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The P I A B A Quarterly

The Newsletter of the Public Investors Arbitration Bar Association

March 1999 Volume 6 Number 1

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The
PIABA
Quarterly

The Newsletter of the Public Investors Arbitration Bar Association

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Editor's Notes

This issue of the *Quarterly* contains an article on Clearing Broker Liability by contributor Joseph C. Long.

The deadline for receiving submissions for the June, 1999 issue of the *Quarterly* is June 10, 1999. All submissions, regardless of length, should be accompanied by a computer disk of the submitted materials in either word perfect or as a text file.

Please send change of address information to Robin Ringo at 1111 Wylie Road, #18, Norman, OK 73069. Toll Free: (888) 621-7484; Fax: (405) 360-2063; E-Mail: piabalaw@aol.com; Web site: www.piaba.org.

Letter From the President

Mark E. Maddox, MADDOX KOELLER HARGETT & CARUSO, Indianapolis, Indiana

Dear Friends:

You realize how quickly a year goes by when you are elected to serve as the President of an organization like PIABA for a one-year term. I cannot believe that my term is about half way over, and I only have about six months left to finish the job as best I can.

I traveled to Washington, DC in late February for two reasons. First, I had meetings with the SEC, SIPC, AARP, and NASAA in order to promote our idea of modernizing and updating the Securities Investor Protection Act. As you might expect, we found support in the usual

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places and opposition in the others. I currently plan to begin meetings on Capital Hill in April in an attempt to build some momentum behind this idea.

My other reason for visiting DC was to meet with the General Accounting Office which is currently updating its 1994 study and report on securities arbitration and investigating the issue of unpaid arbitration awards in securities arbitration proceedings. As discussed later in this newsletter, I am urging every PIABA member to forward any unpaid arbitration awards issued in 1997 or 1998 to Robin Ringo at the PIABA offices immediately. Further, if you are surveyed by the General Accounting Office within the next year as to the subject of unpaid arbitration awards, please take the time and return the survey in a timely fashion.

The SEC has still not made a decision on the NASD's pending punitive damages cap rule. It remains unclear what the time table will be for SEC action on this rule. The prognosticators who watch the SEC tell me that this is likely to be a very close vote, possibly 3-2 either way, with Chairman Leavitt casting the deciding vote. We'll let you know how this turns out.

I've used the NASD's new list selection method of selecting arbitrators in a few cases. It sure is a lot more work than the old way. However, I have already seen a few cases in which the in-house counsel opposing me clearly didn't do his/her homework and the panel that was appointed reflected my top choices.

I am very excited about the PIABA Annual Meeting scheduled for the Marriott Desert Springs Resort and Spa in Palm Desert, California from October 21 - 23. The Annual Meeting Committee is putting together one of the best meeting schedules ever, and I hope to see you in attendance.

Hope you're taking a Spring Break this year!

Mark E. Maddox

From the Professor

Joseph C. Long
Norman, OK

In this issue, I want to address a topic which I thought I had already written on until I reviewed the back issues of the *Quarterly*. This topic is clearing broker liability. Clearing broker liability is becoming increasingly important as many of the smaller and less ethical introducing brokers go bankrupt leaving behind them many unsatisfied arbitration awards. Clearing brokers are also coming under additional attack by the SEC and the SRO's. One of the largest clearing brokers, Bear Stearns, is reportedly about to be indicted fc s part in the clearing of Sterling Foster transactions.

I believe that clearing brokers are and always have been liable under the state securities acts. The clearing brokers will typically cite a number of federal decisions holding that clearing brokers have no liability under federal securities law or under common law agency.

