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The PIABA Quarterly

The Newsletter of the Public Investors Arbitration Bar Association

September 1996 Volume 3 Number 3

In This Issue...

Letter from the President 1

From The Professor 2

The Securities Industry Conference on Arbitration (SICA) Passes New Proposal On Eligibility for Arbitration 6

The First Circuit Opines That Section 15 Question is to be Determined by the Arbitrators 7

Non-Signatory Broker Can Compel Arbitration Even When Signatory-Employer Does Not Join in the Motion 8

New York Court Blocks Introducing Broker From using Clearing Broker's Arbitration Agreement 8

District Court Confirms Award Against Stratton Oakmont 8

Florida Court Redetermines Attorney's Fees From Arbitration Award 9

Eleventh Circuit Refuses to Allow Res Judicata on Section 15 Determination to Bar Judicial Consideration of Securities Claim 9

NASD Extends the Effectiveness of the Arbitration Procedures for Large and Complex Cases 10

The PIABA COPY Quarterly

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September 30, 1996

Volume 3 Number 3

Editor's Notes

Many of our members have now ventured into cyberspace. You can send notices and other regular correspondence to the *Quarterly* via E-Mail. The address is stanlaw@premier.net.

The deadline for receiving submissions for the December issue of the *Quarterly* is December 5, 1996. All submissions, regardless of length, should be accompanied by a computer disk of the submitted material.

The PIABA Quarterly is a publication of The Public Investors Arbitration Bar Association (PIABA) and is intended for the use of its members. Statements and opinions expressed are not necessarily those of PIABA or its Board of Directors. Information is from sources deemed reliable, but should be used subject to verification.

Letter From the President

L. Jerome Stanley, L. JEROME STANLEY, P.C., Baton Rouge, LA

Dear Fellow Members:

It's hard to believe that this is my fourth installment in the *Quarterly* as President — meaning that my year as President is rapidly coming to a close.

Much of our efforts this quarter have revolved around the preparation for the Annual Meeting at Turnberry Isle. The Board of Directors met by teleconference on July 22nd to finalize the agenda for the Meeting. We have 154 people registered. This is a significant portion of our membership and attests to the quality of the program.

Otherwise, it appears that the debate surrounding NASD Code Section 15 will continue into the millennium. In July, the Securities Industry Conference on Arbitration (SICA) passed a proposed rule change which would allow the Director of Arbitration at an SRO to make a "bright-line", six year, trade-date determination of eligibility for arbitration on an administrative basis when the claim is filed. The final text of the proposal is produced in this issue of the *Quarterly*.

In This Issue...

	Page
Eleventy Circuit Refuses to Allow Res Judicata on Section 15 Determination to Bar Judicial Consideration of Securities Claim	9
From the Professor	2
District Court Confirms Award Against Stratton Oakmont	8
Florida Court Redetermines Attorney's Fees From Arbitration Award	9
NASD Extends the Effectiveness of the Arbitration Procedures for Large and Complex Cases	10
New York Court Blocks Introducing Broker From Using Clearing Broker's Arbitration Agreement	8
Non-Signatory Broker Can Compel Arbitration Even When Signatory-Employer Time Does Not Join in the Motion	8
The First Circuit Opines That Section 15 Question Is To Be Determined by the Arbitrators	7
The Securities Industry Conference (SICA) Passes New Proposal on Eligibility for Arbitration	6

In August, the NASDR announced that the NA. Director of Arbitration was going to cease any initial determinations as to eligibility under Section 15, instead leaving it to the parties to raise the issue with the arbitrators in appropriate cases.

The other major front which continues to effect our members and their clients is the industry's continued transgressions of NASD rule 21(f) and NASD Notice to Members 95-16 with regard to the use of New York choice of law clauses and other restrictive language in arbitration agreements to attempt to limit the ability of the arbitrators to award attorney's fees and punitive damages. We are putting together a letter to the SEC calling its attention to these continuing violations of 95-16.

See you in Florida.

