Party Evaluation of Arbitrators: An Analysis of Data Collected from NASD Regulation Arbitrations

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** The views expressed herein are those of the authors and do not purport to reflect the position of the United States Military Academy, the Department of the Army, or the Department of Defense.

Table of Contents

I Executive Summary and Findings

The NASD Regulation, Inc., Office of Dispute Resolution (ODR)is the largest securities arbitration forum in the country. Approximately 5000 securities related arbitration cases were filed at ODR in 1998 and 6,000 cases were filed in 1997. Over 90% of the securities arbitration cases in the United States are handled by ODR, which has over 6,700 arbitrators on its roster. ODR administers arbitration hearings in 46 cities in the United States and has administrative offices in six cities.

Our research involved analyzing the results of a 15-month study designed to measure how parties to ODR arbitrations evaluate arbitrators assigned to their case, and the fairness of the ODR forum. Specifically, we collected data provided by parties to ODR cases that were closed by hearing between December 1, 1997, and April 1, 1999. This data was collected by encouraging all parties to ODR arbitrations to respond voluntarily to a 21 question survey instrument. This survey represents the most comprehensive, independent analysis of the NASD Arbitration Forum.

Findings: NASD Arbitration is Fair

Based upon the analysis of the data collected, we are able to conclude that participants to ODR sponsored arbitrations believe their case was handled fairly and without bias. The data we have analyzed shows the parties to ODR arbitrations are overwhelmingly satisfied with the fairness of the forum. For example, at the conclusion of their arbitration case, 93.49% of those responding indicated that their case "appears to have been handled fairly and without bias."

The same strong and overwhelmingly positive results were found when parties evaluated the arbitrators who heard their case. For example, of those who responded, the following chart reflects the percentage of favorable responses (excellent, or good, as opposed to fair or poor) arbitrators received for each skill or trait arbitrators are expected to exhibit.

Arbitrator Skills or Traits Evaluated	Percentages of responses that were excellent or good
Displayed Professionalism	92.62%
Listened Attentively	94.71%
Used Clear Impartial or Unbiased Language	92.51%
Ability to Understand Material Presented	91.52%
Displayed Sensitivity to Gender, Ethnicity & Culture	96.50%
Displayed Sensitivity to the Parties	92.96%
Displayed Knowledge of NASD Rules and Regulations	89.91%
Displayed Ability to Analyze Problem/Identified Key Issues	89.66%
Displayed Fairness and Appearance of Fairness	91.67%
Displayed Knowledge of the Securities Industry	89.46%

Using the Chi-Square test[1], we found a statistically significant difference in the responses of claimants and respondents to nine of the 17 survey questions that involved measurement of the perceived equity of the ODR arbitration process. The p-value[2] of less than or equal to .05 was considered significant for the purposes of this study.

The usable survey responses represent a response rate of between 10 - 20% of the 2,037 ODR cases that were closed after a hearing during this 15-month period. These responses also provided 1,032 individual arbitrator evaluations which represent approximately 15% of the ODR arbitrator roster.

Of the parties who responded to the survey, 54% identified themselves as the claimant or as representing the claimant,

[1] The purpose of the chi-square test is to determine if a relationship exists between two categorical variables, based upon mathematical properties of the normal curve and the probability of statistical differences between observed and expected outcomes. See, Kachigan, *Statistics and Analysis,* Radius Press, 1986, Chapter 13.

[2] The p-value is the probability that you reject the null hypothesis, given the null hypothesis is correct. The null hypothesis is that there is no association (FE=FO) between your status as a claimant (or representing a claimant) and your status as a respondent (or representing a respondent) and your answer to the survey question.

while 46% of those responding indicated they were the respondent or they represented the respondent.

ODR will continue to survey ODR forum participants and their evaluation of ODR arbitrators and of the ODR forum.

II Background

Although arbitration and mediation have existed as dispute resolution mechanisms for over 200 years,[3] it was not until the decision of the Supreme Court in Shearson/American Express v. McMahon,[4] that arbitration became the most widely used means of resolving disputes in the securities industry.

In McMahon,[5] the Court held that customers who sign predispute arbitration agreements with their brokers could be compelled to arbitrate claims arising under the Securities Exchange Act. As a result, McMahon transformed securities arbitration from a voluntary alternative to civil litigation, to the principal means of resolving securities disputes between investors and broker-dealers. Several subsequent court decisions favorable to the use of arbitration acted to further increase the use of arbitration.[6]

The principal benefit of arbitration is that it provides a prompt, inexpensive alternative to litigation in the courts. Generally, arbitration is final and binding, and is subject to review by a court only on a very limited basis.[7]

The NASD Regulation Office of Dispute Resolution[8] has become the largest securities arbitration forum in the country. In addition to arbitrating disputes between investors and broker-dealers, arbitration is also used to resolve disputes between broker-dealers and their employees as well as disputes between member firms.

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[3] Arbitration at the New York Stock Exchange was first offered in 1872 and the NASD first adopted its Code of Arbitration Procedure in 1968. See, P. Hoblin, Securities Arbitration Procedures, Strategies, Cases 1-2 (1988). The most recent NASD Code of Arbitration Procedure was published in May 1999.

[4] 482 U.S. 220 (1987), reh'g denied, 483 US 1056 (1987).

[5] Id.

[6] In 1989, the Court applied the reasoning of McMahon to compel arbitration of claims arising under the Securities Act of 1933. Rodriguez de Quijas v. Shearson/American Express, Inc., 490 U.S. 477 (1989). See also, Gilmer v. Interstate/Johnson Lane Corp., 500 U.S. 20 (1991).

[7] See Friedman, G., "Securities Arbitration Still Effective as the Millenium Dawns," World Arbitration and Mediation Report, Vol. 10, No. 5, May 1999, pp 133-136.

[8] The NASD is the largest securities-industry self-regulatory organization in the world. It is the parent organization of the Nasdaq-Amex Market Group, Inc., which operates Nasdaq and the American Stock Exchange (AMEX) together under one corporate umbrella. The NASD oversees the activities of the U.S. broker/dealer profession and regulates Nasdaq, Amex, and the over-the-counter securities markets.

Of the forums that offer arbitration, ODR receives by far the largest number of cases and handles approximately 90% of all securities arbitrations in the United States. The charts below show a 19 year history of cases filed at the NASD Office of Dispute Resolution.

Arbitration Cases Filed by Year [9]

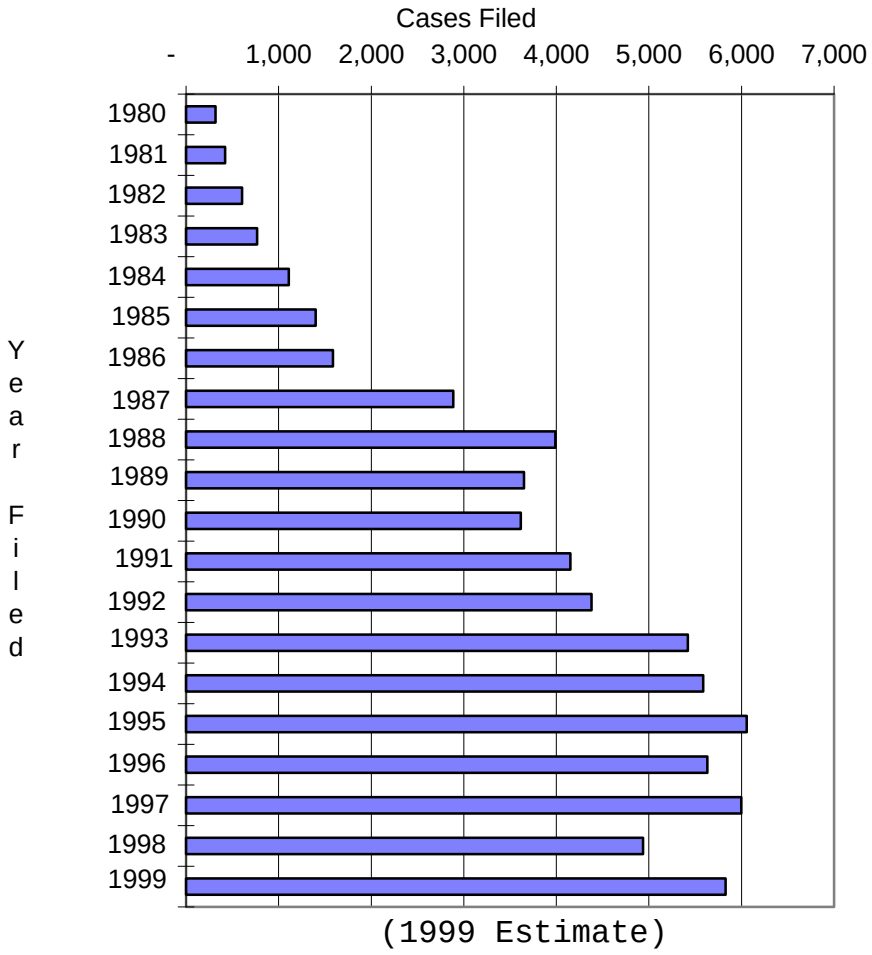
NASD Regulation, Inc.
Arbitration Cases Filed by Year

Year	Cases
1980	318
1981	422
1982	606
1983	768
1984	1,108
1985	1,400
1986	1,587
1987	2,886
1988	3,990
1989	3,651
1990	3,617

Year	Cases
1991	4,150
1992	4,379
1993	5,421
1994	5,586
1995	6,058
1996	5,631
1997	5,997
1998	4,938
Est. * 1999	5,828
2000	-
2001	-

[9] Statistical data provided on July 19, 1999 by ODR.

Yearly Volume Comparison



With the increased use of arbitration as a means of resolving securities disputes also came an increased scrutiny of the process, and a number of newspaper and other articles that were critical of the arbitration process.[10]

The number of articles critical of securities arbitration has decreased over the last two years, and the use of arbitration as a means of resolving disputes continues to grow.

[10] For example see, "Wall Street's Stingiest Judges", Money, November 1996, pp 100-117

III Development of the Survey

As part of its oversight responsibility for arbitration, the National Arbitration and Mediation Committee[11] (NAMC), developed a survey instrument titled "Party Evaluation of Arbitrators." The previous survey instrument used by ODR elicited an extremely low response rate.

The purpose of this new instrument was to obtain evaluations from ODR forum participants regarding their perceptions of case processing and of arbitrator performance.

One of the primary objectives of the party evaluation of arbitrators survey was to comply with the Arbitration Policy Task Force recommendation to take innovative steps to encourage a greater number of evaluations from parties.[12]

Specifically, the Task Force stated:

> "Evaluations of arbitrators by participants in the arbitration process are a vital source of information. They are used by the NASD staff to develop training programs, counsel arbitrators about deficiencies or problems, and to determine if certain arbitrators should continue to be selected. Unfortunately, getting participants to provide evaluations has proven extremely difficult. Nonetheless, a greater effort must be made to obtain candid and complete evaluations from parties, their counsel, and from other arbitrators."[13]

Consequently, the "Party Evaluation of Arbitrators" survey was developed and approved by the NAMC and was implemented on December 1, 1997. Copies of the survey instrument are given to the arbitrators on each case to distribute to parties at the arbitration. The Chairperson of the

[11] The National Arbitration and Mediation Committee advises the NASD Board of Governors on development and maintenance of an equitable and efficient system of dispute resolution that will equally serve the needs of public investors and NASD members.

[12] The Arbitration Policy Task Force was a high-level group appointed in September 1994 by the Board of Governors of the NASD, and was chaired by former Securities and Exchange Commission (SEC) Chairman David S. Ruder. In January 1996, the Task Force issued more than 70 recommendations representing the most comprehensive revamping of securities industry arbitration since it was established to resolve investor disputes more than a century ago.

[13] "Securities Arbitration Reform" Report of the Arbitration Policy Task Force to the Board of Governors National Association of Securities Dealers, Inc., January 1996, p. 101.

arbitration panel advises all parties at the first hearing of the arbitration as follows:

> "Party Evaluations: As part of NASD Regulation's efforts continually to improve the arbitration process, each party or representative(s) will be asked voluntarily to participate in completing a questionnaire concerning this arbitration. You will be provided with an opportunity to complete the questionnaire at the conclusion of the final hearing."[14]

At the conclusion of the hearing, the Chairperson again requests that each party or representative complete the survey and mail their responses to a designated independent educational institution. To facilitate return of the survey, a self-addressed postage paid envelope is provided to the participants.

The parties are given the party evaluation of arbitrators survey at the conclusion of their hearing. While the parties are encouraged to complete the survey before receiving the award, there is no deadline for submitting the evaluation. Therefore some parties may know the arbitrators' decision before they submit their evaluation.

The initial tabulation of data was completed by Gary Tidwell while he was a member of the roster faculty at the College of Charleston.[15] The data analysis was eventually transferred to Majors Kevin Foster and Michael Hummel, both of whom are Assistant Professors in the Department of Social Sciences at the United States Military Academy, West Point. Majors Foster and Hummel received all of the data at West Point and were responsible for tabulating and analyzing all the results.

ODR continues to use the survey allowing all parties to ODR arbitrations to evaluate the arbitrators and the forum.

[14] Office of Dispute Resolution Hearing Script.

[15] On July 13, 1998, Gary Tidwell became Director of Neutral Training and Development, Office of Dispute Resolution.

IV Detailed Findings and Methodology

From December 1, 1997 through April 1, 1999, the authors received 415 completed "Party Evaluation of Arbitrators" surveys. The objective responses to the surveys were transferred to answer sheets that enable the objective data to be scanned by optical scanning machines. The data were converted into a computer statistics package which allowed for data analysis.

The 415 responses represent a response rate of approximately 10 - 20% of the ODR cases that were closed after a hearing.[16] Each party evaluation of arbitrators survey allowed the parties to evaluate all arbitrators assigned to the party's case. Usually, there are three arbitrators assigned to a case. Consequently, there were 1,032 arbitrators evaluated with some arbitrators receiving multiple evaluations. We estimate that approximately 15% of the ODR roster of arbitrators were evaluated.[17]

[16] During the applicable time period of December 1, 1997 to April 1, 1999, a total of 2,037 ODR arbitration cases that were closed after a hearing. If a party evaluation of arbitrator survey was received from one of the parties to a case, this would represent a return rate of 20% for all cases closed after a hearing. If, however, two surveys were returned from a case that was closed after a hearing, this would represent a response rate of 10% for all cases closed after a hearing. Therefore, we estimate that we received a 10 - 20 % response rate based on the 2,037 cases that were closed after a hearing during the relevant time period.

[17] ODR has approximately 6,700 available arbitrators. Therefore, 1,032 arbitrators evaluated reflects approximately 15% of the available arbitrator roster.

Findings

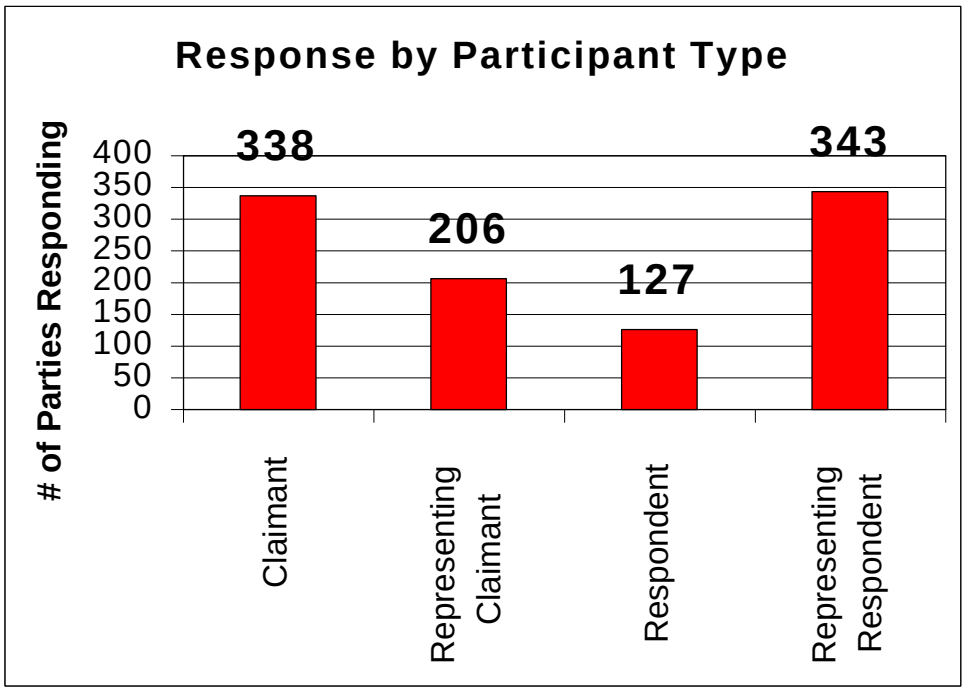
The following table shows the total number of responses received for each question on the survey instrument.

Responses		
Question #	**Summary**	**Responses**
1	Claimant or Respondent	1015
2	Case handled fairly and without bias	999
3	Displayed professionalism	1016
4	Listened attentively	1020
5	Used clear impartial or unbiased language	1001
6	Displayed ability to understand material presented	1002
7	Displayed sensitivity to gender, ethnicity, cultural differences	858
8	Displayed sensitivity to parties	995
9	Displayed knowledge of NASD rules and procedures	951
10	Displayed ability to analyze problems/identify key issues	967
11	Displayed fairness and appearance of fairness	1009
12	Displayed knowledge of securities industry terminology and practices	958
13	Decided discovery and other prehearing motions in a timely manner	738
14	Decided discovery and other hearing motions in a timely manner	790
15	Commenced all prehearing sessions on time	707
16	Commenced all hearing sessions on time	961
17	Conducted efficient prehearing sessions	680
18	Conducted efficient hearing sessions	955
19	Gender	959
20	Race	982
21	Age	1004

In evaluating the data, we first tested the reliability of the data for selection bias and also examined the demographics of those who responded to the survey.

Question one of the survey asks the party participant if, in this particular case, they were: claimant; representing a claimant; respondent; or, representing a respondent. As the charts below reflect, 54% of those responding identified themselves as a claimant or representing a claimant, while 46% of those responding identified themselves as a respondent or representing a respondent.

