

How do Arbitrators Allocate Forum Fees?

Before you read ahead, try to answer these questions from your own experiences. By and large, is it the brokerage firm or the investor who is assessed the forum fees at the end of the arbitration? Does it depend upon whom the victor is or does the brokerage firm usually get tagged with the bulk of the forum fees, even when it wins? Does the type of dispute matter as to these outcomes (for instance, when the broker-dealer is the Claimant or when the investor is the Claimant)? What about the forums — would you expect the fee allocations to be significantly different, depending upon whether you are a party at the AAA or at one of the major SRO forums, e.g., the NASD or the NYSE?

This article utilizes statistics regarding forum fee allocations at the top three securities arbitration forums, that supply some of the answers to these questions. The information was derived from SAC's Award Database and focuses exclusively upon Awards issued during 1994. In the case of the AAA, the only Awards used by SAC were those made publicly available by the AAA under its revised Securities Arbitration Rules (SAR), adopted May 1, 1993.

There were 52 such SAR Awards. Other AAA securities Awards may have issued during 1994, as only those which were filed with AAA on or after May 1, 1993 are disclosed under the Public Award program. That program requires that the party names be redacted from the Public Award. As exclusive distributor of the AAA Public Awards, SAC does the redacting. We are permitted to use all of the Award information in compiling, analyzing, and publishing Award statistics, so long as party names are not related to a specific Award.

Methodology

In preparing this Survey, we reviewed Member/Customer Awards and customer-initiated Awards (claims

of all sizes were treated as a group) from the three major forums, AAA, NASD, and NYSE. Forum fee allocations are classified into four different groups: (1) those in which the broker-dealer is ordered to pay the bulk of the forum fees; (2) those in which the customer is ordered to pay the bulk of the forum fees; (3) those in which the fees are split between the Claimants and Respondents; and, (4) those in which the Arbitrators order a refund of the fees and charge neither party. This last category is least used, as one might expect, making up less than 3% of the allocations at any one of the forums.

Our survey classified fee allocations as Category 1, indicating that it is a "broker-dealer" assessment, even though co-parties on the same side as the broker-dealer might be charged as well. A Category 3 "split" payment does not necessarily mean that the split was even. It also covers circumstances in which both sides were assessed, albeit unequally, so long as the portion charged to a party was more than *de minimus*. Moreover, we look to the ultimate payee in making our classifications. Thus, a party may be ordered to pay forum fees, yet be afforded the opportunity to collect from its adversary. We count that allocation as one assessed against the adversary.

At AAA, the Arbitrators also allocate the arbitrators' compensation. Our survey does not attempt to deal with arbitrator compensation. Compensation is sometimes a higher amount than the forum fees, depending upon the time spent at hearing, but, generally speaking, the allocation made with respect to forum fees is followed as to Arbitrator compensation.

Member/Customer - AAA

Eighteen of the 52 Public Awards at AAA are classified as Member/Customer Awards, in which the broker-dealer sought recovery of a deficit in the former client's account. This is a relatively high percentage of the cases

filed with AAA. At the same time, all of these cases were filed by one broker-dealer. Remember, access to the AAA for a broker-dealer, absent a party stipulation, will rely upon inserting the AAA as a choice in the brokerage firm's customer agreement. Thus, for most of the larger houses, which continue to exclude AAA as a choice from their agreements, AAA is not an option when pursuing a customer debit.

Judging from the record of that one broker-dealer, we wonder whether excluding the AAA may hold some downside. This firm's record, during 1994, reflected an impressive 94% "win" rate. Seventeen of the eighteen cases resulted in monetary Awards and, in each case, almost a full recovery was granted of the amount claimed. Of \$183,800 in claims, the brokerage firm was awarded \$179,300.

