Securities Arbitration Commentator, Inc.

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September 19, 2005

Jonathan G. Katz, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-9303

RE: SR-NASD-2005-094 (Arbitrator Classification)
SR-NYSE-2005-93 (Arbitrator Classification)

Dear Secretary Katz:

I applaud the Commission for lining up these two rule proposals, which derive from the same origins and contain similar text, for public comment together. Both NASD and NYSE seek to revise their arbitration rules to make the "Public Arbitrator" even more removed from having any industry ties or even being related to someone who does. I presume that, in issuing the two proposals contemporaneously, the SEC is seeking public comment on why the two Rules need to be different and, in that effort, I think the Commission is approaching the issue exactly right.

Background-Commentary

To me, it is less important which version of this proposal the SEC approves than it is that the SEC approves the same version for both forums. There is simply no reason why the SROs need to have different versions of a rule that they in philosophical terms agree upon. It makes it more difficult for the individual Claimant or practitioner -- not to mention the neutral who serves both forums and conceivably qualifies as a "Non-Public" Arbitrator at the one forum and a "Public" Arbitrator at the other forum -- to keep straight the nuances of the two Rules and to observe both faithfully.

The NASD, since the early 90's has, with the SEC's tolerance, changed its arbitration rules on a unilateral basis without real consultation through SICA with the other active arbitration forums. Because of its dominance in arbitration, NASD has argued that it has special problems requiring tailored solutions, that it could not wait to act while SICA slowly addressed the issues at hand, and that SICA's raison detre – uniform rulemaking among the SRO forums and the need for a public voice in that process – were outdated and unnecessary. While far more deferential in the past to SICA, NYSE has, in recent times, taken to "going it alone" as well and, when copying NASD Rules, changing the text without good reason from the NASD version.

Generally speaking, this is bad policy the SEC is following. In the arbitration "market," NASD is so dominant that differences in the text and purport of NASD Rules make it more difficult for attorneys to move from forum to forum. Rather than creating competition by having SRO forums with different rules, the SEC is merely securing NASD's place as virtually the only game in town. One need only take a look at the NYSE's claims filing figure for 2005 to see that

this has become more and more the case.

Neither NYSE nor NASD should be encouraged to sidestep the discipline of having to vet rule proposals with SICA and of having to explain to the SEC why text changes vary from SICA's recommended version of a rule. It is a good thing that the SEC apparently wants NASD and NYSE to have the same language in the two rule changes before the Commission. It should also want the SROs to have conferred with SICA and to have sought to iron out textual differences before laying that task before the Commission and its staff.

The two current proposals differ significantly from the Uniform Code of Arbitration's classification rule. If the Commission is going to approve these proposals without compelling the SROs to return to SICA first, I respectfully suggest that the Commission should establish as its standard for approval that rule proposal which most closely adheres to the SICA model. In most ways, this is the NYSE proposal.

Specific Comments

Let me address some of the major differences between the two proposals. The Commission has asked for comment on a unique "registered through" modifier NASD has developed. The statutory definition of an "associated person" is extremely broad and so, too, is the NASD's definition of that term. It does not require an extender in the form of "registered with," but placing "registered with" in a conjunctive position with "associated with" implies that "associated with" is a limited phrase. The Commission can find that the "associated with" language is sufficiently broad to subsume virtually all manner of registration.

Both forums are proposing to make arbitrators ineligible for the "public arbitrator" classification if they are employed not only by securities organizations (e.g., the broker at Smith Barney), but by companies in a control relationship with an "organization that is engaged in the securities business." (e.g., the teller at Citibank as opposed to the broker at Smith Barney) NYSE adopts the "immediate family member" extension (IFM), rather than SICA's "member of the household" extension to exclude, as NASD does, not only related people living together or financially dependent, but also related people without regard to common residence (or, seemingly, financial ties). However, NYSE appears to apply that extension only to exclude "IFMs" of associated persons (e.g., the IFM of the Smith Barney broker), as opposed to NASD's exclusion of "IFMs" of all control-related parties (e.g., the IFM of the Citibank teller). The NASD goes too far. Arbitrators will inadvertently violate this provision.

The most petulant of differences that NASD and NYSE have contrived is the listing of what "relatives" are included in the "immediate family member" extension. Both go well beyond the SICA extension, but in doing so they also take different paths. For reasons that are not well-explained, NASD chooses to include as related parties within the IFM extension, step-parents and step-children, while NYSE's proposed IMF extension does not. On the other hand, NYSE's IMF extension includes in-laws, while NASD's IMF extension does not. If the SEC chooses to settle the matter, rather than getting SICA's advice, it might simply compel each SRO to adopt both the in-law and step-relative extensions.

I think these rule changes should have been brought to the Commission with the same text after being vetted by SICA. If the Commission does not choose to enforce that discipline in this case, it should at the least compel these two organizations to work together to come up with identical solutions to a problem they perceive identically in concept.