Party evaluation data: Reliability



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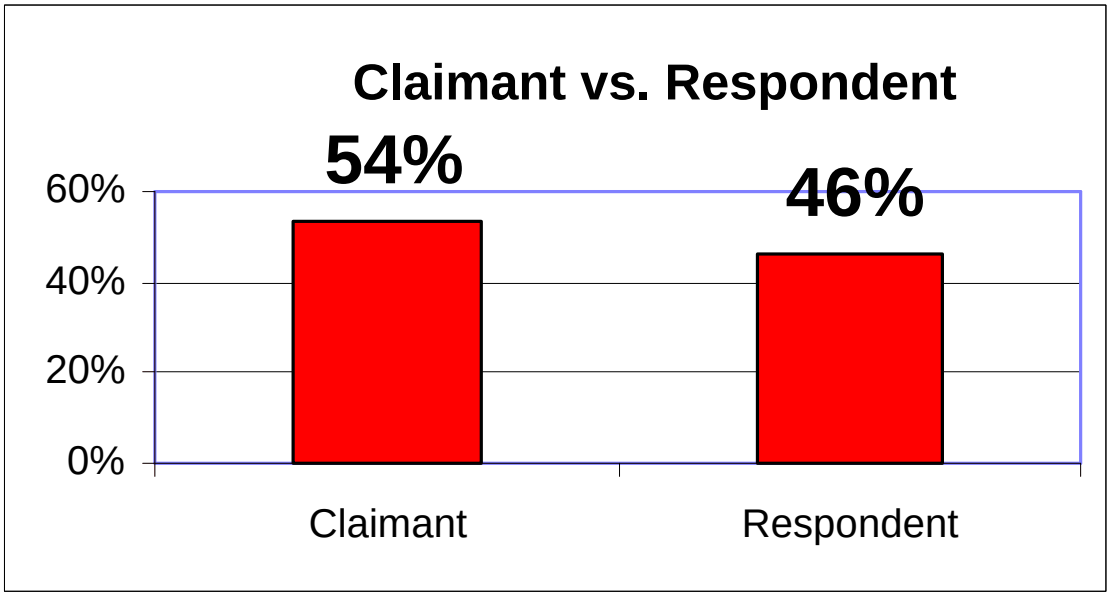
Party evaluation data: Reliability



Questions 19 through 21 examine the demographics of those responding to the survey instrument. The results are as follows:

Party evaluation data: Demographics

- Gender
  - 14% women
  - 86% men
  - Only 959/1032 valid responses
- Race
  - 4 African-American
  - 2 Native American
  - 50 Hispanic
  - 914 White
  - 50 No response

Party evaluation data: : Demographics

Age	*Number*
35 and under	198
36-45	326
46-55	297
56-65	121
Over 65	62

Discussions with ODR staff verifies that the demographics of the data received are consistent with what the staff believes are the demographics of participants in the ODR arbitration forum.

Questions 2 through 18 examine the parties' evaluation of the ODR process and their evaluation of the arbitrators who heard their case.

The following pages provide data analysis for each of these remaining questions. In addition, the charts below show the responses of those individuals who identified themselves as the respondent or representing the respondent, and those individuals who identified themselves as the claimant or representing the claimant.

Question two of this survey evaluates survey participants' views not only of the ODR forum, but also of the fundamental and critically important component of any arbitration: having your case handled fairly and without bias. The responses indicate 93.49% of those who responded believed their case had been handled fairly and without bias. While 53% of the respondents, or those who represented respondents strongly agreed that their case had been handled fairly without bias, an even higher percentage (61%) of the claimants strongly agreed with that statement.

Also of significance is the chi-square analysis of this and other survey questions. The low p-value of the chi-square test of .003 reflects that there is clearly a statistically significant difference between the way claimants and respondents answered question two.

This chi-square analysis with any p-value equal to or less than .05 (95% confidence level) represents a statistically significant difference in the way that claimants responded to a particular survey question versus the way respondents responded to the same survey question.

We found this statistically significant difference between respondents and claimants responses existed not only in the responses to question number two, but also in the responses given to the following survey questions:

Survey Question Number	Question/Topic	Chi-Square P-Value
3	Display professionalism	.05
6	Displayed ability to understand material presented	.029
7	Displayed sensitivity to gender, ethnicity, cultural differences	.000
9	Displayed knowledge of NASD Regulation, rules, and procedures	.019
10	Displayed ability to analyze problems/identify key issues	.003
12	Displayed knowledge of securities industry terminology and practices	.018
16	Commence all hearing sessions on time	.018
17	Conducted efficient prehearing sessions	.003

Also of significance, in each of the survey questions, the claimants had significantly more intense positive responses than the respondents. For survey questions 2 through 18, the claimants were more in agreement with a positive evaluation than were the respondents. While all parties had an overwhelmingly positive evaluation of the arbitrators and of the ODR forum, the data shows the claimants were more positive than the respondents.

The finding of a stronger favorable response from the claimants as opposed to the respondents may contradict some of the literature relating to securities arbitrations (See footnote 10).

Survey Question Analysis

The following pages provide detailed analysis for each of the 17 survey questions that measure the parties' perceived equity of the ODR arbitration process and of the ODR arbitrators who heard their case. Following each survey question is a table that provides the frequency, percent frequency, and cumulative response for that question.

A second table groups the responses of those who responded as being the respondent or representing the respondent, and those who responded as being the claimant or representing the claimant.

This tabular analysis for each question is followed by a chart that depicts for each question the total responses, and then the percentage responses for all respondents and for all claimants.

2. At this point, my case appears to have been handled fairly and without bias:

- ❑ Strongly Agree
- ❑ Agree
- ❑ Disagree
- ❑ Strongly disagree

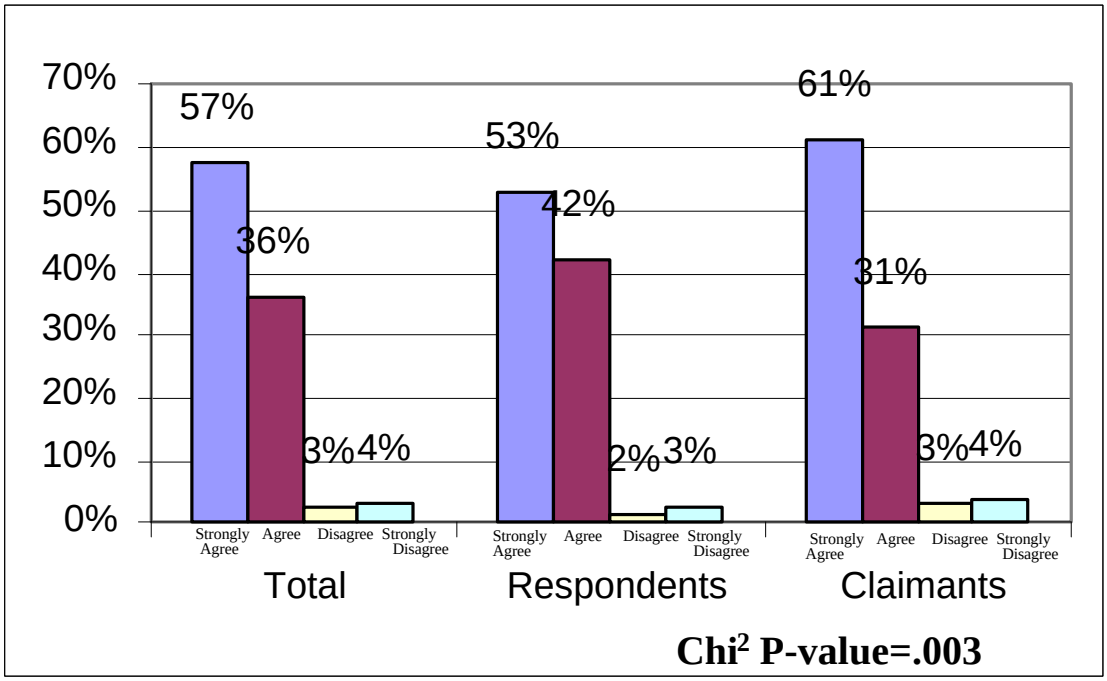
Analysis

Case handled fairly	Freq.	Percent	Cum.
Strongly Agree	573	57.36	57.36
Agree	361	36.14	93.49
Disagree	27	2.70	96.20
Strongly Disagree	38	3.80	100.00
Total	999	100.00	

claim	Case handled fairly: Strongly Agree	Agree	Disagree	Strongly Disagree	Total
Respondent	245	196	9	13	463
	52.92	42.33	1.94	2.81	100.00
Claimant	321	165	18	22	526
	61.03	31.37	3.42	4.18	100.00
Total	566	361	27	35	989
	57.23	36.50	2.73	3.54	100.00

Pearson chi2(3) = 14.2259 Pr = 0.003

At this point, my case appears to have been handled fairly and without bias.



3. Displayed Professionalism

a) Excellent
b) Good
c) Fair
d) Poor

Analysis

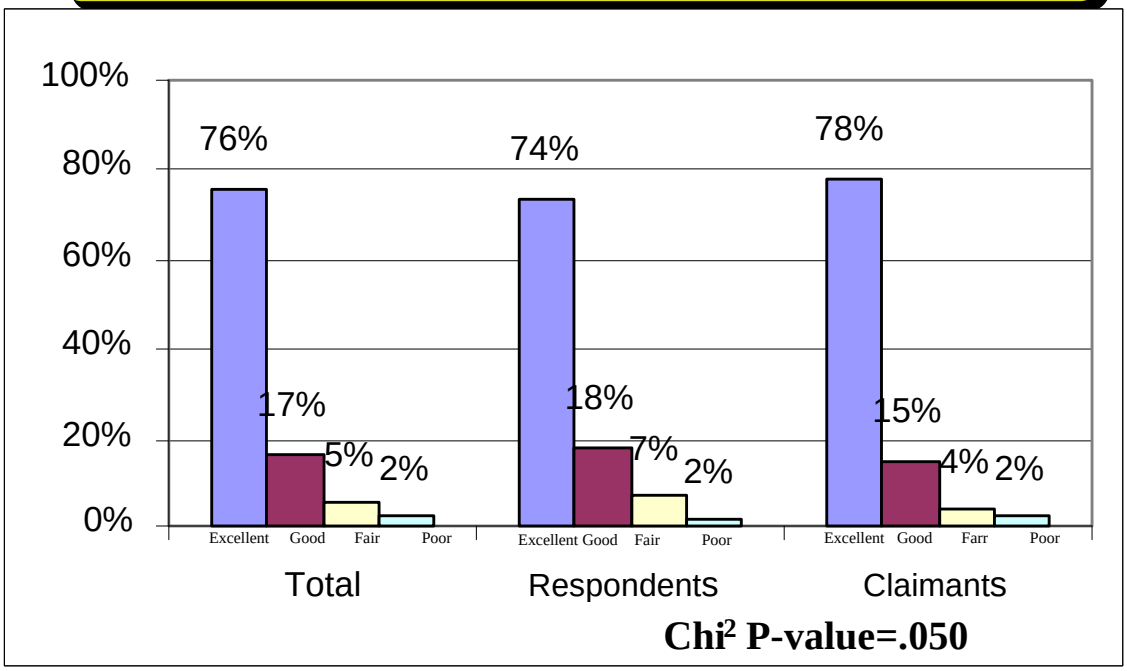
Displayed Professionalism

	Freq.	Percent	Cum.
Excellent	772	75.98	75.98
Good	169	16.63	92.62
Fair	54	5.31	97.93
Poor	21	2.07	100.00
Total	1016	100.00	

	Displayed Professionalism				
claim	Excellent	Good	Fair	Poor	Total
Respondent	344	84	33	7	468
	73.50	17.95	7.05	1.50	100.00
Claimant	415	82	20	13	530
	78.30	15.47	3.77	2.45	100.00
Total	759	166	53	20	998
	76.05	16.63	5.31	2.00	100.00

Pearson chi2(3) = 7.8329 Pr = 0.050

Displayed Professionalism



Chi² P-value=.050

4. Listened Attentively

a) Excellent
b) Good
c) Fair
d) Poor

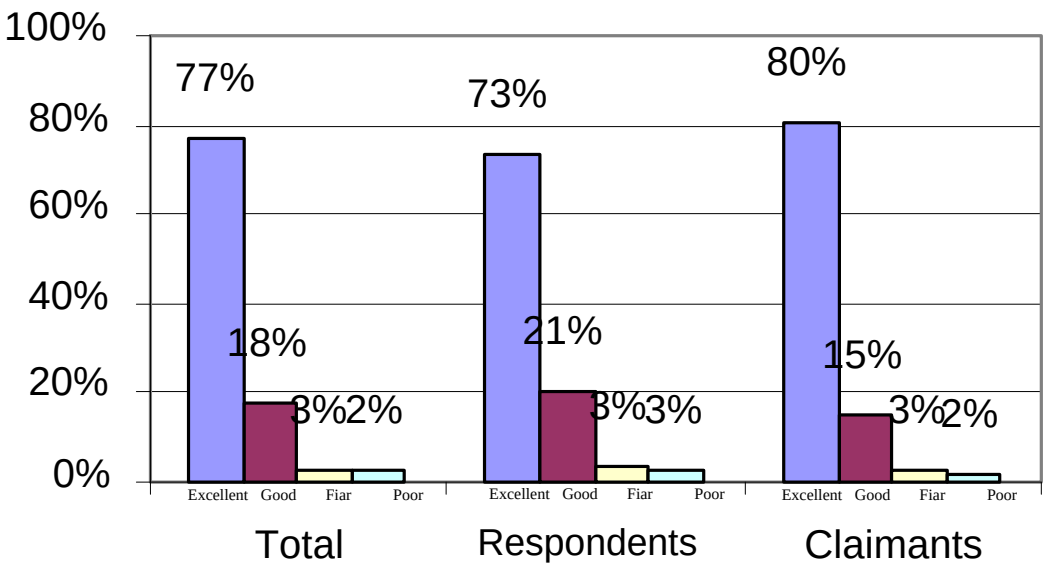
Analysis

Listened Attentively	Freq.	Percent	Cum.
Excellent	786	77.06	77.06
Good	180	17.65	94.71
Fair	31	3.04	97.75
Poor	23	2.25	100.00
Total	1020	100.00	

claim	Listened Attentively: Excellent	Good	Fair	Poor	Total
Respondent	341	97	16	13	467
	73.02	20.77	3.43	2.78	100.00
Claimant	429	81	15	10	535
	80.19	15.14	2.80	1.87	100.00
Total	770	178	31	23	1002
	76.85	17.76	3.09	2.30	100.00

Pearson chi2(3) = 7.3379 Pr = 0.062

Listened Attentively



Chi^2 P-value=.062

5. Used Clear Impartial or Unbiased Language

a) Excellent
b) Good
c) Fair
d) Poor

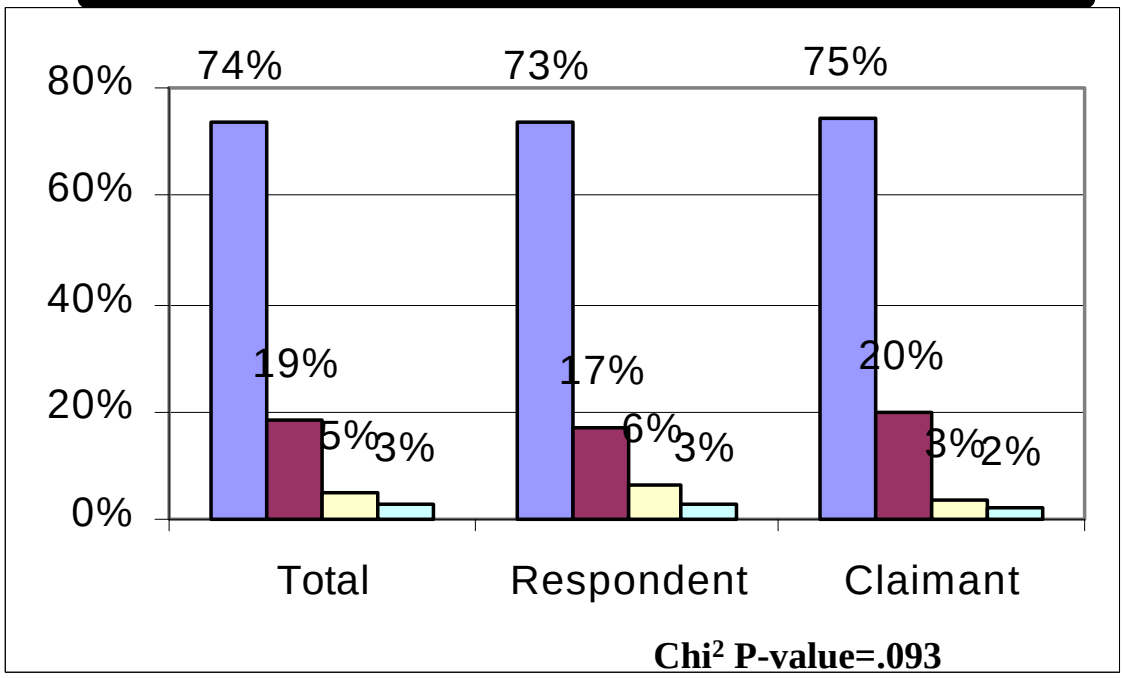
Analysis

Used clear unbiased or impartial language	Freq.	Percent	Cum.
Excellent	739	73.83	73.83
Good	187	18.68	92.51
Fair	48	4.80	97.30
Poor	27	2.70	100.00
Total	1001	100.00	

	Used clear and impartial language				
claim	Excellent	Good	Fair	Poor	Total
Respondent	330	77	29	14	450
	73.33	17.11	6.44	3.11	100.00
Claimant	398	105	18	12	533
	74.67	19.70	3.38	2.25	100.00
Total	728	182	47	26	983
	74.06	18.51	4.78	2.64	100.00

Pearson chi2(3) = 6.4253 Pr = 0.093

Used clear impartial or unbiased language



6. Displayed Ability to Understand Material Presented

a) Excellent
b) Good
c) Fair
d) Poor

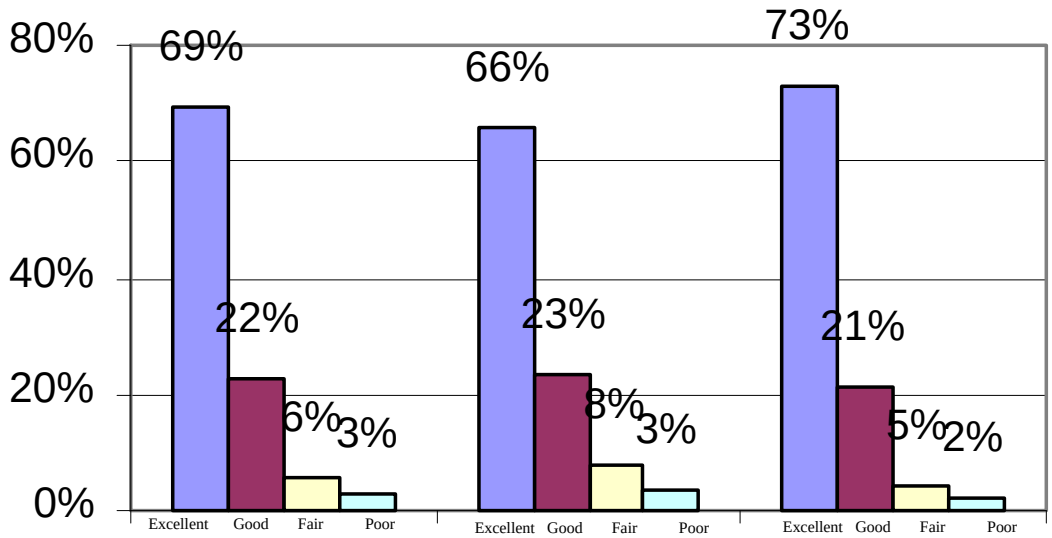
Analysis

Displayed ability to understand material presented	Freq.	Percent	Cum.
Excellent	693	69.16	69.16
Good	224	22.36	91.52
Fair	60	5.99	97.50
Poor	25	2.50	100.00
Total	1002	100.00	

claim	Displayed ability to understand material presented: Excellent	Good	Fair	Poor	Total
Respondent	297	105	36	15	453
	65.56	23.18	7.95	3.31	100.00
Claimant	386	111	24	10	531
	72.69	20.90	4.52	1.88	100.00
Total	683	216	60	25	984
	69.41	21.95	6.10	2.54	100.00