I. COMMON LAW AGENCY LIABILITY

I question whether the latter claim of no liability under common law agency is correct in some instances. Whether there is or is not liability under common law agency will depend upon what the relationship is

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between the customer, the introducing broker, and the clearing broker. If, as most of the brokerage houses claim, this relationship is one of principal (customer), agent (introducing broker), and sub-agent (clearing broker), it will be difficult, if not impossible to establish liability on the part of the clearing broker for the wrongful acts of the introducing broker.[1]

However, this does not mean that the clearing broker may not be liable. A subagent, the clearing broker, owes the same fiduciary duties to the ultimate principal, the customer, that the agent, the introducing broker, does. One of those fiduciary duties is to inform the principal of any information which comes into his possession which would be important to the principal's decision-making process. Therefore, if the clearing broker ***actually*** knows that the introducing broker is violating the law, then it breaches its fiduciary duty to the customer by not telling the principal of the introducing broker-agent's violation. In most states, breach of fiduciary duty is constructive fraud which may result in the award of punitive damages.

On the other hand, the relationship may be principal (customer), agent (clearing broker), and subagent (introducing broker). In such case, under Section 406[2] of the *Restatement of Agency 2d*, the clearing broker will be liable to its principal, the customer, for the conduct of the sub-agent, the introducing broker, as it is for its own conduct. I am not convinced that this is not the accurate characterization of the relationship with many of the large clearing brokers. It appears to me that they go out and recruit the introducing brokers to funnel business to them. In such case, the clearing broker is both the agent of the customer and the principal of the introducing broker. The introducing broker, in turn, is the agent of the clearing broker and the sub-agent of the customer. As a subagent, the introducing broker owns the same fiduciary duties to customer-principal that the clearing broker-agent has

Turning to state securities law, I believe that there are two major liability theories which may apply to a clearing broker. The first is the clearing broker who is "a broker-dealer who materially aided in the sale" of the securities. Section 410(b) of the Uniform Securities Acts and many non-Uniform state securities acts impose secondary liability on such brokers. Second, I believe that a strong case can be made ***under state securities law*** for holding the clearing broker as a "seller" of the securities under Section 410(a) of the Uniform Act. Under ***state securities***, rather than federal securities, law a person who materially aids or abets or who is engaged in a conspiracy can be classified as a seller. Each of these theories will be discussed briefly below.

II SECTION 410(b) LIABILITY

Section 410(b) of the Uniform Securities Act imposes secondary liability upon a number of individuals for the violation of Section 410(a) by a primary violator. Section 410(b) has been held to create more extensive liability than either Sections 12 or 15 of the Securities Act of 1933, the counterpart federal provisions.[3]

As noted above, Section 410(b) states "every broker-dealer who materially aids in the sale is also liable jointly and severally with and to the same extent as the seller." It is important to note that this part of Section 410(b) ***does not talk in terms of "aiding and abetting".*** The term used is "aiding". This term is clearly separate for the concept of "aiding and abetting". Further, the requirements for imposing liability under Section 410(b) are different than those for "aider and abettor" liability.[4] Section 410(b), unlike some other state acts,[5] does not talk in terms of the broker-dealer "participating in the sale". The focus of the two terms "aiding" and "participating" is different. "Participation" focuses on the sales process itself. "Aiding", on the other hand, is broader and focuses upon activities upon

which do not directly lead to the sale, but make it possible.[6]

Section 410(b) liability is vicarious. However, unlike some state securities acts,[7] it is not strict liability. The broker-dealer can avoid liability by proving the affirmative defense that it "did not know and in the exercise of reasonable care could not have known, of ***the facts*** by reason of which the liability is alleged to exist."[8] Obviously, the defense is not available if the clearing broker actually knows of the facts. But more importantly, the defense clearly places a duty on the clearing broker to make a reasonable investigation, if it does want to be liable. ***This duty to investigate is what distinguishes clearing broker liability under the state acts from non-liability under the federal securities acts or, in some cases, common law agency.***

It is also important to realize this defense only applies to ***knowledge of the facts.*** In the case of a non-registration of a security, this means the clearing broker can avoid liability only by showing that it could not have discovered the sale of the securities have been made into the particular state. The need to register the security in the particular state, is a question of ***law, not fact.*** As a result, an opinion of counsel or even the state securities commission itself is not a defense.