Eliminating the Industry Arbitrator

Neither SRO, nor SICA (which has three representatives from the public arena), sees the wisdom of eliminating the “Non-Public” or “Securities” or “Industry” Arbitrator from the classification rules. The SEC should not consider that possibility until it is properly placed before the Commission in the form of a rule proposal or SICA recommendation. That a group of lawyers have combined to suggest, by way of a score or more of individual comments to these Rule proposals, that the SEC should eliminate the Industry Arbitrator classification does not make it worthy of consideration.

The proposal at hand may be adopted without denying the “elimination” issue consideration through the appropriate organs of SRO rulemaking. Our views on the issue are primarily focused on the question of need and, in that regard, we attach a survey of Arbitration Awards that appeared in a recent copy of this writer’s newsletter on securities arbitration.

Thank you for this opportunity to comment.

Sincerely,

Richard P. Ryder

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INDUSTRY ARBITRATOR AWARD SURVEY

Does the Securities Industry Arbitrator's Presence Create a Discernible Shift in Award Outcomes?

Recent Background

At the March 17 hearings to review the securities arbitration process, Congressman Barney Frank (D-MA), the Ranking Member of the House Financial Services Committee (HSFC) was on the attack. Primarily responsible for arranging the afternoon session before the HFSC's Subcommittee on Capital Markets, Insurance, and Government-Sponsored Enterprises, Rep. Frank focused on the "mandatory" nature of the securities arbitration compact between customer and broker-dealer, but the March 17 hearings revealed three major policy points at issue.

Those policy points arise in different ways in the securities arbitration dialogue, but they are basically this: (1) Should brokerage customers be compelled by pre-dispute contractual consent to arbitrate their disputes or should the arbitration option be "voluntary"? (2) If mandatory arbitration remains, should NASD and the other SROs be the arbitration providers for investor disputes or should some independent organization take control of the process? (3) If the SROs remain, should their panel composition rules be altered to eliminate the Non-Public (aka Industry or Securities) Arbitrator? The focus of this article falls upon the final policy question.

Testifying before the Subcommittee was a representational assemblage of the most visible contingents in securities arbitration. Advocates for the investor appeared in the form of **Daniel Solin,** an independent voice, who represents Claimants and has written a book about securities arbitration ("Does Your Broker Owe You Money?"); **Rosemary Shockman**, President of the Public Investors Arbitration Bar Association; and a state securities representative, Secretary of the Massachusetts Commonwealth, **William Francis Galvin**.

Notably, PIABA chooses to work within the arbitration system. Messrs. Galvin and Solin find it irredeemably tainted. Ms. Shockman complained about a number of aspects of the process that require improvement. She singled out the New York Stock Exchange program on issues of delay and fairness, lamenting that, for the time being, investors are left with only one forum they can practicably choose to use. At that juncture, she might have joined the NASAA camp and argued for an "independent" forum. Instead, Ms. Shockman gave neither support to the Franks position that arbitration should be voluntary, nor aid to the Galvin-NASAA position that NASD and NYSE can never be perceived as fair arbitration providers.

Ms. Shockman and SIA President **Mark Lackritz,** who testified in general support of SRO arbitration, sparred

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on the "insider" issue of whether SRO arbitration Panels should include an Industry Arbitrator. It is important to note that these two spokespeople for the very divergent factions of Claimant and Respondent in securities arbitration did not differ seriously on the dangers of Award explanations, the inequity of binding investors to arbitration before a dispute arises, or, quite surprisingly, the structural biases of permitting a SRO forum. The flashpoint of conflict – and it was PIABA's choice – is the use of non-public arbitrators on the three–person SRO panels.

Ms. Shockman maintained that public investors entering arbitration are faced with the fear of partiality as soon as they enter the hearing room and confront an Arbitrator from the industry side. Moreover, that arbitrator, inculcated in the practices of the industry and beholden to an employer, in many instances, which is profiting from the practices at issue in the instant arbitration, are likely to interpret the activity in the context of those practices, instead of applying SRO and SEC Rules or state requirements. PIABA challenges as untrue and unnecessary the response that Industry Arbitrators are valuable for the knowledge and experience that they bring to the Panel.

Mr. Lackritz argues that the Industry Arbitrator reduces hearing time and adds value to the Panels of arbitrators because of his/her knowledge of industry practices and products. If having one "industry" neutral on the Panel creates a bias, then, rhetorically speaking, having two Public Arbitrators on the Panel argues even more strongly for the same consequence, but in the opposite way. Industry Arbitrators help achieve the right result and in less time.

Non-Public Arbitrator Impact Available Measuring Rods

Does the Industry Arbitrator (the Non-Public Arbitrator, following NASD nomenclature) have a measurable effect on the decisions reached by the Panels on which they serve? Certainly s/he does, just as every voting member of a body has an impact. Do these Arbitrators have an undue impact on the arbitral decision because they occupy a superior position afforded by greater knowledge and experience, such that Public Arbitrators are cowed into agreement? If so, is that prerogative of influence lending to abuses that tip the fairness scales in SRO arbitration and can this "bias-tipping" influence be measured by reviewing past Awards?