Best Wishes,

Jerry

From The Professor

Contributed by: Joseph C. Long, Norman OK

In this issue, I would like to discuss the effectiveness of a choice-of-law clauses. Traditionally, the courts have not allowed choice of law clauses to strip plaintiffs of their rights under the federal or local securities acts. See generally, 12 Joseph C. Long, Blue Sky Law §3.04[2][b][i][D](1996) [hereinafter "Long, §____]. There are disturbing indications that this rule is being seriously eroded or abandoned altogether. As many modern brokerage contracts contain such choice-of-laws clauses, Plaintiff's arbitration counsel needs to be alert and anticipate that brokerage defendants will attempt to claim that plaintiff's rights under the local securities act are barred by these clauses. Counsel needs to be prepared to advise either the courts or the arbitrators of the traditional disregard of such clauses and to brief the reasoning for such disregard and the supporting authorities. While the legal environment is clearly swinging away from protecting the investor rights, by recognizing the issue and fully briefing it to the court or arbitrators, counsel will force any further diminution of investor protection in this area to be a conscious, and hopefully reasoned, policy decision.

For many years, the law has been that if an offer or sale of a security was made illegally **in or into** a state, the purchaser had a cause of action under the law of that state to rescind the transaction. *See generally*, Uniform Securities Act §§414(a)(1), 414(c)(1), and 410 as well as Long, §§3.04[1] and [2]. Similarly, if an offer or sale was made from a state, the purchaser had a cause of action under the law of that state to rescind the purchase even though he or she was not located in the state at the time of the purchase. *See generally*, Uniform Securities Act §§414(a)(1), 414(c)(2), and 410 as well as Long, §3.04(3).

The purchaser's right to sue has never been treated as involving a conflict of laws issue. The purchaser may have a cause of action under the law

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of either state A or B or both.[1] The fact that he does not have a cause of action under the law of one state does not prevent the purchaser from asserting his cause of action under the law of another state.

The same position has been applied under federal law. The investor has traditionally been held to have a cause of action under the Securities Act of 1933, if the person to whom the securities were offered or sold was located in the United States at the time of either the offer or sale. Conversely, the purchaser traditionally has been found to have a cause of action if the securities were offered from this country.

For many years, brokers have included in the brokerage agreements both arbitration clauses and choice of law clauses. The choice of law clauses usually provide that the contract is to be construed "according to the laws of X". "X" most frequently is the state of New York. Both arbitration and choice of law clauses are also found, to a more limited extent, in other securities sales contracts outside the brokerage area.

Until recently, both the arbitration and choice of laws clauses were treated as void as violations of the anti-waiver provisions of the state and federal securities acts. *See generally*, Section 14 of Securities Act of 1933, 15 U.S.C. §77n; Section 29(a) of the Securities Exchange Act of 1934, 15 U.S.C. §78c(a); and Uniform Securities Act §410(g). As we all know, beginning in the mid-1980's, the Supreme Court reversed itself and gave validity to arbitration provisions in spite of the state and federal anti-waiver statutes. Defendants, having succeeded in their efforts to validate the arbitration clauses, are now increasingly seeking to legitimize choice-of-law provisions.

In at least two recent cases, *Allen v. Lloyd's of London*, 1996 WL 495553, 1996 U.S. App. LEXIS 23167 (4th Cir. Aug. 27, 1996), and *Paracor Fin., Inc. v. General Electric Capital Corp.*, CV90-03226-CAL (N.D.Cal. Apr. & Dec. 1993), *aff'd on other grounds*, 1996 U.S. App. LEXIS 24726 (9th Cir. Sept. 20, 1996), they appear to have succeeded. The *Allen* case involved claims under the federal securities laws. Certain American members or "names" of Lloyd's of London sued Lloyd's and their member agents for alleged misrepresentations and omissions made in connection with their recruitment as Lloyd's members.[2] Their membership contract provided that all disputes had to be settled by suit or arbitration in England and that the law of the United Kingdom would control. The trial court in an excellent 150-page opinion, 1996 WL (E.D.Va. Aug. ____, 1996), held the choice of law provision violated the anti-waiver provisions of both Section 14 of the Securities Act of 1933 and Section 29(a) of Securities Exchange Act of 1934 and, therefore, was void. The Fourth Circuit reversed, holding that the choice-of-law provision did not violate the anti-waiver provision and would be honored. It did so even though the United Kingdom does not have a securities registration requirement and English law allows Lloyd's to be sued only for actual fraud, not negligence either simple or gross.