Obviously, in most cases, the clearing broker will not be able to sustain this defense. It cleared the transaction and notified the client based upon the address in its own records.[9] In most cases, the transaction will have taken place in the state where the customer resides. The clearing broker clearly knows or, at least, could have known which state that was.

The same is also true of non-registration of either the introducing broker-dealer or its registered representative, agent. The information given by the introducing broker obviously will include the name of the introducing broker and, usually, the name of the registered representative handling the transaction. Again, the information will also indicate in what state the customer is located.

From this information, the clearing broker, if it bothers to investigate, can determine whether the sale is lawful. However, the clearing broker usually argues that it has no legal duty to see if the introducing broker or its employee are registered in a particular state. Section 410(b) imposes such duty on the clearing broker, if it wants to avoid liability for non-registration.

There is little case law which has applied this portion of Section 410(b) to clearing brokers. The only case my research has found is ***Weisman v. Oliver Rose Securities, Inc.***[10] In this case, the clearing broker, Wall Street Clearing, sought to be dismissed from the action on the basis that there was no allegation that Wall Street actually misrepresented or failed to disclose anything to the client. The court refused such dismissal, stating:

> Plaintiff points out that § 36-498(b) [of the Connecticut Act, which is essentially the same as Section 410(b) of the Uniform Act] extends joint and several liability to "ever broker dealer or agent who materially aids in the "fraudulent sale of securities." Plaintiff's theory of liability against Wall Street Clearing relates to the "kickbacks" paid to Condron by Comiteau Levine. Plaintiff maintains that, by clearing trades executed by Comiteau Levine with knowledge that the kickbacks were being made, Wall Street materially aided in the sale of securities. . . .[11]

The court reached a similar conclusion against Bear, Stearns & Company, which also had acted as a clearing broker.[12]

There are three elements under this theory of liability. First, of course, there must be a primary violation by either the introducing broker or its agent.

Second, the clearing broker must be "broker-dealer" within the meaning of the local statute.[13] Certainly a clearing broker will meet this definition. The important factor here to note is that

§ 410(b) does not impose this liability only upon the "sellers'" broker, ***but upon any broker-dealer involved in the transaction.***

The final element is that the clearing broker must "materially aid" in the sale. What constitutes "material aiding" is a question that the courts have not yet fully developed. However, there are two actions most clearing brokers perform which, in my opinion, clearly constitute "materially aiding". First, the clearing broker clears the trades for the introducing broker. This was a necessary act in order to complete the sale as the introducing broker traditionally is not a member of any of the organized exchanges, and, therefore, can not clear the transactions for itself. My belief that the clearing function alone is sufficient to establish material aiding is supported by the above quoted language from the ***Weisman*** case. That language indicates that clearing constitutes "aiding" in the transaction and that the aiding is "material".

Further, most clearing brokers perform the back room paper work in connection with the introducing broker's transactions with its customers and, normally, deliver the confirmations of the transactions directly to introducing broker's customers. Such actions are clearly an important contribution to the transaction as outlined by the court in ***Prince v. Brydon***.[14]

Finally, the claimant can anticipate that most clearing brokers will try to justify their conduct and avoid liability under Section 410(b) by claiming that they are "only providing professional services." Such claim should not fly. The court in ***Prince v. Brydon*** effectively destroyed such defense, when it noted:

> The defense against strict liability, in short was [intended] to be ignorance, ***not the professional role of the person who renders material aid in the unlawful sale.***[15]

III. LIABILITY AS A "SELLER" UNDER SECTION 410(a) AS AN AIDER AND ABETTOR OR CO-CONSPIRATOR

I also believe that clearing brokers can be shown to have primary liability under Section 410(a) of the Uniform Act as a "seller" of the securities. The definition of "seller" has been extended to cover those who "aid and abet" in, or engage in a conspiracy to, sell unregistered securities or securities through material misrepresentations and omissions. The clearing brokers will vehemently argue that the concept of "seller" can no longer include "aiders and abettors" and "co-conspirators" after the Supreme Court decisions in ***Pinter v. Dahl***,[16] and ***Central Bank v. First Interstate Bank.***[17] This position is probably correct under the ***federal*** securities acts. ***However, it is clearly not true under the state securities acts***.[18]