Several hundred Awards each year – about 15-20% of the total number of the Awards that decide customer-initiated disputes — are decided by sole Public Arbitrators. The Public Arbitrator in these cases is free from any influence, whether salutary or corrupting, that a Non-Public colleague might apply. These Small-Claims disputes are not unlike their larger Customer-Member counterparts (claims $25,000 and more) in terms of the factual nature of the dispute and, so, one might reasonably expect similar outcome per-

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centages when comparing representative samples of each.

If the Non-Public Arbitrator is improperly influencing outcomes where three-person Panels decide the case, then a measurable difference in "win" rates (which we define as the percentage of instances in which the brokerage customer receives any monetary award) could appear. A bias could be evident between outcomes in Small Claims cases, which are decided by Public Arbitrators acting alone, and three-person Panel outcomes, if the presence of the Non-Public Arbitrator "helps" the industry Respondent beat the claims against it. That bias should be reflected in the numbers, even if it arises unintentionally, as simply an institutional consequence of industry service.

Focusing the Comparisons

Of course, we recognize other factors are at work that could distinguish outcomes, such as the difference in the claim-size between the cases heard by Small Claims arbitrators and those adjudged by three-person Panels. The greater prevalence of *pro se* representation among Claimants in Small Claims cases, the probable differences in the dynamics of "committee" versus individual decision-making, and variations in the length and intensity of the litigation experience could all contribute arguably to outcome differences.

Whether these other distinguishing factors would themselves explain a difference in "win" rates between the one-Arbitrator decisions and three-Arbitrator decisions was not a proposition for which we tested. We can say this: In the 1992 study of securities arbitration conducted by the General Accounting Office (nka the Government Accountability Office), the GAO tested for quantitative differences caused by attorney representation and other factors. The Study (see 5 SAC 1(1) for a full summary) found that the "win" rates were virtually the same between *pro se* Claimant Awards and those where Claimants were represented. A measurable difference was detected on the recovery side, however. The GAO found that "recovery rates," i.e., the percentage represented by a comparison of the amount awarded to the amount claimed, were substantially greater for customers who were represented by counsel.

Checking "Win" Rates & Dissents

We do not attempt any analysis of recovery rates here. Our comparison of the Small Claims Awards to Customer-Member Awards is restricted to "win" rates, where historically the averages have not diverged greatly from one set of customer-initiated cases to the other. If the Non-Public Arbitrator is somehow pulling on the reins and restraining the entire team in three-Panelist cases, then, presumably, Panel votes in Small Claims cases will reveal that disparity with a decidedly higher "win" rate for customers.

Secondly, a look at the rare instances when Arbitrators dissent, leaving a two-person majority to determine the outcome, should be instructive on the bias issue. If Non-Public influences are biased, some differences may be noted in these Awards, because the Non-Public Arbitrator's position is not completely lost in the unanimity of the Panel. In dissent cases, the Non-Public Arbitrator either sides with the majority, with which one Public Arbitrator differs, or the Non-Public Arbitrator is the dissenting Arbitrator, standing clearly apart from the two Public Arbitrators.

Unfortunately, for our purposes, the instances of Award dissents are rare, so rare that statistical reliability of some conclusions may be questionable. Perhaps, something can be made of the rarity of dissents in securities arbitration, on the premise that a lack of disharmony exists among the two Panelist classifications. Were Non-Public Arbitrators observedly biased, one might expect to see more dissenting Public Arbitrators, who, recognizing their colleague's pushiness for what it is, resist it by registering a vote in opposition. Were Non-Public Arbitrators openly biased or just plain afraid to vote against "industry" interests, more Non-Public Arbitrator dissents might be expected.

We leave to others these arguments about the Non-Public Arbitrator's influence in unanimous-Panel Awards. For now, we have the two blunt instruments that are employed in this survey: (1) a comparison of Small Claims results to Customer-Member results; and, (2) a review of dissent Awards (which, by their nature, are limited to three-person Panels). In addition to the small number of dissent Awards, the reasons why Arbitrators dissent are not always provided and, when they are, the dissents are not always about the primary outcome. Nevertheless, these Awards, as rarities among Awards generally, are interesting for their individual character. As such, they assist a better understanding of the Non-Public Arbitrator's role, by illustration if not by statistical deduction.

Designing the Award Survey Methodology – "Win" Rates

In order to check for a difference in "win" rates between Small Claims Awards, where no Non-Public Arbitrator is present, and Customer-Member Awards, where a Non-Public Arbitrator is almost always part of the deliberating body, we isolated all Awards of those dispute types, regardless of forum. Using SAC's Award Database, we then limited the timeframe to 2004, as the most recent and presumably most relevant year, but we encountered a problem. The "win" rate for the public customer in Small Claims Awards during 2004 was surprisingly low!

We followed a protocol that we describe below for determining the "win" rate for the collected Small Claims Awards and, in doing so for 2004 Small Claims Awards, reached a 31% "win" rate for customers in "paper" cases and a 38% "win" rate for customers who elected to have a hearing. It is not unusual to find a higher "win" rate for Small Claims customers who want to present their case at hear-

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ing, rather than waive hearing and rely entirely upon documentary evidence. What was unusual were the "win" rates themselves — abnormally low from a historical standpoint.