The facts of the *Lloyd's* case admittedly are unique. But, if the principle developed there is applied universally, as it can expect that issuer counsel will argue, it will mean that both local and foreign issuers

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[1] It should be remembered that there may be multiple offers and sales in connection with a single transaction. As a result, it is conceivable that the law of three or more states could be applicable to a single transaction. An offer or offers may be made in or into one or more states, while the offer or offers were made from a third or fourth state. Finally, the actual sale takes place in or into a fifth state. In such case, the offer or sale might be legal in four out of the five states, and the plaintiff would still be able to set the transaction aside under the laws of the fifth state were the offer or sale was illegal.

[2] The "names" claimed that both their membership interests in Lloyd's and their participation in the various Lloyd's insurance syndicates were investment contracts.

will be able to avoid registration and regulation under the United States Securities Acts. They will merely insert a provision that the sale of the securities will be covered by the law of country X. Of course, the country selected will, most likely, be some country such as the Isle of Jersey, the Commonwealth of the North Marianna Islands, Iran, or Iraq, which has no securities laws.

In the *Paracor Fin., Inc.* case, the plaintiff brought a class-action suit against an Oregon resident in the federal district court for the Northern District of California. It claimed a cause of action under the Oregon Securities Act because the securities were sold **from** Oregon. However, the debenture agreement contained a choice-of-laws provision. The clause was similar to that found in most brokerage agreements and provided that the "debentures shall be construed in accordance with and governed by the laws of the State of New York, without giving effect to the principles of conflicts of laws thereunder."

The trial court concluded that this provision prevented the plaintiff from asserting a claim for violation of the Oregon Securities Act. As a result, it held that the plaintiffs were afforded only that protection available under New York law. The appellate court affirmed, but on other grounds.[3] Therefore, the trial court decision remains good law on the choice of laws issue.

This decision is especially important to plaintiff's arbitration counsel because most brokerage contracts contain a New York choice-of-law clause. Most state securities acts provide a right to rescind if the securities or any of the professionals, either the broker-dealer or its registered representatives, are not registered under the local act. Further, most state acts allow rescission based upon the making of material misrepresentations and omission. On the other hand, New York does not register most securities. Nor does the Martin Act, the New York blue sky statute, provide a civil cause of action for securities fraud. *See e.g. Vermeer Owners, Inc. v. Guterman*, 78 N.Y.2d 1114, 585 N.E.2d 377, 578 N.Y.S.2d 128 (1991). Further, most likely, both the broker-dealer and its registered representatives will be registered in New York since New York is frequently the home office and principal place of business of the brokerage house.[4] As a result, the investor, rather than having potentially three causes of action under his local law, winds up having no causes of action under New York securities laws.

There are three reasons why these choice-of-law clauses should not be honored. As noted above, traditionally, these clauses have been held to violate the anti-waiver provisions of Section 410(g) of the Uniform Securities Act. *See e.g. Getter v. R.G. Dickinson & Co.*, 366 F. Supp. 559 (S.D. Iowa 1973); *Boehnen v. Walston & Co.*, 358 F. Supp. 537 (D.S.D. 1973); *Hall v. Superior Court of Orange County*, 150 Cal. App.3d 411, 197 Cal. Rptr. 757 (1983).

Most state courts will honor choice-of-law clauses in private contracts. *Getter v. R.G. Dickinson & Co., supra*. However, the Restatement takes the position that such clauses do not need to be honored in two situations, if: (1) the chosen state does not have a substantial relationship to either the parties or the transaction; or (2) the application of the chosen state's law would be contrary to a fundamental policy of a state with a materially greater interest in

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[3] It held that the defendants as non-parties to the debenture agreement could not claim protection of the choice-of-laws clause, but concluded that the plaintiff did not state a cause of action under Oregon law against the appealing defendants.

[4] Quaere whether the choice-of-laws provision would be honored, if neither the plaintiff nor the broker's principal place of business was located in New York. Also quaere whether the transaction would be considered to have taken place in New York, so that if either the broker or its registered representative were not registered in New York, the investor would have a cause of action under New York law for such non-registration. Normally, the transaction would not be considered a New York transaction unless it originated from New York.

the particular issue. *Restatement (Second) of Conflict Laws* §187 (1971).