Pearson chi2(3) = 9.0379 Pr = 0.029

Displayed ability to understand material presented



Chi^2 P-value=.029

7. Displayed Sensitivity to Gender, Ethnicity, Cultural Difference

a) Excellent
b) Good
c) Fair
d) Poor

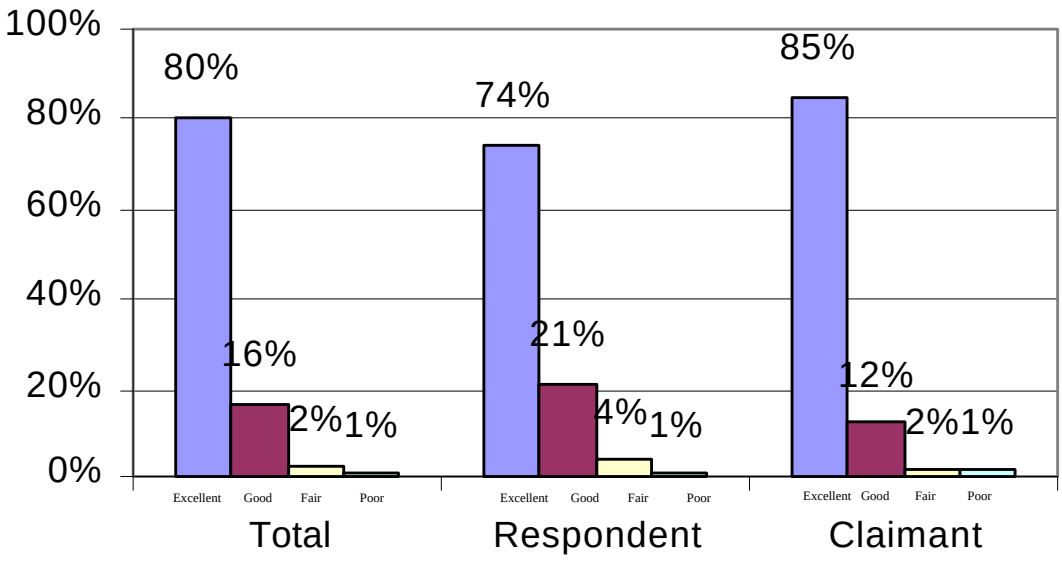
Analysis

Displayed sensitivity to gender, ethnicity, culture	Freq.	Percent	Cum.
Excellent	687	80.07	80.07
Good	141	16.43	96.50
Fair	21	2.45	98.95
Poor	9	1.05	100.00
Total	858	100.00	

claim	Displayed sensitivity to gender, ethnicity, culture				
	Excellent	Good	Fair	Poor	Total
Respondent	283	82	14	3	382
	74.08	21.47	3.66	0.79	100.00
Claimant	392	56	7	6	461
	85.03	12.15	1.52	1.30	100.00
Total	675	138	21	9	843
	80.07	16.37	2.49	1.07	100.00

Pearson chi2(3) = 18.5933 Pr = 0.000

Displayed sensitivity to gender, ethnicity, cultural difference



Chi^2 P-value=.000

8. Displayed Sensitivity to the Parties

a) Excellent
b) Good
c) Fair
d) Poor

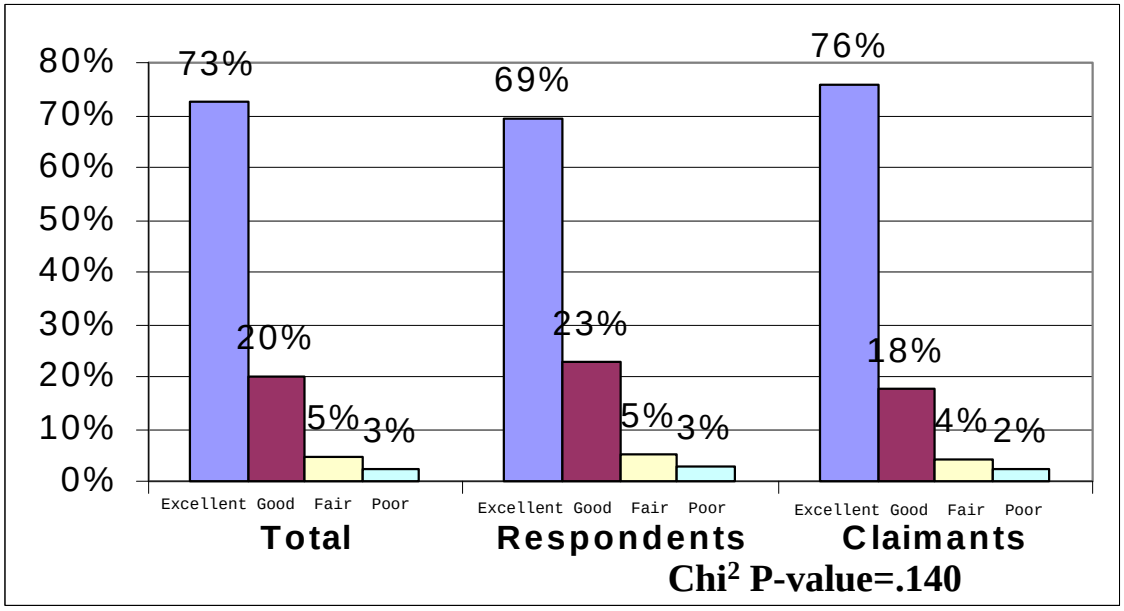
Analysis

Displayed sensitivity to parties	Freq.	Percent	Cum.
Excellent	724	72.76	72.76
Good	201	20.20	92.96
Fair	45	4.52	97.49
Poor	25	2.51	100.00
Total	995	100.00	

claim	Displayed sensitivity to parties: Excellent	Good	Fair	Poor	Total
Respondent	311	103	22	13	449
	69.27	22.94	4.90	2.90	100.00
Claimant	403	94	22	12	531
	75.89	17.70	4.14	2.26	100.00
Total	714	197	44	25	980
	72.86	20.10	4.49	2.55	100.00

Pearson chi2(3) = 5.4827 Pr = 0.140

Displayed sensitivity to the parties



9. Displayed Knowledge of NASD Regulation rules and procedures

a) Excellent
b) Good
c) Fair
d) Poor

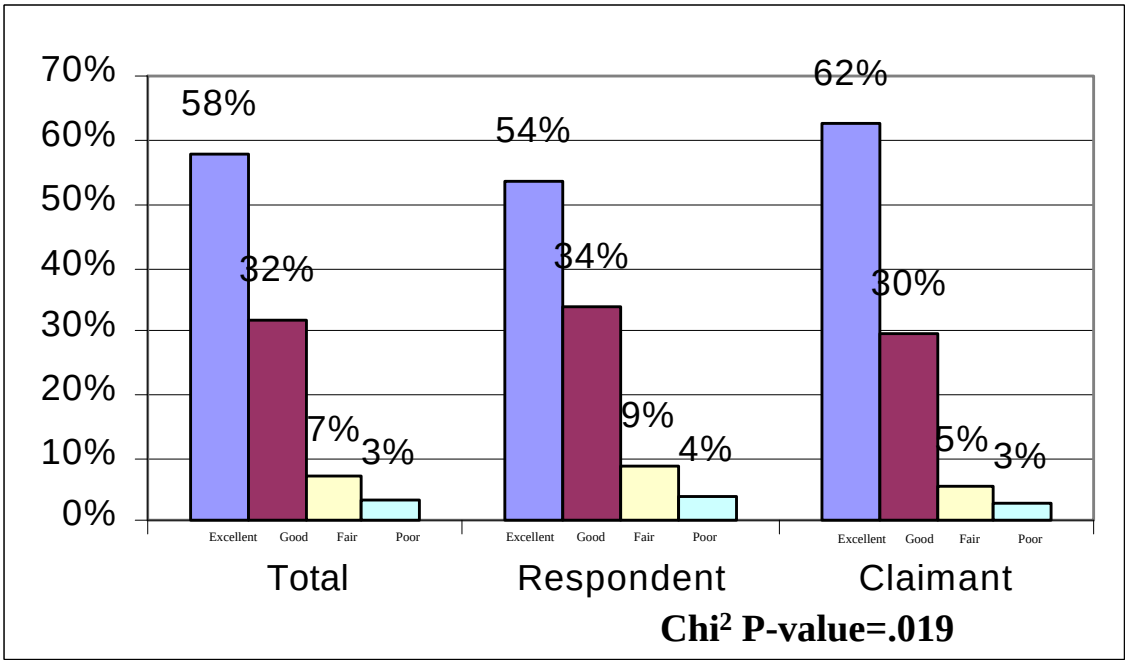
Analysis

Displayed knowledge of NASD rules and regs	Freq.	Percent	Cum.
Excellent	551	57.94	57.94
Good	304	31.97	89.91
Fair	67	7.05	96.95
Poor	29	3.05	100.00
Total	951	100.00	

	Displayed knowledge of NASD rules and procedures				
claim	Excellent	Good	Fair	Poor	Total
Respondent	232	146	39	16	433
	53.58	33.72	9.01	3.70	100.00
Claimant	312	149	26	13	500
	62.40	29.80	5.20	2.60	100.00
Total	544	295	65	29	933
	58.31	31.62	6.97	3.11	100.00

Pearson chi2(3) = 9.9455 Pr = 0.019

Displayed knowledge of NASD Regulation, rules, and procedures



10. Displayed Ability to Analyze Problems/Identify Key Issues

a) Excellent
b) Good
c) Fair
d) Poor

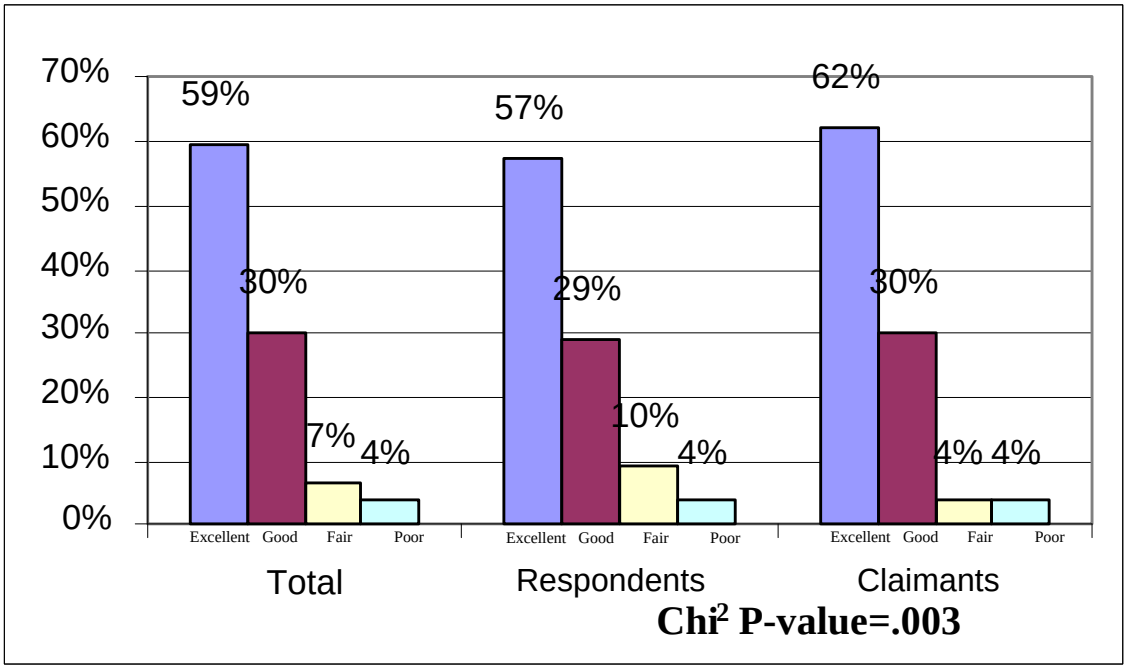
Analysis

Displayed ability to analyze problems/ID issues	Freq.	Percent	Cum.
Excellent	575	59.46	59.46
Good	292	30.20	89.66
Fair	63	6.51	96.17
Poor	37	3.83	100.00
Total	967	100.00	

	Displayed ability to analyze problems/ID issues				
claim	Excellent	Good	Fair	Poor	Total
Respondent	254	129	43	17	443
	57.34	29.12	9.71	3.84	100.00
Claimant	314	153	19	20	506
	62.06	30.24	3.75	3.95	100.00
Total	568	282	62	37	949
	59.85	29.72	6.53	3.90	100.00

Pearson chi2(3) = 13.7926 Pr = 0.003

Displayed ability to analyze problems /identify key issues



11. Displayed Fairness and Appearance of Fairness

a) Excellent
b) Good
c) Fair
d) Poor

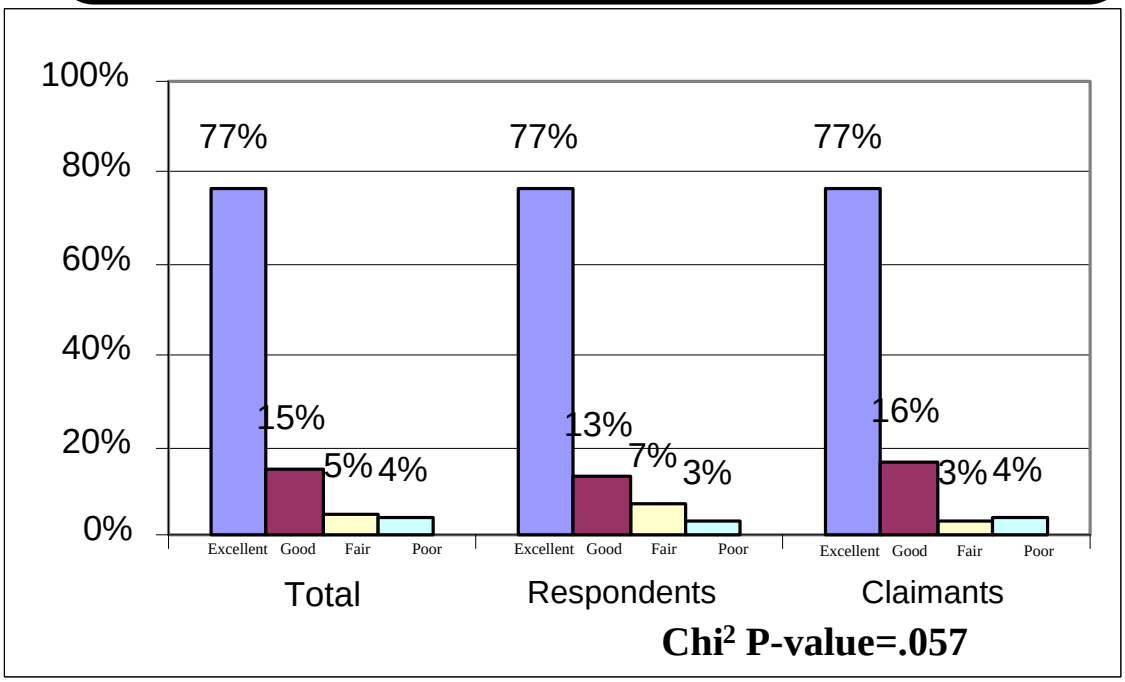
Analysis

Displayed Fairness and appearance of fairness	Freq.	Percent	Cum.
Excellent	774	76.71	76.71
Good	151	14.97	91.67
Fair	48	4.76	96.43
Poor	36	3.57	100.00
Total	1009	100.00	

	Displayed Fairness and appearance of fairness				
claim	Excellent	Good	Fair	Poor	Total
Respondent	352	61	30	15	458
	76.86	13.32	6.55	3.28	100.00
Claimant	409	87	17	20	533
	76.74	16.32	3.19	3.75	100.00
Total	761	148	47	35	991
	76.79	14.93	4.74	3.53	100.00

Pearson chi2(3) = 7.5139 Pr = 0.057

Displayed fairness and the appearance of fairness



12. Displayed Knowledge of Securities Industry Terminology and Practices

a) Excellent
b) Good
c) Fair
d) Poor

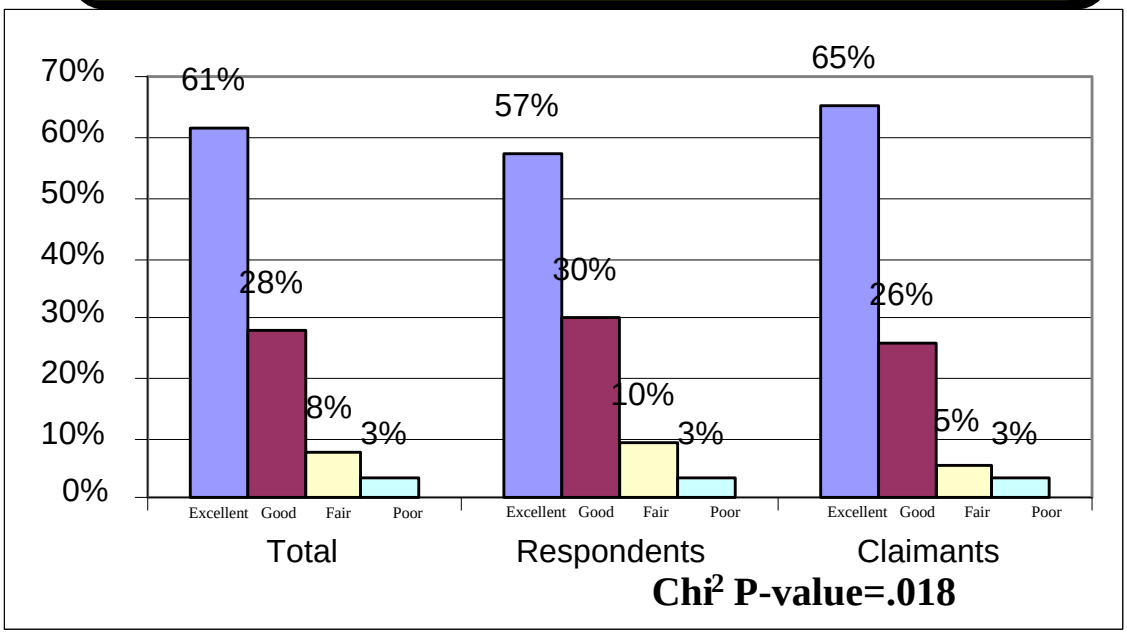
Analysis

Displayed knowledge of securities industry	Freq.	Percent	Cum.
Excellent	589	61.48	61.48
Good	268	27.97	89.46
Fair	73	7.62	97.08
Poor	28	2.92	100.00
Total	958	100.00	

	Displayed knowledge of securities industry				
claim	Excellent	Good	Fair	Poor	Total
Respondent	251	133	43	13	440
	57.05	30.23	9.77	2.95	100.00
Claimant	327	131	27	15	500
	65.40	26.20	5.40	3.00	100.00
Total	578	264	70	28	940
	61.49	28.09	7.45	2.98	100.00