The Kansas Supreme Court in ***State ex rel. Mays v. Riddenhour***,[19] specifically refused to follow the ***Pinter*** limitation on the definition of "seller" and specifically re-affirmed the position taken earlier in ***Mosley v. Unruh***,[20] that aider and abettor and co-conspirator liability were proper theories under the Kansas Act. Addressing the status of conspiracy liability, the court said:

> Even though ***Pinter*** clearly rejects the use of [the conspiracy] theory, we affirm its use in defining the seller of a security under the Kansas Securities Act.[21]

The court went on to hold the defendants liable for the sale of unregistered securities based upon their joining the illegal pyramid scheme, allowing their name to continue in the pyramid, and accepting money when their name reached the top of the pyramid.

Again, the actions of clearing brokers ought to fall within the holding of ***Riddenhour*** and ***Mosley.*** They enter into agreements to clear the sales of securities made by the introducing broker, a conspiracy. The clearing broker sells unregistered securities or securities through misrepresentation or omission of material facts. This is an overt act in the furtherance of the conspiracy. Such sales by the introducing broker were the proximate cause of the claimant's cause of action.[22]

The ***Riddenhour*** court also approved the use of the concept of aiding and abetting to define a "seller". In doing so, the court said:

> However [the] interpretation [in ***Pinter***] does not control in the interpretation of the Kansas Act. We find that the aiding and abetting theory can be used to find an individual liable for the sale of an unregistered security under the Kansas Securities Act. We adopt the "but for" or proximate cause test. Thus, for an individual to be liable for the injury, all that must be established is that the injury flowed directly and proximately from the actions of the person sought to be held liable.[23]

The conduct of a clearing broker in clearing the transaction and sending confirmation to the introducing broker's client clearly meets this ***Riddenhour*** "but for" test.[24]

Quite recently, the Arizona Court of Appeals in ***Grubaugh v. Bank DeCosta*** [25] rejected the application of ***Central*** under the Arizona Securities Act, and re-affirmed an earlier position in ***State v. Superior Court***[26] that aiding and abetting is a valid concept to impose liability as a "seller".

The viability of these liability theories in arbitration is an open question. Certainly, there are a number of cases where the clearing broker has been held not liable. On the other hand, there are a number of cases where clearing brokers have been held liable.[27] In all cases, the clearing broker made a claim of non-liability, yet in all these cases, the arbitrators rejected the clearing broker's defense and imposed substantial liability upon them.

Normally, there are considered three elements to establishing aider and abettor liability. First, as in the case of "material aiding", there must be a violation by the person who is aided or abetted. Second, there must be knowledge on the part of the "aider and abettor." Arguably, this knowledge requirement can be satisfied by simple or gross negligence.[28] Finally, as in the case of "material aiding", the aider and abettor must provide substantial assistance to the primary violator.

One final word of caution. If you are contemplating bringing an action against a clearing broker, expect that the clearing broker will vigorously contest liability. Also, do your homework and present the best case possible for liability. Each case where liability is rejected makes it that much harder for subsequent cases to establish this type of liability.

Footnotes

1. *See* Rest., Agency 2d, §405 (1957).

2. This Section reads:
Unless otherwise agreed, an agent is responsible to the principal for the conduct of a subservant or other subagent with reference to the principal's affairs entrusted to the subagent, as the agent is for his own conduct; and as to other matters, as a principal is for the conduct of a servant or other agent.

