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September 11, 2003

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

Re: File No. SR-NASD-2003-95 -- NASD Proposed Change to Rule 10308: Restrictions of Eligibility to Serve as a Public Arbitrator

Dear Mr. Katz:

The Arbitration Committee of the Securities Industry Association ("SIA")[1] appreciates the opportunity to comment on the referenced NASD rule filing which seeks to amend NASD Rule 10308 and 10312 of the Code of Arbitration Procedure ("Code"). Among other things, the intended purpose of the rule proposal is to implement various changes to the arbitrator disclosure provisions, as well as to the definition of public and non-public arbitrators consistent with the recent Perino Report recommendations.[2]

Overall, the Committee supports and concurs with many of the proposed changes. We disagree, however, with the modifications to NASD Rule 10308(a)(5) subsections (A)(iv) and (B)(i), as we believe them to be overreaching and potentially detrimental to the depth of the NASD arbitrator pool. As detailed below, we believe that these new provisions will yield few benefits to investors and indeed, ultimately, may disenfranchise from the arbitration process altogether increased categories of otherwise qualified individuals who could, and should, serve. Moreover, if adopted, the provision will undoubtedly become the source of protracted information requests and challenges for cause, thereby undermining the efficiency of the

[1] The Securities Industry Association, established in 1972 through the merger of the Association of Stock Exchange Firms and the Investment Banker's Association, brings together the shared interests of more than 600 securities firms to accomplish common goals. SIA member-firms (including investment banks, broker-dealers, and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. According to the Bureau of Labor Statistics, the U.S. securities industry employs nearly 800,000 individuals. Industry personnel manage the accounts of nearly 93-million investors directly and indirectly through corporate, thrift, and pension plans. In 2002, the industry generated $222 billion in domestic revenue and $356 billion in global revenues. (More information about SIA is available on its home page: www.sia.com)

[2] Report to the Securities and Exchange Commission regarding Arbitrator Conflict Disclosure Requirements in NASD and NYSE Securities Arbitrations (Perino Report), on November 4, 2002.

arbitration process itself. Accordingly, we urge the Commission to reconsider those portions of the rule proposal. Alternatively, to the extent the Commission approves these provisions, we respectfully request that it require NASD to add a provision to Rule 10308 that provides additional assurance that individuals whose interests are aligned with the plaintiffs' bar may not serve as industry arbitrators.

I. Rule Proposal

Among the chief objectives of the proposed rule amendments is to ensure that individuals with "*significant*" ties to the securities industry do not serve as public arbitrators. To that end, NASD proposes to modify the definition of non-public arbitrator in Rule 10308(a)(4) of the Code to:

- Increase from three years to five years the period for transitioning from an industry to public arbitrator; and

- Clarify that the term "retired" from the industry includes anyone who spent a substantial part of his or her career in the industry.

In addition, under Rule 10308(a)(5)(A), NASD also seeks to:

- Prohibit anyone who has been associated with the industry for at least 20 years from ever becoming a public arbitrator, regardless of how many years ago the association ended;

- Exclude from the definition of public arbitrator, attorneys, accountants, and *other professionals* whose firms have derived *10 percent* or more of their annual revenue, in the last two years, from clients involved in the activities defined in the definition of non-public arbitrator[3]; and

- Provide that investment advisers may not serve as public arbitrators, and may only serve as non-public arbitrators if they otherwise qualify under Rule 10308(a)(4) of the Code.

The proposed rule change would also significantly amend the definition of "immediate family member" in Rule 10308(a)(5)(B) of the Code to include various family members for purposes of further ensuring that individuals with significant, albeit indirect, ties to the securities industry may not serve as public arbitrators.

[3] We note that the word "not" appears to be inadvertently omitted from proposed new Rule 10308(a)(5)(A)(iv) as it appears in the Federal Register.

II. Specific Comments

While the Committee generally supports these proposed modifications as a step in the right direction toward reinforcing public confidence in the integrity and fairness of the arbitration process and dispelling any lingering perceptions (misguided as they may be) as to potential industry-biases of SRO-arbitration panels, as detailed below, we think that the proposed expansion of Rule 10308(a)(5)(A)(iv) is problematic on several fronts.

A. The Premise Underlying The Proposed Change Is Questionable

As a threshold matter, the Committee seriously questions the NASD's underlying premise that a person's affiliation with a business entity that occasionally represents the broker-dealer community is indicative of such "significant ties to securities industry" to warrant exclusion from service as a public arbitrator. We also question the reasonableness of the proposed 10% threshold, which we believe to be too low.