Pearson chi2(3) = 10.0193 Pr = 0.018

Displayed knowledge of securities industry terminology and practices



13. Decided Discovery and Other Prehearing Motions in a Timely Manner

Excellent
Good
Fair
Poor

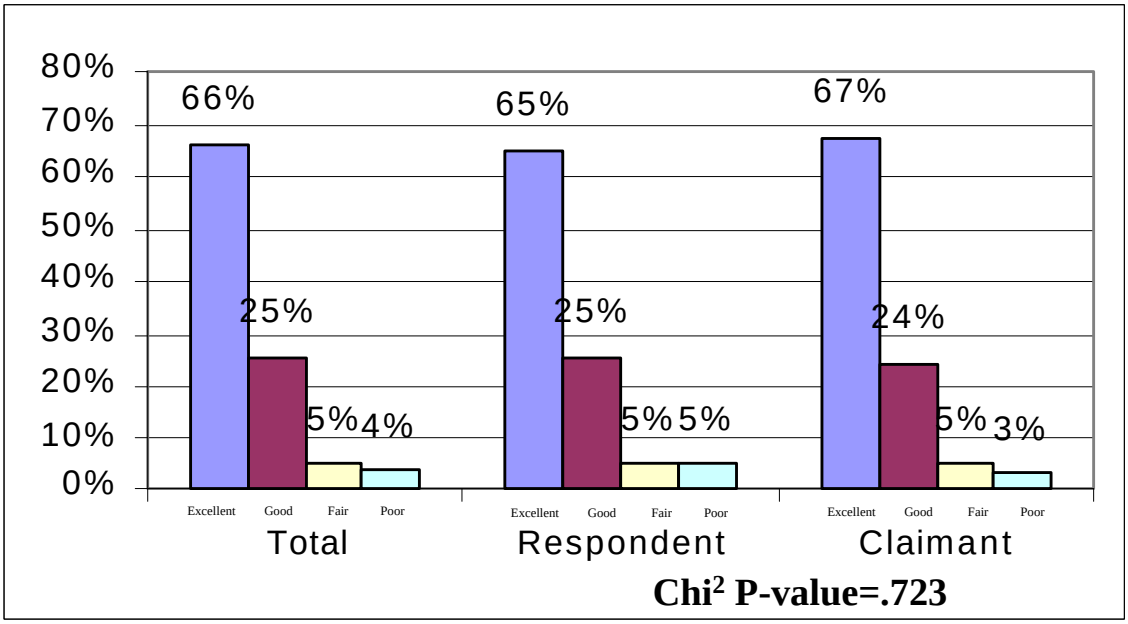
Analysis

Prehearing motions in a timely manner	Freq.	Percent	Cum.
Excellent	488	66.12	66.12
Good	186	25.20	91.33
Fair	37	5.01	96.34
Poor	27	3.66	100.00
Total	738	100.00	

	Prehearing motions in a timely manner				
claim	Excellent	Good	Fair	Poor	Total
Respondent	214	84	17	15	330
	64.85	25.45	5.15	4.55	100.00
Claimant	265	96	20	12	393
	67.43	24.43	5.09	3.05	100.00
Total	479	180	37	27	723
	66.25	24.90	5.12	3.73	100.00

Pearson chi2(3) = 1.3271 Pr = 0.723

Decided discovery and other prehearing motions in a timely matter



14. Decided Discovery and Other Hearing Motions in a Timely Manner

a) Excellent
b) Good
c) Fair
d) Poor

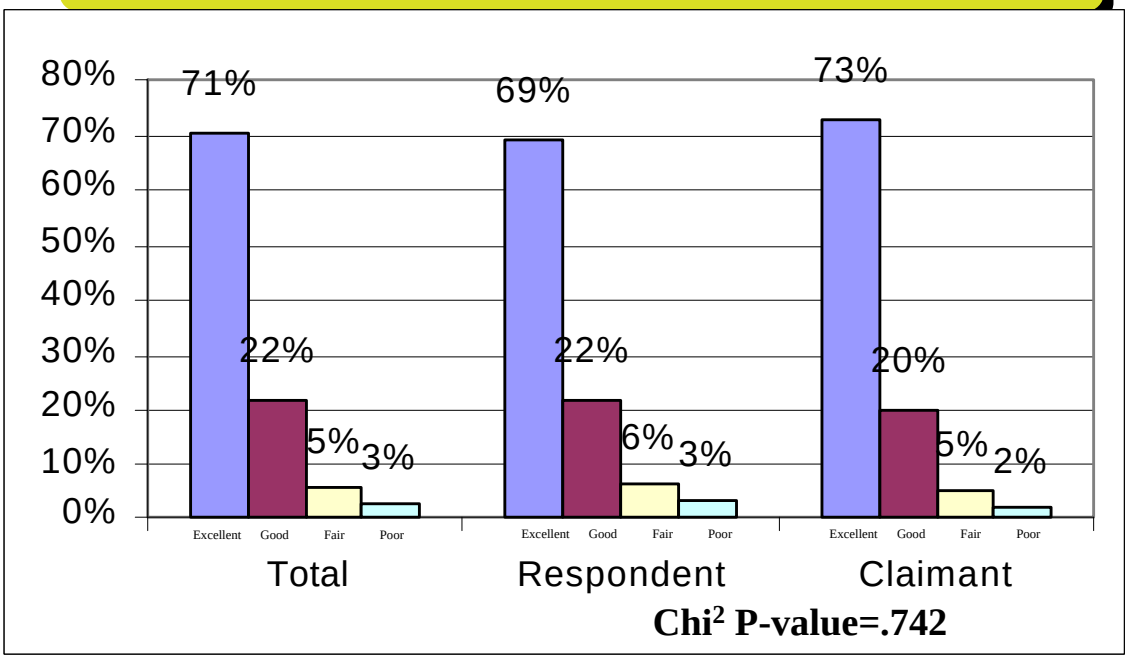
Analysis

Decided discovery in a timely manner	Freq.	Percent	Cum.
Excellent	557	70.51	70.51
Good	171	21.65	92.15
Fair	42	5.32	97.47
Poor	20	2.53	100.00
Total	790	100.00	

claim	Decided discovery in a timely manner: Excellent	Good	Fair	Poor	Total
Respondent	251	80	22	10	363
	69.15	22.04	6.06	2.75	100.00
Claimant	297	82	20	10	409
	72.62	20.05	4.89	2.44	100.00
Total	548	162	42	20	772
	70.98	20.98	5.44	2.59	100.00

Pearson chi2(3) = 1.2447 Pr = 0.742

Decided discovery and other hearing motions in a timely manner



15. Commenced all Prehearing Session on Time

a) Excellent
b) Good
c) Fair
d) Poor

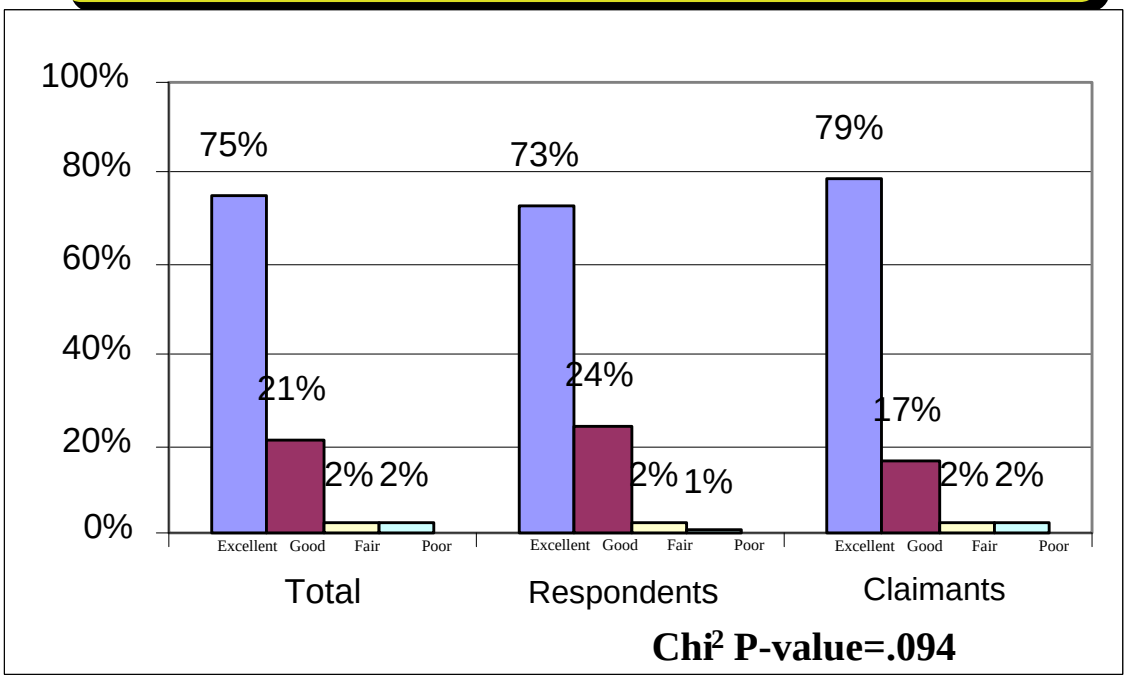
Analysis

Commenced prehearing sessions on time	Freq.	Percent	Cum.
Excellent	532	75.25	75.25
Good	150	21.22	96.46
Fair	14	1.98	98.44
Poor	11	1.56	100.00
Total	707	100.00	

	Commenced prehearing sessions on time				
claim	Excellent	Good	Fair	Poor	Total
Respondent	234	76	8	3	321
	72.90	23.68	2.49	0.93	100.00
Claimant	290	64	6	8	368
	78.80	17.39	1.63	2.17	100.00
Total	524	140	14	11	689
	76.05	20.32	2.03	1.60	100.00

Pearson chi2(3) = 6.3954 Pr = 0.094

Commenced all prehearing sessions on time



16. Commenced All Hearing Sessions on Time

a) Excellent
b) Good
c) Fair
d) Poor

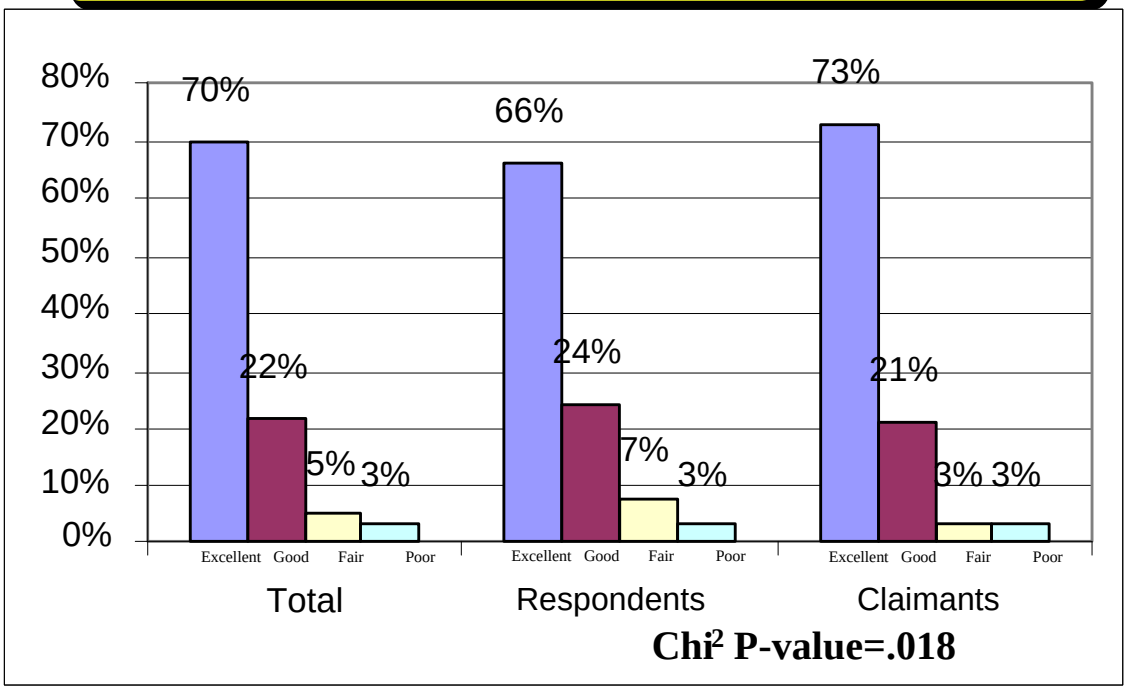
Analysis

Commenced hearing sessions on time	Freq.	Percent	Cum.
Excellent	668	69.51	69.51
Good	215	22.37	91.88
Fair	50	5.20	97.09
Poor	28	2.91	100.00
Total	961	100.00	

claim	Commenced hearing sessions on time: Excellent	Good	Fair	Poor	Total
Respondent	290	104	33	13	440
	65.91	23.64	7.50	2.95	100.00
Claimant	367	104	17	15	503
	72.96	20.68	3.38	2.98	100.00
Total	657	208	50	28	943
	69.67	22.06	5.30	2.97	100.00

Pearson chi2(3) = 10.1235 Pr = 0.018

Commenced all hearing sessions on time



17. Conducted Efficient Prehearing Sessions

a) Excellent
b) Good
c) Fair
d) Poor

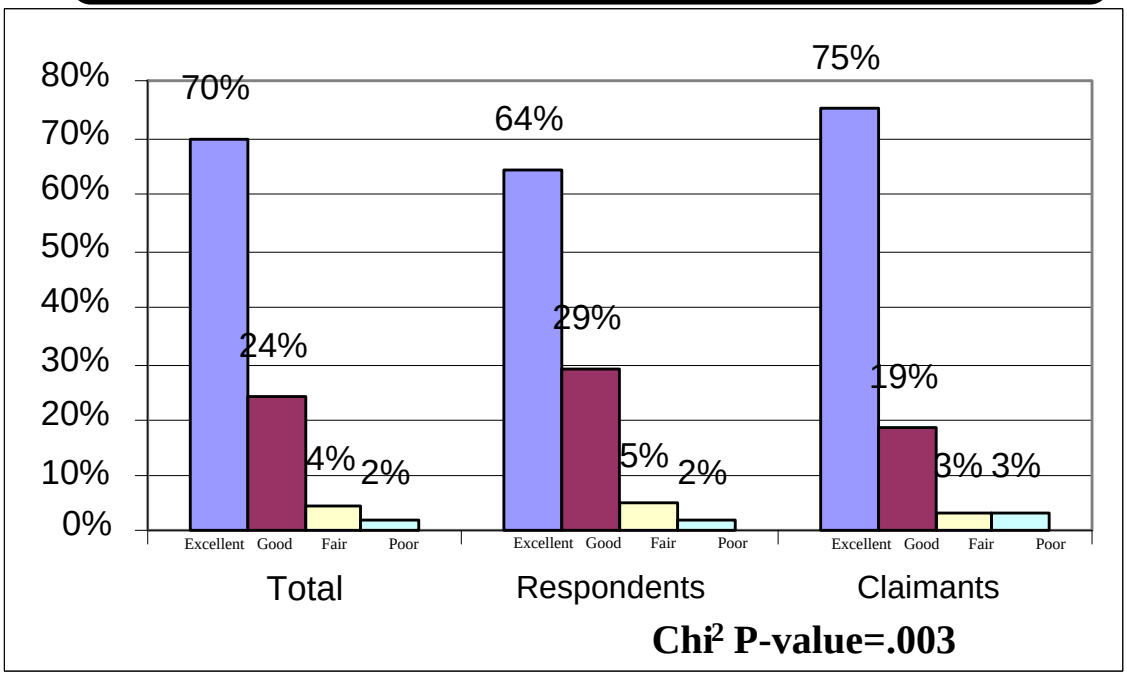
Analysis

Conducted efficient prehearing sessions	Freq.	Percent	Cum.
Excellent	475	69.85	69.85
Good	160	23.53	93.38
Fair	26	3.82	97.21
Poor	18	2.65	99.85
Total	679	99.85	

	Conducted efficient prehearing sessions				
claim	Excellent	Good	Fair	Poor	Total
Respondent	194	90	14	6	304
	63.61	29.51	4.59	1.97	100.00
Claimant	271	67	9	12	358
	75.49	18.66	2.51	3.34	100.00
Total	465	157	23	18	663
	70.03	23.64	3.46	2.71	100.00

Pearson chi2(4) = 15.9207 Pr = 0.003

Conducted efficient prehearing sessions



18. Conducted Efficient Hearing Sessions

a) Excellent
b) Good
c) Fair
d) Poor

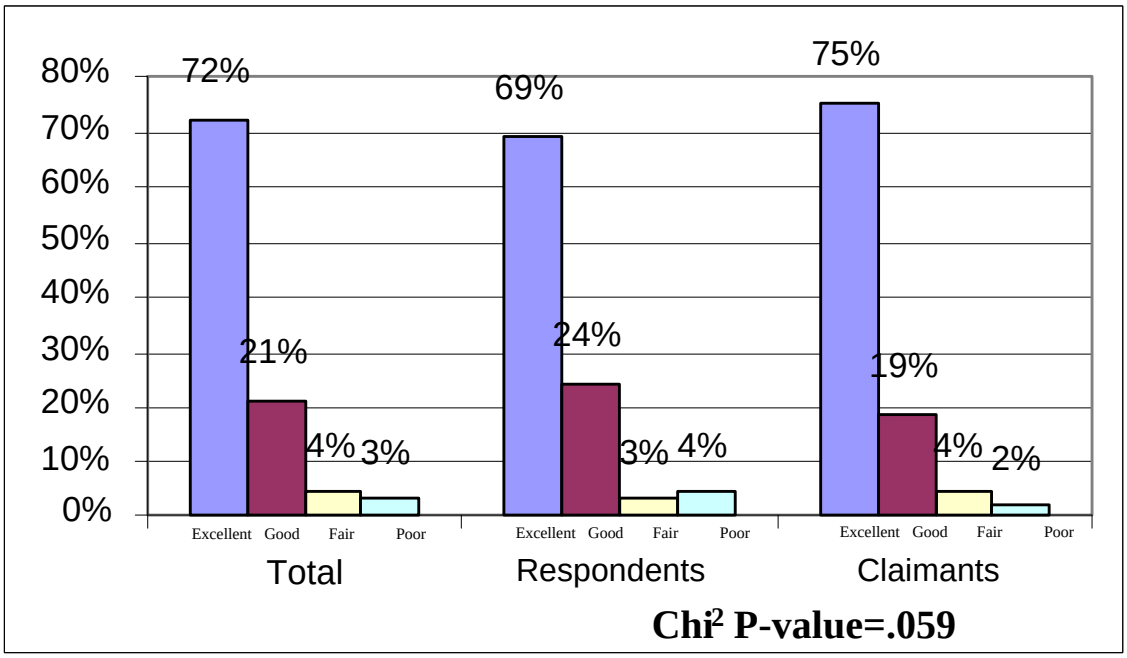
Analysis

Conducted efficient hearing sessions	Freq.	Percent	Cum.
Excellent	689	72.15	72.15
Good	204	21.36	93.51
Fair	36	3.77	97.28
Poor	26	2.72	100.00
Total	955	100.00	

	Conducted efficient hearing sessions				
claim	Excellent	Good	Fair	Poor	Total
Respondent	299	104	15	17	435
	68.74	23.91	3.45	3.91	100.00
Claimant	378	97	18	9	502
	75.30	19.32	3.59	1.79	100.00
Total	677	201	33	26	937
	72.25	21.45	3.52	2.77	100.00

Pearson chi2(3) = 7.4439 Pr = 0.059

Conducted efficient hearing sessions



V Conclusion and Future Studies

Based on our analysis of the data, the over 93% of the parties to ODR arbitrations found their cases had been handled fairly and without bias. The parties also overwhelmingly believed that arbitrators:

- displayed professionalism;
- listened attentively;
- used clear impartial or unbiased language;
- displayed the ability to understand the material presented;
- displayed sensitivity to gender ethnicity and cultural differences;
- displayed sensitivity to the parties;
- displayed knowledge of NASD Regulation Rules and Procedures;
- displayed ability to analyze problems/identify key issues;
- displayed fairness and the appearance of fairness;
- and displayed knowledge of security industry terminology and practices;
- decided motions in a timely manner;
- commenced hearing sessions on time; and
- conducted efficient hearings.