3. *Foster v. Jesup & Lamont Sec. Co.*, 482 So.2d 1201 (Ala. 1986); *Arthur Young & Co. v. Reves*, 937 F.2d 1310 (8th Cir. 1991); *Connecticut Nat'l Bank v. Giacomi*, 233 Conn. 304, 659 A.2d 66 (1995).

4. *See generally*, 12A Joseph C. Long, *Blue Sky Law* §7.08[5][b][i][B] (1998).

5. *See e.g.*, Fla. Stat. Ann. 517.211(1) (1987). The Florida Act does not talk in terms of a "broker" being liable, but rather an "agent of or for the seller" as being liable. Under the Uniform Act, "buyers" clearing broker will be liable as well as "sellers" clearing broker. Under the Florida Act, "buyers" clearing broker would appear to be liable only if the transaction was solicited by the introducing broker. The solicitation of an offer to buy a securities by definition is an offer to sell that security. U. Sec. Act §401(j)(2).

6. *See e.g.*, Fla. Stat. Ann. §517.211(1) (1987).

7. *See e.g.*, Fla. Stat. Ann. §517.211(1) (1987).

8. U. Sec. Act §410(b). Section 517.211(1) of the Florida Act does not have this language. As a result liability is absolute, if the broker "aids or participates" in the sale.

9. The exception would be where the client placed to order from another state. For example, the client lives in Georgia and has his brokerage correspondence directed to his home address in Georgia, but he works in South Carolina. The introducing broker calls him in South Carolina and solicites from him an order to buy the securities. In this case, the South Carolina Act, not the Georgia Act would apply. As noted above, the soliciation of an offer to buy is an offer to sell. U. Sec. Act §401(j)(2). An order to buy causes the provisions of the local act to attach, if an offer to sell is directed into the state. U. Sec. Act §§414(a)(1) and (c)(2). *See generally*, 12 Joseph C. Long, *Blue Sky Law* §3.04[2] (1998). In this case, the clearing broker probably would not know that the call was made from South Carolina.

10. 1987 U.S. Dist. LEXIS 16788 (D. Conn. Nov. 10, 1987).

11. *Id.* at *66.

12. *Id.* at *68-*69.

13. *See* U. Sec. Act §401(c). *See generally,* 12A Joseph C. Long, *Blue Sky Law* §6.03 (1998).

14. 307 Or. 146, 764 P.2d 1370 (1988).

15. *Id.* at 149, 764 P.2d at 1371. [Emphasis added.]

16. 486 U.S. 622 (1988).

17. 511 U.S. 164 (1994).

18. It is also clear that *Central Bank* has no effect on liability imposed by Section 410(b). *Dinco v. Dylex Ltd.*, 111 F.3d 967 (1st Cir. 1997); *Kirchoff v. Selby*, 703 N.E.2d 644 (Ind. 1998).

19. 248 Kan. 919, 811 P.2d 1220 (1991).

20. 150 Kan. 469, 95 P.2d 537 (1939).

21. *Id.* at 248 Kan. at 935, 811 P.2d at 1231

22. *See Riddenhour*, 248 Kan. at 927, 811 P.2d at 1126.

23. 248 Kan. at 940, 811 P.2d at 1234.

24. See also *Grubaugh v. DeCosta*, 1999 Ariz. App. LEXIS 35 (Mar. 16, 1999).

25. 1999 Ariz. App. LEXIS 35 (Mar. 16, 1999).

26. 123 Ariz. 324, 599 P.2d 777 (1979).

27. *See e.g., In re Thomsen and Hillcrest Fin. Corp.*, NASD 97-02167 (Aug. 1998); *In re Saul and Kennedy, Cabot, and Co.*, 1995 WL 447966 (NASD June 21, 1995); *In re Ammann and M. Rimson*, 1997 WL 633284 (NASD Sept. 3, 1997); *In re Leston and American Stock Transfer Co.*, 1997 WL 282879 (NASD Apr. 18, 1997); *In re Almeida,* 1996 WL 779343 (NASD Nov. 21, 1996).