From our statistical analysis of "Research Fraud" Awards (in 2004 SAC 8(13)), we recalled that the great majority of the cases in our sample were decided in 2004 and that a large set of the disputes were decided through the Small Claims procedures. In that survey, we found that the Small "Research Fraud" Claims achieved a very low "win" rate, about 35%. We also noted in that survey that Merrill Lynch and Smith Barney (div. of Citigroup Global Markets) accounted for a large percentage of the "Research Fraud" Awards. Similarly, Merrill Lynch and Smith Barney accounted for approximately 66% of the Small Claims Awards in our 2004 survey collection.

We decided, therefore, to use statistics based upon results in Awards that issued during 2003. In 2003, Merrill Lynch or Smith Barney were named in only 29% of the Small Claims Awards and that percentage compared neatly with the 27% we found upon checking Customer-Member Awards for the presence of either broker-dealer. Based upon this comparison, we concluded that the 2003 sample of customer-initiated Awards is not skewed by the individual phenomenon of "Research Fraud" cases (we also know from our Research Fraud Award survey that a small percentage of such Awards were rendered in 2003).

Once we determined our survey period, we had to determine win rates for each dispute type. "Wins" for customers occur when the Arbitrators determine that some monetary award is merited, based on the claims in the case. Since Stipulated Awards, memorializing with arbitral imprimatur a settlement by the parties, do not reflect merits determinations by the Arbitrators, we eliminated these Awards from our win-rate calculations. The incidence of these Stipulated Awards has grown yearly in the new millennium, constituting 23% of all Awards issued in 2004. Thus, their inclusion in win-rate (or recovery-rate) calculations in recent years would skew results dramatically.

Methodology – Dissent Awards

Finding dissent Awards was easy. The SAC Award Database identifies dissents by Arbitrator name and Public or Non-Public classification. Even where the Award does not identify the Arbitrator by his or her classification, we identify the appropriate classification by viewing other Awards in which the Arbitrator's classification is provided. We were able to determine Arbitrator classification in this fashion for each dissent Award in our sample.

To NASD's credit, its Dispute Resolution forum often does more than the rules call upon it to do and, as its faithful posting of detailed case statistics on its WebSite demonstrates, the forum also discloses more information in many instances than the rules specifically require. In this instance, the classification of the dissenting Arbitrator was vital to our survey. We were able to get that information from NASD Awards. The NYSE does not take the trouble and, as a consequence, we survey only NASD Awards that reflect a dissent.

Customer "Win" Rates

Small Claims Awards

With respect to the 2003 comparison of one-person to three-person Panels, we used Awards from all available forums. 326 Small Claims Awards issued from the forums in a year's time, of which twelve were Stipulated Awards. Of the 314 "merits" Awards, 146 (46%) disclosed some monetary award and qualified as a "win."

The 46% "win" rate for 2003 Small Claims Awards does not distinguish between those Awards that are decided "on the papers" by the sole Public Arbitrator and those that are decided after a hearing. Again, the dynamics are quite different between the two options the complaining customer has and we have found that those distinctions lead to substantial outcome differences. Although the Non-Public Arbitrator is not involved in either type of case, readers should weigh the impact of a hearing waiver, when comparing the Small Claims results to the outcomes in the larger-dollar, three-Panelist Awards.

228 among 314 Claimants in 2003 (73%) chose to waive a hearing and submit the case to the sole Arbitrator "on the papers." Among these 228 Awards, we found 96 instances where the Claimant received a monetary award. That 42% "win" rate for "paper" cases contrasts dismally with the outcomes in the 86 cases tried at hearing before a sole Public Arbitrator. In that milieu, 50 of the Claimants, or 58%, were successful. It may be that the Claimants with the best cases (or who have representation) make the decision to request a hearing, but we did not test for those factors. We did not attempt to parse the sample further. We simply report that a significant "win rate" differential operates when a Small Claims Claimant elects to submit "on the papers" or s/he chooses a hearing.

Customer-Member Awards

That "win" differential – a gap of 16 percentage points among two Small Claims choices – becomes important when we turn to the three-person Panels and the presence on the Panel of a Non-Public Arbitrator. Included in Customer-Member Awards, which we define as customer-initiated Awards reflecting claims exceeding $25,000, will no doubt be some single-member Panels, but very few. With rare exceptions, the forums all utilize three-person Panels with one Non-Public Arbitrator in Customer-Member cases.

Again, we eliminated Stipulated Awards from the Customer-Member Awards decided during 2003 and arrived at a total of 1,389 Awards. We found that 702 of those 1,389 Awards resulted in monetary awards for the customer, which equates to a 51% "win" rate among Customer-Member

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Awards. Trying to extrapolate that finding into a conclusion regarding the presence of a Non-Public Arbitrator is a more difficult calculation. We can clearly state, as to our samples, that the "win" rate for customers in Customer-Member cases clearly exceeds the 46% "win" rate for customers in Small Claims Awards generally.