Of course, the assessment of costs is a substantial consideration. Here, the AAA's overall results were more evenly spread than the SRO forums. As to one of the 18 Awards, we were unable to discern the allocations. As to the remaining 17, four times the customer was charged (25%), 6 times the broker-dealer was charged (37.5%), and 6 times the fees were split (37.5%). In the losing case, the broker-dealer was charged fees and compensation both. In aggregate, though, the broker-dealer's responsibility for fees was either eliminated or mitigated in the majority of its victories. We also noted that the number of hearing days exceeded one on only a single occasion, when three days were required to complete the hearing phase.

Member/Customer - SRO Forums

There is a common assumption that the brokerage firm will be charged, win or lose, particularly when it is the initiating party. That did not appear to be true at the AAA. Would this be the case at the SRO forums as well? To our surprise (because we, too, have been

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ing statistical 'evident partiality' in violation of 9 U.S.C. §10(a)(2)."

Two recommendations flow from these preliminary conclusions. First, the SEC "might well consider conducting a meaningful study into the SRO arbitrator pool selection process so that

a fair and impartial body of arbitrators can once again be created." Secondly, the Panel selection process should be randomized. "PIABA's 1991 legislative platform called for the adoption of a requirement that: 'Each arbitration forum shall timely propose arbitrators

through a fair and impartial, random selection process which insures public confidence in the arbitration system.'" (ed: *We present more on certain of the PSE Awards in "In Brief," this issue.*)

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subject to this assumption), Arbitrators at the SRO forums more commonly avoided the splitting of fees, but also more commonly allocated the bulk of the fees to the Respondent-customer.

The second surprise we encountered, in reviewing the SRO statistics, is the very probable observation that brokerage firms have ceased to place considerable reliance upon the arbitration process for their collection efforts. At NASD, there were only 29 Member/Customer cases carried to decision in 1994. Perhaps, there were many more such cases that were filed, then settled, but other statistics available to us lend doubt to that proposition. At NYSE, it was the same. Only 15 Awards were rendered in this category during 1994.

At NASD, where all registered broker-dealers are members, 11 of the 29 Awards were distributed among small firms. Only Dean Witter (6) and PaineWebber (5) were at all active. At NYSE, Shearson accounted for five cases, Merrill Lynch for two, and Gruntal for two. In the last couple years, NYSE and, particularly, NASD, have made it more expensive to bring the small debit balance case. Both forums assess a non-refundable charge (which may be allocated) to members for filing claims and the NASD tacks on a member surcharge (that is not allocable), whenever the firm is a party to a filed arbitration. This may go far in explaining what appears to be the case, that brokerage firms are now taking their collection matters out of arbitration.

As to the forum fee allocations in Member/Customer Awards at the SRO forums, the results were quite comparable. The investor was assessed the bulk of the fees in 16 of the cases at

NASD (55.2%) and 9 of the cases at NYSE (60%); the broker-dealer was primarily assessed in 8 of the NASD cases (27.6%) and in 4 of the NYSE cases (26.7%); some splitting of the fees occurred in 5 of the NASD cases (17.2%) and in 2 of the NYSE cases (13.3%). NASD had 9 cases which went to multiple hearing sessions and a total of 45 sessions in aggregate; NYSE had 5 cases which went to multiple hearing sessions and a total of 49 sessions in aggregate.

Case outcomes were decidedly in favor of the BD-Claimant, but somewhat more varied at the SRO forums than at AAA. Five of the 29 NASD cases were losers for the broker-dealer Claimant. In one of these five, the customer was charged; in two, the broker-dealer was charged, and in the remaining two, the fees were split. At NYSE, two of the 15 cases were losers for the brokerage firm. In one of the losers, the fees were split, while the broker-dealer was charged in the other.

As to the SRO's, then, the customer is held responsible for the forum fees in the majority of the collection matters. Much of the time, though, the broker-dealer will not recover its non-refundable deposit. It is less likely, in comparison to the AAA, to be charged all of the fees, but also less likely, viewing our admittedly small sample, to emerge victorious.

SAC will continue the results of this survey in the next edition, where we will review the outcomes for 1994 Awards in customer-initiated claims.

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