concurring in the award.

(f) Summary information contained in the awards shall be made publicly available in accordance with the policies of the sponsoring self-regulatory organization.

(g) In addition, arbitrators may award interest as they deem appropriate. All awards shall bear interest from the date of the award until payment at the legal rate, if any, then prevailing in the state where the award was rendered, or at a rate set by the arbitrator(s) in the award.

(h) All monetary awards shall be paid within thirty (30) days of receipt unless a motion to vacate has been filed with a court of competent jurisdiction.

SECTION 29.

Agreement to Arbitrate

This Code shall be deemed a part of and be incorporated by reference in every agreement to arbitrate under the Constitution and Rules of the (name of the SRO) including a duly executed Submission Agreement.

SECTION 30.

Schedule of Fees for Customer Disputes

(a) At the time of filing a Claim, Counterclaim, Third-Party Claim, or Cross-Claim, a party shall deposit with the self-regulatory organization the amount indicated below unless such deposit is specifically waived by the Director of Arbitration.

Amount in Dispute (Exclusive of interest and expenses)	Deposit
\$1,000 or less	\$15
Above \$1,000 but not exceeding \$2,500	\$25
Above \$2,500 but not exceeding \$5,000	\$100
Above \$5,000 but not exceeding \$10,000	\$200
Above \$10,000 but not exceeding \$50,000	\$400
Above \$50,000 but not exceeding \$100,000	\$500
Above \$100,000 but not exceeding \$500,000	\$750
Above \$500,000	\$1000

When the amount in dispute is \$10,000 or less, no additional deposits shall be required despite the number of hearing sessions. When the amount in dispute is above \$10,000 and multiple hearing sessions are required, the arbitrators may require any of the parties to make additional deposits for each additional hearing session. In no event shall the aggregate amount deposited per hearing session exceed the amount of the initial deposit(s) as set forth in the above schedule.

(b) A hearing session is any meeting between the parties and the arbitrator(s), including a pre-hearing conference, which lasts four (4) hours or less.

(c) The arbitrators, in their awards, may determine the amount chargeable to the parties as forum fees (fees) and shall determine who shall pay such fees.

When the amount in dispute is \$10,000 or less, total fees chargeable to the parties shall not exceed the amount of the total initial deposit deposited by the parties, regardless of the number of hearing sessions

conducted. When the amount in dispute is above \$10,000, fees chargeable to the parties per hearing session may equal but shall not exceed the amount of the total initial deposit(s) made by the parties.

Amounts deposited by a party shall be applied against fees, if any. If the fees are not assessed against a party who had made a deposit, the deposit will be refunded. In addition to forum fees, the arbitrator(s) may determine in his awards the amount of costs incurred pursuant to Sections 18, 20, and 25 and, unless applicable law directs otherwise, other costs and expenses of the parties and arbitrator(s) that are within the scope of the agreement of the parties or otherwise is permitted by law. The arbitrator(s) shall determine who shall pay such costs.

(d) If the dispute, claim, or controversy does not involve or disclose a money claim, the amount to be deposited by the Claimant shall be \$300, or such amount as the Director of Arbitration or the panel [of] arbitrators may require, but shall not exceed \$1,000.

(e) In any matter settled or withdrawn within eight (8) business days prior to the first scheduled hearing session, the SRO may retain the amount deposited as forum fees or a portion thereof. This section shall not apply to (small) claims filed under Section 2 of this Code.

(f) Any matter submitted and thereafter settled, or withdrawn subsequent to the commencement of the first hearing sessions may be subject to such refund of assessed deposits, if any, as the panel of arbitrators presiding may determine.

(g) The arbitrators may assess forum fees and costs incurred pursuant to Section 18, 20, and 25 in any matter settled or withdrawn subsequent to the commencement of the first sessions.

(h) The fee for pre-hearing conferences shall be 75 percent of the fees contained in subsection (a).

SECTION 31.

Requirements When Using Pre-Dispute Arbitration Agreements with Customers

(1) Any pre-dispute arbitration clause shall be highlighted and shall be immediately preceded by the following disclosure language (printed in outline form as set forth herein) that shall also be highlighted:

(a) Arbitration is final and binding on the parties.

(b) The parties are waiving their right to seek remedies in court including the right to jury trial.

(c) Pre-arbitration discovery is generally more limited than and different from court proceedings.

(d) The arbitrator's award is not required to include factual findings or legal reasoning and any party's right to appeal or to seek modification of rulings by the arbitrators is strictly limited.

(e) The panel or arbitrators will typically include a minority of arbitrators who were or are affiliated with the securities industry.

(2) Immediately preceding the signature line, there shall be a statement that shall be highlighted and separately initialed by the customer that the agreement contains a pre-dispute arbitration clause. The statement shall also indicate at what page and paragraph the arbitration clause is located.

(3) A copy of the agreement containing any such clause shall be given to the customer who shall acknowledge receipt thereof on the agreement or on a separate document.

(4) No agreement shall include any condition that limits or contradicts the rules of any self-regulatory organization or limits the ability of a party to file any claim in arbitration or limits the ability of the arbitrators to make any award.

