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Via FedEx

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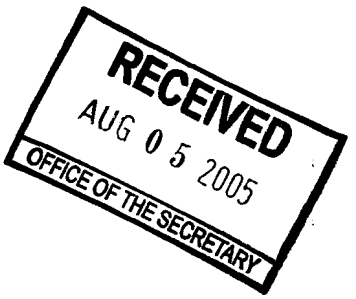
Jonathon Katz
Secretary
U. S. Securities and Exchange Commission
450 Fifth Street, NW
Washington, DC 20549



Re: File No. SR-NASD-2005-032
Proposed Rule Changes to NASD Code of Arbitration
Relating to Written Explanations of Arbitration Awards

Dear Mr. Katz:

We wish to express our concern with Proposed Rule No. SR-NASD-2005-032. This rule change would require arbitrators to issue an "explained decision" when such a decision was requested by a customer or an associated person in an industry dispute.

As further explained below, we believe that this proposed rule will have a negative impact on the National Association of Securities Dealers, Inc. ("NASD") arbitration system for three reasons: first, the change will lead to a stricter application of law to the facts, which will likely be detrimental to customers; second, the explained awards will begin to act as unreliable *de facto* precedent; and third, most arbitrators are not trained to provide the type of disclosures proposed and avoid substantial challenges to the awards.

Application of Law

We firmly believe that, while the proposed rule is meant to protect customers, it will actually result in practical detriment.

One of the primary effects of this proposal will be to increase arbitrators' focus on strictly applying applicable law to the facts of each case. Arbitration panels likely will be motivated to carefully apply the law to avoid challenges to awards. Consequently, based upon our experience serving as NASD arbitrators, panels will be less likely to make equitable awards that provide a customer a recovery when the strict application of the law would dictate no recovery should be awarded.

The existing law in many jurisdictions is both clear and straightforward. The law sets forth distinct tests and requirements for a customer to recover on common customer claim

theories such as negligence, suitability, churning, and misrepresentations and omissions. These standards, however, are not always aligned with the claims and theories advanced by customer claimants in arbitration. In our opinion, customer claimants are increasingly seeking to obtain relief based on sentiments of "equity" or "fairness." Factual presentations and pleadings are based more on the perceived injustice done to the claimant than on legal standards. However, as arbitrators increase their focus on following the law in order to explain an award, cases that previously resulted in what amounts to be "equitable" or "fair" relief will now be denied recovery.

In other words, the compromise process that often characterizes panel deliberations will give way to an all or nothing approach that likely will lead to the customer getting nothing.

Effect as Precedent

Another major concern of significant factual disclosure is the increased potential for use of prior arbitration decisions as precedent in later proceedings. This exposes major problems. First, NASD decisions are very fact specific, making other cases poor guidelines for a panel, despite superficial similarities as communicated by decisions that are not written by judges trained in the common law. Second, arbitrators are not trained to provide opinions either incorporating or excluding legal theories.

Decisions are Fact Specific

The current state of the law, especially with regards to suitability, negligence, and misrepresentations and omissions, is extremely fact specific. It is the individual customer, their broker, their investments, and other individual factors that determine whether there is a basis that leads to recovery.

Under the proposed rule, as panels are faced with increasing numbers of published decisions containing factual summaries and descriptions, they also will be faced with increasing numbers of decisions that appear factually similar. However, due to the individualized and unique nature of the claims that are prevalent in NASD claims, facial similarities between cases are at best irrelevant and at worst dangerously misleading. To the extent that panels can find a decision that appears similar and use that to justify their decision, or, worse, rely on the prior decision as indicative of the proper course of action, parties will be deprived of the individualized fact-based inquiry that currently is an integral part of the arbitration process.

Moreover, the decisions will not be written or applied by individuals trained in the principles of reasoning that drive the common law in United States jurisprudence. Instead, panels will be inundated with decisions and arguments of advocates that do little to resolve the specific dispute before them.

Arbitrators Are Not Trained for This Process

There is no requirement that arbitrators be attorneys, nor that they have any sort of legal training. Yet, this proposal asks the arbitrators to distinguish between legal and factual conclusions for purposes of explaining their decision. The proposed rule acknowledges that requiring legal decisions is impractical. *See* SR-NASD-2005-032; SEC Release 34-52009 at 3-4. However, it puts arbitrators without any legal training in the position of determining which portions of their thought process have a factual basis and which have a legal one.

It is, of course, possible for panels to simply disclose the basis for their opinions without a thorough and reasoned consideration of whether each point is actually fact-based or law-based. The inevitable outcome of this, however, is a range of opinions that may or may not include legal analysis of the facts. This will eviscerate any consistency of disclosure among panels, and result in dramatic variations between customer experiences in NASD arbitration. A decrease in the consistency of the process cannot bode well for customer confidence or for any rational means of predicting outcome on the part of the industry members.

Conclusion

In short, while this proposed rule may be facially attractive as a pro-customer reform, the net effect of the rule likely will be detrimental to customers and the integrity of the process.

Very truly yours,

HONIGMAN MILLER SCHWARTZ AND COHN LLP

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cc: The Hon. William H. Donaldson, Chairman
The Hon. Paul S. Atkins, Commissioner
The Hon. Cynthia A. Glassman, Commissioner
The Hon. Harvey J. Goldschmid, Commissioner
The Hon. Roel C. Campos, Commissioner