It is the second of these situations which doom the brokerage conflict-of-laws clause. Section 410(g) of the Uniform Securities Act provides:

> "Any condition, stipulation, or provision binding any person acquiring any security to waive compliance with any provision of this act or any rule or order hereunder is void." [Emphasis added.]

This language has been held to be a clear expression of public policy by the legislature not to allow the rights of a local citizens under the securities act to be taken away by a conflict-of-laws clause. Discussing the effect of the California equivalent of Section 410(g), the court in *Hall v. Superior Court of Orange County*, said:

> California's policy to protect securities investors, without more, would probably justify denial of enforcement of the choice of [law] provision, although a failure to do so might not constitute an abuse of discretion; but [Section 410(g)], which renders void any provision purporting to waive or evade the Corporate Securities Law, removes that discretion and compels denial of enforcement.

150 Cal. App.3d 411, 418, 197 Cal. Rptr. 757, 762 (1983). [Emphasis added.]

Second, when such choice-of-laws clause is combined with a brokerage arbitration clause, enforcement of the choice-of-laws clause to deprive the investor of his rights under local law would appear to run contrary to the holding of the United States Supreme Court in *Mastrobuono v. Shearson Lehman Hutton, Inc.*, ___U.S. ___, 115 S.Ct. 1212 (1996). In *Mastrobuono*, the Court considered a choice-of-laws clause which would have the effect of depriving the nvestor of receiving punitive damages in arbitration. The Court rejected such effect saying:

> Moreover respondents cannot overcome the common-law rule of contract interpretation that a court construe ambiguous language against the interest of the party that drafted it. [Citations omitted.] Respondents drafted an ambiguous document, and they can not claim the benefit the benefit of the doubt. The reason for this rule is to protect the party who did not choose the language from an unintended or unfair result. That rationale is well-suited to the facts of this case. As a practical matter, it seems un likely that petitioners were actually aware of New York's bifurcated approach to punitive damages, or that they had any idea that by signing a standard-form agreement to arbitrate disputes they might be giving up an important substantive right. In the face of such doubt, we are unwilling to impute this intent to petitioners. *Id.* at 1219 [Footnote omitted.]

This language is equally applicable to a choice-of-laws clause which would deprive the investor of his rights under local law. He does not realize that he is giving up his rights under local law and receiving no reciprocal rights under New York law. Since the clause does not clearly inform him of this effect, the clause should not be enforced.

Finally, the inclusion of such choice-of-laws clause in an arbitration clause by a broker violates Rule 21(f)(4) of the NASD Rules of Fair Practice, NASD Manual ¶2171 (1994). This section provides that it is a violation of the Rules of Fair Practice for a brokerage firm to include in an arbitration clause "any condition...which limits the ability of a party to file any claim in arbitration or which limits the ability of the arbitrators to make any such award." As in the case of punitive damages, such choice-of-laws clause deprives the investor of his right to receive a recovery under his local securities act. Such is not permissible and the NASD arbitrators have the authority to disregard such clause as a violation of the NASD Rules.

The Securities Industry C_nference on Arbitration (SICA) Passes New Proposal On Eligibility for Arbitration

On July 12, 1996, SICA unanimously passed a new proposal on the method by which eligibility for arbitration would be determined and the effect that a negative determination would have on the claimant's ability to take ineligible claims to court. This compromise from the investor's standpoint was born of necessity — brokerage firms were successful in precluding claimants from taking ineligible claims to court under the theory that, by signing an arbitration agreement, the claimant had elected arbitration as his exclusive remedy and had given up any rights to seek remedy in court.

What follows is the text of the SICA proposal.

(a, Eligibility; No Tolling for Fraudulent Concealment

The Director of Arbitration, upon the request of a party pursuant to subsection (c) below, shall find a dispute, claim or controversy to be ineligible for arbitration under this Code when, at the time of filing, six (6) years have elapsed from the occurrence or event giving rise to the dispute, claim or controversy. An allegation of fraudulent concealment does not render an otherwise ineligible claim eligible, but may be considered in connection with any other time bar defense (e.g., statute of limitations). Any damages suffered by the Claimant prior to the period described in this section shall not be part of any award that might be rendered by the arbitrators but may be considered in connection with any other time bar defense (e.g., statute of limitations). Any damages suffered by the Claimant prior to the period described in this section shall not be part of any award thar might be rendered by the arbitrators but may be p. ‿ued in a court proceeding described in subsection (d) below.