(5) The requirements of this section shall apply only to new agreements signed by an existing or new customer of a member or member organization after 120 days have elapsed from the date of Commission approval of this rule.

Appendix C

Sections of the Security Industry Conference on Arbitration Uniform Code of Arbitration as they generally appear in codes of participating Security Regulatory Organizations.

UNIFORM CODE OF ARBITRATION	ASE CODE	CBOE CODE	MSRB CODE	NASD CODE	NYSE CODE	PSE CODE
Section 1: Arbitration	Const. Art. VIII §§1, 2(a)	Rule 18.3	Section 1	Section 12	Rule 600	Section 1
Section 2: Simplified Arbitration	Rule 621	Rule 18.4	Section 34	Section 13	Rule 601	Section 2
Section 3: Hearing Requirements; Waiver of Hearing	Rule 604	Rule 18.5	Section 15	Section 14	Rule 602	Section 3
Section 4: Time Limitation Upon Submission	Rule 605(a)	Rule 18.6	Section 6	Section 15	Rule 603	Section 4
Section 5: Dismissal of Proceedings	Rule 605(b)	Rule 18.7	Section 9	Section 16	Rule 604	Section 5
Section 6: Settlements	Rule 605(c)	Rule 18.8	Section 10	Section 17	Rule 605	Section 6
Section 7: Tolling of Time Limitations	Rule 605(d)	Rule 18.9	Sections 11 and 6	Section 18	Rule 606	Section 7
Section 8: Designation of Number of Arbitrators	Rule 602(a) and (c)(1)	Rule 18.10	Section 12	Section 19	Rule 607	Section 8(a)
Section 8(b): Composition of Panel	Rule 602(d)	Rule 18.10	Section 8	Section 20	Rule 607(b)	Section 8(c)
Section 9: Notice of Selection of Arbitrators	Rule 602(e)	Rule 18.11	Sections 8 and 14	Section 21	Rule 608	Section 9
Section 10: Challenges	Rule 602(f)	Rule 18.12	Section 8	Section 22	Rule 609	Section 10
Section 11: Disclosures Required of Arbitrators	Rule 603	Rule 18.13	Section 13	Section 23	Rule 610	Section 11
Section 12: Disqualification or disability of Arb.	Rule 602(g)	Rule 18.14	Section 14	Section 24	Rule 611	Section 12
Section 13: Initiation of Proceedings	Rule 606	Rule 18.15	Section 5	Section 25	Rule 612	Section 13
Section 14: Designation of Time and Place of Hearings	Rule 608(a)	Rule 18.16	Section 16	Section 26	Rule 613	Section 14
Section 15: Representation by Counsel	Rule 608(b)	Rule 18.17	Section 17	Section 27	Rule 614	Section 15

Appendix C (cont'd)

UNIFORM CODE OF ARBITRATION	ASE CODE	CBOE CODE	MSRB CODE	NASD CODE	NYSE CODE	PSE CODE
Section 16: Attendance at Hearings	Rule 608(c)	Rule 18.18	Section 18	Section 28	Rule 615	Section 16
Section 17: Failure to Appear	Rule 608(d)	Rule 18.19	Section 19	Section 29	Rule 616	Section 17
Section 18: Adjournments	Rule 608(e)	Rule 18.20	Section 20	Section 30	Rule 617	Section 18
Section 19: Acknowledgment of Pleadings	Rule 609	Rule 18.21	Section 21	Section 31	Rule 618	Section 19
Section 20: Pre-Hearing Procedures	Rules 607 and 611	Rule 18.15(e)	Section 22	Section 32	Rule 619	Section 20(b)
Section 20(f): Subpoenas	Rule 610(a)	Rule 18.15(e)	Section 23	Section 33	Rule 619(f)	Section 20(a)
Section 21: Evidence	Rule 612(a)	Rule 18.24	Section 24	Section 34	Rule 620	Section 22
Section 22: Interpretation of the Code	Rule 612(b)	Rule 18.25	Section 25	Section 35	Rule 621	Section 23
Section 23: Determinations of Arbitrators	Rule 613	Rule 18.26	Section 26	Section 36	Rule 622	Section 24
Section 24: Record of Proceedings	Rule 614	Rule 18.27	Section 27	Section 37	Rule 623	Section 25
Section 25: Oaths of Arbitrators and Witnesses	Rule 615	Rule 18.28	Section 28	Section 38	Rule 624	Section 26
Section 26: Amendments	Rule 616	Rule 18.29	Section 29	Section 39	Rule 625	Section 27
Section 27: Reopening of Hearings	Rule 617	Rule 18.30	Section 30	Section 40	Rule 626	Section 28
Section 28: Awards	Rule 618	Rule 18.31	Section 31	Section 41	Rule 627	Section 29
Section 29: Miscellaneous	Rule 619	Rule 18.32	Section 32	Section 42	Rule 628	Section 30
Section 30: Schedule of Fees for Customer Disputes	Rule 620	Rule 18.33	MRSB Rule A-16	Section 43	Rule 629	Section 31
Section 31: Requirements for Pre-Dispute Agreements	Rule 427	Rule 18.35	Section 36	Fair Prac. Rul. Art. III §21(f)	Rule 637	