That 51% "win" rate also materially exceeds the 42% win rate for customers who simply submit documentary evidence in "paper" cases. On a historical basis, a 51% average win rate does not fall outside the boundaries of one's expectations. If we expand the survey period to four recent years, from 2000-2003, the win rate figure for Customer Member Awards, following the same methodology, calculates to 53%. At the March 17 Congressional hearings, Prof. **Michael Perino**, author of the well-known "Perino Report" on arbitrator disclosure standards in SRO arbitration, testified on historic win rates. "From 1980 to 2002," he reported, "SRO arbitrators decided 32,732 public customer cases. Of that total, 17,211 (52.58%) resulted in customer awards."

On the other hand, the 51% win rate for Customer-Member Awards made by mixed Panels lies considerably below the 58% win rate for customers in Small Claims "hearing" Awards made by sole Public Arbitrators. Awards made after face-to-face hearings seem most comparable and that fact prevents our concluding, from a quantitative standpoint, that the Non-Public Arbitrator's presence proves neutral to helpful. We clearly do not think the data indicated a negative conclusion on the issue. *(editor's note: We did check to see how many Customer-Member Awards were decided by all-Public Arbitrator Panel, as opposed to the predominant mixed Panel. Were there enough such Awards – and there was not – the win-rate comparison to the mixed-Panel Awards might be more direct and telling.)*

2003 Awards: By TypeDispute

	Cust. Wins	Cust. Losses	"Win" Rate
Customer-Member (>$25K)	702	687	51%
Small Claims (≤$25K)	146	168	46%
Paper Only Decs (73%)	96	132	42%
Hearing Decs (27%)	50	36	58%

Dissent Awards

Dissents - Generally

We found some surprising aspects and intriguing attributes in our review of the 186 dissent Awards that have been recorded during a five-year period from 2000-2004. There were 7,127 relevant Awards during that same time frame, so that the incidence of such Awards calculates to 2.6% of the whole. While dissent Awards are quite rare, less frequent even than punitive damage awards, they have repeating features. For example, we found that one Arbitrator registered four dissents in the five-year period, one dissent while serving as Chair of the case. His dissents were relatively collegial, but, among the whole, we encountered some fiery comments.

We learned from these observations that dissent Awards are as much a statement of philosophy about one's role as Arbitrator as a tool to register disagreement.. Most times, we expect, arbitrators will work to build a consensus Award, but some Arbitrators view their role as driven more by independent responsibility and the integrity of an uncompromising outlook. In this regard, we noted that 11 Arbitrators had more than one dissent and that these 11 Arbitrators accounted for 25 of the 186 Awards. We also note the example of one experienced Arbitrator with hundreds of Awards during his career. He had only one dissent during the 2000-2004 period we surveyed, but he has registered three others during his career. Moreover, in another four cases in which he participated, dissents were registered by <u>other</u> Panelists.

So, the 186 dissent Awards do reflect some patterns of interest, but none evidencing distortions in geographic distribution or patterns from one brokerage firm Respondent to another. We tested some theories in this regard, such as a hypothetical "hometown" intimidation effect on arbitrators. Checking Raymond James, a Florida-based brokerage firm with a strong presence in Florida (40% of its Awards issue in Florida), we found five dissent Awards, but they all related to out-of-state Awards: Colorado (2x), Georgia, Kentucky and Michigan hearing locations. We found no Florida-based dissents by Non-Public Arbitrators opposing customer "wins."

A.G. Edwards, based in Missouri, appeared in six dissent Awards, but none took place in Missouri and no Non-Public Arbitrator dissented. There was one North Carolina dissent Award in a Wachovia Securities case (#00-05345, *Gregory v. Wachovia Secs.)* <u>and</u> the dissent was registered by a Non-Public Arbitrator. However, the *Gregory* Award dismissed all claims (with which the NPA disagreed), confirming only a $3,600 discovery sanction against a second broker-dealer (with which the NPA agreed).

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Dissent Awards: By Outcome				
Stipulated	**Hearing "Wins"**	**Hearing "Losses"**	**Total ("Win" %)**	
			w/ Stips.	**w/o Stips.**
24	102	60	186 (68%)	162 (63%)
Dissent By Public/Non-Public Arbitraator				
Public (19)	Public (73)	Public (44)	Pub(136)	Pub(117)
Non-Public (5)	Non-Public (29)	Non-Public (16)	NPA(50)	NPA(45)

Dissent – Damages Awarded

We noted that Arbitrators tend to dissent more when there is an award of damages. Among the 186 dissent Awards, 126 Awards (68%) reflected a "win" for the Claimant. However, 24 of those counted as "wins" were Stipulated Awards, where the purpose of the "dissent" was not to oppose settlement, but to abstain from or disagree with the awarding of expungement relief. That still leaves 102 "win" Awards in which dissents were registered among 162 Awards – about 63% of the whole.

Sorting for unusual remedies or relief, we located five awards of **punitive damages** to customers among the dissenting Awards. Non-Public Arbitrators might be expected to dissent from punitive sanctions, if some bias or fear dominated their decisionmaking. Two of the punitive-damages Awards reflected dissents by Non-Public Arbitrators, but they dissented on other grounds. In one case (#99-01790, *Basabe v. JW Barclay*), the dissent disagreed with the compensatory award, stating that she would award a "different amount," but she expressly supported the punitive award. The other Non-Public dissent disagreed with the finding of liability as to one of the individual respondents, who was not the subject of the punitive award in any case (#00-02283, *Leibschner v. MPI*).