(b) Occurrence or Event Defined

"Occurrence or event" means the trade date for the security upon which the claim is based. If the claim does not arise from a trade, then the occurrence or event refers to the date that the Respondent engaged (or omitted or refrained from engaging) in the activity that is the subject of a claim.

(c) Challenge to Eligibility

(i) If any responding party has a good faith basis to allege that a claim is ineligible, then such party, within twenty (20) business days after service of the claim upon it, shall request that the Director of Arbitration decide whether the claim is ineligible or eligible. The opposing party may submit a response to the Director of Arbitration no later than ten (10) days after service upon the party of the request. The period within which to file a responsive pleading to an eligible claim shall be tolled from the date a request is filed under this subsection until twenty (20) business days after service upon it of the Director's decision. The Director shall decide the issue of eligibility and shall endeavor to notify the parties of its decision within thirty (30) days of the request. The Director's decision shall be deemed a final decision for purposes of court jurisdiction.

(ii) Any party may dispute the Director's decision by filing an action against the opposing party in a court of competent jurisdiction challenging the Director's eligibility decision under subsection (c) (i) above. Such court action must be filed within twenty (20) business days after service of the Director's decision. The filing of an action challenging the Director's decision that a claim is eligible shall constitute a stipulation by the filing party that the claims are ineligible for arbitration and the opposing party may immediately proceed with the claim in court as allowed in Sec. 4(d).

(iii) If no action is filed within the aforementioned period, then the Director's decision shall be final and may not be subsequently challenged in any forum. If an action is filed challenging the Director's decision, then the filing date of any responsive pleading in the arbitration shall continue to be tolled until twenty (20) business days after the date that the action is finally resolved.

(d) Ineligible Claims
Any claim determined to be ineligible for arbitration may be filed in a court of competent jurisdiction by any Claimant, notwithstanding that a submission agreement had been filed and as if no arbitration agreement had been entered into by the parties. All applicable law and/or Section 7 during the pendency of any arbitration claim filed pursuant to the rules of this forum, and for twenty (20) business days after the service of the Director's decision.

(e) Statute of Limitations
This section shall not extend or limit applicable statutes of limitations, nor shall it apply to any claim which is directed to arbitration by a court of competent jurisdiction upon the motion of an opposing party.

The First Circuit Opines That Section 15 Question Is To Be Determined By the Arbitrators

In PaineWebber v. Elahi, 1996 WL 360012 (1st Cir. Mass. July 3, 1996), the First Circuit added its name to the list of Federal Circuits which have determined that NASD Code of Arbitration Section 15 questions are to be resolved by the arbitrators and not the courts.

The Third, Sixth, Seventh, Tenth and Eleventh Circuits have held that the courts must decide the applicability of Section 15. The Second, Fifth, Eighth and Ninth Circuits have held that Section 15 determinations are for the Arbitrators.

Importantly, the arbitration agreement that the Elahi's signed contained a New York choice of law clause. Not surprisingly, PaineWebber argued that because New York courts have held that courts must decide arbitrability (Merrill Lynch v. Ohnuma 630 N.Y.S. 2d. 724 (N.Y. App. Dir. 1995); Merrill Lynch v. DeChaine 600 N.Y.S. 2d. 459 (N.Y. App. Dir.), the choice of law clause in this case dictated the same result and the court must determine eligibility.

The Elahi Court, however, chose to examine the effect of the New York choice of law clause in light of the U.S. Supreme Court's reasoning in Mastrobuono v. Shearson Lehman Hutton, 115 S.Ct. 1212 (1995).

The Court noted that the Mastrobuono court also dealt with a New York choice of law clause, and held that the choice of law clause could restrict the award of punitive damages only if the agreement indicated an intent by the parties to the arbitration contract to adopt New York case law barring arbitrators from awarding punitive damages.

The Elahi court found that the breadth of the arbitration clause signed in that case mitigated against reading the choice of law clause from acting as a limit on the arbitrators' powers. Moreover, and most importantly, the Court noted that the agreement provided that the arbitration shall be in accordance with the rules in effect of the NASD, which, according to the Court, further undermined the likelihood that the parties intended to adopt arbitration rules contained in New York case law, whereby the Courts made the determination as to arbitrability under Section 15.

