Public Investors Arbitration Bar Association

August 23, 2004

Jonathan G. Katz, Secretary
SECURITIES & EXCHANGE COMMISSION
450 Fifth Street, N.W.
Washington, DC 20549

RE: File # SR-NASD-2004-088

Dear Mr. Katz:

Please accept the following as the comments of the Public Investors Arbitration Bar Association (PIABA) to the above-referenced NASD rule filing ("the Proposed Rule"). It is PIABA's understanding that the NASD has requested accelerated approval of the Proposed Rule. Therefore, PIABA has chosen to not await publication of the Proposed Rule in the Federal Register to submit its comments.

PIABA is wholly in agreement with the underlying premise of the Proposed Rule; *i.e.,* "that compliance with the discovery rules . . . is a critical component of the NASD arbitration process." It is an argument that the NASD has heard for years from PIABA and its members as well as others routinely involved in NASD arbitration. To that extent, PIABA commends the spirit of the NASD's rule filing and is encouraged by the recent actions the NASD has taken to correct these all-too-common and recurring abuses.

However, PIABA is concerned that the Proposed Rule - specifically section (f)(2), which purports to imbue arbitrators with the authority to sanction "a party's representative" - is not supported by existing law and is an unnecessary, premature and misguided attempt to curb discovery abuses in arbitration which could better be addressed by proper training and consistent application of the authority arbitrators already possess to govern the conduct of the parties and proceedings.

[the remainder of this page intentionally left blank]

Section (f)(2) of the Proposed Rule is Not Supported By Existing Law

To the extent the Proposed Rule purports to grant arbitrators the "explicit authority" to impose sanctions on a party's representative who is not otherwise an associated person, the Proposed Rule cuts against the great weight of legal authority. As the SEC and NASD are undoubtedly aware, the entire basis of arbitrator authority under both federal and state law rests on the notion of contract. Quite simply, a party to a dispute can not be forced to arbitrate that which he/she has not agreed to arbitrate. In the case of SRO arbitration, the authority of arbitrators emanates from contracts to which a "party's representative" is not typically a party: a customer agreement, Form U-4, BD application for membership and/or Uniform Submission Agreement. Notwithstanding the NASD's references to an arbitrator's "broad power to control the proceedings and enforce compliance with their orders," that power and authority does not extend to those persons who are not parties to some sort of arbitration agreement. PIABA suggests that the intent of the NASD in proposing this rule is not merely to codify existing arbitrator authority, but rather to expand it in a way which is contrary to established law.

The Proposed Rule is Premature and Unnecessary

As noted above, PIABA, its members and others involved in NASD arbitration have complained for years about discovery abuse in arbitration. Beginning late last year and presumably in response to those complaints, the NASD took "several proactive steps" designed to "emphasize the importance of complying with the discovery rules." The NASD notes in its submission that, notwithstanding its recent efforts, parties continue to complain about discovery abuse in arbitration and hence the need for accelerated approval of a rule originally proposed as part of a comprehensive rewrite of the entire code of arbitration.[1] PIABA suggests that the NASD's earnest efforts to curb discovery abuse are so new that no conclusions can legitimately be drawn from what the NASD characterizes as "continuing complaints about discovery abuse."

The NASD's attempt to imbue arbitrators with the authority to sanction party representatives is also unnecessary. There can be no doubt that the arbitrators have the authority to sanction the **parties** who have contractually agreed to submit themselves to the arbitrators' jurisdiction. Counsel are responsible to their clients for any action counsel takes which results in the client being sanctioned. If the NASD were to properly train and instruct its arbitrators to implement and enforce the policy against discovery abuse, as reflected its various pronouncements since November of last year, the instances of discovery abuse in arbitration would likely diminish significantly. Any punishment of counsel for his/her role in such abuse

1. In addition to the proactive measures referenced on pages 4-5 of the NASD's submission, and subsequent to the filing thereof, the NASD fined 3 of its larger member firms $250,000 each for abuse of the discovery process in arbitration. The Proposed Rule was originally filed prior to any of the "proactive measures" referenced in the NASD's rule filing.

will emanate from counsel's client - as it should. There is simply no need to interject the judgment of a NASD arbitrator between a party to the arbitration and his/her counsel.

