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July 21, 2005

Secretary Jonathan G. Katz  
Securities and Exchange Commission  
450 Fifth Street, NW  
Washington, DC 20549-0609

**Re: File No. 4-506, Request for Rulemaking  
Appeal of Erroneous and/or Corrupt NASD decisions to an Administrative Judge**

Dear Mr. Katz:

Thank you for this opportunity to comment on The Petition submitted by Avery B. Goodman.

For several years I have been researching NASD arbitration. In particular, I am conducting a statistical study on the relationship between damage claims and awards.

The Petition gives some irrefutable examples of flagrant failures by the NASD to honestly apply its own rules for arbitrator selection. The NASD allows persons to serve as arbitrators who have close associations to the securities firms that are parties to the arbitration. The NASD ignores complaints to remove the inappropriate arbitrators resulting in extreme bias in favor of securities firms. At present there is no mechanism to address the NASD's misconduct. The Petition proposes that an SEC administrative judge resolve such complaints.

I support the Petition's proposal.

Moreover, the problem identified by the Petition is just one of countless similar problems – many of which result from the NASD's conflict of interest. I recommend that the SEC as well address the other problems.

### **The NASD is Breaking its Own Rules**

The Petition gives some egregious examples where the NASD allowed persons to serve as arbitrators who had close associations to the securities firms that were parties to the arbitration. In both cases the parties did not select the problem arbitrator but rather the NASD unilaterally appointed them. And in one case the problem arbitrator was actually affiliated with the firm that

was also a party to the arbitration. The Petition quotes the NASD rules that explicitly prohibit the problem arbitrators from serving. The NASD ignored numerous complaints to remove the problem arbitrators resulting in a bias in favor of the securities firms. Clearly these examples evidence the NASD's unconscionable conduct.

If the NASD is so openly and blatantly denying justice to clients of a counsel as savvy, resourceful, and tenacious as Goldman, then on numerous other issues they also must be denying justice to hundreds of other customers and employees.

Indeed, routinely both arbitrators and the NASD break the NASD's own rules when it gives an advantage to securities firms. Many arbitrators have been known to steer document production, examination, and cross-examination in favor of securities firms. They narrow or broaden cases in support of securities firms. Some arbitrators grant or deny motions and argument so as to confer a benefit to securities firms. They ignore obvious abuses of the arbitration process or evidence of illicit business practices by securities firms. In short, arbitrators make a series of unusual, irrational, inconsistent comments and decisions whose only purpose is to help securities firms. And even when customers and employees prevail in spite of the blatant hostility and obstacles, arbitrators have been known to ignore the facts and the law and decide in favor of securities firms.

At present there is no mechanism to address the NASD's appointment of problem arbitrators or any of the other above-cited problems. If in the course of an arbitration hearing, employees or customers realize that the arbitrators or the NASD are breaking the rules, there is no way to fix the trouble. Persons who have raised their concerns have been ignored or even punished by even harsher treatment from the arbitrators and the NASD.

Even after the hearing, there is no way to address these problems. Usually arbitrators do not report misconduct by their fellow arbitrators. And even when customers and employees complain to the NASD about arbitrators' conduct, the NASD snubs the complaints. Virtually all misconduct by arbitrators and securities firms goes unpunished. The NASD does not even prevent further abuses. In fact, since the NASD does not enforce its rules, many arbitrators and securities firms break the rules as part of a deliberate and calculated strategy.

As a result the NASD is denying customers and employees fair arbitrations. Decisions are almost impossible to appeal – regardless of how egregious they may be.

I recommend that the SEC investigate the appointment of problem arbitrators. The SEC should discipline the responsible parties and then ensure that the problem does not occur again. Likewise the SEC should address the above-cited similar problems.

## Conflicts of Interest

The Petition correctly states that a conflict of interest within the NASD is the main cause of appointment of problems arbitrators. It explains:

The governing officials of NASD are involved in conflicts of interest, involving member brokerage firms. These conflicts cause many written rules to be ignored. NASD has been involved in incidents, which can be characterized as nothing less than institutionalized bias against customer claims.

The Petition goes on:

The interweaving, and interdependence, of NASD's staffers, with the NASD membership, is a recipe for erroneous decision-making, and outright corruption. Arbitration cases, administered by NASD, are essentially lawsuits against NASD members. Because the brokerage firms being "sued" are indirectly appointing the NASD officials, those appointees cannot be counted on to administer the system impartially. Obviously, brokerage firms do NOT want to lose cases, but they DO want to insulate themselves against money awards to former customers.

The Petition mentions two NASD administrators in particular:

NASD Director, George Friedman, and NASD President Linda Feinberg, both serve at the pleasure of a Board of Governors, elected by the same securities brokerage firms who are involved in NASD arbitration cases.

Actually a much stronger indictment can be made. The NASD creates the false illusion of fairness. It seeks to lull customers and employees into a false sense of security. The NASD makes numerous misleading or outright false proclamations of its diligence to protect the "integrity of the markets." It deceptively disguises itself as their friend. In the rare occasion that it appears that the NASD has disciplined a securities firm, it is merely administering a slap on the wrist to an industry that could easily afford to pay minor fines.<sup>1</sup>

Obviously the NASD and its administration are advocates for the industry. It is their job to hide the industry's conduct – even immoral and illicit conduct - from the public and to evade punishment. In particular, it is their job to minimize reparations to injured customers and employees. While the NASD administration has the right to chose to be the toadies of the

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<sup>1</sup> For example, for several years securities firms have manipulated cases involving tens-of-millions of dollars or more in damages by simply refusing to abide by document discovery rules. The NASD's crass press releases bragged, for instance, that it finally fined Morgan Stanley \$250 thousand dollars for abusing document discovery. While that fine may seem large when compared to a customer's or employee's life savings, it is negligible when judged against to what a single securities firm manager may take home in only one week.

industry, they do not have the right to deceive and cheat customers, employees, regulators, and legislators.

To evaluate NASD claims in any other context would be naive and, therefore, detrimental to customers and employees as well as the country's fiscal health. I urge the SEC to scrutinize and investigate the NASD administration's various proclamations and their ill-affect on the securities markets.

### **There needs to be a Mechanism to Address Complaints**

The Petition astutely concludes, "People who are burdened with conflicts of interest should not be making important legal decisions which can be directly affected by their conflicts." It proposes that an SEC administrative judge resolve such complaints:

If the Director refuses to remove, or reclassify (as either a public or non-public arbitrator), an arbitrator for cause, upon petition by the claimant, an administrative judge of the SEC, appointed pursuant to 5 USC 3105, shall review the matter on an expedited basis, and shall determine whether or not to order removal or reclassification of the arbitrator. He shall send a copy of his decision, directly to the parties, and also to the Director. The right to have a review by an administrative judge of the SEC shall be retroactive.

Likewise:

If the Director refuses to remove an arbitrator for failure to disclose, upon petition by the claimant, an administrative judge of the SEC, appointed pursuant to 5 USC 3105, shall review the matter on an expedited basis, and shall determine whether or not to order removal of the arbitrator. He shall send a copy of his decision, directly to the parties, and also to the Director. The right to have a review by an administrative judge of the SEC shall be retroactive.

I support the Petition's proposal.

Thank you for your consideration.

Sincerely,



Richard Skora