The Court then considered the Supreme Courts' directive in First Options of Chicago v. Kaplan, 115 S.Ct. 1920 (1995), that a court must make a preliminary determination as to whether the agreement creates a duty to arbitrate, unless the court first determines that the parties to the agreement clearly and unmistakably provided otherwise.

The Elahi Court noted the fact that the NASD had proposed an amendment to provide that the Director of Arbitration would make the eligibility determination (July 1994), and therefore concluded that the NASD's position was unclear as to who was empowered to make the determination of eligibility.

In the end, the Court used a common sense approach. "We believe that parties who have agreed to arbitrate a given subject most likely intend and expect that the arbitrator should resolve all issues that arise concerning the subject; if they do not, we think they would clearly express their contrary intent."

In an area of the law where common sense is rarely consulted, it would be refreshing if the United States Supreme Court, when it considers this question, as inevitably it must, chooses to bypass the semantic rhetoric which has created the division in the federal circuits as to Section 15 and adopt the common sense approach of the Elahi court.

Non-Signatory Broker Can Compel Arbitration Even When Signatory-Employer Does Not Join in the Motion

In Klein v. Boyd, 1996 WL 437052 (E.D. Pa. August 2, 1996), the Court considered whether a broker, who did not sign the arbitration agreement, could compel arbitration even though his firm, which h[illegible] igned the arbitration agreement, did not join in the motion to compel.

Citing cases which had held that both officers of a corporation and an agent of a signatory to an arbitration agreement have standing to enforce the arbitration terms of an agreement, the Court stayed the proceeding and ordered arbitration.

This result should be of particular interest especially to those practitioners who have claims against second tier brokerage firms of limited financial resources and are attempting to make recovery by pursuing a claim against the individual broker who handled the account.

New York Court Blocks Introducing Broker From Using Clearing Broker's Arbitration Agreement

In Monisoff v. American Eagle Investments, 927 F. Supp. 137 (S.D.N.Y.1996), the court rejected the introducing broker's argument that it was a third-party beneficiary of the arbitration agreement signed in favor of its clearing broker. The introducing broker had argued, citing Moses H. Cone v. Mercury Construction, 103 S.Ct. 927 (1983), to the effect that "any doubts concerning the scope of arbitration issues should be resolved in favor of arbitration."

The Monisoff Court declined to apply the Cone reasoning to the case, concluding that the presumption towards arbitrability only applies to the issues subject to arbitration, not to the threshold issue of the existence of an agreement to arbitrate between the parties.

District Court Confirms Award Against Stratton Oakmont

A Minnesota District Court has confirmed a $1,552,000 award against Stratton Oakmont (Card v. Stratton Oakmont, Inc. 933 F.Supp. 806 (D.Minn. July 8, 1996)).

Stratton Oakmont attempted to vacate the award on several grounds, the most interesting being the panels' consideration of the SEC injunction against Stratton and prior settlements involving the Stratton broker.

As to the SEC proceedings, Stratton cited Lipsky v. Commonwealth United Corp., 551 F.2d. 887 (2nd Cir. 1976), and Beck v. Cantor Fitzgerald & Co., Inc., 621 F. Supp. 1547 (D.C. Ill. 1985), wherein both courts granted motions to strike references to SEC complaints from petitions filed in Federal Court, pursuant to the Federal Rules of Evidence.

In rejecting Stratton's argument, the Card court summarily dismissed any reliance on federal rules cases by stating: ". . . this Court agrees, that any reliance on Lipsky or Beck is misplaced as the Federal Rules of Evidence do not apply to arbitration proceedings."

As to the introduction of prior settlement ffers, the Card Court also rejected Stratton's argument, and quoted Bowles Financial Group v. Stifel, Nicolaus & Co., 22 F.3d 1010 (10th Cir. 1994), which held that the rules of court do not apply to arbitration: "By agreeing to arbitrate, a party trades the procedures and opportunity for review of the courtroom for the (perceived) simplicity, informality and expedition of arbitration."

