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Richard P. Ryder, President

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Jonathan G. Katz, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-9303

RE: SR-NASD-2005-046
NASD Fees on Statutory Discrimination Claims

Dear Secretary Katz:

The NASD's proposal to cap an employee's contribution to forum fees at $200 presents a surprising and fairly revolutionary concept. The idea that the broker-dealer will pay virtually all of the fees if there is a statutory discrimination claim involved in the dispute with a former or current employee will create unnecessary distortions in the arbitration process and lead to cries from other disputants for similar treatment. The question is why is this change needed?

The distortions that we foresee if the brokerage firm is charged the fees for both sides are the following:

1. Arbitration hearings will be longer. If employees no longer have to fear that protracting the proceedings will lead to being charged with the hearing session fees, tactical considerations will favor protracting the proceedings.

2. Employees who have colorable discrimination claims will assert those claims, even when the heart of a dispute really relates to lost compensation or wrongful termination. Asserting such claims in any proceeding, even when the broker-dealer initiates the arbitration, will convert the fee structure into a "BD pays all" case. The Rule, then, encourages claims that might otherwise not be pursued.

3. To the extent that Item 2 above is accurate, the outcome of bringing discrimination claims that are really tangential will be (1) the arbitration will last longer than it would otherwise have been and (2) the discrimination claims will be dismissed. We understand that, in theory, attorney fees may be assessed against Claimants who bring frivolous claims, but think it unlikely that arbitrators who are not permitted to charge the employee any forum fees will feel empowered to assess that employee the other side's attorney fees.

4. The greater incidence of fee-driven discrimination claims and the consequent dismissals will create a terrible outcome record for employee discrimination claims in arbitration. This will lead to another "black mark" for SRO arbitration that will likely be blamed on arbitrator bias arising from the fact that the brokerage firms are repeat players who pay virtually all of the arbitrators' fees.

5. A fee structure so radically different from that which governs all other forms of dispute before NASD arbitration panels encourages dissatisfaction among other claiming parties who have to share or risk paying the forum fees to have their cases decided. The question, why just discrimination claims, will be forcefully put by consumer and investor advocates.

6. The establishment of a blanket rule that ties the hands of arbitrators simply displays a patronizing disregard for the ability of arbitrators to stay within appropriate boundaries. It takes away an important tool arbitrators have for controlling party conduct at hearing and for encouraging expeditious proceedings.

Why is this change good for arbitration or good social policy for that matter? Why is there an urgency to implement this drastic re-structuring of the traditional fee schedules, when it otherwise seems inadvisable? NASD seems to state that this change is being pushed by compelling case law among the federal circuits. There may be justification for developing review standards to allow fee waivers, but there is no compelling reason to offer this blanket fee waiver, especially when it constitutes bad arbitration policy.

NASD has a process for waiving fee charges when parties can justify a financial need for special treatment. Were waiver grants increasing in number, NASD could supply real justification for the Rule proposal, since the brokerage firm would be paying its share of the forum costs and NASD would be shouldering the remainder. NASD offers no evidence that the incidence of such waiver requests has increased.

NASD cites two federal court decisions, one that took place in 2000 *(Green Tree v. Randolph)* and the other which was decided in 1997 *(Cole v. Burns Intl.)*, in support of its premise that the time is now for adopting this radical fee change One might merely note that the two decisions were rendered five and eight years ago, but, besides that, *Green Tree* dealt with the truth-in-lending claims of a mobile home owner. The lessons of *Green Tree* are applicable to all federal statutory claims, not just employment discrimination claims.

This U.S. Supreme Court case did indeed opine that forum costs could constitute a barrier to a party's ability to vindicate her statutory rights and, from that standpoint, there is validity to NASD's concern that onerous arbitration fees must be avoided. However, the *Green Tree* Court also found that the burden was on the claiming party to prove the existence of a barrier and that a case-by-case examination of the question was appropriate. NASD appears to be using *Green Tree* to justify a blanket fee exemption when a more liberal fee waiver program would work better and more pointedly address "vindication of rights" concerns.

The *Cole* decision in 1997 did involve statutory discrimination claims by a former Burns International employee, but *Cole* did not hold that forum fees had to be paid by the employer. As NASD notes in its Rule filing, the *Cole* Court objected to any requirement that the employee pay "all or even part of the arbitrator's fees and expenses." In a subsequent case before the D.C. Circuit, which examined how the principles enunciated in *Cole* would work in practice, one can see the difference between *Cole's* approach to fee sharing and the NASD's more radical fee-shifting proposal.