Attorney fees granted to Claimants might be a form of relief against which a Non-Public Arbitrator with an industry bias would rebel. There were 24 instances among the 186 dissent Awards where attorney fees were awarded. Of those 24, the dissent was registered in 16 of the Awards by the Public Arbitrator and in 8 by the Non-Public Arbitrator. Only one Industry Arb directly objected to the awarding of attorney fees. He differed with the majority on its finding of liability under Florida securities law (#01-02785, *Homsie v. MLPFS*), upon which the fee award was founded.

Finally, on the theory that a **large compensatory damages award** would cause a biased Non-Public Arbitrator to dissent from the two Public Arbitrators, we isolated five NPA dissent Awards in which the amount awarded exceeded 60% of the compensatory amount claimed by the customer. Two of the dissenting Non-Public Arbitrators offered no explanation (#99-03994, *Yunger v. Siebt Finl.;* #02-05981, *Roantree v. Prudential Equity*), while three others did. Two of the "explained" dissents were covered above (*Basabe* and *Liebschner*) and neither disagreed with the size of the award. The third "explained" dissent (#98-03364, *Burton v. Creative Captl.*) concurred on an award of treble damages as to an individual Respondent, but not as to the firm or the other named individuals.

Eighteen Public Arbitrator dissents were registered in cases where the amount awarded exceeded 60% of the compensatory damages claimed – versus five Non-Public Arbitrator dissents. In seven instances, the Public Arbitrator dissented silently and, in another (#02-00354), the dissent's explanation indicated disagreement with the amount, but not which way. Five of the remaining ten dissents clearly would have voted for a smaller monetary award or a narrower finding on liability (##99-00218; 99-03489; 99-04669; 99-03260; 03-00426). The final five stated a desire for a bigger monetary award or a broader finding of liability (##01-05914; 00-04128; 99-04380; 99-04558; 04-00385).

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Dissent Awards: By Special Damages					
Punitive Damages		**Attorney Fees**		**Large Compens. $$**	
Punis	All Wins	AttyFees	All Wins	LgComps	All Wins
5	102	24	102	23	102
Dissent By Public/Non-Public Arbitraator					
Pub (3); NPA (2)		Pub (16); NPA (8)		Pub (18); NPA (5)	
NPA Opposed: 0		NPA Opposed: 1		NPA Opposed: 1	

INDUSTRY ARBITRATOR SURVEY *cont'd from page 6*

Dissent – By Classification

We next checked the breakdown of dissents, based upon the seat occupied by the dissenting Arbitrator. We guessed that Chairs would be least likely to dissent, given their leadership and consensus-building role on the Panel — and they were – but they were also less reticent about dissenting than we anticipated. Chairpersons dissented in 39 instances, constituting about 21% of the total dissents. The Non-Public Arbitrator came next, with 50 dissent Awards, less than a third (27%), and the "other" Public Arbitrator, the one who does not sit as Chair, accounted for the remainder of the 186 dissent Awards. That remaining 97 Awards, constituting more than one-half of the whole (52%), seems important, but in what regard?

Perhaps, the "other" Public Arbitrator is a "Freshman" Arbitrator who adopts his/her role with unjaded sincerity and unmoderated enthusiasm only to find that s/he cannot follow the path taken by the Non-Public Arbitrator and the Public Chair. We tested for experience by reaching back in these Arbitrators' Award history to determine their length of service. In other words, we measured the years of service from an Arbitrator's first Award to his or her first dissent Award. While we did not check all of the dissent Awards for this feature, we checked a large minority of the "other" Public Arbitrator Awards. Among approximately 40 Awards tested in this fashion, we found that half of the dissenting "other" Public Arbitrators had been Arbitrators for at least five years before dissenting. Many of the dissenting Arbitrators as a group have a score or more of Awards in which they have participated.

On the other hand, we found five instances where "Freshman" Arbitrators dissented during their early months of service or on their first Award. Here, we did encounter something in terms of a possible pattern, although we stress that the sample is quite small. Three of five "Freshman" dissents offered no explanation (#99-05002, *Butler v. AG Edwards;* #03-06514, *Baade v. Citigroup Global;* #04-04783, *Scher v. Banc of America*), but the three occurred in instances where the majority dismissed the customer-Claimant's case. A dissent in these circumstances signifies perhaps that the dissent believed liability should have been found.

The two "Freshman" Arbitrators who do offer an "explained" dissent both disagree with the amount awarded and one expressly states that the awarded amount "does not go far enough." (#99-02222, *Rieley v. Wheat First Secs.;* #99-00482, *Steinberg v. Gary Goldberg & Co.*). Given these very tenuous indications, there might well be some disillusionment among first-time Arbitrators and that possibility warrants forum attention. Whether these examples reflect a perception by these dissenting Arbitrators of a bias element is conjectural.