Lastly, the Card court made reference to the submission agreement in which the parties agreed to arbitrate under the rules of the NASD and the NASD Code of Arbitration Procedure and then cited Rule 34 of the NASD Code of Arbitration Procedure which provides that the arbitrators determine the materiality and relevance of evidence. This, the Court reasoned, gave further credence that NASD arbitrators are not bound by the federal rules concerning evidence.

The Claimant in Card was represented by 1ark Briol, former PIABA director.

Florida Court Redetermines Attorney's Fees From Arbitration Award

In Dean Witter Reynolds v. Wood, 676 So.2d 464 (Fl.App.5th Cir.1996), the Claimant had argued successfully in the arbitration that the arbitrator had the authority to determine the amount of attorney's fees. Under Florida statute, Section 682.11, the parties to an arbitration have a statutory right to have a state circuit court determine attorney's fees in an arbitration proceeding.

After the arbitration panel awarded attorney's fees of $36,108.32, the Claimant filed an action in state court, claiming that there was no agreement to allow the arbitrator to determine attorney's fees, and that, absent any express agree-1ent, the claimant wished to exercise his statutory right to have the fees judicially determined. The Court held that there was no agreement to allow the arbitrator instead of the court to determine attorney's fees and awarded the Claimant $128,193.75 in attorney's fees — almost four times the arbitrator's attorney's fee award.

Eleventh Circuit Refuses to Allow Res Judicata on Section 15 Determination to Bar Judicial Consideration of Securities Claim

In Sewell v. Merrill Lynch 1996 WL 490169 (11th Cir. Sept. 13, 1996), the investor had filed an NASD claim and Merrill Lynch then filed for a permanent injunction from a New York court staying, as ineligible under Section 15, Sewell's Arbitration Claims. Merrill Lynch cited numerous New York and federal decisions (Edward D. Jones v. Sorrells, 957 F.2d 509 (7th Cir.1992) and Merrill Lynch v. Cohen, 62 F.3d 381 (11th Cir. 1995)) holding that Section 15 was a jurisdictional eligibility requirement. The investor chose not to make an appearance in the New York proceeding. The New York court granted Merrill Lynch a default judgment.

When Sewell then filed in state court in Florida, Merrill Lynch removed the case to federal court and successfully argued to the district court that the issue had been litigated in New York and res judicata precluded the re-litigation of the merits of the case.

The Eleventh Circuit reversed, based on the

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fact that it found that the issues involved in New York were not dispositive of the Florida action and therefore re- judicata did not attach.

The Eleventh Circuit stated that the only issue of the Florida case was the effect of the New York proceeding on the Florida proceeding. Nonetheless, Merrill Lynch attempted to entice the Court into consideration of the merits of the case. Merrill Lynch cited Castellano v. Prudential-Bache 1990 WL 87575 (June 19, 1990), Calabria v. Merrill Lynch 855 F.Supp. 172 (N.D. Tex. 1994) and C.D. Anderson & Co. V. Lemos 832 F.2d. 1097 (9th Cir. 1987), for the proposition that even if res judicata did not attach, that the investor had no right to litigate the claim because the customer agreement provided for arbitration as an exclusive remedy.

The Sewell Court rejected the exclusive remedy argument, citing Section 1B of Moore's Federal Practice for the effect that when prior unsuccessful litigation has established that one remedy is unavailable, a litigant is not always precluded by the mistaken choice from invoking the appropriate remedy, and Davis v. Chevy Chase Financial, 667 F.2d 160 (D.C. Cir. 1981), to support its position that the investor did r-- waive or forfeit his right to a judicial determination of arbitrability by first submitting the question to an arbitrator.

NASD Extends the Effectiveness of the Arbitration Procedures for Large and Complex Cases

The NASD has extended the trial period for the Arbitration Procedure for Large and Complex Cases until August 1, 1997. (Formerly Rule 4(b); now Rule 10334 of the new NASD Arbitration Code that went into effect in July 1996).

The Rule regarding large and complex cases became effective on May 2, 1995, for a one year pilot program. In the fourteen months since its effective date until July 25, 1996, there have been 578 NASD cases filed that were eligible for disposition as large and complex cases. Of those, there have been 178 administrative conferences and in 25 of those cases, the parties agreed to proceed under the Large and Complex Case procedures.

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