28. Further, there is some indication that the second element may not be required in some states. The *Riddenhour* court held:

> [F]or an individual to be liable [as an aider and abettor under Kansas law] for the injury, all that must be established is that the injury flowed directly and proximately from the actions of the person sought to be held liable.
>
> 248 Kan. at 940, 811 P.2d at 1234.

NASD Intake Staff Harassment of Public Customers

Scot Bernstein
Sacramento, California

True to form, the NASD is engaging in *de facto* rulemaking designed to erect barriers to the filing and service of claims. This time, the rulemaking takes the form of rules establishing what will constitute an "adequate" claim that the NASD will serve on respondents.

Whether a claim is adequate, however, is a question for neutral arbitrators. The NASD – an industry trade association – has no right to review claims for adequacy.

The NASD's position regarding intake staff review of claims was set forth in a February 16, 1999, memorandum titled "Streamlining the Service of Claims Process - Deficiencies in Claims." Much of that memorandum is uncontroversial. Item 2 of that memorandum, however, overreaches in its attempt to set forth requirements for statements of claim. Item 2 states as follows:

"2. The Statement of Claim states the claimants' names and addresses (sufficiently stated to enable ODR staff to set a hearing location), the name and number of the account(s) at issue, when the dispute arose, and the damages sought (sufficiently stated to enable ODR staff to assess the appropriate filing fee and hearing session deposit). This is the minimum information required to give notice of the pleading and allow the arbitrators to determine eligibility and timeliness.

Here are the problems with Item 2:

a. Claimants' Addresses. As Item 2 admits, all that the NASD needs is information sufficient to enable the staff to set a hearing location. Thus, the claimants' city of residence is all that the NASD needs; their address is not necessary. Purporting to require an address when a city of residence is all that is needed is unnecessarily invasive of claimants' privacy. Many claimants – particularly elderly claimants – may not want to give their residential addresses to parties against whom they are making claims.

Moreover, since city of residence information is needed only for the purpose of setting hearing locations, it should be able to be included in the cover letter rather than in the statement of claim, if the claimants or their counsel so desire.

b. Account Number(s). Account numbers should not be required. No rule in the Code of Arbitration Procedure states that people with incomplete records are not entitled to arbitrate claims. Nor should claimants be asked to hem themselves in with that kind of detail.

A broker-dealer that has changed a claimant's account number during the course of the broker-customer relationship may try to assert that a claim relates only to the account number(s) set forth in the statement of claim, and not to those which the claimant inadvertently (or through inadequate records) has failed to list. Thus, this unilaterally imposed "requirement" may act primarily to create defenses for the NASD's member firms.

Moreover, some broker-dealers – particularly high-payout houses whose business consists primarily of pushing limited partnerships – have not been in the habit of sending statements to their customers. Are those customers' claims suddenly inadequate because the customers do not know their account numbers?

c. When the Dispute Arose. This is perhaps the most problematic of the "requirements." For starters, "when the dispute arose" does not even track the language of Rule 10304. More importantly, what "occurrence or event" gave rise to a controversy is a question for the arbitrators in five federal circuits and for the courts in five more. *Nowhere* is it a question for the NASD. This was, of course, the reason for the NASD's decision in 1996 to halt the practice of having its arbitration administrators ande staff attorneys issue preliminary rulings on 6-year-

rule dismissal motions. Setting a trap so that the intake staff can do the same thing is improper as well.

Moreover, this unapproved pleading "requirement" may lay a trap for inexperienced counsel or *pro per* claimants who do not understand the implications of the question. For example, a prospective claimant who reads the NASD's memorandum may assume erroneously that the purchase date is "when the dispute arose," even though the broker successfully concealed his lies until very recently. That claimant's claim might be rejected by the NASD notwithstanding its validity.

Worse still, an inexperienced attorney or a pro per claimant may have a claim rejected after relying on an NASD intake staffer's informal advice that purchase date determines "when the dispute arose."