Our data reflects the parties' overwhelming approval of the arbitrators who heard their case. As noted earlier, these extremely strong favorable responses, especially from the claimants or those who represented the claimants, seem to contradict previously written articles critical of ODR arbitrators and of the ODR process.

The authors plan to do additional analysis of this data to further evaluate the statistical significance of our findings. In addition, ODR is in the process of revamping its party evaluation of arbitrators survey instrument.

Continued evaluation of this and other data are essential to properly monitor the parties' evaluation of ODR arbitrators and the parties' belief that they were treated fairly and in an unbiased manner.

APPROVED JUNE 13, 2003

Minutes of the
January 13, 2003 Meeting of the
Securities Industry Conference on Arbitration
Fordham Law School, New York, NY

Members Present
Amal Aly, SIA
Robert S. Clemente, NYSE
Ted Eppenstein, Public Member
Linda Fienberg, NASD
Jim Flynn, CBOE (by phone)
George Friedman, NASD
Betsy James – Deputy General Counsel and Director of Arbitration, Pacific Exchange (phone)
Constantine Katsoris, Public Member and Chair
Steve Sneeringer, SIA
Tom Stipanowich, Public Member and Secretary

Invitees Present
Jim Buck, Formerly NYSE Secretary
Pam Chapiga, Fordham Law School Clinic
Mary Anne Gadziala – SEC
India Johnson, AAA
Robert Love – SEC
Lewis Maltby
Helene McGee – SEC (phone)
Prof. Mike Perino – St. John's Law School

The Securities Industry Conference on Arbitration ("Conference" or "SICA") convened on January 13, 2003 at 9:00 a.m., Professor Katsoris, presiding. Agenda items are presented in the order in which they were discussed.

1. Approval of Minutes

Upon a motion duly made and seconded, the Conference unanimously approved the October 2, 2002 minutes with minor revisions. (Attachment A)

8. Perino Report (Tab 8)

Mike Perino, a Professor at St. John's Law School, briefly reported on the background of the report prepared for the SEC on the California Ethics Code for Arbitrators. Professor Perino noted that the subsequent suits by the NASD and NYSE, and SEC's amicus in support of the latter, were in the background of the SEC's request that he study the current SRO rules on arbitrator disclosure. The first question was, are the current standards for disclosure adequate? Second, what are the relative costs and benefits of the California standards?

Working under severe time constraints, Prof. Perino tried to read as much as he could on the issue. He looked at academic and empirical research, conducted interviews. He summarized the Executive Summary of the Report, to wit:

1. The current rules appear adequate; minor changes (on pages 4 and 5 of the report) may be in order.
2. It would be advantageous to review the current classifications of public and non-public arbitrators.
3. Additional studies are in order.
4. The California Standards ("Standards") are likely to yield very few additional benefits for investors. A new set of conflicts standards does not really address the problem, if any. Moreover, there is considerable overlap. They are obviously based on very different philosophy. The Uniform Code is based on standards; California's approach with a list of disclosure is also covered to a great extent by UCA standards. Some of the additional requirements of California are very burdensome, and may disqualify arbitrators with expertise.
5. California's Standards do not mesh well with the SRO arbitrator disclosure and disqualification rules. Under the Standards, a party could easily disqualify arbitrators and providers based on disclosure standards that don't make sense for securities arbitrators who have no financial interest in the SRO. Also, read literally, a party could under the Standards effectively challenge an SRO from administering an arbitration.

Mr. Clemente indicated that SICA has taken action on 3 of 4 recommendations by Mr. Perino. He indicated that it would be valuable to have a study of the operation of existing standards, but noted that funding is a problem.

Mr. Perino indicated that the GAO studies only deal with arbitration outcomes. That, however, does not address the particular issue here. The other study is the Tidwell study that surveyed forum users' perceptions of the arbitration process.

The problem with that study is that someone under the auspices of NASD developed it. An independent approach is needed. He would like to see a broader, randomized survey of participants. Depending on the data that are available from the SROs, we may be able to do additional empirical studies on arbitration outcomes, or how challenges are handled.

Mr. Maltby was surprised that Mr. Perino's report did not reflect greater concern with possible liability of arbitrators under the new California standard. Mr. Perino said there are real concerns about imposing the California Standards.

Mr. Eppenstein asked whether the SEC requested the report before or after the filing of its amicus brief. Mr. Perino said that his report was to be issued by mid-November, after the amicus brief was filed. He noted that the brief focused on preemption issues, while his report was on the bona fides of different disclosure approaches.

9. Changes to UCA Sections 18, 19

Mr. Love noted that the proposed changes to the arbitrator disclosure are to the newer version of the UCA, the Plain English version. He noted that the UCA has not actually been used by anyone in the new version; this does not address the existing rules. Mr. Perino responded that his recommendations were based on the current NASD and NYSE rules.

Mr. Friedman indicated that what the SROs seek is a signal from SICA that it does not allow permissive language – i.e., that establishes a guidepost for changes to the current SRO rules. Mr. Love concurred.

Mr. Friedman moved that SICA make a specific statement that the SROs should adopt language along the lines of the Perino report on disclosure, and that this is consistent with the spirit of the current language of Section 19 of the UCA. Specifically, the proposal to change Section 19 "must" references to "shall" was withdrawn as moot, since the Uniform Code already uses such language.

Mr. Clemente moved that the proposed language to change Section 18(b) be amended to delete the final portion of the proposal (referencing to examples of circumstances). Mr. Friedman seconded. With this amendment, the proposal to change 18(b) was adopted to add the language beginning "A challenge for cause . . ." and ending ". . . remote or speculative."

6. Lewis Maltby (re Public Citizen Report on the Cost of Arbitration and Need for Further Empirical Research)

Mr. Friedman introduced Lewis Maltby, Director of the Workplace Rights Institute. The organization filed comments on the proposed California standards. He indicated that Mr. Maltby was one of the early proponents of looking closely at the facts of outcomes in employment arbitration.

Mr. Maltby explained the role of his "civil rights organization that believes in employment arbitration." It espouses a different view from much of the trial bar, which tends to disfavor arbitration of employment disputes. In view of the fact that 95% of civil litigations are settled, it is important to study the effectiveness of arbitration. This led him to do empirical research on outcomes, which showed that outcomes for employees were actually better in arbitration than in litigation. He also noted that previous studies showing employee "win" rates in arbitration compared to litigation did not include the effect of summary judgment in litigation (about 60% of the cases); the reviewers only included the outcomes in court cases resulting in a jury verdict. His position is that voluntary and fair arbitration is the best approach for resolving employment disputes, and works best for the employee.

Mr. Maltby said that when you read the press on arbitration, it is always abysmal, unfair. He indicated that the press tends to be biased, because they have not heard an independent and credible approach. He noted, his organization submitted comments that were highly critical of proposed standards. He said that no arbitrator will ever meet these standards, and that it will hurt, not help, the typical employee and consumer. He said his group is working on an amicus brief for the SROs' appeal to the 9th Circuit of its declaratory relief action against the California Standards. They do not to improve on what the SROs' outside counsel prepare, but will try to make the case to the court that SRO arbitration is not about "the big guys sticking it to the little guys."

Turning to the rather negative report on arbitration issued by Public Citizen, Mr. Maltby said he fears that the report, which is conclusory and based on sloppy research, will be cited as empirical evidence in future post-*Greentree* litigation. He said his group is writing a report about this. He stated that there is a need to look at total costs for employee or consumer, that in reality are "astronomically lower" in arbitration. He noted his group would like to do more work on public education. In Mr. Maltby's view, NELA is trying to destroy consumer and employment arbitration.

Mr. Maltby acknowledged limits of AAA data, but researchers do not have much other data to work with. He did not look at NASD, NYSE cases. Mr. Friedman indicated that SRO statutory employment case filings are now dwindling. Mr. Maltby also noted that settlements were not tracked. Mr. Eppenstein wondered how that would affect data. Also, he wondered about win/loss ratios. Mr. Maltby indicated that arbitration clearly is better for employees in terms of win/loss ratios, especially when one factors in dismissals and summary judgments. Mr. Maltby noted that Ted Ericson at Cornell is doing sophisticated work to come to similar conclusions. Sam Estreicher has also done an empirical study, with similar results. Mr. Stipanowich mentioned Chris Drahozal's work. Mr. Maltby says that much more work needs to be done to convey information about this approach.

Ms. Fienberg observed that SICA and SROs are moving toward resolving the last of the fairness issues regarding securities arbitration – classification of industry vs. non-industry arbitrators. Mr. Friedman queried whether Mr. Maltby's group could do empirical research on fairness of securities arbitration (one of the suggestions in the "Perino Report"). Mr. Maltby indicated that someone should do it, on an independent basis.

2. Proposal to Amend UCA Section 16(c) Arbitrator Classification

Mr. Sneeringer moved to table the proposal to amend Section 16. Mr. Eppenstein indicated his willingness to table this item. It will be addressed at the April SICA meeting.

3. Subpoena of Third Parties

Mr. Friedman indicated that the NASD's National Arbitration and Mediation Committee (NAMC) had referred the subpoena rule back to a subcommittee. The NAMC is working on notice requirements related to discovery subpoenas to non-parties, and also on arbitrator resolution objections filed by the other side. The NAMC subcommittee will also look at exceptions to an advance notice period. Hopefully, these will be addressed at the February NAMC meeting. Mr. Friedman will provide a status update at the April SICA meeting.

Mr. Eppenstein wondered whether or not there had been consideration of an attempt to table such discovery until a preliminary hearing. Mr. Friedman indicated not.

Questions were raised regarding the source of the document at Tab 3. Mr. Love raised a questions about subparagraph g(1) in the proposal at Tab 3, asking about various perspectives on the additional time that might be involved.

He also raised a question about subparagraph g(2): will there always be an arbitrator to deal with unresolved subpoena issues? Mr. Friedman indicated that there would be scenarios where there would be no arbitrator in place at the time the issue arises. Current NASD practice is to refer such issues to the arbitrators (to be resolved when they are appointed).

Finally, Mr. Love asked for clarification about subparagraph g(3), regarding what is "a court of competent jurisdiction." Mr. Stipanowich made reference to current provisions in federal and state law for limited judicial authority to enforce subpoenas or "summonses." Mr. Eppenstein noted that challenges to subpoenas are a common problem.

In light of the fact that no SICA representative is sponsoring the document at Tab 3, and in light of NAMC action to date, the discussion was concluded. Mr. Friedman offered to report back to the group on the NAMC's effort. Mr. Eppenstein agreed to follow up with Mr. Lipner on the proposal at Tab 3.

(No Tab Number): Securities Arbitration Commentator – Letter from Mr. Ryder

Professor Katsoris distributed a letter from Rick Ryder, Publisher of the SAC, regarding public awards. He suggested that it should be addressed at the next meeting.

11. Law School Securities Arbitration Clinics

Prof. Katsoris introduced Pam Chepiga, director of the Fordham Clinic on Securities Arbitration.
Ms. Chepiga indicated that the securities arbitration clinics serve a population of people with limited means, limited experience in markets, and limited educational backgrounds. She reported that the Fordham Clinic's clients are people who tend to have no comprehension of the system. She noted that there are six operating clinics, all in New York: Pace, Brooklyn, Buffalo, Fordham, and, pending, at Hofstra.) There are clinics opening in other law schools as well. Fordham takes cases from the New York City Bar, which places a ceiling of $50,000 on matters referred. Fordham does not charge a fee to clients; Buffalo does.

Fordham hosted a roundtable meeting recently for the clinic directors. The focus was the common problems. All clinics are inundated with requests for representation, often by people from outside New York. The students here are permitted to work on matters under court order. There is a need to open clinics in other states to give people an opportunity to learn about arbitration. The Fordham group gets many calls from Florida, Colorado, California, etc. Generally speaking, unless a case involves at least $200,000, parties find it difficult to retain counsel.

Ms. Chepiga indicated that the Fordham Clinic represented clients in about 15 arbitration matters.

4. Proposal to Ban Secret Settlements

Mr. Eppenstein once again drew attention to the report at Tab 4, and the action of South Carolina federal judges and the courts of Michigan forbidding secret settlements. He proposed perhaps SICA should take action forbidding secret settlements in the arbitration context. He suggested that regulatory referrals might be an appropriate approach.

Ms. Fienberg explained that an NASD expungement rule was filed with the SEC but has not yet gone out for comment. The notice to members captures what will be proposed (it is on the NASD website): a court must approve expungement orders, and NASD Regulation must oversee to determine whether they will oppose them. PIABA filed extensive comments to the proposal, along with about 30 others.

Mr. Eppenstein indicated that current reporting requirements leads to watered-down disclosures, without much detail. Ms. Fienberg noted that in court, the complaint would be a public document even if settlement is not. In arbitration, that is not the case; and many cases settle for a variety of reasons. She expressed the view that if settlements are public documents, it might undermine the ability to settle, to the detriment of investors.

Mr. Eppenstein suggested that there should be not only early review, but also later regulatory review in big cases.

Mr. Sneeringer said the reality is that a client cannot be prevented from speaking with a regulator, settlements must be reported where the broker is released, and in substantial matters regulators tend to make inquiries. For all these reasons, it is

unlikely that there will be a large settlement that escapes regulatory scrutiny.

Ms. Fienberg indicated that the NASD has assumed a huge burden of oversight, and is uncertain that there is more that can be done beyond what is already being done. Regulators look not just arbitration awards, but at any evidence of misconduct and irregularity.

The matter was tabled for further observation.

5. Fitzpatrick/Beckley Workshop

Mr. Clemente reported that the arbitrator training video is being edited, and will shortly be duplicated and distributed to all participants. The NYSE plans to use it in interactive training.

7. California Arbitration Ethics Standards

Mr. Clemente reported that the California Standards were amended as of January 1st (the Judicial Counsel originally issued them in July 2002). Meanwhile, the litigation challenging the Standards continues. NASD and NYSE are only proceeding with arbitration in cases in that state where the parties have waived the Standards (firms must agree to waive the Standards when the customer does so).

The *Mayo* case, in which NYSE and NASD are intervening, is addressing the issue of preemption under a motion to vacate an order compelling arbitration. The case is scheduled to be heard in February. Mr. Clemente agreed to provide a status update at the April meeting.

10. Proposal to Conduct Independent Research to Evaluate Fairness of SRO Arbitrations

Professor Katsoris initiated a further discussion of the possibility of sponsoring independent research on SRO arbitrations. Mr. Friedman said the issue was trying to assess attitudes without looking at specific cases. Various options were discussed, including the Consumer Federation of America, the ABA Litigation Section (planning a survey), RAND, and the group working with Kaiser on current perceptions of their ADR system. Pros and cons of different groups, the problem of funding, and the possible structuring of a survey, were discussed.

Mr. Friedman and Mr. Clemente agreed to look at options. Perhaps SICA could

commission the survey, and SROs could fund it. Messrs. Clemente and Friedman agreed to provide a status report at the April SICA meeting.

12. NASD Rule Filings

Mr. Friedman noted that NASD has a rule taking effect today to give refunds of the member surcharge where the arbitrator completely denies the claim *and* also allocates *all* forum fees against the customer.

An NASD rule took effect in October requiring the specificity of the answer to meet the specificity of the claim.

There was a proposed change to the eligibility rule that was withdrawn in December in light of the Supreme Court's decision in *Howsam v. DeanWitter*. A new rule will be proposed shortly, expressly giving arbitrators the power to rule on eligibility disputes.

Mr. Clemente suggested that SICA should address the question of the effect of the six-year rule. Mr. Clemente will prepare a proposal for review at the next meeting. Ms. Fienberg indicated that NASD would probably support a rule making clear that the six-year provision does not amount to an election of remedies.

13. NYSE Rule Filings

Mr. Clemente noted an amendment of the small claims rule, bringing the ceiling up to $25,000, and an extension of the mediation pilot (making the mediation program a permanent part of the NYSE rules).

New Business

14. Items Raised by Public Members

Item 2. Payment of Awards; Bonding. Mr. Eppenstein recapped the issues associated with the problem of non-payment pending appeal of an award. Mr. Eppenstein noted that in some cases the payment of award is delayed by as much as a year. He proposes that the Uniform Code require payment, or bonding of an award, within 30 days.

Ms. Fienberg raised the issue of whether or not the bonding arrangement might be

similar to that issued upon appeals of court judgments. Although major firms can obtain bonds quite regularly, it may be onerous for small firms. There may be an issue respecting the availability of such bonds. There is a need to know how this will work and how much it might cost.

Mr. Sneeringer also stated that there is an interest requirement on awards not paid within 30 days; moreover, the cost of a bond would be unrecoverable. He questions whether it will accomplish its primary objective, which is how to get those who routinely don't pay awards to pay. All the bond is doing is making sure the money is there to pay – not get payment made earlier.

It was agreed that Mr. Eppenstein would prepare a proposal, and touch base with Mr. Banks and Mr. Mason of PIABA to solicit their assistance. Ms. Aly agreed to put the matter before an appropriate SIA committee before the next SICA meeting if Mr. Eppenstein can pass along a proposal.

Item 3. Pre-hearing motion practice.

Mr. Eppenstein raised the question whether dispositive motions should be allowed in arbitration. Professor Katsoris noted that in his experience dispositive motions are rarely if ever granted.

Mr. Sneeringer indicated that such motions have been more successful in recent years. There may be a special arbitration hearing on 6-year rule issues. Ms. Aly noted that some claimants' counsel bring in "everyone under the sun," and a pre-hearing procedure to dismiss those parties who have nothing to do with the case is critical.

Ms. Fienberg said that the NASD is examining this issue, and will report during the June meeting. She indicated that the result may be some form of guidance for arbitrators' discretion.

Item 4. Classification of Arbitrators: Reviewing the Pool

Mr. Eppenstein proposed that there be a committee made up to look at the public arbitrator biographies.

Ms. Fienberg responded that the GAO, SEC and the NAMC all look at the NASD pool, and the NASD is unwilling to submit to another review process. They have about 6,000 arbitrators. Mr. Sneeringer indicated that being on that NAMC

subcommittee, he looks at 200-300 bios a quarter. The NAMC committee for arbitrator selection consists primarily of public members.