Section (f)(2) of the Proposed Rule Should Not Be Considered Until the NASD Has Propounded Specific Standards for the Imposition of Sanctions and the SEC Has Reviewed and Approved All Training Materials to Be Used in Conjunction With the Arbitrators' Expanded Authority

PIABA's most serious concern about the Proposed Rule is the absolute lack of any published standards or guidance for either the parties or the parties' "representatives" whom the arbitrators will be newly empowered to sanction.

In recognition of the extraordinary nature of sanctions against attorneys, federal and state courts have articulated well defined standards governing the conduct of counsel appearing before them and those standards have been tested, reviewed and refined through a well developed body of case law. There are no such standards or any other guidance submitted with the Proposed Rule, nor is there any indication in the NASD's rule filing that it intends to promulgate such standards or guidance or what those standards might be.[2] Prior to approval of the Proposed Rule, the SEC should require that any authority granted arbitrators to sanction "party representatives" be clearly delineated; that the entire pool of NASD arbitrators (or, at a minimum, those qualified to serve as chairpersons) be required to undergo extensive training in the use of sanctions against party representatives; and, that all such training materials and other guidelines in this regard be submitted to the SEC for public comment prior to their utilization and the ultimate implementation of the Proposed Rule.

In addition to the guidance offered by well developed standards and case law, attorneys subject to sanctions in a court setting have the benefit of appellate review under an "abuse of discretion" standard. As the SEC is well aware, appellate review of arbitration awards is far more circumscribed. Moreover, it is well established that arbitrators are not required to state reasons for their awards. Lack of any meaningful appellate review dictates that any rule purporting to empower arbitrators to sanction party representatives must provide for some avenue of appeal other than traditional post-award vacatur actions brought under the federal and state arbitration acts. One solution may be to allow for immediate appellate review of all

[2] Page 6 of the NASD's filing makes parenthetical reference to "egregious circumstances" in connection with its suggestion that arbitrators have the inherent authority to sanction party representatives. It is noteworthy that the "egregious circumstances" standard is not set forth in the text of the Proposed Rule itself, nor is there any reference to what would constitute "egregious circumstances" sufficient to warrant sanctions.

orders of sanctions against party representatives by the Director of Arbitration.[3] Given the current state of the law immunizing the NASD from suit based on matters arising from its administration of the arbitration process, it may also be necessary to couple the Director's review of sanctions orders with a consent by the Director to the jurisdiction of any court reviewing such decision in a post-award proceeding.[4] Additionally, the Proposed Rule should require written findings of the facts upon which any decision to issue sanctions against a "party's representative" was based.

In conclusion, while PIABA commends the spirit and apparent goal of the Proposed Rule, it appears - as written - to be a premature and somewhat "knee jerk" reaction to a problem which could better be addressed by comprehensive arbitrator training in the consistent application of the authority arbitrators already possess to curb discovery abuses. The expansion of arbitrator authority to encompass individuals or entities which themselves are not parties to any agreement to arbitrate is so fraught with serious legal and equitable issues, problems and questions that the approval of the Proposed Rule will cause far more problems than it will solve and will likely open a Pandora's box of collateral litigation and post-award proceedings. The overall effect will be to undermine the arbitration process rather than enhance it.

Accordingly, for all of the reasons set forth herein, PIABA urges the SEC to reject the Proposed Rule unless the NASD can demonstrate the necessity for such a rule **after** a demonstrated commitment on the NASD's part to consistent enforcement of the policies already in place and provides for public comment detailed guidance and arbitrator training materials relating to the implementation of the arbitrators' expanded authority to render sanctions against non-parties.

Respectfully,

Original Signed

Charles W. Austin, Jr.

CWAjr:mmi

---

[3] Such oversight by the Director of Arbitration is already being utilized in the context of removing arbitrators from panels.

[4] PIABA also suggests that there is a very real question as to whether an attorney sanctioned by an arbitrator would have standing to bring a post-award proceeding in court to challenge the sanction. If not, then the sanctioned "party representative" is effectively deprived of all review of the sanctioning arbitrator(s)' decision.