The NASD's assertion that this information is required "to allow the arbitrators to determine eligibility and timeliness" misses the point. If the arbitrators want additional information, they will ask for it. It is not the NASD's place to require it.

For quite some time, the NASD has accepted my representation that "this dispute arose within six years prior to the filing of the Statement of Claim." See below.

d. Damages Sought. As the NASD admits, it needs to know the "damages sought" only for the purpose of determining the appropriate filing fee and hearing session deposit. Thus, by its own admission, it does not need to know the exact amount sought. Rather, it only needs to know into which numerical range (as set forth in Rule 10332) the damages will fall. Telling the NASD what that range is, therefore, ought to suffice.

Moreover, the damages for purposes of Rule 10332 exclude interest, expenses, attorneys' fees, punitive and exemplary damages, and statutory and other damage enhancements. This is so notwithstanding occasional attempts by the intake staff to compel claimants to state the amount of punitive damages sought and to include that sum in the total for purposes of filing fee and forum fee calculations.

A Form of Cover Letter

For some time, I have been filing statements of claim under a form of cover letter that provides the NASD with the information that it says it needs. That cover letter is reproduced at the end of this article.

Conclusion

It is disturbing that the NASD is persisting in its practice of making rules without SEC approval. More disturbing still is that the NASD's pronouncements often seem designed to work to the disadvantage of public customers. Practitioners should not allow the NASD to assert authority that it does not have.

FORM OF STATEMENT OF CLAIM COVER LETTER

\\Date

\\
Director of Arbitration
National Association of
Securities Dealers, Inc.
125 Broad Street
Thirty-Sixth Floor
New York, New York 10004

Attention: \\

VIA OVERNIGHT DELIVERY

Re: **\\ v. **
Case No. 9\-

Dear \\:

Enclosed are \\ clipped sets of documents, each containing the following:
[\\# of sets = # of Respondents + 4]

(1) a statement of claim setting forth the basis of Claimants' claims against the Respondents identified above; and

(2) a Submission Agreement signed by Claimants.

Also enclosed is a check in the amount of $\\.00 covering the NASD's $\\.00 filing fee and the $\\.00 hearing session deposit.

Additionally, I provide the following information:

a. City and state of Claimant(s)' residence when the dispute arose:

\\, California.

b. This dispute arose within six years prior to the filing of the Statement of Claim and therefore meets the eligibility criteria set forth in Rule 10304. See, *inter alia*, the \\ paragraph on page \\ of the Statement of Claim.

c. All sums invested by Respondents for Claimants have been lost. See, *inter alia*, the \\ paragraph on page \\ of the Statement of Claim. The amount in dispute in this case (exclusive of interest, expenses, attorneys' fees, punitive and exemplary damages, and statutory and other damage enhancements) is greater than $\\100,000 and less than or equal to $\\500,000.

d. Claimant(s) request a panel of \\three arbitrators.

The \\ are nearly \\ years old. Accordingly, I request that this case be expedited to the maximum extent possible.

Thank you for your courtesy and cooperation in connection with this matter.

Very truly yours,

U.S. First Circuit Overturns Rosenberg in Rosenberg v. Merrill Lynch

In ***Rosenberg v. Merrill Lynch***, 1999 WL 80964 (1st Cir. (Mass.)), the U.S. First Circuit Court of Appeals overturned a Massachusetts District Court ruling which had initially held that pre-dispute arbitration agreements could not be enforced in employment cases involving Title VII and the ADEA.

The District Judge had based her ruling, at least in part, on her finding that NYSE arbitration procedures were inadequate to ensure fair adjudication of the discrimination claims. The Judge had noted that the NYSE Director of Arbitration selects the pool of arbitrators, that the make-up of the arbitration pool favored the industry defendants, and lastly, and most critically, that the arbitrators rely heavily on the arbitration staff personnel when making important decisions during the arbitration process.