Under the proposal, if a "firm" derives 10% of its annual revenue from business transactions with individuals or entities associated with the securities industry, then any "professional" associated with this firm is deemed inherently pro-industry and is precluded from serving as a public arbitrator. Because most of these individuals would not qualify as "nonpublic arbitrators," their exclusion as "public arbitrators" means they will be unable to serve as arbitrators at all. The public's trust and confidence in the arbitration process will hardly be enhanced by excluding from the process broad groups of people based solely on their employment status regardless of the how far removed that the relationship is to the broker-dealer community.[4]

Indeed, in its current form, the proposal effectively removes from the public arbitrator pool members of the plaintiffs' bar employed by a law firm that predominately represents brokers in employment actions against their former employers. Thus, in some instances, the new modifications are counter-productive to the very goals articulated by the NASD.

B. The Language Of The Proposed Change Is Imprecise.

Our concerns are further exacerbated by the rule's usage of such terms as "professional" and "firm". Although these terms exist in the current rule, we believe that the new amendments should more precisely define the category of individuals to which they apply. Specifically, it is unclear what is meant by the phrase "other professional" since the term "professional" can apply to a broad range of individuals in varied positions. One view is that the word "professional" applies to almost any individual with

[4] Notably, the Perino Report does not recommend lowering of the existing 20% threshold.

a skilled labor job.[5] This could include, for example, paralegals, secretaries, information technology staff, bookkeepers or other support staff. Equally imprecise is the word "firm" since this too is fairly broad and without further definition can apply to a range of businesses. Thus, when applied, the practical effects of the rule can be irrational, as well as counterproductive to the goal of strengthening investor protection and public confidence in the NASD arbitration forum. The following examples illustrate how under the new rule certain otherwise qualified individuals might be prevented from serving as public arbitrators.

Example 1: Law firm that has large employment practice derives a significant percentage of its revenue from representing brokers in employment disputes against their former employers. All professionals, including director of human resources, are precluded from serving as public arbitrator.

Example 2: An accountant in private practice with her own accounting firm prepares tax returns for clients. Ten percent (10%) of the accountant's clients are either brokers, dealers or firms registered under the Commodity Exchange Act. The accountant is not eligible to serve as a public arbitrator.

Example 3: A full service financial corporation with thousands of employees has a subsidiary brokerage business that generates ten percent (10%) of the corporation's revenue. All "professionals" at the corporation are precluded from serving as public arbitrators.

Certainly, this cannot be the intention of the NASD. Accordingly, we urge the NASD to reconsider this portion of the proposal.

C. <u>The Full Implications of The Proposed Change Are Uncertain.</u>

As detailed above, approval of the NASD's proposal could severely reduce the number of competent candidates eligible to serve in the role of public arbitrators. Because NASD has offered no empirical evidence or data to support the rule proposal, the full impact upon the depth of the eligible arbitrator pool is unclear at this point. What is certain is that those individuals that fall within the newly expanded definition will likely not serve <u>at all</u> -- either as public or industry arbitrators. Equally certain is the protracted and cumbersome information requests relating to revenue, business relationship, and the like, that will naturally flow from the new rule.

[5] The noun "professional" is defined as, *inter alia*, "a person who does something with great skill." *See* WEBSTER'S NEW WORLD DICTIONARY, Third College Edition (Simon & Schuster 1988). Accordingly, the word "professional" can mean a skilled employee who is good at his or her job.

D. The Expansions to Section 10308(a)(5)(B) are Overbroad

The Committee also finds problematic the proposed expansions to the definition of "immediate family" which would preclude from service as a public arbitrator any parent, child, stepparent and stepchild of an individual who spent a "substantial part" of his or her career in the securities industry, whether or not they share the same home or have any financial interdependency. As with the proposed expansions to subsection (a)(5)(A)(iv), this provision also is too overbroad and needlessly reduces the universe of otherwise qualified public arbitrators while providing nominal benefits to investor protection. No credible evidence supports banning adult children and stepchildren from arbitrator service based solely on the fact that their parents or stepparents might once have been employed, in one capacity or another, by a broker-dealer. Nor is there support for precluding people who have entered retirement simply because their adult children and stepchildren have business ties, direct or indirect, to the industry. We therefore respectfully recommend that the Commission decline to approve this modification as well.

III. Conclusion

In light of the foregoing, the Committee respectfully requests that the Commission not approve the portions of the rule filing discussed above. If you have any questions or require further information, please contact the undersigned or Amal Aly, SIA Associate General Counsel at 212 618-0568.

Sincerely,

Edward Turan
Chair, SIA Arbitration Committee