Mr. Stipanowich seconded Mr. Eppenstein's motion. By a 3-3 vote, the motion was not carried.

Item 5. Arbitrator Bios

Mr. Eppenstein queried whether it is possible to make the bio form clearer, and to update the disseminated information more frequently. One issue has to do with the nature of the form – that is, does it show how recently it has been updated.

Ms. Fienberg indicated that under NASD's new computer system, arbitrators will be able to update their own forms. Many already do this. The NASD representatives will report at the next meeting on their updating procedure.

Item 6. Arbitrator Appointment or Replacement

Mr. Eppenstein proposed that administrative appointments or replacements be reviewed to see if they can be accomplished more quickly. Mr. Clemente said he would have to see specific examples of problems;. Ms. Fienberg said the same on behalf of NASD. Both SROs were interested in being aware of problems with slow appointment of arbitrators. Mr. Love indicated the SEC would also be interested in specific instances of this kind. Ms. McGee encouraged Mr. Eppenstein to copy her on letters referring to specific examples.

Item 7. Timing of Arbitrator Disclosures

See Item 5 above.

Item 8. Lack of Responsiveness by Arbitrators

Mr. Eppenstein pointed out a continuing problem with lack of responsiveness to questions by proposed panelists. He queried whether the NASD would be willing to toll the time to permit responsiveness to questions. Ms. Fienberg indicated that NASD would not toll time limits without mutual agreement (as provided in current NASD Code of Arbitration Procedure).

It was explained that responses are not mandatory under the current rules. Ms. Fienberg said NASD encourages its arbitrators to answer questions. Mr. Friedman

indicated that if an arbitrator fails to respond to questions, that fact might serve as a basis for a challenge for cause.

Ms. Aly raised a question about what kinds of information might be requested over and above the disclosures required by the Uniform Code. Mr. Eppenstein will bring a form with examples of questions for the next meeting. The NASD will bring in information on current training information on responses to questions.

Item 9. Preliminary Review of SRO Proposals Before Filing.

Mr. Eppenstein proposed that SICA be permitted to review all SRO proposals prior to SEC filing so that there will be an opportunity to comment. Ms. Fienberg indicated that SICA usually sees NASD rule proposals during the development process – sometimes even before the NAMC does. NASD typically vets proposals with SICA, PIABA, the SIA Arbitration Committee, and of course the NAMC.

Mr. Clemente indicated that the NYSE routinely vets proposals with SICA.

Item 10. Agenda Books to Invitees.

Mr. Eppenstein expressed concern that invitees get agenda books. Mr. Love pointed out that fewer people get the agenda books than are listed in the minutes. Mr. Clemente noted that representatives from organizations such as NFA and AAA do not receive meeting books.

16. Future Meetings

Spring meeting: The next meeting of SICA will be conducted on the morning of April 9. Members of the SIA arbitration committee will join SICA.

Summer meeting: Messrs. Eppenstein and Stipanowich are unavailable for the late June dates. The meeting ultimately was rescheduled for Friday, June 13 in New York at the NASD offices at One Liberty Plaza.

Fall meeting: The fall meeting will be held in conjunction with the PIABA meeting in late October in Palm Springs. Based on past experience, we are likely to meet on the day before the official start of the conference (Oct. 21 or 22), but this needs

to be resolved.

The meeting adjourned at 3:05 p.m.

Respectfully submitted,

Thomas J. Stipanowich
Secretary

From: Love, Robert A.
Sent: Thursday, January 23, 2003 5:34 PM
To: McGuire, Catherine
Cc: Love, Robert A.; Jenson, Paula R.; Corcoran, Joseph P.; McGowan, Thomas K.; Harmon, Florence E.; Pennington, Mark R.
Subject: notes from SICA

Summary of key issues, including those that may need follow-up, from Monday January 13 SICA meeting. (Tom, a portion of item D is for your attention.)

[redacted]

A. Perino Report. Mike Perino attended SICA to discuss his report stemming from the California ethics standards. His report included four recommendations. SICA discussed moving forward on these.
(1) Amend arbitration rules to clarify that all conflict disclosures are mandatory. All agreed with Perino this should be done. On the agenda was a proposal to amend the Uniform Code to effect the change. But the Uniform Code is now the Plain English version, and I pointed out that the proposed change weakened the obligations (switching "must" to "shall" instead of Perino's requested change in SRO rules from "should" to "shall") - (I was also concerned that the Uniform Code not become inconsistent with a unique use of 'shall' when a different norm had been chosen).

All SROs now have rules based on the non-PE format (whose eventual adoption is not imminent). The result of the discussion is that no change is to be made to the Uniform Code, and there instead is a resulting "sense of SICA" for the SRO members to report to their respective boards so that the individual SROs will make the necessary change (of "should" to "shall") to their rules.

(2) Public and Non-Public arbitrator definitions. Perino thought any bias perceptions stemmed from arbitrator classifications, not from the disclosure provisions, and recommended that SROs consider broadening the industry category. SICA had been scheduled to conclude a revision to the arbitrator classification provisions at the meeting, but the item was withdrawn by the SIA. No discussion on this was held at the meeting - [redacted]

(3) Challenges for cause. Perino recommended that the challenge for cause standard in the Arbitrators Manual be incorporated into the rules. This was done by SICA. The proposal in the manual would have included both the standard, and a page of examples accompanying the standard in the Manual, going. Once it became clear what the recommendation was, SICA adopted the standard - the full text remains in the manual.

(4) Independent research to evaluate fairness of the SRO arbitrations. While there was a general agreement that this would be fine, there was no consensus on how to achieve it. There are both funding issues (SROs assume they'll have to pay) and independence issues - what formulation would avoid taint by connection to the SROs? Stipanowich'sCPR Institute for Dispute Resolution, Barbara Roper's Consumer Federation, Gallup, National Work Rights Institute all discussed. This is one where they are looking for ideas/guidance. If we have any, now would be the time to mention them - this has been delegated to Fienberg and Clemente. (The work Perino had liked best was that done by Gary Tidwell for the NASD, and that was not independent.)

B. National Workrights Institute. Lewis Maltby of the NWI has a very different take on arbitration than the National Employment Lawyers Association, (NELA), and its leader, Cliff Palefsky. Much more in favor of arbitration. Group spun off of ACLU. Says that Palefsky and NELA get the 5% of cases that are big money cases, and want court. Maltby is more interested in 95% of cases that need access to arbitration. He views outcomes in arbitration as favoring employees (note, not securities specific research), because he says other studies didn't account for those cases dismissed on summary judgment. Recovery he found was 18% in favor of plaintiffs in arbitration versus 10% in court. His group commented critically on CA standards. He commented briefly on the Public Citizen report on the costs of arbitration, and asserted that it had been requested by Palefsky, with a foretold result. (Note, the study compares forum fees, but discounts the transaction costs of litigation such as discovery and legal fees. He is working on further public education. Represents that NELA is focussed on destroying consumer arbitration. Asserted that some other academic work supports his (at NYU and Cornell I think). Note, while he speaks well, NWI has a staff of three including Maltby. I have their 'promotional" literature.

C. Subpeonas on 3rd parties. This discussion followed an issue raised first by former SICA member Tom Grady, and then PIABA. The issue concerns an industry party sending a subpoena by express post to a non-party, with a delayed

regular mail copy to a party. There would then be no way to stop compliance if that was necessary. No public member was capable of explaining the proposal. No one owned to have written it. There was surprising agreement that a rule amendment could address this. I deferred to them, but was a little surprised that they (including NASD) thought the routine 10-day period built into the rule to allow for challenges and a referral to an arbitrator was acceptable. (NASD said its NAC was considering a version of this, with some discussion of whether allowing a non-party firm to supply certain responsive data without waiting for the arbitrator would be perceived as fair. I told them that as drafted, the proposal would not be acceptable here because it the time frames do not match the existing rules (it assumes that a panel of arbitrators has been appointed to hear an objection which is not accurate under the sequence of events in the rule). I said no assumptions - if an arbitrator would then be appointed, or the 10 day period extended, the rule must say it. Also, the rule makes another vague reference to a court of competent jurisdiction. I told them no more unclear references to court. [redacted]

D. Law school arbitration clinics. Pam Chepiga of Fordham's law school reported on the clinic. She is very high on the clinics' usefulness, which at Fordham is always oversubscribed. Her 3 issues are (1) need for more clinics nationwide (they field hundreds of inquiries from out of state, (2) more generous and objective fee waiver guidelines so that parties don't decline going forward because of the risk of fees being assessed against them; and (3) unnecessary litigation tactics by firms trying to avoid payment. Even joint and several awards aren't paid (but the sole solvent respondent.) The tactics including post-award settlement discussions demanding low settlement, or that the parties join them in court to obtain expungement, at the risk of multiple delaying appeals and bankruptcy threats. Because the firms at issue file motions to vacate within the rule timeframes, they are not enforcement candidates, and settlement discussions can't be used outside the discussions in proceedings. [redacted] Chepiga noted that the various clinic organizers meet periodically, and would like to renew contact with SEC staff. I have since briefed Joe more fully on the discussion, and linked him up with Chepiga.

Note, a related discussion later in the meeting concerned a PIABA proposal. The idea would be that losing respondents should be required, as now, to pay within 30 days, or if they elect to pursue a motion to vacate, must post a bond to assure that money is there if the motion fails or the firm goes under in the ensuing delay. Some thought this would only hasten the demise of firms that are likely to fold (but that this could stop them sooner from hurting others). Some thought the larger firms could obtain bonds pretty inexpensively, while the smaller firms could not. [redacted] [It seems that under the current NASD rule approach, a member now has to show that it either has paid, or filed a motion to vacate within 30 days; under this proposal, the member showing it had filed a motion to vacate would also have to show that it had obtained a bond.] Eppenstein, who brought this forward as an idea, stubbornly refused to do any work related to it— are such bonds obtainable? by whom, from whom, and at what cost? apparently there is no similar current bond/product anyone knew of. Buck noted that even for some large firms this could be relevant - Drexel had $800 million in excess net capital shortly before it went out of business. Fienberg said NASD thinking a little along these lines, but perhaps trying to find a way to direct the burden to firms that are more of a problem (limited capital or extensive disciplinary problems). [redacted]

E. Case volume, analysts. NASD reported that it expects a number of analyst-related cases against Smith Barney and Merrill Lynch. Reports as of the time of the meeting suggested 1000s of cases immediately. The numbers so far are smaller, more controlled. NASD's Friedman advises that:

A Florida attorney named Weiss filed 71 small claim cases against Smith Barney and Grubman, with 100s more coming.

Today, a $30 million claim against Merrill was filed by a NJ couple ($10 Million compensatory).

Boyd Page in coming weeks/months intends to file 1-5 thousand small claim cases against both Merrill and Smith Barney (not naming Blodgett and Grubmann). [Some of these to be filed at NYSE.]

All known cases so far involve customers with accounts at these firms, not investors who reacted to the analysts reports and executed at e-trade, etc.

NASD arb will try to work with the parties to coordinate the cases in conferences to expedite. They will keep us posted in order to assure conformance with rules, and Rule 19b-4.

F. Secret Settlements. Eppenstein would like SICA to weigh in on secret settlements, showing bans now in place in

some courts. Fienberg noted that expungement rule is now being considered by SEC (PIABA and SIA both filed comments.) LF noted settlements have to be reported, Eppenstein says they are watered down – disagree as to whether there are "secret settlements" above the threshold. Fienberg noted 70% cases settle, and that if public documents, the number would go down, with the public hurt. Noted that all statements of claim reviewed by regulation staff when filed (before, when resolved, but that approach considered to be too late). TE thinks all larger settlements should be reviewed closely - NASD says what he asks already done.

G. Training Tape. The be nice tape is being edited, and should soon be added to the training protocol.

H. California arbitration. NASD noted that it had appealed. NASD noted that it and NYSE took a different approach to the CA than the Pacific exchange because it believed the true California legislature's intent is that it doesn't apply to them, as reflected in the bill vetoed by the Governor. NASD/NYSE are different on requiring the signing of waivers by associated persons - NASD requires, NYSE thinks it happens by rule, even without a signature.

I. NASD noted it filed a rule on January 13th effective immediately that would refund the non-refundable filing fees to members who prevailed in arbitration on all counts (a rule requested by small firms.)

NASD noted that on 12.17 it withdrew its proposed change to the eligibility rule giving the decision to the director of arbitration, in light of Howsam.

Discussed other various NASD/NYSE rule amendments, not written out here.

J. Public Member proposals. In addition to the bonds for award payments, written out above, SICA discussed: Dispositive motions. NASD thinks a black & white rule would be too harsh (but that statute of limitations issues should not be resolved by dispositive motions). NASD is working on guidance in this area, with the discretion remaining with the arbitrators - therefore leaning to education, not strict rule. Eppenstein requested to review the whole public pool – it wants all the arbitrators with disclosure information to review. NASD said it would not turn over its files to PIABA. Eppenstein could not explain why his and other plaintiffs lawyers review of the same information over time was not useful in the SICA task of assuring that classification rules drew the line correctly. He didn't accept Fienberg's observation that SEC and GAO inspectors regularly looked at their files (SEC staff in fact checking proper classification). His motion for this failed, with a 3-3 vote. Eppenstein complained that disclosure reports were 'misleading', raising an issue of whether the date on the forms was as of the date printed or some other date. SROs will check - at most a computer programming issue, [redacted] SROs will make sure it is clear to parties. Brief discussion of whether administrative appointments (when the lists fail) occur soon enough, or too soon to the hearings - no clear data for us to react to. Discussion of how to address follow-up questions by parties that are not responded to by the arbitrators – it seems they may move to education. Reasonable that arbitrators should either reply, or state that they won't reply because intrusive. Or if particular issues can be identified, perhaps standard disclosures could be expanded. Asked that all SRO filings be vetted first with SICA – without promises, SROs [correctly] stated that all substantive matters have been discussed in SICA (although final versions approved by Boards are not then brought to SICA before filing).

RAL

Linda D. Fienberg
President, Dispute Resolution
Executive Vice President and Chief Hearing Officer, Regulatory Policy and Oversight

January 26, 2007

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Re: Letter of January 12, 2007 Regarding the Proposed Consolidation of the NASD and NYSE Regulation Arbitration Programs

Dear SICA Public Members:

This letter responds to your January 12, 2007[1] letter (letter) to SEC Chairman Christopher Cox sent in your capacities as past and present members[2] of the Securities Industry Conference on Arbitration (SICA). The letter, while reflecting your keen interest in the arbitration process, contains many conclusory statements that have no evidentiary basis. NASD would like to address these potentially misleading statements.

Single Dispute Resolution Forum

Your letter states: "The prospect of a single securities arbitration forum maintained and funded by the securities industry will only heighten the suspicion long held by many public investors that the system they are compelled to use is less than independent and hence less than fair."

[1]Although a SICA meeting was planned for and held on Tuesday, January 16th, you sent the letter without prior consultation with SICA's other members.
[2] The letter was signed by the three current public SICA members, Theodore G. Eppenstein, Constantine N. Katsoris, and J. Pat Sadler, and the three past public members, Peter R. Cella, Thomas R. Brady, and Thomas J. Stipanowich.

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First, we must challenge any notion that NASD's arbitration program is unfair; this is not the case. In 1999, NASD engaged the United States Military Academy at West Point to conduct an independent analysis of surveys submitted by our forum's constituents. The West Point report stated:

> Based upon the analysis of the data collected, we are able to conclude that participants to ODR[3] sponsored arbitrations believe their case was handled fairly and without bias. The data we have analyzed shows the parties to ODR arbitrations are overwhelmingly satisfied with the fairness of the forum. For example, at the conclusion of their arbitration case, 93.49% of those responding indicated that their case "appears to have been handled fairly and without bias."[4]

That study found the same strong and overwhelmingly positive results when parties evaluated the arbitrators who heard their case.

In 2002, the SEC commissioned a study and report by Professor Michael A. Perino[5] on the adequacy of arbitrator conflict disclosure requirements at NASD and NYSE. Professor Perino's report also touched on user perceptions of fairness, finding that "[a]vailable empirical evidence suggests that SRO arbitrations are fair and that investors perceive them to be fair."[6] The report also suggested that, to resolve any doubts about investor perceptions regarding the fairness of self-regulatory organization (SRO) arbitration programs, the SROs should sponsor an independent user survey. This survey is about to be conducted under SICA's auspices by the Pace Investor Rights Project (affiliated with the Pace University School of Law).

NASD believes that it is the quality of the forum that dictates fairness rather than an investor's ability to select one dispute resolution forum over another. As shown by SICA's reported statistics, there has been a steady migration by investors to NASD's arbitration forum even without consolidation; the result is that NASD already administers over 94 percent of the investor-broker disputes filed every year.[7] We note also that the Commission has approved the consolidation of arbitration programs at several SROs with NASD over the past decade with no adverse effects.[8]

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[3] Prior to July 2000, NASD's dispute resolution program was part of NASD Regulation and was known as the "Office of Dispute Resolution" (ODR).

[4] G. Tidwell, K. Foster, and M. Hummel, Party Evaluation of Arbitrators: An Analysis of Data Collected from NASD Regulation Arbitrations, at 3 (Aug. 5, 1999) http://www.nasd.com/web/groups/med_arb/documents/mediation_arbitration/nasdw_009528.pdf>.

[5] Visiting Professor of Law, Columbia Law School when the report was issued; currently Professor of Law, St. John's University School of Law.

[6] M. Perino, Report to the SEC Regarding Arbitrator Conflict Disclosure Requirements in NASD and NYSE Securities Arbitrations, at 51 (Nov. 4, 2002) <http://www.sec.gov/pdf/arbconflict.pdf>.

[7] The SICA 13th Report (2005) shows that NASD's share of total arbitration cases received by SROs increased from 65 percent in 1988 to nearly 89 percent in 2004. Using statistics on the NASD and NYSE Regulation Web sites, NASD estimates that its share for 2006 will be over 94 percent.

[8] The NASD Code of Arbitration Procedure applies not only to NASD firms and their associated persons, but also to members and associated persons of the following SROs pursuant to agreements under which NASD administers their arbitration processes: Municipal Securities Rulemaking Board (MSRB), the Philadelphia Stock Exchange (Phlx), the American Stock Exchange (Amex), the International Securities Exchange (ISE), and The NASDAQ Stock Market LLC (Nasdaq). Exchange Act Release No. 39378 (Dec. 1, 1997), 62 Fed. Reg. 64417 (Dec. 5, 1997) (MSRB); Exchange Act Release No. 40517 (Oct. 1, 1998), 63 Fed. Reg. 54177 (Oct. 8, 1998) (Phlx); Exchange Act Release No. 40622 (Oct. 30, 1998), 63 Fed. Reg. 59819 (Nov. 5, 1998) (Amex); Exchange Act Release 45094 (Nov, 21, 2001), 66 Fed. Reg. 60230 (Dec. 3, 2001) (ISE), and Exchange Act Release No. 53128 (Jan. 13, 2006), 71 Fed. Reg. 3550 (Jan. 23, 2006) (Nasdaq).