If one assumes that the "other" Public Arbitrator who dissents from a "no-money" Award for the customer expresses a conviction favoring liability, perhaps the same assumption applies when the Non-Public Arbitrator dissents from a "no-money" award. Among the 50 Awards reflecting NPA dissents, there were 16 in which the majority of Public Arbitrators determined that the customer should take nothing. In two of those cases, the dissent indicated agreement with the dismissal, but expressed disagreement on subsidiary matters. One Non-Public Arbitrator stated with displeasure about a pre-hearing dismissal (#01-04543, *Perlman v. DH Blair*) that it constituted "a refusal to hear evidence pertinent and material to the controversy." Five expressly indicated that liability should have been found and the remaining eight stand as dissents without explanation.

Dissent Awards: By Classification

	Chairperson	"Other" Public	Non-Public
Total (186)	39 (21%)	97 (52%)	50 (27%)
Stipulated Awards (24)	3	16	5
Wins: Monetary Awards (102)	24	49	29
Loss: No Monetary Awards (60)	12	32	16

Conclusion

The case against the "Industry" Arbitrator rests upon innuendo, *ad hoc* observations, and suspicions about the mysteries and dynamics of the deliberative process. Unless suspicion is sufficient to warrant change in the name of reform, the case must be made more convincingly. Suspicion, sincerely and articulately stated, may justify investigation, but a satisfactory review requires examination of the Award results for clues in support of the premise.

Study after study has upheld the general fairness of SRO arbitration in terms of the frequency with which investors win on their claims and even the amounts they recover when they win. Those studies, though, have not focused directly on the role of the Non-Public Arbitrator in achieving those outcomes. It has been enough that the Non-Public Arbitrator has had a long-standing involvement and that no harm appears to have come from that partici-

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INDUSTRY ARBITRATOR SURVEY *cont'd from page 7*

pation. Our effort in this analysis was to put a finer point on the impact of the Non-Public Arbitrator. Stated another way, our review sought indications, if they exist, that the Non-Public Arbitrator's role has become inimical to the process.

We use words like "improper" and "inimical," despite their subjective nature, to emphasize that a difference in outcome does not in and of itself demonstrate bias. For example, support for the Non-Public Arbitrator is sometimes expressed in terms of the "moderating" role s/he plays. If true, awards to customers might be greater in frequency and amount without the Non-Public Arbitrator, but that does not necessarily spell justice. Isolated indications of a moderating prospect surfaced in our analyses: the Small Claims "hearing" Award win rate; the three NPA dissents from sizeable damage awards, and the "Freshman" Arbitrator dissents. These findings might indicate bias, but alternative explanations exist. Approximating justice is arbitration's goal; maximizing outcomes for the customer-Claimant is only supportable within that context.

Generally speaking, our comparison of the win rates when the Non-Public Arbitrator is absent from the decision-making versus when s/he participates reveals very little to suggest that the Non-Public Arbitrator performs a less neutral role than his or her Public counterparts. Similarly, when we examine the Awards in which Non-Public Arbitrators have dissented, we find little or no evidence that fear of reprisal or outright bias affects NPA decision-making. During the five-year survey period, when several hundred punitive-damage awards issued, no Non-Public Arbitrator refused openly to join Public Panelists in voting for such sanctions. The one Non-Public Arbitrator who dissented from an attorney fee award did so, based more, it appeared to us, on legal grounds than on opposition to such relief.

By the same token, examining the dissents uncovered some strong statements by Non-Public Arbitrators in favor of liability and against pre-hearing dismissal. We also noted that more Non-Public Arbitrators dissented from a majority dismissal than did Public Chairs. These and other observations about the dissent Awards, when considered in combination with recent Award statistics that compare well with historical results, fail to support charges of bias. The Non-Public Arbitrator's participation in three-person SRO Panels discloses no material impact on customer "wins," when compared to win rates on Small Claims Awards, where Public Arbitrators adjudicate alone.

This statistical review was begun with the recognition that bias, or the absence of it, was unlikely to be conclusively established. Nevertheless, the study seemed worthwhile, as a contribution to the ongoing NPA debate of relevant, quantitative evidence. The Awards we reviewed are the single public manifestation of proceedings in which Non-Public Arbitrators have participated. Their role in those proceedings can be unlocked and revealed to some degree by these Awards and, with that in mind, we gathered the data for publication in this article. Its further interpretation we leave to our readers, with the knowledge that the debate about the NPA's place at the decision table will surely continue. ■

(SEE SIDEBAR ARTICLE on p. 9)

(Editor's Note: (1) By way of disclosure, the author of this article sits as a Non-Public Arbitrator. Because this subject generates so much controversy, SAC will make the Award subset of 186 Awards used in the Dissent Award section of this article available for viewing on the "SCAN Standards" section of our SCAN (SAC-CCH Awards Network) WebSite for the next 30 days In order to gain entry to the Dissent Awards subset, visit the WebSite (http://scan.cch.com), click on the "SCAN Standard" button at the top middle of the HomePage, and a new Page with two entry windows will appear. Enter this "USER ID No.:" 2005052302 and this "Password:" dissent. A listing of the Award ID Numbers will appear, which numbers will serve as links to actual PDF images of the Awards; the subset will also be available for word-searching. (2) A PDF-formatted report providing information in a standardized report format about the 186 dissent Awards may be purchased for $50. (3) SAC thanks to Paul Litteau, a Tucson, AZ-based securities expert, for inspiring this Award survey and for advising as we proceeded.)

