Fordham Law Review

Volume 63 | Issue 5 Article 10

1995

Welcoming Remarks (December 5, 1994)

Recommended Citation

Welcoming Remarks (December 5, 1994), 63 Fordham L. Rev. 1599 (1995).
Available at: https://ir.lawnet.fordham.edu/flr/vol63/iss5/10

INTRODUCTORY REMARKS

PROF. COFFEE: Good morning, and thank you for coming.

As you know, I missed the last meeting of this body. I was caught somewhere between here and Tokyo, which is at least a partial excuse. But I missed it, and it was a loss because over the weekend I read the transcript of the first session, and I learned a great deal from it. I realized going through the details of punitive damages, the *Mastrobuono*[166] case, the six-year rule, and other topics, that there is very little I can tell you. You know a great deal, and you were very good last time at presenting clear, concise statements that I think will be very useful.

However, while I can't tell you more about what you already are doing, I think what academics can sometimes do is look a little bit over the horizon and say what issues are creeping up on us—what issues are about to surface. Then, with those issues in mind, we can discuss the policy responses that may be appropriate, both today and tomorrow.

First, while I was in Japan, we had an election in the United States. It was an election, by the way, that was very hard to explain to the Japanese, who like certainty and stability. One upshot of that election is a lot of new legislation that is either pending or likely to be soon introduced.

One such effort is a draft bill that I have with me drafted by the House Republicans called the Common Sense Legal Reforms Act of 1995.[167] I received this bill recently from the General Counsel's office of the SEC, and it looks like it will receive some serious legislative attention.

I don't know what will happen to it, but I am using this as a straw in the wind. One provision in this bill would amend section 21 of the Securities Exchange Act[168] to add a simple loser-pays provision,[169] the so-called English Rule, under which the loser must pay, in the case of

166. Mastrobuono v. Shearson Lehman Hutton, Inc., No. 94-18, 1995 U.S. LEXIS 1820, at *21 (U.S. March 6, 1995), *rev'g* 20 F.3d 713 (7th Cir. 1994).

167. H.R. 10, 104th Cong., 1st Sess. (1995). For a discussion of the bill, see Peter Passell, *Civil Justice System Is Overhaul Target*, N.Y. Times, Jan. 27, 1995, at B7; Richard B. Schmitt, *Republican Insurgents Request Wider Legal Reform*, Wall St. J., Feb. 15, 1995, at B3.

168. Securities Exchange Act of 1934, 15 U.S.C. § 78u (1992).

169. H.R. 10, *supra* note 167, § 203(a). In a recent speech, however, Securities and Exchange Commission Chairman Arthur Levitt said that he opposes the loser-pays rule in securities litigation. *See Subcommittee to Hold Another Hearing on Securities Litigation Reform Measure*, 27 Sec. Reg. & L. Rep. 168 (1995). Republican Senator Orrin Hatch of Utah, the Chairman of the Senate Judiciary Committee, also said he does not support a loser-pays rule. *See* Paul M. Barrett, *Warily, Hatch Mulls Changes in Civil Justice*, Wall St. J., Jan. 31, 1995, at B1. The United States House of Representatives recently passed a bill that would require someone who brings an unsuccessful lawsuit to pay all of the court costs and legal fees of the defendant if the judge

any Securities Act or any Securities Exchange Act claim, the prevailing parties' reasonable attorneys' fees plus all of their other expenses. A similar provision in this bill, by the way, says the same for diversity litigation, whether or not it raises a Securities Act claim.[170]

A final provision that I particularly want to direct your attention to would amend and add a new section 39 to the Securities Exchange Act of 1934. It is entitled, "The Alternative Dispute Resolution Procedures Act," and it would authorize either side in any action filed under the Securities Exchange Act to "offer to proceed pursuant to any voluntary, nonbinding alternative dispute resolution procedure established or recognized . . . under the rules of the court in which such action is maintained."[171]

The other side in the litigation normally would have to respond within ten days, but the court could stretch the proceeding out ninety days to identify what kind of alternative dispute resolution procedures might be employed.

Now, my point here begins with the observation that with the *McMahon*[172] case, back in 1987, arbitration suddenly exploded. Securities arbitration went from voluntary to mandatory, and the volume of arbitration proceedings before the SROs doubled in two years. Maybe SROs weren't fully prepared for the volume that suddenly hit them.

Well, with the approaching prospect of two new developments, (1) the possibility of the English Rule applied to the securities claims and (2) the possibility that courts will have to start every proceeding that involves a Securities Exchange Act claim with a discussion of whether there are available alternative dispute resolution procedures that the parties can employ, we may again find a substantial migration of cases to arbitration.

Of course, I recognize that the alternative dispute resolution provision is voluntary, but through their docket control and through their body language, the courts often can make what is in theory voluntary, in reality a little bit less than voluntary. We may be at a point where we are going to see another major quantum leap within the next year or so in the volume of arbitration, and this raises one of those important questions: Are the SROs going to be able to adjust easily, hitch their belts up two notches, and vastly increase arbitration?