The First Circuit reversal was based, in part, in its finding that the District Court had "misinterpreted" certain facts regarding the structure of the NYSE's arbitration system. The First Circuit recited the Supreme Court's comment in Shearson/American Express, Inc.--that the NYSE is subject to the regulation of the SEC, including its arbitration procedures, and that the SEC possesses "expansive power to ensure the adequacy of the arbitration procedures" employed by all SRO's, including the NYSE.

[*Note: Recent NASD rule changes exclude employment discrimination claims from the scope of cases required to be arbitrated.*]

NY Court Refuses to Allow Introducing Broker to Benefit From Clearing Broker's Arbitration Agreement

In ***Warner v. U.S. Securities & Futures Corp.***, 1999 WL 44344 (N.Y.A.D. 1 Dept.), the Court refused to allow the introducing broker to compel arbitration by using its clearing broker's agreement, in spite of the fact that the agreement stipulated that the introducing broker was a third-party beneficiary of the agreement.

Not withstanding this language, the Court held that the motion to arbitrate was properly denied in the absence of evidence affirmatively establishing that the parties expressly agreed to arbitrate their disputes.

North Carolina State Court Holds that Eligibility is To Be Determined by Arbitrators

In ***Smith Barney v. Bardolph***, 509 S.E. 2d 255, the North Carolina Court of Appeals was asked

to rule on a petition for declaratory judgement which sought to preclude the arbitration of claims which were more than six years old.

The parties had agreed to stay the NASD arbitration and allow Smith Barney to seek declaratory relief.

The Court reported on the scorecard of arbitrability--the First, Second, Fifth, Eighth, and Ninth Circuits allow for a determination by arbitrators, while the Third, Sixth, Seventh, Tenth and Eleventh Circuits have held that the trial court must resolve the issue of timeliness.

Since the Fourth Circuit does not have a decision squarely on point, the Court considered what the Fourth Circuit might do when it is faced with the question of arbitrability.

Citing ***Glass v. Kidder Peabody***, 114 F. 3d. 446 (4th Cir. 1997), the Court found that defenses of laches, statutes of limitations, and delay are waiver defenses that are matters of procedural arbitrability, and therefore, to be decided by the arbitrators and not a court.

Additionally, the Court noted Section 10324 of the NASD Code of Arbitration Procedure, and found that it evidenced the parties' clear and unmistakable intent to leave the question of arbitrability to the arbitrators.

U.S. Eight Circuit Confirms Arbitration Award Against Stratton Oakmont Control Persons Including Punitive Damages

In ***Sav-A-Trip, Inc. v. Belfort***, 164 F. 3d 1137, the Eight Circuit confirmed an award against the respondents which included punitive damages in spite of the fact that punitive damages are not allowed under the Kansas Securities Act.

As to punitive damages, the Court confirmed without so much as a mention of ***Mastrobuono*** The Court simply noted that the claimant had asserted federal, state, and common law claims which could sustain a punitive damage award.

As to the issue of whether the individual respondents could be held liable as controlling persons, the Court noted that the respondents occupied various supervisory positions during their tenure at Stratton Oakmont that gave them direct or indirect control over the individual brokers who handled the claimant's account. Moreover, the Court concluded that the respondents did not carry their burden, under the Kansas Securities Act, to prove that they did not know nor could have known of the fraud committed by their subordinate employees.

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PIABA recognizes that not everyone has a website, the information or knowledge necessary to develop a website. It was noted at the Directors' Meeting in March, that PIABA has the ability to host websites for its members. While the details have not been finalized, members interested in having PIABA host a website, may contact the PIABA Office for more information. There will be a hosting fee.

PIABA is unable to provide the design for your site. There are, however, several avenues you may consider in preparing the information for and design of the website. Many software packages now have website design packages included on their installation CDs. You may also contact members who have sites on-line to find out who designed their website. The PIABA webmaster can also assist you in designing a website. You may contact Bryan Dickinson at bryan@generationz.net. Mr. Dickinson is not employed by PIABA nor does PIABA receive any remuneration should you choose to utilize his services.