Customer Case Results

Your letter states: "[C]ustomers' chances of winning an award had substantially dwindled to around forty-three percent by 2006." The conclusion that outcome rates over a specific period of time define the fairness of the forum is empirically dubious. There are many factors that influence particular outcomes. Publicity about a regulatory crackdown on a particular practice can cause an increase in claims, including some without merit. For example, investors filed hundreds of claims after regulatory actions regarding misleading analyst reports, but arbitrators dismissed many of those claims due to lack of a relationship between the claimant and the analyst. Similar outcomes occurred where investors took these cases to court.[9] Moreover, as an impartial forum, NASD cannot ensure that a particular side will win more cases than another. Certainly, the court system is not evaluated in this manner.

As a regulated SRO, NASD is proactive in ensuring that its rules and procedures are fair and understandable to investors. NASD does not require customers to arbitrate. Rather, under NASD rules, brokerage firms and their associated persons have a duty to arbitrate upon the demand of a customer, whether or not there is a predispute arbitration agreement.[10] Moreover, NASD's rules provide that, if broker-dealers elect to use predispute arbitration agreements, those agreements must contain enumerated safeguards and disclosures to protect investors. Customers already have the right to take their claims against defunct firms directly to court. A 2001 amendment to the rules prohibits a firm that has been terminated, suspended, or barred from the NASD, or that is otherwise defunct, from enforcing a predispute arbitration agreement against a customer in the NASD arbitration forum,[11] but, importantly, does not preclude a customer from filing a claim in the NASD arbitration forum.

Your letter draws a sweeping conclusion in note 6: "NASD's statistics also show a drop of around 20% in the customer's chances from 2000 levels to 2005 levels." In fact, over the last six years, the percentage of customers awarded damages has fluctuated between 43 and 54 percent. (With regard to the reported outcome rates in particular, we also note that NASD changed retroactively the method of calculating the so-called "win" rate in 2005, resulting in a slight drop in the numbers.) Numerous factors can cause changes in recovery statistics. For example, arbitrators awarded damages in less than one third of the analyst cases described above.

The United States General Accounting Office (GAO)[12] in a 2000 report recognized that one should not draw conclusions about the fairness of the arbitration process based on case outcome statistics, stating that "GAO could not reach conclusions about the fairness of the arbitration process from

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[9] *See, e.g.*, In re Merrill Lynch & Co. Research Reports Sec. Litig., 273 F. Supp. 2d 351, 2003 U.S. Dist. LEXIS 11005 (SDNY 2003); *aff'd in part and rev'd in part sub nom.* Lentell v. Merrill Lynch & Co., 396 F.3d 161 (2d Cir. 2005) (holding that plaintiffs failed to plead loss causation); *cert. denied*, 126 S. Ct. 421, 163 L. Ed. 2d 321, 2005 U.S. LEXIS 7318 (Oct. 11, 2005).

[10] NASD Code of Arbitration Procedure Rule 10301(a).

[11] See Exchange Act Release No. 43998 (Feb. 23, 2001), 66 Fed. Reg. 13362 (Mar. 5, 2001) (File No. SR-NASD-2001-08).

[12] Now the Government Accountability Office.

case outcome statistics." The report also noted that a declining investor win rate "could indicate little or no change in the fairness of the arbitration process."[13]

Seth Lipner, former president of the Public Investors Arbitration Bar Association (PIABA), wrote in his article entitled: *Study of Arbitration Recovery Statistics:*[14]

> Because risk-willing investors generally have weaker cases than risk-averse investors, the pool of suitability cases going to award is abundant with relatively weak cases. By studying awards in those cases, we learn little about how the average or good suitability case will fare at a hearing.

In addition, experienced respondents' attorneys tend to settle the strongest cases filed by investors. The fact remains, however, that an individual investor's chances of prevailing in arbitration depend primarily on the strength of the investor's case as presented by the investor or the investor's counsel, and not on the results of other cases.

Finally, the above statistics on results of customer cases reflect only cases that were resolved by award. Such cases represent only a small fraction (approximately 25 to 30 percent) of all arbitrations. Investors settle or withdraw more than half of their cases prior to hearing. In most of these cases, the investor receives compensation. Thus, the overall recovery rate for investors is much higher than that reflected in the table on results of customer awards, a point noted by the GAO in its 2000 report.

Independent Arbitration Forum

Your letter states that the proposed single arbitration forum "maintained and funded by the securities industry" is less than independent. This statement distorts the nature of NASD's dispute resolution forum, which is not "maintained and funded by the industry." NASD's arbitration program is financially self-sufficient, and is funded by fees paid by the forum's users: firms, individual brokers, and investors. The fees are structured such that investors bear about 25 percent of the overall fees, with the balance borne by the industry. And, as noted below, we are subject to extensive regulatory oversight, and we invite significant investor and public input in shaping our program.

Referring to a supposed investor fear of unjust outcomes, your letter suggests that the Commission consider a new organization: "A single, independent securities arbitration forum, with SEC oversight and public investor and securities industry participation, [that] would serve to contribute to the reduction of this negative perception." The goal of the NASD-NYSE Regulatory consolidation, and indeed the trend in all of NASD's actions, has been to create a regulator completely independent from the commercial concerns of markets and broker-dealers.

There is strong public representation on all internal advisory and governing bodies impacting NASD's dispute resolution program. The NASD Dispute Resolution Board contains a majority of

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[13] Actions Needed to Address Problem of Unpaid Awards, at 4-5 (GAO/GGD-00-115, June 2000) ("2000 GAO Report").

[14] The article appeared in *The Neutral Corner*, NASD's newsletter for arbitrators and mediators - June 2006, page 3.

public directors. Sharon Smith,[15] our present chairperson, and John Sexton,[16] our immediate past chairperson, are both academics and public representatives. The National Arbitration and Mediation Committee (NAMC), a standing committee that proposes rule and policy changes to the NASD Dispute Resolution Board, is comprised of fourteen members. Eight of the fourteen NAMC members are public representatives, including the current chair who is also a former president of PIABA. In fact, five of PIABA's presidents have served as Chair or members of the NAMC. Finally, as you know, NASD actively participates as a member of SICA, and supports it financially by absorbing, along with the other SRO members, the public members' travel and other expenses. You are also aware that, in addition to voting members representing the public, the SROs, and industry organizations, SICA has several "invitee"[17] member organizations such as the SEC, the North American Securities Administrators Association, the National Futures Association, the Commodity Futures Trading Commission, and the American Arbitration Association.

NASD's dispute resolution program is subjected to extensive regulatory oversight. The SEC must approve all arbitration and mediation rules. NASD must file with the Commission proposed changes to the rules, as well as significant changes to our processes. After publication in the *Federal Register*, there follows an extensive period for comments by the public, and NASD must address the issues raised by the commenters. We often amend rule filings in response to comments from the public. SEC's Office of Compliance Inspections and Examinations conducts periodic inspections of our dispute resolution program. The GAO also conducts reviews of our program from time to time. A new combined NASD-NYSE arbitration entity would presumably operate under the same or a heightened level of scrutiny, because regulators would be able to focus their resources on one rather than two arbitration programs.

Finally, it is worth noting that the GAO in a 1992 report[18] observed that there was no statistically significant difference in award outcomes in SRO and non-SRO arbitration forums:

> Our statistical analysis of case results and comparison of results between arbitration forums showed no evidence of pro-industry bias at industry-sponsored forums. Investors received awards in more than half the disputes they initiated, and the awards received in industry-sponsored forums were not statistically different from awards at AAA or NFA.[19]

The GAO repeated this observation in its 2000 report.[20]

In sum, NASD already is an independent forum; there is no need to create another forum.

Allowing Investors to Choose Another Forum

Your letter states: "Another alternative to compulsory SRO arbitration would be to again provide the public investor with the right to choose to bring grievances to court or to arbitration. While not

[15] Provost and Vice Chancellor of Academic Affairs, National University; formerly Dean of Fordham University Graduate School of Business Administration.
[16] President of New York University, formerly Dean and Professor of Law, New York University School of Law.
[17] As you know, SICA invitees attend meetings and actively participate in discussions, although they do not have voting rights.
[18] Securities Arbitration: How Investors Fare (GAO/GGD-92-74, May 11, 1992)
[19] Id. at 60
[20] 2000 GAO Report at 4-5.

all cases would be susceptible to resolution in court (for example, claims under $25,000), it would permit the public investor the choice as was their right prior to 1987." This proposal seeks to overturn federal case law dating back 20 years, as articulated by the United States Supreme Court.

In the 1987 case of *Shearson/American Express, Inc. v. McMahon*[21] the Court held that the use of predispute arbitration clauses in customer-broker agreements did not violate the Securities Exchange Act of 1934. Two years later, the Court ruled in *Rodriguez de Quijas v. Shearson/American Express*[22] that the use of predispute arbitration clauses in customer-broker agreements did not violate the Securities Act of 1933. Two years thereafter, in *Gilmer v. Interstate Johnson/Lane Corp*[23] the Supreme Court again supported SRO arbitration programs. Although this last case involved an employment dispute between a broker and his former employer, the Court's views of arbitration in an SRO forum (in this case the NYSE) are nonetheless instructive:

> In arguing that arbitration is inconsistent with the ADEA, Gilmer also raises a host of challenges to the adequacy of arbitration procedures. Initially, we note that, in our recent arbitration cases, we have already rejected most of these arguments as insufficient to preclude arbitration of statutory claims. Such generalized attacks on arbitration "res[t] on suspicion of arbitration as a method of weakening the protections afforded in the substantive law to would-be complainants," and, as such, they are "far out of step with our current strong endorsement of the federal statutes favoring this method of resolving disputes." [citing *Rodriguez*].

When investors (and other parties) were offered a choice of another arbitration forum under the 2000 SICA Pilot, there was little interest. In 2002, SICA concluded a two-year pilot program, in which seven major brokerage firms agreed to allow investors the choice of having their arbitration dispute administered by a non-SRO arbitration forum (either JAMS or the American Arbitration Association, depending on the participating brokerage firm). The SICA *Twelfth Report* sums up the pilot's results this way: "From its inception few investors (or their attorneys) elected to proceed at a non-SRO forum." Based upon responses to a survey of investors, SICA reported that investors' main reasons for not using the alternative forums were the higher fees at non-SRO forums, and a general degree of comfort with existing and more familiar SRO procedures. [24]

Improvements to the NASD Code of Arbitration Procedure

NASD continues to make significant improvements to the dispute resolution forum to make the process more transparent, fair, and efficient for investors and others who use the forum. On January 24, 2007, the SEC approved a complete reorganization of the NASD Code of Arbitration Procedure[25] that included simplification of the Code language. To eliminate confusion regarding which rules apply to which disputes, NASD separated the Code into three parts: the Customer Code, the Industry Code, and the Mediation Code. The rules now follow the sequential order of a typical case making them more logical and user-friendly.

---

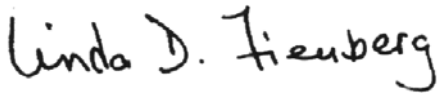
[21] 482 U.S. 220 (1987).
[22] 490 U.S. 477 (1989).
[23] 500 U.S. 20 (1991).
[24] SICA Twelfth Report at 5-6 (2003).
[25] See Exchange Act Release No. 34-55158.

The new rules incorporate improvements to the discovery process, including codifying the power of arbitrators to sanction parties for non-compliance with the rules, which should significantly reduce the number of discovery disputes in NASD arbitrations. We also established uniform procedures for filing, responding to, and ruling on motions in NASD arbitrations. The new code refines the arbitrator selection process by creating a new roster of public arbitrators who are qualified to serve as chairpersons in cases involving investors. Arbitrators must have a specific amount of training and experience to qualify to serve as a chairperson. These and other revisions codify best practices and provide more guidance to parties and arbitrators in the NASD DR forum.

Conclusion

The consolidation of the NASD and NYSE dispute resolution forums will continue to serve the interests of the investing public. The combined entity would continue to be subject to full SEC oversight and inspections, and its rules subject to approval by the Commission as at present. The economies of scale and increased efficiencies will make it more efficient to recruit, train, and maintain a unified roster of neutrals; there will be better coordination on disciplinary referrals arising out of arbitrations, and on suspending or terminating firms for non-payment of awards; and the single set of rules will reduce confusion for investors.

Very truly yours



Linda D. Fienberg

cc: The Honorable Christopher Cox
The Honorable Paul S. Atkins
The Honorable Roel C. Campos
The Honorable Kathleen L. Casey
The Honorable Annette L. Nazareth

The Honorable Max Baucus
The Honorable Christopher J. Dodd
The Honorable Daniel K. Inouye
The Honorable Chuck Grassley
The Honorable Richard C. Shelby
The Honorable Ted Stevens

The Honorable Rick C. Boucher
The Honorable John Conyers, Jr.
The Honorable John David Dingell, Jr.
The Honorable Barney Frank
The Honorable Edward John Markey
The Honorable Spencer Bachus
The Honorable Lamar S. Smith
The Honorable Joe Barton

The Honorable Fred Upton

The Honorable Joseph P. Borg
The Honorable Bryan Lantagne
The Honorable Melanie Senter Lubin
The Honorable Tanya Solov
The Honorable Patricia D. Struck
The Honorable Karen Tyler

Catherine McGuire, Esq., Chief Counsel, SEC Div. of Market Reg.
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George H. Friedman, Director of Arbitration, NASD DR
Richard G. Ketchum, CEO, NYSE Regulation
Dan Beyda, Chief Administrative Officer, NYSE Regulation
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April 8, 2007

VIA EMAIL: rule-comments@sec.gov

Ms. Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090.

Re: Consolidation of the Member Firm Regulatory Functions
SR-NASD-2007-023

Dear Ms. Morris:

This letter comments upon the prior comments submitted by the "Public Members" of the Securities Industry Conference on Arbitration ("SICA") dated January 12, 2007 and the NASD Dispute Resolution ("NASD") dated January 26. 2007. They discuss the issue of whether mandatory securities arbitration offered by the consolidated regulatory forum would be "fair" to customers of the securities industry.

I. My Background

From 1971 to 1973, I served as the Associate General Counsel and/or Compliance Director of Mitchum, Jones & Templeton, Inc., a regional New York Stock Exchange ("NYSE") Member Firm.

From 1973, I have been engaged in the private practice of law as a sole practitioner where substantially all representation dealt with financial/investment litigation. I have represented many individual investors and more than twenty (20) regional securities brokerage firms before arbitration panels and in various state and federal courts in hundreds of securities industry related disputes. I no longer represent securities brokerage firms.

I was admitted to the NASD panel of arbitrators in 1976. I have served on the panels of arbitrators of the American Arbitration Association, Pacific Stock Exchange,

NYSE and Municipal Securities Rule Making Board. Further, I serve the Los Angeles civil courts and the Los Angeles County Bar Association as an arbitrator.

In May 2005, I filed Petition for Rulemaking (SEC File No. 4-502)[1] with the Securities and Exchange Commission ("SEC"), which requests the creation of arbitration rules designed to:

(1) Specifically permit arbitration panel members, should they elect to do so, to conduct legal research, or, in the alternative, forbid Self-Regulatory Organizations ("SROs"), e.g., NASD, sponsored arbitration forums from restricting arbitrators from conducting legal research;

(2) 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;

(3) Require SROs to conduct continuing evaluations of ability of every arbitrator on their panels to perform his/her duties, including, but not limited to mandatory peer evaluations;

(4) Require SROs to train arbitrators in applicable law;

(5) Require SROs to reveal in pre-dispute arbitration agreements whether their arbitrators are required to follow the law in their decision-making process, the training of their arbitrators in the law, their process, if any, to evaluate their arbitrators on a continuing basis; and,

(6) Require the SEC's Division of Market Regulation to specifically oversee SROs to determine whether they are in compliance with rules adopted pursuant to items (1) through (5), inclusive.

Essentially, the Petition seeks to correct many aspects of the arbitration process, which make the process unfair to the investing public.

II. SICA and NASD Comments

The "Public Members" of SICA contend that the proposed consolidation of the arbitration departments of the NASD and NYSE will negatively affect the fairness of the mandatory securities arbitration process. They state, "Indeed, the public has been warned by a well-respected journalist that: 'If you're an investor who has filed an arbitration case against your stockbroker, you would be wise to steel yourself for an irrational and unjust outcome.'"

[1] A copy of the Petition is available at: http://www.sec.gov/rules/petitions/petn4-502.pdf. A copy of Supplemental Information is available at: http://www.sec.gov/rules/petitions/4-502/lgreenberg062205.pdf.

In its letter dated January 26, 2007, the NASD responds by challenging "any notion that the NASD's arbitration program is unfair" by citing various studies, reports and surveys and claiming the existence of effective oversight by the SEC.

There are material aspects of those studies, reports, surveys and oversight that need further discussion.

III. The Tidwell Report

The NASD states that, in 1999, it "engaged the United States Military Academy at West Point to conduct an independent analysis of surveys submitted by our forum's constituents." The NASD cites, "G. Tidwell, K. Foster, and M. Hummel, Party Evaluation of Arbitrators: An Analysis of Data Collected from NASD Regulation Arbitrations, at 3 (Aug. 5, 1999)" ("Tidwell Report").

The results of the Tidwell Report and the alleged "independent analysis" are suspect for several reasons:

(1) The Tidwell Report was prepared by a person employed by the NASD, who was, in reality, performing a self-critical analysis;

(2) The sample was not representative, as 90% of the possible evaluators declined to respond;

(3) Those who did respond were biased, as they knew the results of the respective arbitration hearing in which they participated;

(4) The Tidwell Report erroneously assumed that only two parties were involved in each hearing, which enhanced the evaluator response rate; and,

(5) There was no survey of parties who settled before hearing, whichis the situation in the vast majority of cases.

The degree of bias/independence of the Tidwell Report and the so-called "independent analysis of surveys" was raised by the fact that Gary Tidwell taught at the United States Military Academy and/or he was employed or prospectively employed by the NASD. A NASD Press Release dated January 19, 2000 states, "The National Association of Securities Dealers, Inc. (NASD®) announced that it has launched the NASD Institute for Professional Development (NIPD). Gary L. Tidwell, who was recently elected Vice President, NASD Regulation, Inc., has been named Executive Director of the Institute. … Tidwell was named Vice President of NASD Regulation in December 1999. He joined the self-regulatory organization in 1998 as Director of Neutral Management in the Office of Dispute Resolution. Tidwell maintains a tenured

professorship at the College of Charleston and also teaches at the United States Military Academy at West Point."

The NASD claims that "93.49% of those responding" indicated of how their cases were handled. However, only 10% of those surveyed responded. Thus, only 7% of those surveyed felt the process was "fair." Another report, upon which the NASD relies, considers the number statistically insignificant. (See, Section IV, below.)

IV. The Perino Report

The NASD cites," M. Perino, Report to the SEC Regarding Arbitrator Conflict Disclosure Requirements in NASD and NYSE Securities Arbitrations, at 51 (Nov. 4, 2002)" (Perino Report"). The NASD states that the Perino Report "touched on user perceptions of fairness, finding that '[a]vailable empirical evidence suggests that SRO arbitrations are fair and that investors perceive them to be fair.'"