The other issue that I believe deserves highlighting at the outset involves not a quantitative issue, but a qualitative one: How much can one Uniform Code of Arbitration really attempt to do?

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deems the suit to have been poorly grounded. Neil A. Lewis, *House Passes Bill That Would Limit Suits of Investors*, N.Y. Times, Mar. 9, 1995, at A1.

170. H.R. 10, *supra* note 167, § 101.

171. S. 687, 103d Cong., 1st Sess., § 102(a) (1993).

172. Shearson/American Express Inc. v. McMahon, 482 U.S. 220 (1987).

This year, in the *Salomon* litigation,[173] Judge Patterson of the Southern District stayed a derivative action proceeding in the Southern District of New York to permit the New York Stock Exchange to decide if the subject matter of that arbitration, the derivative claim, was subject to arbitration under the New York Stock Exchange's rules.

As many of you know, New York Stock Exchange Rule 600(d) excludes from the scope of claims subject to arbitration those submitted as a class action and claims filed by persons who are members of a putative class action.[174] Let's call this simply the "class action exclusion provision."

The issue that Judge Patterson decided to stay in deference to the New York Stock Exchange (and which is on the Exchange's agenda in the near future) is this one: Is a derivative action sufficiently like a class action that it should also be excluded, or is it different enough, because at bottom it is the corporation's claim against its officers that is being decided, so that it should be covered by the New York Stock Exchange's arbitration rules?

I don't mean to attempt to decide this case this morning. It is on the Exchange's agenda. They will look at it in due course. But it is illustrative of my point: There are some very different claims, claims not involved in classic, "plain vanilla" arbitration of disputes between broker and client, that are now arguably the subject of broker-dealer arbitration agreements.

Without prejudging the issue, I will remind you that Judge Patterson, in his decision, expressed some doubt that the square peg could fit into the round hole—that is, that derivative litigation could be melded into an arbitration procedure.

Indeed, defendants as well as plaintiffs may have reason to doubt that arbitration is adequate to resolve derivative claims without the process distorting the substance. In a normal derivative action there is something called the "demand rule" and also the "business judgment rule." Both of those are very important protections for corporate officers and directors.

In an arbitration proceeding where the arbitrators may examine the substantive issue from a more equitable perspective, the business judgment rule, and maybe the demand rule, may get less attention than they would receive in the Delaware Chancery Court.

In any event, my basic point is that derivative actions, much like the area of employment discrimination cases, which we'll be talking about later today, involve very different kinds of substantive claims and possibly very different kinds of procedures than we ordinarily see in arbi-

173. *In re* Salomon Inc. Shareholders Sec. Derivative Litig., 91 Civ. 5500, 1994 U.S. Dist. LEXIS 13874 (S.D.N.Y. Sept. 28, 1994).
174. NYSE Rules, *supra* note 14, Rule 600(d), ¶ 2600.

tration. Hence, can all these new claims sensibly be resolved within the tent of one Uniform Code of Arbitration, or, as we look at the future, will there have to be special little subchapters?

The process of taking a uniform code and making it a little less uniform and adopting special rules for special contexts—whether it is employment discrimination cases or derivative actions—may over time erode the uniformity of the Uniform Code. Indeed, I can imagine a whole bunch of other disputes that will be brought to the arbitration forum as well.

All that I am saying is that the concept of arbitration has been stretched by various means—by contract, as we discussed last time, by proposed legislation (which may only be a straw in the wind), and by new claims that are being brought within the arbitration clause without the parties having been aware of the degree of breadth that was inherent in their contract. Inevitably, the nature of arbitration will change under the pressure of both qualitative and quantitative expansion. Given that arbitration is being stretched out over distant terrain, current thinking must focus on whether there have to be changes, subtle and otherwise, in the procedures used.

Having said that, I am going to turn the proceedings over to a real authority on arbitration, Gus Katsoris.

PROF. KATSORIS: Thank you, Jack.

Jack mentioned the Uniform Code, and perhaps one size doesn't fit all. It is an interesting observation because in the nearly fourteen years since we've had the Code, arbitrations filed with the SROs have grown from slightly over eight hundred to over six thousand per year.

Not only have the numbers grown dramatically, but the cases coming into arbitration are now far more complex. With this influx, many problems of the courtroom have similarly surfaced.

The purpose of this Symposium is to discuss these issues frankly and honestly.

I commend the New York Stock Exchange for initiating this dialogue. What we say here today not only has relevance to securities arbitration, but in the future will be a blueprint for many other industries that are following in this alternative-dispute-resolution mode.

Let me emphasize one rule of protocol that was established at the last meeting. We all feel very strongly about some of the issues, and we have people here with opposing views. We don't want the discussion to get personal. We encourage frankness, but we are not here to offend or embarrass anybody. We're here to put the issues on the table with a view towards resolving them.

The format that was established at the last session and worked rather smoothly is as follows: Each panelist will speak for about ten or fifteen minutes on the particular subject, and then we'll open it up for comments. When we are through with the comments, we will then open it up for questions and answers.

We'll try to limit the discussion of each topic to about an hour or so.