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INDUSTRY ARBITRATOR SURVEY *cont'd from page 8*

PANEL COMPOSITION: PROPOSALS FOR CHANGE

All SRO Arbitrators take an Oath to serve in their vital role as neutrals, so the bias that people perceive in surveying the role of the Non-Public Arbitrator is often characterized as structural in nature, an institutional bias borne of the NPA's work in or close association with the securities industry. Arbitration has traditionally valued such experienceand knowledge as a plus, so casting it as a negative has placed the burden upon those who would seek to eliminate the Non-Public Arbitrator's role in SRO arbitration.

Given the Panel composition rules that govern NASD arbitrations, eliminating the Non-Public Arbitrator position on the three-person Panel would create a vacancy that would presumably be occupied by a person qualified, just as the other two Panelists, to be a Public Arbitrator. PIABA President Rosemary Shockman, in her Congressional testimony, and PIABA, in a March 15 Policy Statement on this subject (visit the PIABA WebSite, under "2005 Press Releases"), both advocate elimination of the "mandatory" Non-Public Arbitrator slot; however, neither indicates what would follow.

We think it likely that PIABA anticipates that another Public Arbitrator would fill the vacant slot, but there are plentiful alternatives to a three-Public Arbitrator Panel. One suggestion comes from well-known Mediator Mark Buckstein, who spoke in favor of eliminating all classifications at the SIA Compliance & Legal Conference (see "Conference Highlights" article on the program). Qualification criteria would be merits-based, seeking well-credentialed individuals to serve, and leaving it to list selection strikes to deal with party concerns about a particular arbitrator's "institutional" biases.

In an open letter dated April 26, 2005 to Linda Fienberg, well-known defense lawyer (and SAC Board member) Joel E. Davidson suggested retaining the NPA slot, but distinguishing between the two Public Arbitrator slots. Mr. Davidson challenged the practice of permitting Claimant's attorneys to serve as Chairpersons, arguing as follows: "Presumably, there is a feeling afloat that an industry arbitrator may have a bias…. A claimant's attorney also may have a bias and this is not taken into account in the rules. A claimant's attorney is not a true 'public arbitrator.'"

Mr. Davidson suggests that, just as Non-Public Arbitrators are excluded from service as Chairpersons in customer-related disputes and are limited in number, the "other" Public Arbitrator seat should be the one seat available to claimant's attorneys and claimant's experts. Such "'non-public, non-industry' arbitrators should not be permitted to serve as chairpersons of panels without the consent of all parties," he recommends. This idea would build upon the NASD's plan to establish a special pool of qualified Chairpersons to fill one Public Arbitrator slot, while minimizing the "institutional" bias potentialities with roughly parallel and opposing restrictions against Chairperson service.

The Davidson model bears resemblance to the tri-partite model used in other areas of arbitration. Within the tri-partite context, two arbitrators would be selected in terms of background, but all three arbitrators would take an oath of neutrality. One slot would be filled by a Non-Public Arbitrator and the "Other" Public Arbitrator slot would be filled by a person who is Claimant-oriented and truly free of industry ties. Instead of these two "party-type" Arbitrators picking the third Arbitrator, the parties would make the selection, per the NASD Code proposal, from a special Chairperson pool. Qualified Chair Panelists would be subject to Public classification criteria, but would be first and foremost equipped to serve as Chair.

While PIABA has labeled "[e]limination of mandatory industry arbitrators" as "the number one way to improve mandatory arbitration in customer cases," the NASD has not signaled an intention to go that route; moreover, the Securities Industry Conference on Arbitration (SICA) does not appear to support such change. Even if change is not at hand, the debate itself is constructive, as it contemplates arbitration reform, instead of condemning the current process as irrevocably tainted. Positive focus concentrates on the *sine qua non* of arbitration, i.e., ensuring appropriate standards of arbitrator competence and impartiality.

Actually, those opposing the "mandatory" Non-Public Arbitrator slot do have a path to follow. They might support one Arbitrator's efforts to attract SEC rulemaking on the subject. California Arbitrator Herbert Leslie ("Les") Greenberg, who has a long history of service as a SRO Arbitrator (more than 40 Awards — including one dissent), has been engaging other arbitrators in e-mail chats about arbitration and circulating the contents of that discourse to other arbitrators (SAA 2005-10 & -18). In his most recent installment, Mr. Greenberg reports the filing of a petition under SEC Rule 192 to seek rulemaking to "abolish the requirement that a securities industry arbitrator be assigned to each three-person panel hearing customer disputes or, in the alternative, require that information presented to a panel of arbitrators by a securities industry arbitrator be revealed to the parties during open hearing." The Petition may be reviewed at http://www.sec.gov/rules/petitions/petn4-502.pdf and comments, citing Petition 4-502, may be directed to comments@sec.gov.