In *LaPrade v. Kidder Peabody*, a securities arbitration case decided in 2001, the D.C. Circuit considered the fee assessments by a NASD Panel in an arbitration (NASD ID #93-04030 (1/8/99)) that dealt with statutory discrimination claims and charges of defamation. The Panel assessed almost $9,000 against a victorious Claimant (total forum fees were $70,000), who then sought to invoke *Cole* to avoid any assessment. The *LaPrade* Court confirmed the charges, ruling that *Cole* "does not bar the assessment of all forum fees against an employee."

Arbitrators are not prohibited by the *Cole* decision from assessing an employee that portion of the forum fees which does not constitute arbitrator compensation and that portion of arbitrator compensation that reasonably relates to non-statutory claims. *LaPrade* also placed the burden on the employee to demonstrate that the arbitrators' assessment offended those boundary lines. Despite this explanation of the *Cole* precepts, NASD has opted for a "BD pays all" approach that shifts virtually all forum fees to the employer and requires no showing by the employee of need or unfair fee allocations.

Cole, it should be noted, dealt with allegations of statutory discrimination, but the holding with respect to forum costs is not restricted to that particular type of statutory claim. Both *Cole* and *LaPrade* make this clear. Closer examination of both the *Green Tree* and *Cole* precedents demonstrates that neither evinces a concern about forum costs that is limited to statutory employment discrimination claims in particular and neither advocates a complete fee-shifting on a blanket basis.

NASD offers no other justification for its automatic fee-shifting proposal than the *Cole* and *Green Tree* precedents and no justification is offered for why these precedents require radical action at this juncture. Given that the rationale of *Cole* and *Green Tree* extends to all or many statutory claims, we believe that this NASD action, if approved, will accelerate demand for fee-shifting revisions in arbitrations dealing with investor's federal and state statutory claims.

I personally find it difficult to justify having this kind of fee structure applicable only to statutory employment discrimination claims. No Appellate Court of which we are aware has held that forum costs must be paid by an employer and then expressly limited that holding strictly to statutory employment discrimination claims. The California Supreme Court has developed a five-factor test for determining the fairness of arbitration agreements in the *Armendariz* [v. Foundation Health Psychcare Services, 24 Cal.4th 83 (2000)] case, one facet of which was that the employer had to pay the forum costs. That

case involved a state statutory discrimination claim under the California Fair Employment and Housing Act.

Since that time, the *Armendariz* principles of arbitration clause enforcement have been extended by the Court to unwaivable non-statutory claims that impact public rights (*Little v. Auto Siegler, Inc.,* No. S101435 (2003)*)*. Just recently, the Court ruled in an insurance case *(Boghos v. Lloyd's of London,* No. S075492, 7/21/05) that the *Armendariz* principles do not extend to common law claims. Both the *Little* and the *Boghos* decisions leave a negative inference that statutory claims of all kinds may be covered by *Armendariz.* We have seen California rulings in securities employment cases that apply *Armendariz's* fee-shifting edict (*McManus v. CIBC, 134 Cal.Rptr.2d 446 (Cal. App., 2Dist., 2003); Irwin v. UBS PaineWebber,* 324 F.Supp.2d 1103 (C.D. Cal. 2004)) and there may soon be California rulings following *Armendariz* in other statutory claim contexts.

We cannot believe that NASD is adjusting its fee policies based upon the decisions under California state law. To the extent that it might be, NASD would be advocating the extension of a policy adopted in one state to disputes in all of the states of the Union. In any case, this examination of expanding California case law projects the considerable likelihood that a fee-shifting policy that is initially restricted for no principled reason to statutory employment discrimination claims will inexorably extend to other areas where significant statutory claims are in dispute.

The Commission may not care to interfere with a SRO decision that appears restricted to a change in how fees are assessed, particularly when the fee-shifting does not favor the broker-dealer. This fee change, though, bears implications for the arbitration process that require considerable deliberation and may well cause negative changes in the workings of a relatively speedy and efficient arbitration process. The Commission should be concerned with changes that will reduce the effectiveness of the SRO arbitration process and should not favor radical changes when modest adjustments would suffice. The Commission should not endorse blanket exemptions when an occasional waiver would work just as well.

Sincerely,

Richard P. Ryder