The Perino Report states, "Given the unquestioned significance of securities arbitrations, it is crucial that the SROs resolve any lingering concerns about pro-industry bias. To date, available empirical evidence, particularly with respect to investor perceptions of the arbitration process, is fairly limited.... As a result, this Report recommends that the SROs sponsor additional independent studies to further evaluate the impartiality of the SRO arbitration process. ... In 2000, the GAO could not reach a conclusion on the fairness of the process...." (Emphasis added.)

A few years after issuing the Perino Report, Perino revealed his securities industry clients by stating, "EXPERT ENGAGEMENTS AND CONSULTANCIES: U.S. Securities and Exchange Commission; New York Stock Exchange; Morgan Stanley Dean Witter; UBS PaineWebber, Inc.; U.S. Bancorp Piper Jaffray; National Union Fire Insurance Company … New York Life Insurance Co. … BankAmerica Corporation." (Is Securities Arbitration Fair for Investors? Written Testimony of Professor Michael A. Perino St. John's University School of Law Before the Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises of the Committee on Financial Services United States House of Representatives March 17, 2005)

Perino criticizes the Tidwell Report by stating, "Two limitations of the study suggest that its findings must be interpreted with caution. First, few arbitration participants completed the surveys; the authors concluded that the evaluations response rate was only between 10%-20%. Second, these responses may reflect selection bias problems. ... [I]t is still possible that individuals that were more satisfied with the fairness of the process or that achieved favorable outcomes were more likely to complete the surveys." Id.

V. Securities Arbitration Fairness "Survey"

The NASD adopted the Perino Report's suggestion of another "survey" by stating, "This survey is about to be conducted under SICA's auspices by the Pace Investor Rights Project (affiliated with the Pace University School of Law)."

In response to a Freedom of Information Act ("FOIA") request directed to the SEC, I obtained copies of SICA Meeting Minutes, which described SICA's efforts with respect to its anticipated "independent research." It appears obvious that the securities industry exercised a heavy hand in designing the "survey," selecting the persons who are to "administer the survey" and who are not engaged full time in the "survey" business, and financing the "survey." The "survey" lacks credence even before the public is informed of its purported results. Excerpts of SICA Meeting Minutes dated January 16, 2004 to March 21, 2006 are as follows:

> Independent Research on Fairness of SRO Arbitrations ...
>
> George Friedman (NASD) stated that it would not be appropriate for SROs to drive the process of collecting information on the fairness of SRO arbitrations.
>
> ...
>
> Mr. Friedman updated the Conference on the work of the subcommittee, consisting of Mr. Friedman (NASD), Chairman Katsoris, Ms. Kupersmith (NYSE), and Kenneth Andrichik (NASD). They are currently working on picking a vendor to administer the survey on the perceptions of fairness between SRO arbitration and litigation.
>
> ...
>
> [T]he Subcommittee has chosen Professors Barbara Black and Jill Gross of Pace University School of Law to administer the survey. The Subcommittee will meet again shortly to design the questionnaire. ... Professors Black and Gross have sent him a first draft of the survey. He will distribute the draft to the Conference members to return to him with their comments.
>
> ...
>
> Pat Sadler distributed various proposed changes (from NASD, SIA, PIABA, Chairman Katsoris) to the draft survey prepared by the outside vendor (Professors Black and Gross of the Pace Law School Investor Rights Clinic). There was a prolonged discussion, with several suggested amendments. ... ● Linda Fienberg (NASD) observed that some of PIABA's suggested questions (e.g., eliminating mandatory arbitration and getting rid of the industry arbitrator) were somewhat inflammatory, and beyond the scope of the original suggestions in the "Perino Report"

> that gave rise to the survey project. She reserved the right to reconsider NASD's participation if the final survey contained such questions.
>
> ...
>
> Professors Black and Gross will incorporate SICA's suggestions and present a new draft of the survey to the Conference before its March meeting. The survey will be presented as a SICA survey, administered by Pace Law School.
>
> ...
>
> Linda Fienberg (NASD) called participants' attention to an open contractual issue, i.e., a lack of clarity as to who owns the data. Pace desires to publish an article based on the results of the survey. While this is not necessarily problematic, several Committee members expressed concerns about maintaining confidentiality of the data. Linda Fienberg agreed provide copies of the contract to interested SICA members.

The SROs drove the process of collecting information on the fairness of SRO arbitrations in spit of SICA's clear acknowledgement that "it would not be appropriate for SROs to drive the process of collecting information on the fairness of SRO arbitrations."

While anticipating the results of the Securities Arbitration Fairness Survey, one might observe SICA's prior experience with "surveys." From January 2000 until January 2002, pursuant to SICA's recommendation and guidance, the NASD and NYSE arbitration forums provided claimants with alternative forums before which their claims could be heard. Of 277 eligible cases, eight claimants elected to participate (to some degree). In response to my FOIA request, the SEC produced a copy of various documents relating to that pilot program.

SICA informed the SEC, "At the time of implementation of the program, we were aware of the possibility that the program might not see a lot of cases. ... Thus far, only four responses have been received, all from attorneys."[2] SICA debated how the results of the "survey" would be portrayed to the public. A SEC representative described the internal debate by stating, "After tedious debate on how to characterize the replies (with the SROs wanting them to be a proxy for widespread joy with the process, and public member Ted Eppenstein asserting that he was privy to secret information indicating great woe with the process), I suggested that someone draft a short, flat report that doesn't say too much...."[3]

One should wonder whether there will be a "tedious debate on how to characterize the replies" to the Securities Arbitration Fairness Survey and whether the SEC will advise

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[2] Email dated December 8, 2000 from Thomas Stipanowich, Chairman of SICA, to Robert Love, SEC.
[3] Email dated January 24, 2001 from Robert Love, SEC, to Catherine McGuire, SEC.

another "short, flat report that doesn't say too much." If the past is prologue, one would expect the NASD and NYSE to push for a proclamation of "widespread joy with the process," and they have been driving and financing the "survey."

VI. SEC Oversight

The NASD states, "[W]e are subject to extensive regulatory oversight.... NASD's dispute resolution program is subjected to extensive regulatory oversight. The SEC must approve all arbitration and mediation rules. ... SEC's Office of Compliance Inspections and Examinations conducts periodic inspections of our dispute resolution program. The GAO also conducts reviews of our program from time to time."

The NASD claims that SICA presented "conclusory statements that have no evidentiary basis." However, the NASD presented no evidence as to what the SEC does or does not do with respect to the "periodic inspections" or what the GAO does or does not do with respect to its "reviews."

The Petition, at page 21, deals with lack of SEC oversight. One wonders how so many problems exist in the securities arbitration process, as described fully in the Petition, if there is adequate SEC oversight. In March 2005, via a FOIA request, I sought records from the SEC concerning its alleged "inspections" of the NASD's arbitration program by requesting:

> Please send to me a copy of all writings, e.g., reports of findings of inspections, letters, emails, audits, reports, notes of oral communications and/or interviews, notices, that evidence that the Securities and Exchange Commission, including its staff, (collectively "SEC") from January 1, 1996 to the date hereof has exercised oversight over NASD Dispute Regulation (and/or any predecessor organization)(collectively "NASD") arbitration with respect to:
>
> (a) The degree of fairness to the respective parties of arbitrator awards rendered in NASD arbitration proceedings;
>
> (b) The adequacy of training, other than with respect to procedural matters, provided by the NASD to its arbitrators;
>
> (c) The adequacy of the process by which the NASD evaluates the competence of NASD arbitrators after the respective arbitrators have first been assigned to their first case; and,
>
> (d) The NASD's implementation of recommendations contained in the Report of the Arbitration Policy Task Force To The Board of Governors National Association of Securities Dealers, Inc. (January

> 1996) with respect to arbitrator training in the substantive law and methods for arbitrator evaluations.

The SEC refused to provide any such information. The NASD will only provide conclusory statements. Thus, in essence, one is asked to trust, but denied all ability to verify.

We have previously seen how the SEC exercises some "oversight" by advising SICA, which primarily consists of securities industry members, to "draft a short, flat report that doesn't say too much...." The NASD states, "Customers already have the right to take their claims against defunct firms directly to court." On that subject, in its email dated January 24, 2001, the SEC representative stated:

> NASD gave only the briefest of presentations of its rule that would allow investors access to court in cases against a defunct broker-dealer. I expanded in order to advised (sic) the exchanges of the need to protect themselves. After the meeting, I asked Nancy Nielson, the secretary, to please make certain she looked at and understood the rule and possible implications for the exchanges so that the minutes reflect this, and help them protect themselves with similar filings if they feel exposed.

It is obvious that the SEC interprets "oversight" to mean protection of the securities industry from the investing public.

VII. The Securities Arbitration Process Will Remain Unfair As It Lacks Decision Making Standards, Arbitrator Training In the Law and Mandatory Arbitrator Evaluation

One of the main topics of the Petition, at pages 5 through 20, is that the arbitration before securities industry sponsored forums cannot be "fair" when the NASD discourages use of the applicable law in the decision making process, has no effective arbitrator evaluation procedure and has discontinued training arbitrators in the applicable law.

In 2006, I conducted a multi-month internet based study of NASD arbitration, which involved communications with more than 1,000 NASD arbitrators. The study showed that the NASD impliedly informs arbitrators to, in effect, "do justice," but does not provide the tools to accomplish that goal. One very active and candid NASD arbitrator informed me, in part:

/ / / / /

> Although we receive from both parties, reams of papers with case law, not once in any case during a hearing or during any deliberations has any one referred to them. … We do not need case law. Simply, does one plus one equal two. That's what we try to determine.

An arbitrator's knowledge of the law applicable to disputes is especially important. In order to determine the facts that are relevant and their significance, an arbitrator must understand the applicable law. He/she has no standard upon which to base a decision. Thus, justice is not served. Current ambiguous NASD guidelines to arbitrators to "do justice" or render "fair and equitable" decisions are, effectively, no guidelines and an excuse to foster and enable incompetence.

A. 1987 SEC Correspondence

"In his 1987 letter, Mr. Ketchum was blunt. The self-regulatory organizations, he said, 'have administered virtually no formal training for arbitrators on matters relating to either arbitration law, relevant state law or securities law. The current level of training should be addressed promptly.'" ("When Naiveté Meets Wall Street," New York Times, 12/3/89.)

On September 10, 1987, Mr. Richard G. Ketchum, Director, Division of Market Regulation, SEC wrote to all members of SICA, including the NASD, stating:

> The Commission staff has been examining self-regulatory organization-sponsored arbitration over the past 18 months. The focus of the review was broad and was designed to test both the fairness and efficiency of self-regulatory organization ("SRO") arbitration programs. This review reflects the Commission's belief in the need for thorough oversight of SRO arbitration systems.... The staff has presented its findings to the Commission, which has endorsed recommendations set out in this letter.

With respect to "Arbitrator Training," the letter states:

> Our review found that the SROs have administered virtually no formal training for arbitrators on matters relating to either arbitration law, including the scope of arbitrators' authority, relevant state law, or securities law. The current level of training should be addressed promptly. (Emphasis added.)

B. GAO Report (1992) Recommended Arbitrator Training

Congress requested that the GAO study the arbitrator education process. ["In response to the concerns of industry members and individual investors, the Chairmen of the House Committee on Energy and Commerce and its Subcommittee on Telecommunications and Finance, and the Chairman and four members of the Senate Committee on Banking, Housing, and Urban Affairs requested that we examine arbitration practices in the securities industry. As agreed with the Committees and Subcommittee, we examined issues related to … the selection and training of arbitrators." Securities Arbitration --- How Investors Fare, United States General Accounting Office, Report to Congressional Requestors, May 1992, GAO/GGD-92-74 ("GAO Report"), p. 21.]

The GAO Report partially responded to the Congressional request, which dealt with "training." ["Recommendations to SEC. GAO recommends that the Chairman, SEC, require SROS that administer arbitration forums to … establish a system to ensure these arbitrators are adequately trained…." GAO Report, p. 61.]

By 1992, the GAO, SEC and NASD were able to examine years of arbitration experience with respect to thousands of arbitration hearings. Yet, they suggested an additional study as to providing "better" arbitrator training. ["Finally, with respect to our recommendation concerning arbitrator training, SEC stated that 'it would be appropriate to study whether there are cost-effective means to assess arbitrators' training needs and provide better training.' This action is consistent with the intent of our recommendation, and the SROS told us they plan to begin such a study." GAO Report, p. 63.]

The SEC commented to the GAO that the NASD needed to expand arbitrator training and evaluation efforts. ["Nevertheless, while the SROs should expand their training efforts, the Staff does not believe that a prescription of specified courses should, or could, become an acceptable substitute for careful, varied evaluation by the arbitration departments to assure the independence and capability of arbitrators." GAO Report, p. 102.] Subsequently, the NASD eliminated its training program related to applicable law and informally advised panelists to ignore applicable securities under threat of being recused from serving as an arbitrator on the ground of bias. (Details are set forth in the Petition.)

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/ / / / /

C. Ruder Task Force Report (1996) Recommended that the NASD Implement a Program to Train Arbitrators in Substantive Law

The "Securities Arbitration Reform --- Report of the Arbitration Policy Task Force to the Board of Governors National Association of Securities Dealers, Inc." (January 1996) ("Ruder Task Force Report") recommended that the NASD improve arbitrator training as to applicable law and implement an effective evaluation procedure concerning arbitrator competence. The Ruder Task Force Report stated, in part:

> Many securities arbitration participants expressed concerns about the selection, quality, and training of arbitrators. .... Commentators also complained about the quality and training of the arbitrators. They felt that the arbitrators lacked sufficient expertise in the relevant substantive law…
>
> ….
>
> The two characteristics for which arbitrators received the lowest ratings in both the 1993 and 1994 surveys were "ability to cope with complex material" and "ability to analyze problems and identify key issues."
>
> ….
>
> We recommend that the scope and frequency of arbitrator training be expanded even further. In particular, we believe that there should be a continuing education requirement beyond the introductory session presently required of new arbitrators. Appropriate programs should be available for all levels of experience, emphasizing … relevant areas of substantive law.
>
> ….
>
> The training requirements should be applied flexibly based upon an arbitrator's demonstrated knowledge of relevant substantive law.... The requirements should be structured, however, to ensure that arbitrators remain current with important new developments in … and relevant law. (Emphasis added.)

Ms. Linda D. Fienberg, Esquire, served as the "Task Force Reporter" of Ruder Task Force Report. She is President of NASD Dispute Resolution. The NASD has not implemented the previously mentioned recommendations.

Since, 1993, the NASD has ceased offering training in applicable law. However, in 2004, the NASD sought authority from the SEC to charge arbitrators additional training fees to provide a "two-hour … session… on … videotaped training on civility." (SR-NASD-2004-001)

VIII. Conclusion

Comments by the "Public Members" of SICA reveal the public's perception that the mandatory securities arbitration process in unfair. The response by the NASD does nothing to dispel that perception. The NASD's flawed use of reports, studies and surveys is disingenuous, at best. Reform of the securities arbitration process is badly needed. Until that reform occurs, the arbitration process will remain unfair.

Please communicate with me in the event that further information is desired.

Very truly yours,

LES GREENBERG

LG:pg

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April 11, 2007

VIA EMAIL: rule-comments@sec.gov

Ms. Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090.

Re: Consolidation of the Member Firm Regulatory Functions
SR-NASD-2007-023
Supplement to Comment dated April 8, 2007

Dear Ms. Morris:

This letter is written to supplement the information contained in my letter dated April 8, 2007. On this date, the Securities and Exchange Commission provided me with additional records in response to my Freedom of Information Act request dated August 5, 2006. Those records, primarily consisting of copies of minutes of meetings of the Securities Industry Conference on Arbitration ("SICA") further substantiate my prior comments upon the purported reports, studies and/or surveys discussed by the NASD Dispute Resolution ("NASD") in its response to comments of the "Public Members" of SICA.

III. The Tidwell Report

On January 13, 2003, Professor Michael Perino spoke before SICA. The minutes reflected his comments as follows:

> Mr. Perino indicated that the ... other study is the Tidwell study that surveyed forum users' perceptions of the arbitration process.
>
> The problem with that study is that someone under the auspices of NASD developed it. An independent approach is needed. ...
>
> ...

> Mr. Eppenstein asked whether the SEC requested the (Perino) report before or after the filing of its amicus brief. Mr. Perino said that his report was to be issued by mid-November, after the amicus brief was filed.

V. Securities Arbitration Fairness "Survey"

The minutes of SICA meetings reflect steady degradation of alleged "independent research." After considering use of the Consumer Federation of America or RAND, SICA opted to draft its own "survey," where the NASD and NYSE are cover all costs. SICA meeting minutes from January 13, 2003 to October 22, 2003, reveal the following:

> Professor Katsoris initiated a further discussion of the possibility of sponsoring independent research on SRO arbitrations. ...Various options were discussed, including the Consumer Federation of America, the ABA Litigation Section (planning a survey), RAND, and the group working with Kaiser on current perceptions of their ADR system. Pros and cons of different groups, the problem of funding, and the possible structuring of a survey, were discussed.
>
> Mr. Friedman (NASD) and Mr. Clemente (NYSE) agreed to look at options. Perhaps SICA could commission the survey, and SROs could fund it. Messrs. Clemente and Friedman agreed to provide a status report at the April SICA meeting.
>
> ....
>
> Mr. Friedman reported that NASD has one proposal from an outside vendor that has done previous work for NASD. The cost was over $100,000. NASD has also asked Lew Maltby (President of the Workplace Rights Project), who appeared at our January 2003 meeting, to submit a bid for conducting the survey. Mr. Maltby is in the process of preparing his bid, which is due April 30th. After a brief discussion, the Conference coalesced around some key issues: 1) the survey should be conducted under SICA's auspices; 2) the survey should be paid for by NASD and NYSE; 3) to ensure that the results are perceived to be truly independent, editorial control over the final questions should repose in SICA. ...
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> ....
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> Mr. Friedman and Mr. Clemente reported that NASD and NYSE are evaluating their options. They will provide an update at the October SICA meeting.
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> ....
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> George Friedman stated that the NASD is looking at proposals to do research on fairness of SRO arbitrations, and was told the California Dispute Resolution Institute had a meeting in Sacramento with various

> ADR providers to discuss a California survey. Bob Clemente said they are looking to a study in California of all forms of arbitration, hoping to put to rest some of the clichés that have existed about arbitration being valuable for one party only.

It is illuminating that, before the "survey" has been conducted, the NYSE is already "hoping to put to rest some of the clichés that have existed about arbitration being valuable for one party only" vis-à-vis learning the results of the "survey" and making any corrections necessary to improve "fairness" of the arbitration process. Further, SICA, when stating, "to ensure that the results are perceived to be truly independent, editorial control over the final questions should repose in SICA," confused "editorial control" with professional analysis of the responses to the final questions.

At the SICA meeting on January 16, 2004, "George Friedman (NASD) stated that it would not be appropriate for SROs to drive the process of collecting information on the fairness of SRO arbitrations."

VIII. Conclusion

Comments by the "Public Members" of SICA reveal the public's perception that the mandatory securities arbitration process in unfair. The response by the NASD does nothing to dispel that perception. The NASD's flawed use of reports, studies and surveys is disingenuous, at best.

Please communicate with me in the event that further information is desired.

Very truly yours,

LES GREENBERG

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